

Proposal: Reduce the sales tax rate from 6.5% to 6%. (HF 2762/SF 3322 authored by Representative Rostberg and Senator Stevens and HF 2948, by Representative Lenczewski).

What are the distributional effects?

Currently, Minnesotans of all incomes pay around the same percentage of income in total state and local taxes; however, the sales tax is a greater part of the tax obligation for low-income household and becomes a smaller part as household income rises. The chart shows for each decile (which contains 10% of the state's households) how much each group pays in sales tax, how much would be saved under a 0.5% sales tax reduction, and how much this savings would be as a percentage of income.

Population Decile	Average Income	Current Sales Tax as a percentage of income	Sales Tax Savings in dollars	Sales Tax Savings as a percentage of Income
First	\$4,254	8.0%	\$26	0.62%
Second	\$8,887	5.0%	\$34	0.38%
Third	\$13,432	4.4%	\$45	0.34%
Fourth	\$18,698	4.3%	\$62	0.33%
Fifth	\$24,595	3.9%	\$74	0.30%
Sixth	\$31,549	3.5%	\$85	0.27%
Seventh	\$40,179	3.2%	\$99	0.25%
Eighth	\$51,237	3%	\$122	0.24%
Ninth	\$66,970	3%	\$149	0.22%
Tenth	\$165,330	2%	\$254	0.15%

Calculations based on the Department of Revenue's *1999 Tax Incidence Study* data for 1996 taxes. Sales tax includes both consumer sales tax and business sales tax passed through to individuals. This analysis assumes that the sales tax savings to business would be passed on to individuals in the same portion in which they pay the tax. If not all the sales tax savings is passed on to individuals, actual sales tax savings would be lower than shown in the chart above.

How Would This Proposal Affect Long-Term Funding Stability?

This tax cut would spend a little over \$663 million in the 2001 and 2002 fiscal years, out of the projected \$1.8 billion surplus expected by June 20, 2001.

What are the trade-offs?

The legislature will weigh the cost of this proposal against other spending, savings, and tax cut possibilities. Some of the major tax cut alternatives now being considered include the House Republican income tax rate cuts (which cost slightly over \$1 billion for tax years 2000 and 2001), creating a Minnesota personal dependent exemption (\$847 million for 2000-01 biennium), the "1-2-3" rate compression of property taxes (\$309 million for the 2002-03 biennium), or capping auto tabs at \$75 (\$276 million in 2001 and increasing in following years).

Who are the ultimate winners and losers?

In terms of dollars saved, upper-income families will see the largest reductions, but as a percentage of income, low- and moderate-income Minnesotans would benefit the most. Non-residents who make purchases in Minnesota would also receive some of the tax savings.