

Iowa Nonconformity: The Federal Consolidated Appropriations Act of 2021

On December 27, 2020, President Donald Trump signed Public Law 116-260, the Consolidated Appropriations Act, 2021. This federal law includes a number of federal tax changes, some with retroactive effect.

Iowa generally conforms with the federal tax changes to the extent they affect Iowa income taxes for tax years beginning on or after January 1, 2020, except as described below or as otherwise specified by Iowa law.

Iowa has not conformed with any of these federal tax changes to the extent they apply to a tax year beginning prior to January 1, 2020.

This guidance focuses primarily on Iowa's nonconformity with this federal law for tax years beginning prior to January 1, 2020. Not all provisions of the Consolidated Appropriations Act, 2021 are covered by this guidance. Changes in this federal law that affect prior-year federal income tax payments may affect the computation of the federal income tax deduction or refund for Iowa tax purposes for those years, and are outside the scope of this guidance.

- **Deductibility of business expenses related to Paycheck Protection Program (PPP) loans under sections 276(a) and 278(a) of Division N of the Consolidated Appropriations Act, 2021**

Sections 276(a) and 278(a) of Division N of the federal Consolidated Appropriations Act, 2021, enacted on December 27, 2020, provide in part that no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of the income exclusion for forgiven PPP loans. For federal tax purposes, these provisions supersede the IRS's previous positions in Notice 2020-32 and Rev. Rul. 2020-27 which disallowed deductions for business expenses paid using forgiven (or expected to be forgiven) PPP loans. Due to the enactment of section 276(a), the IRS has issued Rev. Rul. 2021-2 which obsoletes those previous positions.

Application to Iowa: For any tax year beginning on or after January 1, 2020, Iowa is conformed with the income exclusion for forgiven PPP loans, as well the provisions of section 276(a) and 278(a). In other words, for tax year 2020 and beyond, a taxpayer's income tax treatment of PPP loans and related expenses should be the same on their Iowa tax return as it is on their federal tax return.

For tax year 2019 (fiscal-year filers), Iowa is conformed with the income exclusion for forgiven PPP loans, but is not conformed with the deductibility of qualifying expenses or other tax benefits provided in sections 276(a) and 278(a). In other words, taxpayers who have their PPP loan forgiven and properly excluded from federal gross income in tax year 2019 will also qualify for the exclusion from income in tax year 2019 for Iowa tax purposes, but those taxpayers will not be eligible to deduct business expenses in tax year 2019 that were paid using forgiven (or expected to be forgiven) PPP loans or to otherwise rely on sections 276(a)

and 278(a). These Iowa taxpayers must follow the guidance set forth in IRS Notice 2020-32, Rev. Rul. 2020-27, and Rev. Proc. 2020-51, without regard to Rev. Rul. 2021-2. To the extent a taxpayer deducts business expenses on their 2019 federal tax return pursuant to section 276(a) or 278(a), those business expenses must be added back on their IA 101 Nonconformity Adjustments form, line 12, for tax year 2019.

Additional Background: The CARES Act of 2020 established a loan program for qualifying small businesses to incentivize such businesses to keep workers on payroll despite possible financial strain due to the COVID-19 pandemic. Under the PPP as enacted in the CARES Act, loans may be fully forgiven if the funds are used as permitted under the program, and such forgiven loans are excluded from federal gross income under section 1106(i) of the CARES Act. Following that federal legislation, the Internal Revenue Service (IRS) issued binding guidance in Notice 2020-32, Rev. Rul. 2020-27, and Rev. Proc. 2020-51, which disallowed certain deductions for business expenses paid using forgiven (or expected to be forgiven) PPP loans, and provided a safe harbor for deducting expenses related to a loan that subsequently does not receive forgiveness.

Due to “rolling conformity,” Iowa automatically conformed with this income exclusion for forgiven PPP loans for tax years beginning on or after January 1, 2020. Also, pursuant to 2020 Iowa Acts, House File 2641, section 109, Iowa conformed with this income exclusion for forgiven PPP loans for fiscal-year taxpayers whose 2019 tax year ended after March 27, 2020. By conforming with this income exclusion for tax years 2019 and later Iowa also conformed with the disallowance of business deductions paid using forgiven (or expected to be forgiven) PPP loans as set forth in IRS Notice 2020-32, Rev. Rul. 2020-27, and Rev. Proc. 2020-51. As described above, Iowa is now conformed with the deduction provisions of 276(a) and 278(a) and Rev. Rul. 2021-2, but only for tax years beginning on or after January 1, 2020.

- **Clarification of tax treatment of certain loan forgiveness and other business financial assistance under sections 278(b), 278(c), and 278(d) of Division N of the Consolidated Appropriations Act, 2021**

Section 278(b) of Division N of the federal Consolidated Appropriations Act, 2021, enacted on December 27, 2020, provides in part that certain Economic Injury Disaster Loan (EIDL) Grants under CARES Act section 1110(e) and Targeted EIDL Advances under the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Title III of Division N of the federal Consolidated Appropriations Act, 2021) shall not be included in the recipient’s gross income, and no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of that income exclusion.

Application to Iowa: For any tax year beginning on or after January 1, 2020, Iowa is conformed with the income exclusion for certain EIDL grants and Targeted EIDL Advances, as well the other provisions of section 278(b). In other words, for tax year 2020 and beyond, a taxpayer’s income tax treatment of EIDL Grants and Targeted EIDL Advances and related expenses should be the same on their Iowa tax return as it is on their federal tax return.

For tax year 2019 (fiscal-year filers), Iowa does not conform with section 278(b), so to the extent a taxpayer received an EIDL grant during a tax year beginning before January 1, 2020, those grants must be included in the taxpayer’s Iowa income to the same extent they would have been included in federal income prior to the enactment of the Consolidated Appropriations Act, 2021, and related expenses may only be deducted in computing Iowa income to the same extent they would have been deductible prior to the enactment of the Consolidated Appropriations Act, 2021. These required nonconformity adjustments, if any,

should be made on the taxpayer's IA 101 Nonconformity Adjustments form, line 12, for tax year 2019.

Section 278(c) of Division N of the federal Consolidated Appropriations Act, 2021, enacted on December 27, 2020, provides in part that subsidies received for certain covered loan payments under CARES Act section 1112(c) shall not be included in the recipient's gross income, and no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of that income exclusion.

Application to Iowa: For any tax year beginning on or after January 1, 2020, Iowa is conformed with the income exclusion for subsidies received for certain covered loan payments under CARES Act section 1112(c) and the other provisions of section 278(c) of Division N. In other words, for tax year 2020 and beyond, a taxpayer's income tax treatment of subsidies received for certain covered loan payments under CARES Act section 1112(c) and related expenses should be the same on their Iowa tax return as it is on their federal tax return.

For tax year 2019 (fiscal-year filers), Iowa does not conform with section 278(c), so to the extent a taxpayer received a subsidy for certain covered loan payments under CARES Act section 1112(c) during a tax year beginning before January 1, 2020, those subsidies must be included in the taxpayer's Iowa income to the same extent they would have been included in federal income prior to the enactment of the Consolidated Appropriations Act, 2021 and related expenses may only be deducted in computing Iowa income to the same extent they would have been deductible prior to the enactment of the Consolidated Appropriations Act, 2021. These required nonconformity adjustments, if any, should be made on the taxpayer's IA 101 Nonconformity Adjustments form, line 12, for tax year 2019.

Section 278(d) of Division N of the federal Consolidated Appropriations Act, 2021, enacted on December 27, 2020, provides in part that grants for shuttered venue operators made under section 324 of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Title III of Division N of the federal Consolidated Appropriations Act, 2021) shall not be included in the recipient's gross income, and no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of that income exclusion.

Application to Iowa: For any tax year beginning on or after January 1, 2020, Iowa is conformed with the income exclusion for these shuttered venue operator grants, and the other provisions of section 278(d) of Division N of the Consolidated Appropriations Act, 2021. In other words, for tax year 2020 and beyond, a taxpayer's income tax treatment of subsidies received for shuttered venue operator grants provided under section 324 of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act and related expenses should be the same on their Iowa tax return as it is on their federal tax return.

- **Election to waive application of certain modifications to farming losses under section 281 of Division N of the Consolidated Appropriations Act, 2021**

The CARES Act (P.L. 116-136) included substantial changes to the federal treatment of net operating loss (NOL) deductions for tax years 2018-2020. Division N of the Consolidated Appropriations Act, 2021 (P.L. 116-260) added further clarification to these CARES Act changes for farming losses. Iowa NOLs are calculated independently of federal NOLs, so these federal changes do not directly apply to the Iowa treatment of NOL deductions.

Prior to the CARES Act, under the Tax Cuts and Jobs Act (TCJA), federal NOL carrybacks were only allowed for farming losses and certain other taxpayers for tax years beginning after

December 31, 2017. Under the CARES Act, taxpayers must carry federal NOLs arising in tax years 2018, 2019, or 2020 back five years by default, but taxpayers may elect to waive all carryback under IRC section 172(b)(3). Under section 281 of Division N of the Consolidated Appropriations Act, 2021, farmers who elected the two-year carryback for an affected tax year before the CARES Act passed may keep that election, rather than applying the five-year CARES Act carryback period. Additionally, farmers who waived their carryback period for federal purposes for tax years 2018 or 2019 may revoke that waiver for federal purposes.

Application to Iowa:

Iowa sets its own carryback and carryforward provisions for NOLs, and these Iowa carryback and carryforward provisions are not directly affected by the federal changes. However, Iowa Code section 422.9(3)(c) only allows taxpayers to waive the Iowa carryback period if they also waive the *federal* carryback period under IRC section 172(b)(3) for the same tax year. As noted on the 2018 and 2019 IA 123 Net Operating Loss (NOL) Schedule instructions, this means that for tax years 2018 and 2019, most taxpayers have no way to waive their Iowa NOL carryback because, under the version of the IRC with which Iowa conforms, there is no federal carryback to waive for those years or the deadline to waive the carryback has passed. In summary, generally only taxpayers with a farming loss may waive their carryback period for Iowa purposes in tax years 2018 and 2019, and may only do so if they timely elected to waive their carryback period for federal tax purposes by the due date of the 2018 or 2019 federal tax return, including extensions. Taxpayers who chose to waive their federal farming loss carryback on an original and timely-filed 2018 or 2019 return are not permitted to revoke that waiver for Iowa purposes, even if they would be permitted to do so for federal purposes under section 281 of Division N of the Consolidated Appropriations Act, 2021.

Accrual basis taxpayers are required to accrue federal income tax refunds resulting from NOL carrybacks or carryforwards to the year in which the NOL occurred for Iowa purposes. See Iowa Admin. Code r. 701—40.18(1)“a”(1), and Iowa Admin. Code r. 701—53.2(1)“a”(1). Taxpayers who amend a 2018 or 2019 federal return to carry back an NOL under the new CARES Act provisions may also need to amend their Iowa returns for that year to account for any refunds received.

2020 Iowa Acts, House File 2641, which Governor Reynolds signed into law on June 29, 2020, allows taxpayers to make an Iowa-only election to waive an Iowa NOL carryback, independent of whether the taxpayer chose or was required to carryback an NOL for the year at the federal level for tax years beginning on or after January 1, 2020. See the 2020 IA 123 Net Operating Loss Schedule for more information.

- **Extension of federal residential energy efficient property tax credits and federal business energy credits under sections 132 and 148 of Division EE of the Consolidated Appropriations Act, 2021**

Section 132 of Division EE of the federal Consolidated Appropriations Act, 2021, extends the availability and credit rates of the federal business energy credit under Internal Revenue Code (IRC) section 48, including solar energy electrical business property under IRC section 48(a)(2)(A)(i)(II) and solar fiber optic business property under IRC section 48(a)(2)(A)(i)(III). The federal credit availability was extended by two years, from property that begins construction before January 1, 2022, to property that begins construction before January 1, 2024. The phase-out of the credit rate for solar energy electric property was also extended.

Section 148 of Division EE of the federal Consolidated Appropriations Act, 2021, extends the availability and credit rates of the federal residential energy efficient property tax credit under IRC section 25D, including the residential solar electric property under IRC section 25D(a)(1) and residential solar water heating property under IRC section 25D(a)(2). The federal credit availability was extended by two years, from property placed in service before January 1, 2022, to property placed in service before January 1, 2024. The phase-out of the credit rate was also extended.

Iowa provides its own solar energy system tax credit under Iowa Code 422.11L, calculated in part using a percentage of the taxpayer's allowable corresponding federal credits. However, Iowa's solar energy system tax credit is based on the IRC in effect on January 1, 2016, so Iowa is not conformed with any extension or modification to the corresponding federal credits after that date, including the extensions in section 132 and 148 described above. Therefore, Iowa's remaining credit availability and rates for 2021 and later are as follows:

- Qualified residential solar electric property described in IRC section 25D(a)(1), and qualified residential solar water heating property described in IRC section 25D(a)(2): The Iowa tax credit rate will be 11% of qualifying expenditures for installations placed in service in calendar year 2021. The Iowa credit is not available for any installation placed in service on or after January 1, 2022.
 - Qualified solar electric business property described in IRC section 48(a)(2)(A)(i)(II): For property that begins construction in calendar year 2021, the Iowa credit rate will be 11% of qualifying expenditures for installations placed in service in calendar years 2021-2023, or 5% of qualifying expenditures for installations placed in service in calendar years 2024 or later. The Iowa credit is not available for any installation that begins construction on or after January 1, 2022.
 - Qualified solar fiber optic business property described in IRC section 48(a)(2)(A)(i)(III): The Iowa credit for this type of property has not been available since January 1, 2017, for any property placed in service on or after that date.
- **Depreciation of certain residential rental property over a thirty-year period under section 202 of Division EE of the Consolidated Appropriations Act, 2021**

Section 202 of Division EE of the Consolidated Appropriations Act, 2021 changes the Alternative Depreciation System (ADS) recovery period for tax years beginning after December 31, 2017, to 30 years for residential rental property held by an electing real property trade or business that was placed in service prior January 1, 2018, but that was not subject to ADS prior to that date.

Application to Iowa:

Iowa does not conform with this change for tax years beginning after December 31, 2017 and before January 1, 2020. Therefore, affected taxpayers' Iowa depreciation deductions for this property in those tax years should not be amended to reflect this change. Taxpayers filing an original Iowa return for any of these years should calculate depreciation deductions for affected residential rental properties based on the depreciation method that would have applied prior to this change. Iowa depreciation adjustments are made on the IA 4562 A/B, Iowa Depreciation Adjustment Schedule. For tax years beginning on or after January 1, 2020, Iowa fully conforms to the applicable federal depreciation method for these properties.

- **Qualified disaster relief contributions by corporations under section 304 of Division EE of the Consolidated Appropriations Act, 2021**

Section 304 of Division EE of the Consolidated Appropriations Act, 2021 establishes a new category of “qualified disaster relief contributions” for which corporations are allowed an additional charitable deduction and increased limitation for qualified disaster relief contributions as defined in section 304(a)(2) of the Act paid during the period beginning on January 1, 2020, and ending on the date that is 60 days after the enactment of the Act.

Application to Iowa:

Iowa does not conform with this change for tax years beginning before January 1, 2020. If a corporation filing on a fiscal-year basis makes a “qualified disaster relief contribution” during their 2019 tax year, the taxpayer is subject to the regular corporate charitable contribution limit (10% of taxable income) without regard to the increased limitation and deduction provided in section 304. Affected corporations must make required adjustments to their tax year 2019 charitable contributions on the IA 101 Nonconformity Adjustments, line 12. Any contribution carryforward resulting from this nonconformity for Iowa purposes may be deducted in future years on the IA 101 Nonconformity Adjustments, line 12, according to the regular contribution carryforward rules under the IRC. For tax years beginning on or after January 1, 2020, Iowa fully conforms to this additional charitable deduction and increased limitation.

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