Estimates Revised for New Information

Sales and Use Tax Proposal Regarding Pipelines
($000s)

	FY 2006	FY 2007	FY 2008	FY 2009
Compressor Fuel	$8,040	$9,370	$8,730	$8,000
Capital Equipment	$1,070	$2,350	$2,350	$2,350
General Fund Total	$9,110	$11,720	$11,080	$10,350
Assumed effective August 1, 2005	20,330		21,430	

The proposed law change reverses a 2002 Minnesota Supreme Court ruling that natural gas used by pipeline companies to power their compressors is fuel used in the industrial production of tangible personal property to be sold ultimately at retail, and that it therefore qualifies for the general exemption of materials consumed in production. Because the compressor gas was deemed "used in production," machinery and equipment used to transport the natural gas, such as pipelines and the compressors themselves, also qualify for the exemption by refund of capital equipment.

The law change provides that (1) transportation, transmission, or distribution of petroleum, gas, water, or steam through pipes, mains, or other means do not qualify for the exemption of materials used or consumed in industrial production, and (2) machinery or equipment used in transmission or distribution of petroleum, gas, water, or steam through pipes, mains, or other means do not qualify for the capital equipment exemption.

- The original estimate had two components: materials used in industrial production and capital equipment. It is the industrial production component that is here revised; the capital equipment part remains unchanged.
- The original estimate of tax on the natural gas moving through pipelines that is diverted to power pipeline compressors was based on claims submitted by companies in response to the court decision. These amounts under-represented the entire universe of potential tax on gas used to power gas pipeline compressors.
- This revised estimate for compressor gas consumption is based on Minnesota data from the U.S. Department of Energy, Energy Information Administration.
- The estimate of the price of natural gas for 2006 through 2009 is taken from natural gas futures prices from the New York Mercantile Exchange. It shows declining prices over the next four years, which are reflected in the revenue estimate.
- The estimate for FY 2006 was adjusted for an August 1, 2005, effective date.
- Regarding capital equipment, the revenue estimate is $2.35 million per year. The estimate is held constant because expenditures for pipeline equipment can vary from year to year. The estimate for FY 2006 was reduced because capital equipment refunds would be paid in FY 2006 for purchases made before the assumed effective date of August 1, 2005.
- An estimated seven companies would be affected.

Minnesota Department of Revenue
Tax Research Division
June 28, 2005

pipelines/tfe

Governor/House Republican Proposal

June 28, 2005 (evening)

Revenue Target — $30.506 billion

- Accept Governor Level — $30.238 billion
  Includes Health Impact Fee (75 cents)
- Racino — $ 218 million
- Consensus corporate items — $ 33 million
  (as previously agreed upon by Tax Working Group)
  - $17 million tax shelter re-costing
  - $16 million Great Lakes Pipeline re-costing
- Net Impact (after July erosion) of extending HIF to all tobacco products — $ 17 million

Health Impact Fee (net effect - general fund)	$380 million
• Education	$280 million
• Health and Human Services	$100 million

Racino	$218 million
• Transit/Transportation *(Transit: $40 million; Rural Roads: $6 million)*	$46 million
• Salary Supplement	$21 million
• Ag/Environment/Jobs	$ 5 million
• Pension (Minneapolis teachers)	$ 6 million
• AMT	$17 million
• Single Sales	$ 5 million
• Local Government Aid	$55 million
• Clean Water Legacy	$53 million
• Excess to cover overall target number	$10 million

E-12

- Per pupil funding increase - 4.5/4.5
- Equity
- Reform
  - QComp (Governor/House)
  - Get Ready, Get Credit (Governor/House)
  - Meaningful Parental Choice (Buesgens/Hann)
- Remove previously offered discretionary education levy ($45 million) in response to DFL property tax concern

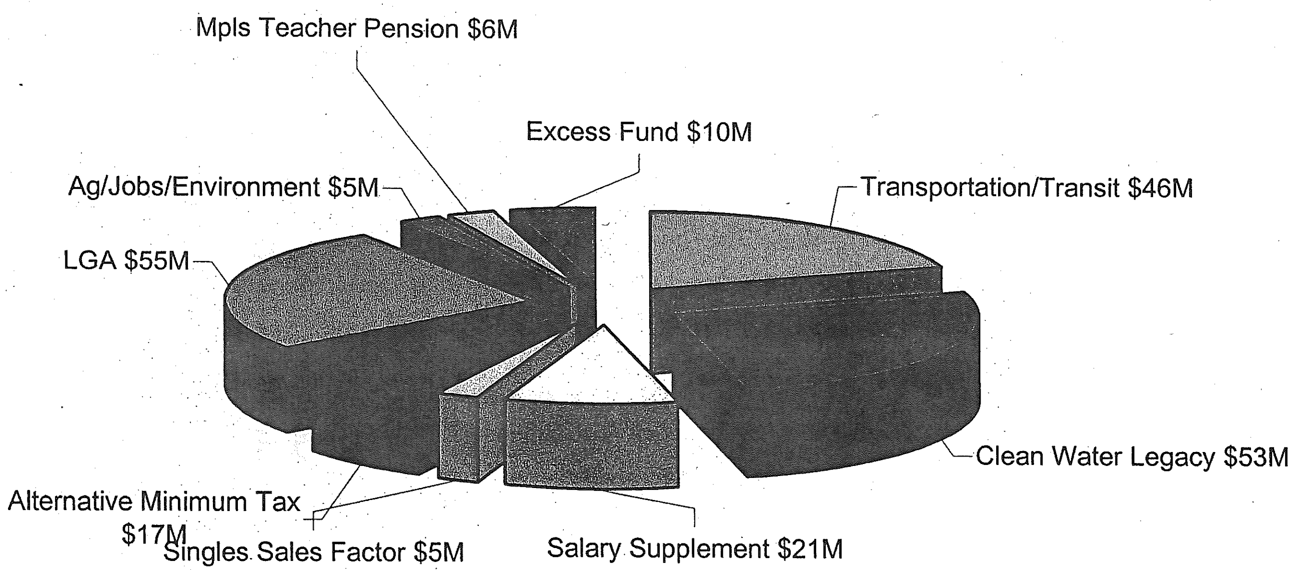
HHS

- Restore MinnesotaCare eligibility
  175% of poverty level for adults, no children; 225% of poverty level for adults, with children.
- Raised Outpatient Benefit Caps to $10,000
- Limited Benefit Set Enhancement (Supplies for Diabetics)
- COLA for caregivers at 2 percent per year
- Agreed upon "tails" to contain future costs
- Fully utilize dedicated health care revenues

Initiative and Referendum

Racino Spending

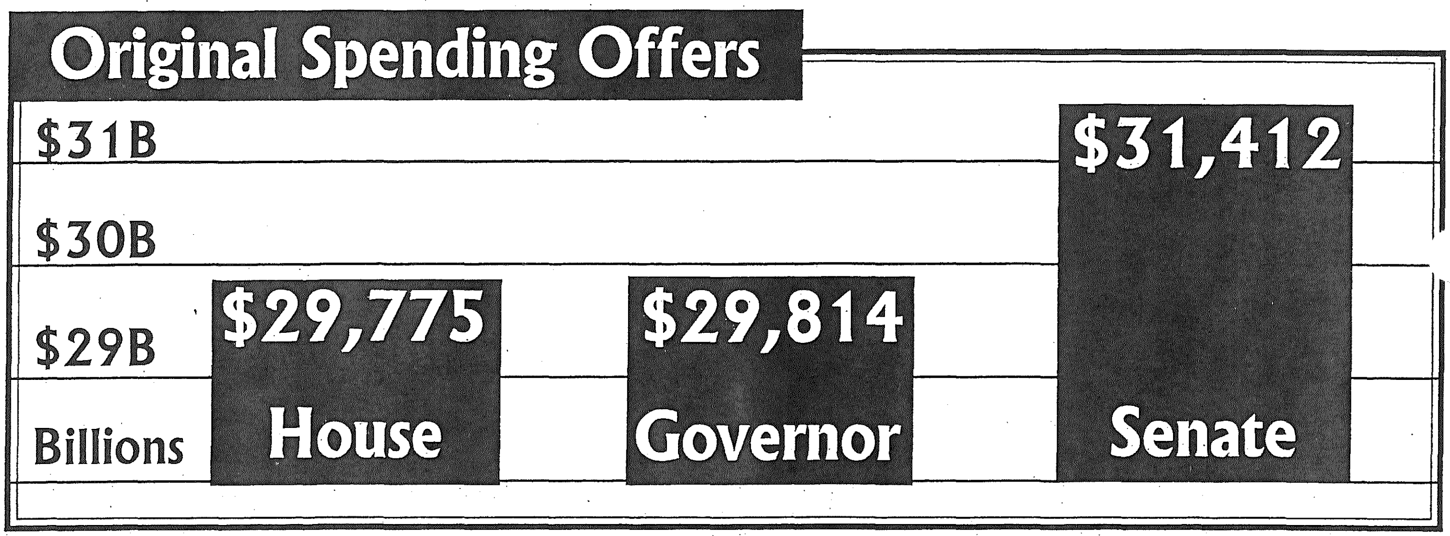
($218 Million)

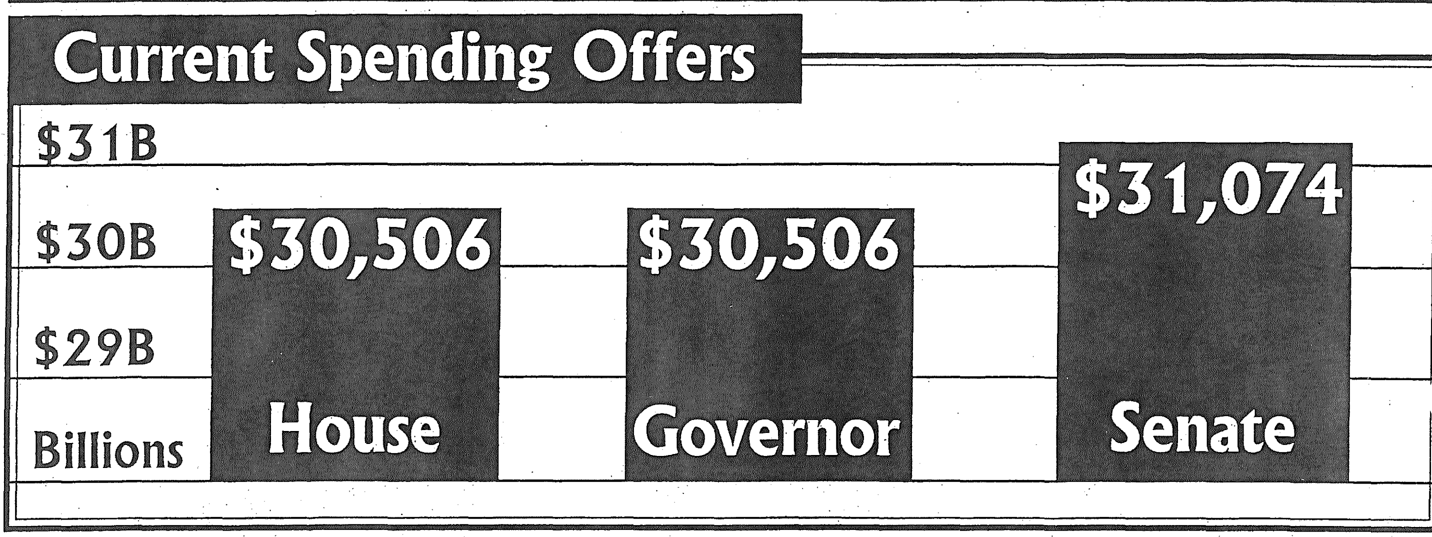


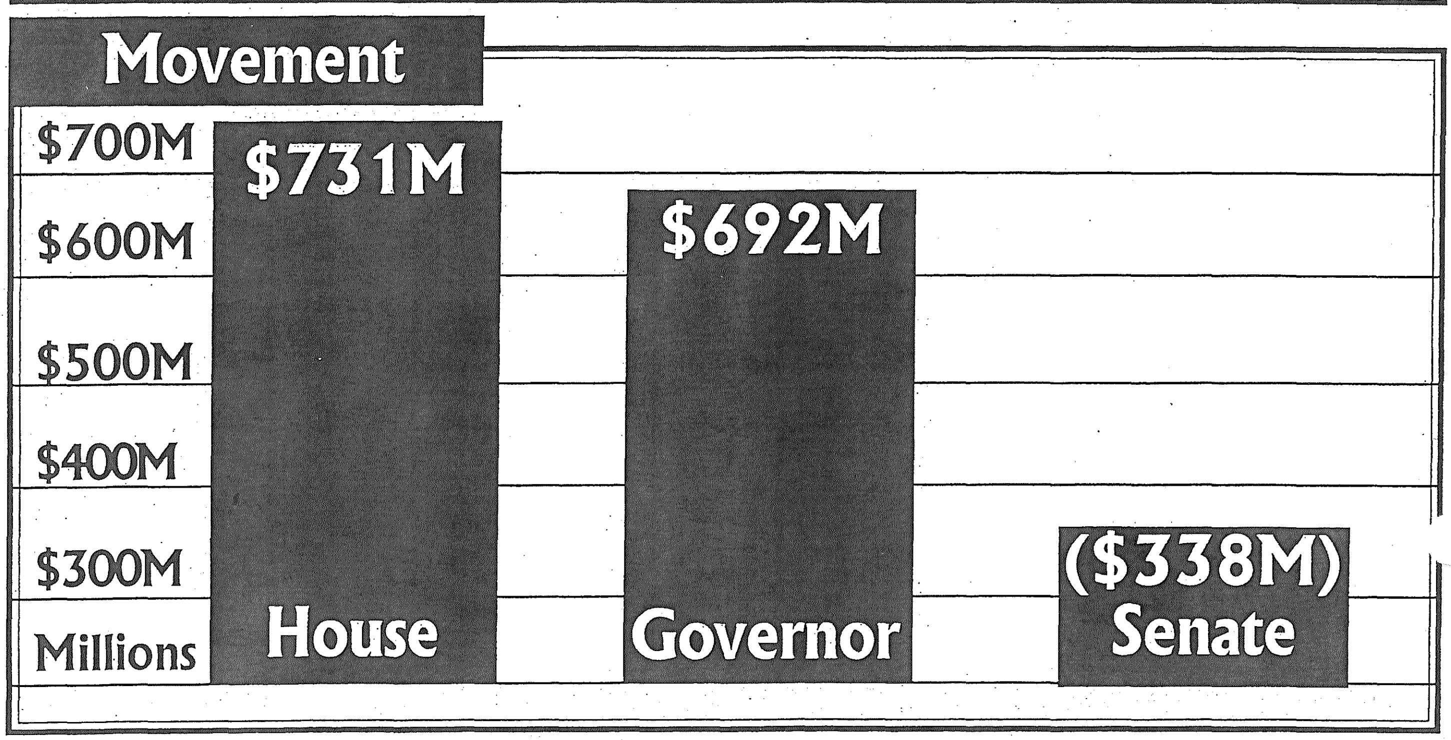
Original Spending Proposals

House	$29.775 billion
Senate	$31.412 billion
Governor	$29.814 billion
Average	$30.334 billion
Latest GOP Offer	$30.506 billion

Budget Negotiation Movement







Gov's Offer from June 28, 2005, Morning

E-12

4.5/4.5 Formula
Take out 45m discretionary levy
Gov's language on Q Comp
Best Practices Early Childhood - $3m

HHS

2%/2% COLA, paid for with corporate compliance ($50m)

To be Paid for by the $100m from the Cig Tax:

- Adults without children: go to 175% ($63m)
- Adults with children: go from 190% to 225% ($12m)
- Raise MnCare cap from $5000 to $10,000 ($22m)
- Buy back diabetic strips ($3m)

Taxes

$50m in corporate compliance (existing provision; pays for COLA)

Env/Ag/ED

Add $5m to the target
Accept Ozment/Bakk LCMR Proposal: 50% Legislators, 50% Citizens. Legislature retains right to alter the package.

Hot Topics – Pick your Favorites (Speaker proposes this could be paid for with Racino monies)

Salary Supplement	$21m
Pensions	$ 6m
Transit	$46m
LGA	$60m
AMT	$17m
Clean Water	$60m
Singles Sales Factor	$10m

#1

Tobacco Products Rate Increase

Increase rate from 35% to 90%

	FY 2006*	FY 2007	FY 2008	FY 2009
		(000's)		
Excise Tax	$16,265	$20,197	$20,802	$21,521
Sales Tax	$183	$227	$234	$242
General Fund Net Impact	$16,448	$20,424	$21,036	$21,763

* 10 months of collections

The proposal is to increase the excise tax on tobacco products other than cigarettes from the current 35% of wholesale price to 90% of the wholesale price. The proposal would not include a floor stocks fee (i.e. a fee on current inventories).

The proposal would be effective August 1, 2005.

- February 2005 forecast amounts are used.
- For the excise tax rate increase to 90%, an elasticity factor of -0.650 is used.
- It is assumed that the increase in refunds will be minimal.
- Fiscal year 2006 is adjusted for 10 months of collections.

Minnesota Department of Revenue
Tax Research Division
June 28, 2005

State Tax Rates on Other Tobacco Products

#2

January 1, 2005

State	Tax Rate/Base (1)	State	Tax Rate/Base (1)
Alabama		Michigan	32% Wholesale Price
Cigars (2)	4.0¢-40.5¢/ 10 cigars	Minnesota	35% Wholesale Price
Tobacco/Snuff	0.6¢-5.25¢/ ounce	Mississippi	15% Manufactures Price
Alaska	75% Wholsale Price	Missouri	10% Manufactures Price
[illegible]na		Montana	50% Wholesale Price
Cigars (2)	26.3¢-$2.60/ 20 cigars	Nebraska	20% Wholesale Price
Tobacco/Snuff	13.3¢/ounce	Nevada	30% Wholesale Price
Arkansas	32% Manufactures Price	New Hampshire	19% Wholesale Price
California (3)	46.76% Wholesale Price	New Jersey	30% Wholesale Price
Colorado	40% Manufactures Price	New Mexico	25% Product value
Connecticut (5)	20% Wholesale Price	New York	37% Wholesale Price
Delaware	15% Wholesale Price	North Carolina	2% Wholesale Price
Florida		North Dakota	
Tobacco/Snuff	25% Wholesale Price	Cigars & Tobacco	28% Wholesale Price
Georgia		Chew Tobacco/Snuff	16¢-60¢/ounce
Little Cigars	2.5¢/10 cigars	Ohio	17% Wholesale Price
Other Cigars	23% Wholesale Price	Oklahoma	
Tobacco	10% Wholesale Price	Cigars (2)	27¢-90¢/ 10 cigars
Hawaii	40% Wholesale Price	Tobacco/Snuf	30%-40% factory list price
Idaho	40% Wholesale Price	Oregon	65% Wholesale Price
Illinois	18% Wholesale Price	Rhode Island	30% Wholesale Price
Indiana	15% Wholesale Price	South Carolina	5% Manufactures Price
[illegible]	22% Wholesale Price	South Dakota	10% Wholesale Price
K[illegible]sas	10% Manufactures Price	Tennessee	6.6% Wholesale Price
Louisiana		Texas	
C[illegible]	8%-20% Manufacture Price	Cigars (2)	1.0¢-15.0¢/10 cigars
Tobacco/Snuff	33% Manufactures Price	Tobacco/Snuff	35.213% Manufactures Price
Maine		Utah	35% Manufactures Price
Chewing Tob./Snuff	62% Wholesale Price	Virginia (6)	10% Wholesale Pri
Smoking Tob./Cigars	16% Wholesale Price	Vermont	41% Manufactures Price
Maryland	15% Wholesale Price	Washington	129.42% Wholesale Price highest
Massachusetts		West Virginia	7% Wholesale Price
Smokless Tob.	90% Wholesale Price	Wisconsin	25% Manuafactures Price
Smoking Tob./Cigars	30% Wholesale Price	Wyoming (4)	20% Wholesale Price

Source: Compiled by FTA from various sources.
(1) The volume based tax rates were converted to cents per 10 cigars or per ounce for consistency.
(2) Tax rate on cigars varies based on the selling price.
(3) Tax rate is adjusted annually by the state, effective July 1st of each year.
(4) or 10% of the retail price.
(5) Snuff tobacco taxed at 40 cents per ounce.
(6) New tax effective March 1, 2005.

Staff Language - 6-23-05

24-Jun-05

Tax Shelter Fiscal Analysis *(dollars in millions)*

Based on Illinois Experience

- New, large penalties on specific listed transactions
- IRS listed transactions only
- Three month grace period to file and pay to avoid new penalties
- $100 M estimated, $135 Million actual collected
- Payments came from 54% individual, 46% Corporate (latest)
- Two Options: Waive future appeal or retain future appeal (most waived appeal rights)

Working Group Compromise Language (6/23/05)

- Two options for look back *(Language suggested by staff)*
- Additional "Son of BOSS" provision *(suggested by staff)*

Extrapolating from Illinois to Minnesota		
Population adjustment factor	**40%**	
Collection Potential Adjustment Factor	**147%**	[(54% x 180%) + (46% x 108%)]
per capita income tax collections -MN 180% of IL		
per capita corporate tax collections - MN 105% of IL		
High Income Adjustment	**85%**	
Illinois has proportionately more high income people (> $250K)		

Illinois Experience "Base"	**$ 135.0**	**Actual Collections**
times population adjustment	40%	
times collection potential adjustment	147%	
Times high income taxpayer adjustment	85%	
Potential Minnesota One-time Revenue	**$ 67.4**	
Ave Collection per tax year (IL six year)	$ 11.2	
Minnesota Specific Legislation Choice		
Broader look back and Son of BOSS adjustment	*105%*	
Minnesota One-Time Potential	**$ 70.8**	
MN Ongoing Potential	**$ 5.6**	
(50% of ave ann collection from above)		

	FY 06	FY 07	Biennium	FY 08	FY 09	Biennium
Revenues						
One time collection during grace period	$ 70.8		$ 70.8			$ -
On-going collections	$ 2.8	$ 5.6	$ 8.4	$ 5.6	$ 5.6	$ 11.2
Future Audit/Penalty Collections	$ -	$ 0.8	$ 0.8	$ 0.8	$ 0.8	$ 1.5
Future Refunds from appeal actions	$ -	$ (3.5)	$ (3.5)	$ (3.5)	$ -	$ (3.5)
(20% challenged - 50% lost)						
Subtotal	$ 73.6	$ 2.8	$ 76.4	$ 2.8	$ 6.4	$ 9.2
Expenses						
DOR Administrative	$ (0.1)	$ (0.6)	$ (0.7)	$ (0.6)	$ (0.6)	$ (1.2)
Subtotal	$ (0.1)	$ (0.6)	$ (0.7)	$ (0.6)	$ (0.6)	$ (1.2)
TOTAL	**$ 73.5**	**$ 2.2**	**$ 75.7**	**$ 2.2**	**$ 5.7**	**$ 8.0**

Department of Revenue Recommendation

Conscience choice to be conservative

	FY 06	FY 07	Biennium	FY 08	FY 09	Biennium
75%	$ 55.1	$ 1.7	$ 56.8	$ 1.7	$ 4.3	$ 6.0
Original Senate Estimate	*$ 60.5*	*$ 2.0*	*$ 62.5*			*$ 6.9*
Original House Estimate	*$ 36.4*	*$ 3.9*	*$ 40.2*			*$ 9.4*

Get it Done!

Budget	Bipartisan Solution	Senate's Offer		Governor's Offer	
		Senate 6/23 offer	Difference	Gov.'s 5/20 offer	Difference
Human Services: spending	**$8,340**	$8,390	-$50	$8,259	$81
Education: spending	**$12,646**	$12,851	-$205	$12,646	$0
Taxes: spending	**$3,011**	$3,026	-$15	$2,888	$123
Environment/Ag: spending	$703	$703	$0	$703	$0
Transportation: spending	$159	$159	$0	$159	$0
Pension (misc. spending)	$0	$42	-$42	$0	$0
Salary Supplement (misc. spending)	$21	$21	$0	$0	$21
Closed Bills	$5,843	$5,843	$0	$5,843	$0
Total Spending	***$30,723***	***$31,045***	***-$322***	***$30,495***	***$228***
Total Revenues	**$30,694**	$31,045	-$351	$30,495	$199
Total Spending	**$30,723**	$31,045	-$274	$30,495	$228
Reserves Drawdown	$29	$0	$29	$0	$29
Balance	**$0**	-$0	-$0	$13	$13

***Accepts Governor's $[illegible] plus $150 in FOC and an additional 25 cents on tobacco.*

Bipartisan Plan to End 2005 Special Session

Spending Agreements

Health and Human Services

$50 million less than the 6/23 Senate offer; could maintain MinnesotaCare, and a 2%/2% COLA for long-term care.

Education

Spending target allows formula at 5%/5%, but increases property taxes net statewide by $139 million and yields a property tax recognition shift of $95 million. Target also allows Senate early childhood increase. The property tax would be levied consistent with the Senate consolidated levy so that the tax burden is even across the state.

Taxes

Spending is $125 million less than Senate Tax Bill and $15 million less than the 6/23 offer. Within target, the Tax Working Group could fund an $87 million LGA increase. The revenue target does not include the alternative minimum tax reduction or conformaty with the federal marriage deduction.

Revenue Agreements

No Income Tax Increase

No new 4th tier and no increase to the 3rd tier.

Accepts the Governor's 5/20 Revenue Amount and Property Taxes

$603 million in additional revenue.
$139 million E-12 property tax target
$95 million recognition shift

Closes the F.O.C. Corporate Loophole

($150 million in revenue)

Accepts Governor's May 20 Revenue from Tobacco

75 cents per pack increase and raises an additional 25 cents per pack tobacco tax, **setting the rate at $1.00.** ***(Total of $72 million in revenue)***

The negative balance at the bottom line, $48 million, is taken from the Cash Flow Account.

: notwithstanding sections
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instrumentality of the state, provided that the property continues to be used for a qualifying purpose for at least five years from the date that the property was acquired.

Subd. 7a. **When additional taxes not imposed.** Notwithstanding subdivision 7, when real property ceases to qualify under subdivision 3 because of failure to comply with prohibitions against discrimination on the basis of sex, payment of additional taxes imposed under subdivision 7 is not required.

Subd. 8. **Lien.** The tax imposed by this section shall be a lien upon the property assessed to the same extent and for the same duration as other taxes imposed upon property within this state. The tax shall be annually extended by the county auditor and shall be collected and distributed in the manner provided by law for the collection and distribution of other property taxes.

Subd. 9. [Repealed, 1987 c 268 art 6 s 53]

Subd. 10. **Continuation of tax treatment upon transfer.** When title to real property qualifying under subdivision 3 is transferred, no additional taxes shall be extended against the property if (a) the property continues to qualify pursuant to subdivision 3 and (b) the purchaser files an application for continued deferment of taxes pursuant to subdivision 6 within 30 days after the sale.

History: *1969 c 1135 s 1; 1973 c 582 s 3; 1Sp1981 c 1 art 2 s 5; 1983 c 222 s 9,10; 1986 c 412 s 1-4; 1988 c 719 art 5 s 84; art 6 s 5,6; 1989 c 277 art 2 s 20,21; 1Sp1989 c 1 art 2 s 11; 1990 c 604 art 3 s 10; 1991 c 291 art 1 s 13; 1993 c 375 art 5 s 14,15; 1994 c 587 art 5 s 7; 1997 c 187 art 1 s 21; 1997 c 231 art 2 s 14-16; 1998 c 389 art 3 s 3-5*

273.115 [Repealed, 1987 c 268 art 6 s 53]

273.116 [Repealed, 1987 c 268 art 6 s 53]

273.117 CONSERVATION PROPERTY TAX VALUATION.

Real property which is subject to a conservation restriction or easement shall be entitled to reduced valuation under this section if:

(a) The restriction or easement is for a conservation purpose as defined in section 84.64, subdivision 2, and is recorded on the property;

(b) The property is being used in accordance with the terms of the conservation restriction or easement.

History: *1Sp1981 c 1 art 2 s 6*

273.118 TAX PAID IN RECOGNITION OF CONGRESSIONAL MEDAL OF HONOR.

An owner of homestead property who submits to the commissioner of revenue a property tax statement and reasonable proof that the owner of the property:

(a) is a veteran as defined in section 197.447;

(b) was a resident of this state for at least six months before entering military service, or has been a resident of this state for five consecutive years before submitting the statement and proof; and

(c) has been awarded the congressional medal of honor;

shall be paid by the commissioner of revenue, within 30 days after the commissioner receives the statement and proof, the amount of the owner's property tax liability as shown on the statement, up to $2,000. The surviving spouse of a property owner who has received a payment under this section may receive payment of property taxes under this section as long as the spouse continues to own and occupy the property for which the taxes were paid under this section and the property continues to be a homestead. Property taxes paid under this section reduce property taxes payable for purposes of chapter 290A.

History: *1983 c 301 s 177; 1984 c 655 art 1 s 46; 1Sp1985 c 14 art 4 s 40; 1986 c 444*