April 4, 2022

The Honorable Carla Nelson
Chair, Senate Taxes Committee
3235 Minnesota Senate Building
95 University Avenue W.
Saint Paul, Minnesota 55155

Dear Chair Nelson:

I am writing on behalf of the Minnesota Department of Revenue regarding the SF3692 as proposed to be amended. The Department of Revenue appreciates the work this committee has done to assemble this bill.

When Governor Walz and Lt. Governor Flanagan proposed their budget in February and revised supplemental budget in March, they prioritized expanding economic opportunities for all Minnesotans; supporting children and families; and protecting Minnesotans' health, safety, and well-being. The Governor also recommended investing in local jobs and projects through a proposed $2.7 billion in bonding projects.

Given the responsible stewardship of Minnesota's budget, we have a remarkable opportunity to invest in public safety, health care, and education while also supporting the middle class, working families, and small businesses. Governor Walz understands that we can reduce costs and grow our economy while protecting the health and safety of Minnesotans and ensuring every child receives a high-quality education, no matter their race or zip code. This bill has a large price tag but does not increase the fairness of our tax system. It does not help low- to middle-income Minnesotans or allow for significant investments in public services as part of the rest of the budget. At the same time, it does provide hundreds of millions in tax cuts for the wealthiest Minnesotans.

**Responding to Federal Changes**

We all agree on the importance of responding to the federal tax changes enacted since our tax statutes were last updated in 2019. Individual taxpayers, CPAs, and businesses have all expressed the need to update our tax code to reduce complexity and compliance costs. This bill adopts the Governor's approach to update the general conformity date and provide important conformity for individuals and businesses. We look forward to continuing to work with members of the committee and stakeholders on the best approach to administer this update that could impact multiple years of returns and adjustments for taxpayers.

The Governor's budget proposes conforming with many of the tax changes made by the federal government over the past three years. At least six federal bills with tax changes have been enacted since our last general update of state tax laws. Adopting the federal changes for businesses and individuals provides an investment in Minnesota's tax system to ensure that it is stable, predictable, and less complex. Much of the state tax code is based on the federal calculation of income, so conforming with these federal tax changes will allow the benefit to flow through to state taxes.

**Administration's Priorities are not Included**

It appears that a primary focus of the bill is an income tax rate cut. However, most of the tax decreases will benefit Minnesotans in the top deciles of income. Minnesota's lowest wage earners, who don't earn enough to file taxes but still pay sales taxes property taxes, and excise taxes, will receive no benefit at all from the tax bill.

The bill also provides a subtraction for all Social Security income – benefiting the state's highest earners. Social Security recipients already pay tax on only a portion of their social security income. After the federal exclusion and Minnesota subtraction, about 53% of recipients pay no state tax on benefits. Even the highest income seniors pay tax on only 85% of their social security income.

The bill also provides relief for the wealthiest Minnesotans through changes to the estate tax by allowing a larger amount of the estate to go untaxed. This bill enacts portability for the Minnesota estate tax, allowing a second decedent spouse's estate to use any unused exclusion amount left over from the first decedent spouse's estate. In other words, this allows a second decedent's spouse estate to increase their general exclusion amount. In some cases, that may double the amount of the exclusion.

The bill also fails to include important changes to refundable income tax credits that Minnesota families rely on: Minnesota's Child and Dependent Care credit and the K-12 Education credit. The Governor's budget recognizes the challenges Minnesota parents face in paying for quality, affordable childcare by increasing the income threshold and maximum credit amount for Minnesota's refundable Child and Dependent Care Credit, which will lower taxes for more Minnesotans. Eligibility for the refundable K-12 credit for families with expenses for children in school is also expanded.

**Other Areas of Concern**

The bill does not include any of the department's policy and technical changes intended to clarify the administration of the tax statutes. One of our key strategies to achieve our mission is to engage in meaningful interaction with customers to provide superior service. During those interactions, we often hear or notice items in the tax code that could be clarified, updated, or corrected. These items may be small, but they're important to ensure we are providing customers with the information, education, and services they need to efficiently navigate

Minnesota's tax opportunities and obligations. We hope we can continue to work with the committee to adopt these changes.

The department would like to reaffirm our commitment to making sure policies included in the final tax bill can be administered. As this bill move through the process, we will continue to share policy and administrative feedback on these proposals. Additionally, we will provide information about the administrative costs for the changes in the bill.

Sincerely,

Robert A. Doty

Robert A. Doty
Commissioner

Cc: Senator Ann H. Rest
Ranking Minority Member, Senate Tax Committee