



Tax Changes in the 2000 Legislative Session

Much of the 2000 session was dominated by a disagreement about the basic budget numbers and what they meant for decision-makers. The Department of Finance’s financial forecast stated there was a \$549 million “structural balance” for fiscal year 2003, meaning that ongoing new spending or tax cuts could not exceed this amount. House Republicans argued that the forecast underestimated the amount of resources available.

In the end, the House, Senate, and Governor split \$525 million of ongoing resources three ways, with each party having \$175 million to spend as they chose. The House spent their share on tax cuts, primarily income tax rate reductions. The Governor used his third to reduce vehicle registration fees, and the Senate used their one-third for investments, mainly in K-12 education. The shrinking of the tax reductions – from a House bill that originally cut taxes by over \$850 million a year — brought about a tax bill that is fiscally responsible and that benefits all Minnesota taxpayers to some degree.

Income Tax Rate Cuts

The Minnesota income tax rates in all three brackets have been lowered, for a total tax reduction of over \$150 million per year.

Bracket	Current Rate	New Rate
Taxable income below: \$17,570 single \$21,630 head-of-household \$25,680 married filing jointly	5.5%	5.35%
Taxable income of: \$17,570 - \$57,710 single \$21,630 - \$86,910 head-of-household \$25,680 - \$102,030 married filing jointly	7.25%	7.05%
Taxable income over: \$57,710 single \$86,910 head-of-household \$102,030 married filing jointly	8%	7.85%

Note: taxable income is income after subtracting exemptions and deductions.

Minnesota Working Family Credit

The Minnesota Working Family Credit (WFC) is the state’s counterpart to the federal Earned Income Tax Credit (EITC), a refundable credit for low-income households based on their earned income and family size. The 2000 tax bill increases the WFC by around \$12 million per year, approximately \$10 million of which is funded by the TANF Reserve (federal welfare dollars). This is an increase of 13.8%. The average Working Family Credit is now is \$483, or about 33% of the federal EITC.

Since the legislature implemented an increase in the Working Family Credit as a counterpart to income tax cuts, it makes sense to consider the effects of these two tax changes together. To

demonstrate the effect of these tax cuts on total tax burden and therefore on a household's budget, column 3 of the chart below shows the tax reduction as a percentage of income. The chart shows that in dollar amounts, the tax savings increase as income increases. However, the reductions are roughly the same percentage of income for all income groups, although slightly higher in the bottom incomes, for whom the WFC makes a significant impact on overall tax obligations, and on the top of the income scale, for whom the income tax makes up the largest part of the total tax burden.

Tax Savings by Income Level: Income Tax Rate Reductions and Working Family Credit Increase		
Federal Adjusted Gross Income	Average Tax Cut	Average Tax Cut as a Percentage of Income
Less than \$9,999	\$7	0.18%
\$10,000 - \$19,999	\$24	0.16%
\$20,000 - \$29,999	\$28	0.11%
\$30,000 - \$49,999	\$42	0.11%
\$50,000 - \$74,999	\$73	0.12%
\$75,000 - \$99,999	\$111	0.13%
\$100,000 - \$149,999	\$161	0.14%
\$150,000 - \$199,999	\$231	0.15%
\$200,000 - \$499,999	\$367	0.15%
\$500,000 or more	\$1,301	0.15%
ALL FILERS	\$66	0.13%

Calculations based on data from House Research and the Minnesota Department of Revenue

2000 Sales Tax Rebate

Once again, the legislature is providing a sales tax rebate to return funds the state has on hand. The rebate will return \$635.6 million to Minnesota taxpayers, ranging from \$168 to \$2,400 for married and head-of-household filers and \$95 to \$1,200 for single filers.

The basic eligibility criteria for the 2000 Sales Tax Rebate is similar to the 1999 rebate; the taxpayer must meet one of the following criteria:

1. Filed for a property tax rebate on a 1998 Minnesota income tax return
2. Filed a 1998 income tax return and had at least \$1 of tax liability before refundable credits and was not claimed as a dependent on another taxpayer's return
3. Had homeowner property taxes reduced to \$0 in 1998 due to tornado relief
4. Was a non-resident but paid at least \$10 in Minnesota sales tax on non-business purchases

In addition, taxpayers who do not meet the above criteria qualify for the following the rebate amounts:

1. Dependents age 18 or older with wage income will receive 35% of the rebate amount for non-dependents of the same income level
2. Individuals who receive social security or railroad retirement benefits will receive an automatic rebate of \$95
3. Persons who were not dependents and filed a 1998 income tax return in order to claim a refundable credit or to get a return of withholding or estimated tax payments will receive the minimum rebate amount for their filing status

Minnesota residents will receive their rebates automatically in the mail in August; non-residents need to file an application. Taxpayers must file their 1998 income tax returns by November 30, 2000 to be eligible. An additional \$8.5 million will be mailed to persons who were eligible for the 1999 rebate but whose income tax returns were not filed by last year's rebate deadline but are filed by June 15, 2000.

Persons who have not already filed an income tax return for 1997 or 1998 still have time to do so to qualify for the 1999 or 2000 rebate. People needing assistance filing their returns can contact AccountAbility Minnesota at 612-288-9476.

In addition to the sales tax rebate, \$18 million in agricultural disaster relief will be distributed to farmers in distressed areas.

The combined effects of the income tax rate cuts, WFC changes, and the sales tax rebate are indicated below:

Tax Savings by Income Level and Family Type: Income Tax Rate Reductions, Working Family Credit Increase, and Sales Tax Rebate			
Family type and federal adjusted gross income	Dollar amount income tax/WFC reduction	Percentage income tax reduction from rate changes and WFC increase	Estimated Sales Tax Rebate
\$10,000 income			
• Married couple, 2 dependents	\$117	13.6%	\$168
• Head of household, 1 dependent	\$73	14.1%	\$168
• Single filer, no dependents	\$7	4.8%	\$116
\$25,000 income			
• Married couple, 2 dependents	\$61	27.5%	\$231
• Head of household, 1 dependent	\$33	5.5%	\$253
• Single filer, no dependents	\$27	2.7%	\$210
\$50,000 income			
• Married couple, 2 dependents	\$42	3%	\$312
• Head of household, 1 dependent	\$56	2.7%	\$338
• Single filer, no dependents	\$64	2.7%	\$259
\$100,000 income			
• Married couple, 2 dependents	\$120	2.8%	\$476
• Head of household, 1 dependent	\$134	2.8%	\$523
• Single filer, no dependents	\$133	2.5%	435
\$500,000 income			
• Married couple, 2 dependents	\$647	2.1%	\$1,522
• Head of household, 1 dependent	\$634	2.0%	\$1,522
• Single filer, no dependents	\$622	2.0%	\$1,128

Data Source: House Research. Assumptions: Taxpayers have the same income in 1998 and 2000; married spouses have equal shares of income; taxpayers making under \$50,000 claim the standard deduction and families making \$50,000 or more claim itemized deductions of 22% of gross income; taxpayers receive the Working Family Credit when eligible.

Auto Tabs Reduction

The motor vehicle registration tax (commonly called "tabs") is made up of two portions: a \$10 flat fee and an additional tax amount. The additional tax is 1.25% of the base value of the vehicle, but the amount of base value subject to the additional tax is reduced as the vehicle ages. For the first two years of the vehicle's life, the additional tax is levied on 100% of the vehicle's base value, for years 3 and 4, the tax is based on 90% of the value, and so on until the 10th year when the tax is based on 10% of the vehicle's value. At the 11th and following years, the additional tax is set at \$25. In all years, the additional tax is never less than \$25, making the total minimum tabs fee \$35.

This year's tax bill made changes to the maximum tabs amount. The tax will be calculated as usual and the amount due in the first year of the vehicle's life will be the same. In the second year, the total amount of tax is capped at \$189 and in the 3rd and all other years, it is capped at \$99. The minimum remains at \$35. It is difficult to get a good estimate of who benefits from this change. The majority of vehicles already are registered for less than \$99; the owners of these vehicles will receive no tax reduction. In addition, the motor vehicle registration tax is a regressive tax, meaning it takes a larger share of income from lower-income families. Reducing the tax only on more expensive vehicles is likely to increase the regressivity of the tax.

Tabs are a dedicated revenue source to the highway user trust fund; therefore reducing tab fees means a loss in funding. The 2000 tax bill transfers money for the lost tab revenue directly in the highway user fund in 2001 and 2002, then in following years dedicates 32% of the motor vehicle excise tax (collected when a vehicle is purchased) into the highway fund. There are concerns that this transfer will be insufficient and leave a funding hole in the fund in the future.

Property Tax

There were no changes in property tax rates this session, despite a lot of attention to the issue. The agricultural education credit was increased by \$22 million starting in the 02-03 biennium, which should lighten the property tax obligation on farms. It is likely that significant changes to the property tax system will be part of the "Big Plan" effort to reform the state's tax system in the 2001 session.

Sales Tax

Only small changes were made to the sales tax, mainly exempting certain purchases from the sales tax, for a total reduction of about \$2 million per year. These include exemptions for two types of purchases by nonprofits: large vans, buses, and trucks used for charitable purposes (purchased or leased), and construction materials to be used to make homes handicapped accessible. Purchases by state agency libraries are also now exempt. Most other items exempted from the sales tax are business inputs, including plant nursery equipment, snow-making equipment for ski resorts, maple syrup production equipment, patent drawings, cemetery maintenance expenses, construction materials for two meat processing facilities, poultry feed, and certain metalcasting materials. In addition, persons who receive motor vehicles as gifts will no longer have to pay a sales tax on that vehicle.

A more technical matter is a partial repeal of the June accelerated sales tax. Currently, merchants must remit a portion of their estimated sales tax collections for June in advance. This has the effect of moving some of the sales tax into the prior fiscal year. This has a one-

time cost of \$44.4 million in the 02-03 biennium, which is largely a matter of moving the June sales tax payments back into the appropriate fiscal year.

Other Tax Changes

Lawful gambling taxes (pull tabs, etc.) were reduced 5.5%, a reduction of \$3 million per year.

Although there was a lot of discussion of eliminating the provider tax on health care providers, this was not included in the final tax bill. However, the premiums tax on HMOs was delayed for two years, and the imposition of the tax is no longer dependent on the balance of the Health Care Access Fund.