

Rev. Rul. 79-315, 1979-2 CB 27, IRC Sec(s). 61

ISSUE

Are rebates of Iowa income taxes received by individuals includible in their gross incomes under section 61 of the Internal Revenue Code?

FACTS

By House File 693, 68th General Assembly, approved on May 22, 1979, the State of Iowa enacted legislation providing for an individual income tax rebate for 1978 taxes.

Section 1 of the Act treats each individual as having made an additional payment of Iowa state income tax for the individual's tax year beginning in 1978. Section 4 provides that the payment is deemed to be made on the last day prescribed by law for the filing of State income tax returns for the tax year beginning in 1978 (April 30, 1979, for calendar-year individuals), including any extensions thereof. A payment is not deemed to be made unless the return is filed on or before the due date or the extended due date.

Section 2 of the Act sets forth the method of computing the additional payment. If the individual's tax liability is equal to or less than \$15, the additional payment is the amount of the tax liability. If the individual's tax liability is greater than \$15 but less than \$150, the additional payment is \$15. For all other individual taxpayers, the additional payment is 10 percent of the individual's tax liability, limited to \$250.

Section 5 of the Act treats the deemed payment of tax as an overpayment of tax. This overpayment will be credited by the State Department of Revenue against any income tax due from the individual deemed to have made the overpayment or, if no income tax is due from the individual, the amount will be refunded by the Department.

The Act became effective May 27, 1979, and will not be effective after June 30, 1980. It is intended that credits and refunds will be made within 120 days after the date a return is due, including extensions.

LAW AND ANALYSIS

Section 61 of the Code and regulations thereunder provides that, except as otherwise provided by law, gross income means all income from whatever source derived.

Section 111(a) of the Code provides, in part, that gross income does not include income attributable to the recovery during the taxable year of a prior tax, to the extent of the amount of the recovery exclusion with respect to the tax.

Section 111(b)(2) of the Code provides that the term "prior tax" means a tax for which a deduction was allowed for a prior year.

Section 111(b)(4) of the Code provides, in part, that the term "recovery exclusion" means the amount of the deduction allowed on account of the prior tax that did not result in a reduction of the taxpayer's income tax.

Under section 4 of the Act, the State of Iowa treats each individual as having made a State income tax payment on the due date of the individual's 1978 State income tax return. This deemed payment results in an overpayment of tax for 1978, thereby giving rise to a cash refund or credit. The end result of the Act is the issuance by the State of cash payments to all individual income taxpayers. Thus, the Act is merely a

means of effecting a statutory decrease in the tax liability of each individual taxpayer.

HOLDINGS

The conclusions stated below assume that the individuals' use the cash receipts and disbursements method of accounting, file state and federal income tax returns on a calendar year basis, and receive their rebate in 1979. The same principles apply to individuals who file their returns on a fiscal year basis or who receive their rebate in 1980.

(1) If an individual paid the individual's 1978 Iowa state income tax in 1978 and deducted the amount paid as an itemized deduction on the individual's 1978 federal income tax return, the amount of the refund is includible in the individual's gross income under section 61 of the Code for 1979 to the extent it exceeds the recovery exclusion provided in section 111. See Rev. Rul. 79-15, 1979-1 C.B. 80, for examples illustrating the computation of the recovery exclusion.

(2) If an individual paid the individual's 1978 Iowa state income tax in 1978 and did not deduct the payment on the individual's 1978 federal income tax return, no amount of the refund is includible in the individual's gross income for 1978 because the individual received no benefit in 1978. Rev. Rul. 79-15.

(3) If all or a portion of an individual's refund is credited against tax due for 1978, the amount credited is treated as a reduction of the outstanding liability. The amount credited against unpaid 1978 tax is neither includible in the individual's gross income for 1979 nor deductible under section 164(a)(3) of the Code as a state income tax paid in 1979.

(4) If all or a portion of an individual's refund is credited against tax due for a year prior to 1978, the amount credited against the prior year's unpaid tax is treated in the same manner as a cash refund in holdings (1) and (2) above.