

Iowa Tax Reform Guidance: Deemed Repatriation of Deferred Foreign Income

On December 22, 2017, President Donald Trump signed Public Law 115-97, commonly referred to as the Tax Cuts and Jobs Act (TCJA). The law added new section 965 to the federal Internal Revenue Code (IRC). Section 965 requires U.S. shareholders of specified foreign corporations to include in their federal income for the last tax year beginning before January 1, 2018 (generally, tax year 2017), accumulated post-1986 deferred foreign income. For more information on which taxpayers are affected and which income is included, see IRC section 965 and [IRS guidance](#).

Iowa has not conformed to any changes included in the TCJA for tax year 2017. As a result, any accumulated post-1986 deferred foreign income included in a taxpayer's 2017 federal income tax return pursuant to Section 965 should not be included on that taxpayer's 2017 Iowa income tax return.

This publication is intended to reflect tax year 2017. Certain taxpayers may be eligible for special elections under Section 965 that would cause some of this income to be able to be included in later years. Due to changes in IRC conformity from year to year, Iowa may treat the amounts included in federal income in future years under Section 965 differently for Iowa purposes than as described here.

Participation Exemption

Section 965 includes a deduction from the amount of income included under that section known as the "participation exemption." Iowa has not conformed to this deduction meaning taxpayers may not use it to reduce their income on their Iowa return.

Iowa Adjustments by Tax Type:

Because Section 965 income is reported in different ways for federal purposes, depending on tax type, any Iowa conformity adjustment to account for this income will depend on the tax type.

Individuals: For federal purposes, individuals are required to report the net amount of Section 965 income as a single figure showing the income reduced by the deduction. This means the net Section 965 amount entered on federal form 1040 (line 21) should not be included on the IA 1040.

Trusts & Estates: For federal purposes, trusts & estates are required to report the net amount of Section 965 income distributed to beneficiaries as a single figure showing the income reduced by the deduction. This means the net Section 965 amount distributed to beneficiaries entered on federal form 1041 (line 8) should not be included on the IA 1041.

According to the IRS guidance, Section 965 income and deductions not



Mission Statement:

The mission of the Iowa Department of Revenue is to serve Iowans and support state government by collecting all taxes required by law, but no more.

distributed to beneficiaries are not reported on the federal 1041 but are only reported on the Transition Tax Statement required by the IRS. Therefore, no adjustment should be needed to the amounts shown on the IA 1041; taxpayers are not required to submit the Transition Tax Statement to the Department.

Corporations: According to the IRS guidance, Section 965 income and deductions are not reported on the federal 1120, they are only reported on the Transition Tax Statement required by the IRS. Therefore, no adjustment should be needed to the amounts shown on the IA 1120 or IA 1120F. If income or a deduction attributable to Section 965 were included on the 2017 federal 1120, the income would need to be subtracted and the deduction added back on the Iowa form for that year.

S-Corps: The amounts of Section 965 income and deductions reported by S-Corporations flow through from the federal 1120S Schedule K to the IA 1120S. Therefore, adjustments for Section 965 income and deductions are necessary on the IA 1120S. Any Section 965 income on line 10 of the federal Schedule K must be subtracted from Iowa income on line 8 of the IA 1120S. Any Section 965 deduction on line 12d of the federal Schedule K must be added back to Iowa income on line 3 of the IA 1120S.

Partnerships: The amounts of Section 965 income and deductions reported by Partnerships flow through from the federal 1065 Schedule K to the IA 1065. Therefore, adjustments for Section 965 income and deductions are necessary on the IA 1065. Any Section 965 income on line 11 of the federal Schedule K must be subtracted from Iowa income on line 6 of the IA 1065. Any Section 965 deduction on line 13d of the federal Schedule K must be added back to Iowa income on line 3 of the IA 1065.

Partners/Shareholders/Members: The amounts shown on the *Other Income* and *Other Deductions* lines on any 1065 or 1120S K-1 (either Iowa or federal K-1) may include amounts attributable to Section 965 income and deductions, respectively. Per IRS guidance, the Partnership, S-Corp, LLC, or similar entity should have provided each partner, shareholder, or member with information about the partner's, shareholder's, or member's share of Section 965 income and deductions. Any amounts of income or deductions attributable to Section 965 included on any K-1 should be excluded when entering amounts from any K-1 on the partner's, shareholder's, or member's own Iowa income tax return.

Deduction for Federal Income Taxes

Iowa law allows taxpayers to deduct federal income taxes paid or accrued during the tax year. This deduction is for 100% of taxes paid or accrued for individuals and for 50% of taxes paid or accrued for corporations. Taxpayers are permitted to include the amount of any federal taxes paid during the tax year on income from Section 965 deemed repatriation in calculating the Iowa deduction for federal taxes for that year.

Section 965 offers taxpayers subject to this deemed repatriation the option to pay any tax due on that income in installments over the course of eight years. If a taxpayer makes this election for federal purposes, that taxpayer may only include the amount of the current year federal installment payment in calculating the Iowa deduction for that year.

What does this mean?

- No income or deductions resulting from Section 965 should be included on any 2017 Iowa income tax return.
- Iowa taxpayers may include the amount of any federal taxes paid during the tax year on Section 965 income in calculating their Iowa deduction for federal taxes paid.
- The steps a taxpayer needs to take to ensure Section 965 income and deductions are not included on their Iowa return may be different depending on tax type.