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LEGISLATIVE RESEARCH COMMITTEE

BUDGET MESSAGE OF GOVERNOR ORVILLE L. FREEMAN

Delivered Before a Joint Session of the Minnesota
Legislature on Tuesday, January 15, 1957

Mr. Speaker, Mr. President, and Members of the 60th Session of the
Minnesota Legislature:

Pursuant to the authority vested in me as Governor, I present herewith the
biennial budget message. This message supplements the recommendations contained in
the biennial budget, copies of which were released today to all legislators.

I. Introduction

When I came before you two years ago to present my first budget message, we
faced extremely serious problems in developing a balanced budget. We were approaching
the current biennium with virtually no balance in the General Revenue Fund and with
the necessity of using most of the existing balance in the Income Tax Fund. I am
pleased to observe now that our budgetary situation today is much improved and that
we can view the next two years with confidence and optimism.

1. Two Years of Study and Analysis.

Two years ago the preparation of the budget was an unusually difficult task.
I had only a few weeks to develop my recommendations, and I frankly stated in my
1955 message that I would have wished much more time. Today I am pleased to report
that the recommendations I am laying before you have had what may very well be the
most intensive and continuous study ever given the preparation of a State budget.

Behind my recommendations are a new approach to the entire budgeting
process and the extensive findings of many special studies. These include the
Minnesota Self-Survey project, the Governor's Tax Study Committee, and your own

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Legislative Interim Commission to Study State Building Needs -- to mention only three that have special relevance for the budget process.

The many studies completed during the interim since the 1955 Session place us in a greatly strengthened position to deal with our financial problems. It is fair to say that, compared with other states, all of whom face problems similar to ours, we are relatively better prepared to deal with these problems. I attribute our good situation to the cooperative spirit and dedicated service of so many members of the legislature, administrative officials and employees, and private citizens who took part in the many interim projects. I wish here to express my gratitude to all of you who participated in the Self-Survey and who contributed to the success of the many interim committees.

2. Economy of the State Continues Strong.

As I noted in my inaugural address, the general condition of the State's economy continues to be strong. In 1956 our per capita income increased and our employment level reached a new high. The recession on the Iron Range which I noted two years ago appears now to have lifted, and, while we still view farm conditions with some concern, we are hopeful that improvement will be forthcoming in this area of our economy, too.

We have begun to realize the benefits from our program to attract new industry to the State. Our revenue receipts have continuously increased, exceeding the estimates that we felt were justified two years ago. On the whole, our economic condition and outlook gives cause for optimism.

3. A Strengthened Budgeting Process.

The budget document is presented in a new format designed to facilitate your review and evaluation. It includes, among many other improvements and innovations, explanatory notes for most accounts requiring legislative action and summary

statements covering all state funds. Basic to its scheme of organization is a clear identification of expenditures and proposed financing.

In preparing the budget we employed an entirely new approach. In previous years it has been customary for the Governor to determine his recommendations with little or no consultation with the departments that would be affected by his decisions. This time we undertook extensive consultation with the departments. Wherever practicable we reviewed with them the decisions that it was necessary for us to make. We carefully examined all departmental requests to make certain that our recommendations would be fully justified by both need and by our capacity to finance.

In developing their requests, the departments followed what we termed "hard criteria," and I am confident that my recommendations cover only basic and essential needs, because, in determining my recommendations, I followed firm guide lines that provided appropriations to cover essential salary adjustments, to acquire equipment that will reduce total operating costs, and to employ new personnel only in cases where their need could not be denied.

I regret that it was again necessary to withhold support for many requests that I know have merit. As you understand, the budgeting process involves, on the one hand, the determination of basic and essential needs and, on the other hand, the setting of an outer limit beyond which we cannot go without overtaxing our resources:

4. Increased Needs Reflect Basic Factors.

Underlying the need for increased appropriations which are presented in the budget are three basic factors that should be noted:

(1) The larger part of the increases I am recommending are in the fields of welfare and education. This is directly related to the character of our

population distribution. We have today a disproportionate number of very young people who require education and of aging citizens who require welfare assistance. Therefore, to maintain minimum levels in these areas inevitably requires substantially increased appropriations.

(2) My recommendations are intended to meet the pressing need of providing adequate salaries for state employees. The budget document contains the new salary assignments certified by the Civil Service Board in August of 1955.

The Board's action was consistent with the strong recommendation made by the Self-Survey Task Force on Employees Salaries that the state take immediate steps to provide pay rates comparable to those of private industry.

(3) My recommendations also recognize the necessity of raising the quality of our services to the level intended by the governing legislation. In such specific areas as parole supervision, mental health care, and our inspectional programs, I have attempted to ensure adequate support. Unfortunately in the past a number of activities have had such inadequate financial support they have not been able to develop proper standards.

5. Framework for Budgetary Presentation.

The presentation of the budgetary information will be unusually complex because of the need to make clear the relationship between the recommendations for appropriations and the financing program.

It may, therefore, be helpful if I pointed out here that, following this introduction, I will review the recommendations and present condition of each major fund, after which I will turn to a detailed explanation of my financing program for the next biennium.

II. The General Revenue Fund

I turn now to the General Revenue Fund, which, as you know, supports the bulk of state operations.

1. Description of the Fund.

The General Revenue Fund receives all revenues not earmarked by law for specific purposes. It finances some 75 different functions, as is shown in Table I. These functions include, among many other, the cost of general administration, our extensive welfare programs, support of the University and State Teachers Colleges, the Civil Service System, aid to veterans, control of the liquor traffic, the Live Stock Sanitary Board, the Departments of Conservation, Health, Agriculture, and Business Development, the regulation of banking, insurance, and securities, the Railroad and Warehouse Commission, and many other agencies.

TABLE I

**General Revenue Fund
Major Services Financed**

Mental Hospitals	Children's Welfare	Youth Conservation
State Prison	Conservation	Commission
Old Age Assistance	Administration	Courts
University	Health	Business Development
Teachers Colleges	Agriculture	Crime Bureau
Railroad and Warehouse	Veterans Affairs	Liquor Control
Commission	Taxation	Labor Conciliator
	Military Affairs	

The General Revenue Fund receives revenue produced by taxes and by charges for services that are not earmarked for specific purposes. These include gross earnings taxes on utilities, 45 per cent of the occupational tax on iron ore, the taxes on insurance gross premiums, beer, inheritances and gifts, the state's share in liquor and cigarette taxes, and, currently, a portion of the state property tax. (See Table II.) In addition, the 1955 session, as you will recall, enacted for a

two-year term a series of temporary taxes, including a surtax on iron ore occupation and royalty taxes, a tobacco products tax, an annuity premium tax, and a surtax on individual income taxes and an increase in corporation income taxes.

TABLE II

General Revenue Fund Tax Sources

1. Continuing

Gross Earnings	Cigarette
Insurance Premiums	Liquor and Beer
Normal Iron Ore Occupation	Inheritance and Gift
Normal Iron Ore Royalty	

2. Temporary

Iron Ore Surtaxes	Individual Income Surtax
Tobacco Products	Corporate Income Tax
Annuity Premium	Surtaxes

2. \$16,075,000 Balance at End of Biennium.

We entered this biennium with an extremely small balance in the General Revenue Fund. I am pleased now to report that we will complete this biennium with a balance of \$16,075,000. The existence of this balance has greatly eased our budgeting operation for the next biennium and is one factor that makes possible the consideration of a tax adjustment program that I will discuss later in this message.

You will recall that two years ago we were completing a biennium in which our rate of spending from the General Revenue Fund was exceeding income by \$15,000,000 for the biennium. My 1955 recommendations called for an increase of \$10,000,000 in appropriations over the preceding biennium, which meant that we faced the need to find \$25,000,000 in additional revenue. Our situation today is obviously greatly improved.

The existence of a balance reverses a trend of the last ten years which has seen the gradual decline in the General Revenue Fund balance as is shown in Table III.

TABLE III

General Revenue Fund
Unencumbered Balances 1948-1957

June 30, 1948	\$21,777,000
June 30, 1949	25,239,000
June 30, 1950	21,133,000
June 30, 1951	22,400,000
June 30, 1952	15,381,000
June 30, 1953	7,654,000
June 30, 1954	7,248,000
June 30, 1955	652,000
June 30, 1956	9,487,000
June 30, 1957 (Est.)	16,075,000

3. Budgeted Recommendations Total \$190,800,000.

Departmental requests for appropriations from the General Revenue Fund for the next biennium totaled \$204,600,000. After reviewing the requests with great care, I reduced them by \$13,800,000 for a net of \$190,800,000 as shown in Table IV.

TABLE IV

General Revenue Fund
Departmental Requests and Governor's Recommendations
1957 - 1959

Departmental Requests	\$204,600,000
Governor's Reductions	13,800,000
Governor's Recommendations	\$190,800,000

The recommended appropriation of \$190,800,000 represents an increase of \$25,000,000 over the appropriation for the current biennium. At first glance the increase may appear rather large. However, careful study will show, I am confident,

that it represents a minimum figure, if we are to maintain our services at adequate levels.

The increase includes almost \$9,000,000 for necessary salary adjustments for state employees and substantial additional amounts for the faculties of the University and the Teachers Colleges. These are an inescapable obligation if we are to avoid a disastrous decline in the morale and quality of our state personnel. Additional salary costs are summarized in Table V which shows the costs to the General Revenue Fund of the salary adjustments certified last August by the Civil Service Board. Base costs are estimated at \$4,028,000. Merit increases total \$2,400,000 and interim costs, which cover such adjustments as new positions, reclassifications, reallocations, and merit increases granted during the current biennium and which become a continuing and normal liability for the next biennium, total an estimated \$2,500,000.

TABLE V

General Revenue Fund
Cost of Salary Adjustments for 1957-59

Base Costs	\$4,028,000
Merit Increases	2,434,000
Interim Adjustments	<u>2,529,000</u>
Total	\$8,991,000

Of the total \$25,000,000 increase, more than half is required for welfare purposes. Another \$3,815,000 is needed for the University of Minnesota, and an additional \$3,095,000 for the State Teachers Colleges.

The major increases are summarized in Table VI.

Table VI

General Revenue Fund
Major Increases Recommended

Welfare-State Institutions	\$9,007,000
Welfare-Aids and Administration	4,150,000
University of Minnesota	3,815,000
Teachers Colleges	3,095,000
Railroad and Warehouse Commission	1,075,000
Conservation	537,000
Health	484,000
Legislature	445,000
Military Affairs	317,000
Youth Conservation Commission	316,000
Taxation	228,000
Parole Board	206,000
Soil Conservation Commission	205,000

It should be noted that the General Revenue Fund increase recommended for the University is in addition to the new income which the University will receive from passage of the constitutional amendment permitting the use for current operations of iron ore occupation tax receipts which previously were dedicated to the Permanent University Trust Fund.

4. Additional Unbudgeted Items.

The recommended figure of \$190,800,000 covers all accounts included in the printed budget document. These accounts are all governed by existing legislation. In order that my recommendations will reflect not only existing accounts but also new programs that have my support and that will require financing, I should like to indicate those programs which will require new legislation and which, therefore, are not included in the budget document.

These items are given in Table VII.

Table VII

General Revenue Fund
Unbudgeted Items 1957-1959

Employees Retirement	\$ 5,330,000
Removal of Old Age Assistance Ceiling	1,330,000
State Aid to Counties for Welfare Administration	300,000
Additional Civil Service Ranges	150,000
Department Heads Salaries Increase	150,000
State Aid for Out-Patient Mental Health Clinics	100,000
Program for the Aging	160,000
Blood Bank	50,000
Training Public Assistance Workers	20,000
State Art Society	20,000
Minnesota Academy of Science	20,000
Liberalizing Aid to Dependent Children	10,000
Total	<u>\$ 7,640,000</u>

Inasmuch as the unbudgeted items are not described in the budget document, I should like to describe several of the major recommendations briefly.

(1) Employees' Retirement. A matter of vital importance to the welfare of state employees is the improvement of their retirement system. Your interim Public Retirement Study Commission has reviewed this problem and I am advised will recommend alternative plans for strengthening the state's participation in the retirement system. This could mean either the inclusion of state employees under the Old Age Survivors Insurance provisions of the Social Security Act combined with a continuation of a modified state retirement system, or the increasing of benefits under the existing system. While the cost to the General Revenue Fund will be determined by the nature of the plan ultimately adopted, the figure of \$5,330,000 is sufficient to cover either arrangement, allowing for retroactive coverage to January 1, 1956, if Social Security is adopted.

(2) Removal of Old Age Assistance Ceiling. Your action two years ago increasing the maximum grant under Old Age Assistance to \$65 a month provided

much-needed help, but in many cases \$65 fails to meet urgent needs. Since the purpose of Old Age Assistance is to provide an amount equal to a recipient's budgetary needs, determined as fairly as possible, this purpose can be defeated by the application of any arbitrary ceiling. We already recognize the validity of this principle in our program of Aid to Dependent Children and Aid to the Blind, and I believe we should also recognize it with reference to aid to our senior citizens. I therefore recommend the removal of the ceiling on Old Age Assistance grants, and which will require an estimated \$1,330,000.

(3) State Aid to Counties for Welfare Administration. The state's many welfare programs constitute an increasing burden upon counties which are called upon to administer them. We cannot expect to maintain adequate administration if the counties are not given sufficient assistance for this purpose. The Department of Public Welfare places a high priority on this need and is developing a proposal that will assure improved administration and more adequate staffs as the result of state aid to the counties. This program should be launched during the next biennium with an appropriation of \$300,000.

(4) Additional Salary Increases. Additional money will be needed to pay salaries of those high level technical and professional employees who will be assigned to new Civil Service ranges that I am recommending. It will also be necessary to provide additional money to adjust salaries of unclassified employees in order to retain a proper relationship with classified personnel. Each category will require an appropriation of \$150,000.

(5) State Aid for Out-Patient Mental Health Clinics. To advance our mental health program and to encourage development of mental health facilities in all parts of the state \$100,000 is recommended as state aid to cities and counties to operate out-patient mental health clinics. The Department of Public Welfare proposes that the four clinics which the state now operates directly be converted to locally operated centers, financed on a 50-50 state-local basis.

(6) Program for the Aging. An adequate and comprehensive program to meet the needs of our increasing number of aging citizens is long overdue. To launch such a program and to stimulate and encourage the development of adequate community programs under local auspices, I recommend \$160,000 for the biennium, of which \$60,000 would be used on the state level and \$100,000 to match local funds to provide community coordinators who would, under local authority, promote, encourage and coordinate community resources in the development of appropriate programs.

(7) Blood Bank. The Department of Health reports an urgent need to assist hospitals and blood bank centers in developing further the present program of assuring an adequate supply of whole blood in case of war or community disaster. The cost of the program will be shared equally by the federal government and would require \$50,000 for the biennium.

(8) Training Public Assistance Workers. Under a new program the federal government will provide 80 per cent of the cost of providing training for county public assistance workers if the state provides the other 20 per cent. For this purpose I recommend \$20,000 for the biennium.

(9) State Art Society. The Minnesota State Art Society, which was established in 1947 by state action, has been reactivated during the present biennium under able leadership that now proposes a constructive program for enriching our cultural life. This Society merits state support, and I therefore recommend an appropriation of \$20,000 for the biennium.

(10) Minnesota Academy of Science. In another area of our community life is the work of the Minnesota Academy of Science. This organization has undertaken the extremely important task of stimulating interest and encouraging activity in science among the young people of the State. Here again leadership is provided by a number of our outstanding citizens. This activity is also worthy of state support and for this purpose I recommend \$20,000.

(11) Liberalizing Aid to Dependent Children. A recent federal enactment will liberalize the administration of aid to dependent children permitting the inclusion of a limited number of additional families under the program. For this purpose I recommend \$10,000.

5. Financing the General Revenue Fund.

At this point I should like to summarize the situation with respect to the General Revenue Fund. We begin the next biennium with the balance of \$16,075,000. I am requesting appropriations of \$190,800,000, which are presented in the printed document, and an additional \$7,640,000 for the unbudgeted items. Inasmuch as the financing of the General Revenue Fund is so closely related to the proposals that I will make for tax adjustment, I will postpone further discussion of General Revenue Fund financing until I have reviewed the overall fiscal program.

III. Income Tax Fund

(To Be Renamed Education Fund)

I turn now to the appropriation needs and the present financial condition of the Income Tax School Fund. First, I should like to indicate that I am recommending that this fund be renamed the Education Fund in recognition of the fact that adoption of the Constitutional Amendment No. 3 will direct into the fund substantial receipts from the occupation tax on iron ore in addition to the receipts from the income tax. I believe a more general designation will be less confusing. However, I shall refer to this fund by its present name in further references in this message and until such time as the legislature chooses to redesignate the name.

1. Description of Fund.

The Income Tax School Fund receives all monies collected under state individual and corporate income taxes, except the \$5 filing charge and the surtax

on individual incomes, which currently go into the veterans compensation fund, and a second surtax on both corporate and individual income tax which during this biennium has been assigned to the General Revenue Fund.

The Income Tax Fund supports virtually all state aids to public schools and finances the administration of the Department of Education and those functions of the Department of Taxation that relate to income tax collection. Also, the fund supports certain educational activities performed by the Department of Public Welfare and the Youth Conservation Commission.

2. Began Biennium With \$32,000,000 Balance.

We began the present biennium with a balance of \$32,000,000 in the Income Tax Fund. It was contemplated by the 1955 Session that the needs for public schools would require the expenditure of most of this balance. As we enter the new biennium there will be a balance of approximately \$1,000,000 in this fund. Meanwhile, we have approved the use for current operations of receipts from the occupation tax on iron ore. This means that for the next biennium an estimated \$30,674,000 will be available for this fund in addition to the income tax receipts.

It is estimated that the carry-over balance and the income tax receipts during the next biennium will total \$154,663,000 as shown in Table VIII.

TABLE VIII

Income Tax School Fund
Beginning Balance and Estimated Receipts
1957 - 1959

Balance	\$ 1,013,000
Receipts Year ending 6/30/58	75,700,000
Receipts Year ending 6/30/59	77,700,000
Veterans Bonus Fund Reimbursement for Administrative Costs	250,000
Total	\$ 154,663,000

3. \$185,337,000 Available for Biennium.

There will therefore be available in the Income Tax School Fund a total of \$185,337,000 during the next biennium. This total, as is shown in Table IX includes the beginning balance, the estimated receipts from the income tax, and the new money now available as a result of the constitutional amendment.

TABLE IX

Income Tax School Fund
Estimated Amount Available
1957-1959

Receipts, Including Balance	\$ 154,663,000
Occupation Tax Diversion	<u>30,674,000</u>
Total	<u>\$ 185,337,000</u>

As is well known, the requirements of our public school system have enormously increased in recent years as a result of the unusually large number of children of school age. This means that the amount required for the state aid program has skyrocketed as the large number of children born during the war and post-war period become of school age. Existing legislation provides a basic state aid of \$82 per pupil unit in average daily attendance and a per-pupil aid of \$10 for each child of school age resident in school district, in addition to certain other special aids for transportation, handicapped children, vocational education, and equalization aid.

4. Recommendations total \$185,262,000.

The aid program together with administrative costs for the departments of Education and Taxation, and the support for educational programs of the Department of Public Welfare and Youth Conservation Commission, will require a total of \$185,262,000 during the next biennium as is shown in Table X.

TABLE X

Income Tax School Fund
Recommended Appropriations 1957-1959

\$10 per pupil Aid	\$13,950,000
Special State Aids to Schools	151,020,000
Tax Replacement Aids	3,323,500
State Institutions	5,684,000
Youth Conservation Commission	2,194,000
University of Minnesota Transportation Aid	144,000
Equalization Aid Review Committee	200,000
Administrative Costs, Department of Taxation	4,259,000
Administrative Costs, Department of Education	3,037,500
Refunds for Income Tax Overpayments	1,400,000
Payment to General Revenue Fund for Overhead Costs	50,000
Total	\$185,262,000

In determining my recommendations for appropriations from this fund, the same guide lines were used as in the case of the General Revenue Fund. Here, however, the bulk of the appropriations are represented in the aid programs and are, as a result, in large measure automatically determined by the number of pupils involved.

For purposes other than financing state aids, the departments involved requested a total of \$16,650,000. This amount was reduced to \$15,374,500, representing a reduction of \$1,275,500 in the departmental requests, as is shown in Table XI.

TABLE XI

Income Tax Fund
Requests, Recommendations, and Reductions

	Department Requests	Governor's Recommendations	Reductions
Department of Education	\$ 3,591,000	\$ 3,037,500	\$ 553,500
Department of Taxation	4,810,000	4,459,000	351,000
Department of Public Welfare	5,819,000	5,684,000	135,000
Youth Conservation Commission	2,430,000	2,194,000	236,000
Totals	\$16,650,000	\$15,374,500	\$1,275,500

In summary, the situation confronting us with respect to the Income Tax School Fund shows that, under existing legislation, the amount available will exceed by \$75,000 the estimated requirements for the next biennium. Table XII shows the relationship between expenditures and amount available.

Table XII	
Income Tax Fund	
Expenditures and Available Income 1957-59	
Total Available (From Chart IX)	\$185,337,000
Estimated Expenditures (From Chart X)	185,262,000
Balance	\$ 75,000

5. Recommended Non-Budgeted Items Total \$14,360,000.

It is also necessary to consider additional appropriations which will require new legislation and which are therefore not reflected in the printed budget document. These non-budgeted needs total \$14,360,000 as is shown in Table XIII.

Table XIII	
Income Tax Fund	
Non-Budgeted Items 1957-59	
Increase Basic Aids to \$87	\$ 5,892,500
Increase Equalization Aid	6,000,000
Junior College Aids at \$200	1,000,000
Taxation - Withholding	715,000
Rural Library Aid	350,000
Employees' Retirement	372,500
Department Heads Salaries Increase	15,000
Additional Civil Service Ranges	15,000
Total	\$14,360,000

Among these items are the following:

(1) Increase Basic State Aids to \$87. The plight of our school system is so well known that it is perhaps unnecessary to elaborate the reasons why an

increase in this basic aid is essential for the next biennium. I recommend that the basic aid be increased to \$87, which will cost an estimated additional \$5,892,500 for the biennium.

(2) Equalization Aid. Many school districts are greatly in need of additional state aid that would enable them to achieve educational standards comparable to those maintained by districts having greater financial resources. In some respects, equalization aid is a more vital need than are the other forms of state assistance in that it more nearly equalizes educational opportunity which is the underlying objective of the entire state program. For this purpose I recommend an appropriation of \$6,000,000.

(3) Aid to Junior Colleges. The problem of higher education has also intensified as a result of the increasing numbers of young people seeking admission to colleges and universities. One of the ways by which we can meet this problem is to encourage and assist the junior college program. I therefore recommend that we provide \$200 per student aid for junior colleges. It is estimated that such a program would involve 5,000 students during the next biennium, requiring an appropriation of \$1,000,000.

(4) Administration of Withholding. Later in this message I will recommend the installation of the withholding system for the payment of individual state income taxes, which will increase the receipts of this fund. It should be indicated here, however, that withholding will require an additional \$715,000 for installation and initial administration of the system.

(5) Rural Library Aid. Under new federal legislation Minnesota may receive \$172,972 annually for development of rural libraries provided a matching appropriation is made available. This program is deserving of our support because it will bring to our rural citizens an opportunity that is now available to the

residents of our more populous areas. I therefore recommend an appropriation of ~~\$375,000~~^{350,000} for the biennium for this purpose.

(6) Employees' Retirement. The strengthening of the retirement system for state employees will require the appropriate contribution from this fund as it will from all funds that finance employees salaries. In the case of this fund, the estimated amount is \$372,500.

6. Financing the Income Tax Fund

The total cost of the unbudgeted income tax fund items is ~~\$11,467,500~~^{14,360,000}, virtually all of which will require additional financing beyond the estimates I have given you based upon existing legislation. Here again the financing of this fund is closely related to the tax adjustment proposals that I will discuss as part of my overall financing program.

IV. Building Fund

I wish to turn now to a brief discussion of the State Building Fund. You have before you, as a companion document to the budget, the excellent report of your Legislative Interim Commission to Study State Building Needs. This report, in which I have formally concurred, contains what may be described as the first capital outlay budget in the state's history. This report presents detailed findings and recommendations with respect to the state's entire physical plant. Because these recommendations are so fully documented by the commission's report, I see no need in this message to amplify further these recommendations. They have my full support and I am confident that they will serve as a proper base for your review and analysis of building needs.

You will find that the recommendations for the next biennium total \$56,337,311 covering all institutions and agencies maintaining physical plants. I support the commission's recommendation that these projects be approved and that money for them be appropriated and that these appropriations be financed on

a thirty-year basis. While the amount of recommended appropriations is substantial, I am convinced that all recommended projects are essential and that it would be a mistake to delay them further.

The Commission's program is designed to accomplish several basic objectives: (1) to rehabilitate and prevent further deterioration in our state physical plant; (2) to provide essential new buildings for state programs, in particular in the fields of welfare and higher education; and (3) to institute a program of systematic and long-term planning.

The entire program, even though large, will not represent an undue burden upon the building fund. Certain offsetting factors will make it possible, even with adoption of the recommended program, to hold the total property tax millage for state purposes at approximately its present level.

V. The Tax Program

Now, as I turn to the revenue side of our budget picture, I must salute the remarkable achievement of the Governor's Minnesota Tax Study Committee. No other state has had the benefit of such a thorough analysis of its tax structure by a group so broadly representative of labor, industry and agriculture. Nor has any other state provided such a broad base of private financial support for an effort of this kind. Nearly \$60,000 was contributed by the constituent business organizations, labor unions, and agricultural groups, not to mention the invaluable contributions by our University.

1. Conflicting Viewpoints Harmonized.

Yet, it was with considerable apprehension that I established this committee a year and a half ago and appointed to it the 18 men nominated by agriculture, industry, and labor, together with two fiscal experts from the University. Taxation is a field full of emotion and controversy. Opinions differ as to the

impact of taxes on economic growth. Each person has his own idea of what fairness and equity means in taxation. Too often, it means to tax the other fellow. So it was expecting a great deal of the 20 members of the Committee to harmonize their vigorously conflicting viewpoints and achieve a genuine nonpartisan consensus.

To our great good fortune as Minnesota citizens, this is precisely what they have done. As a result of months of hard work based on solid and unbiased research, and by submerging their special concerns to serve the common good, this outstanding group has achieved an unprecedented meeting of minds on Minnesota's tax problems. Their unanimous recommendations squarely face up to the rising tide of dissatisfaction and criticism of our state and local tax system.

2. Will Help Achieve Four Objectives.

Copies of the Committee's report have been placed on your desks. After you have had an opportunity to study them, I am convinced you will agree with the Committee that enactment of its program would go a long way toward accomplishing four vital objectives:

- (1) To provide a friendly and fair tax environment for the expansion of Minnesota's industry and agriculture.
- (2) To give Minnesota a tax system second to none in its fairness and equity among taxpayers.
- (3) To tighten up tax enforcement and ease the taxpayer's job of complying with the law.
- (4) To strengthen the financial position of the State of Minnesota and its subdivisions, so that our state and local governments will be able to maintain a strong, independent, and responsible position in our federal system of government.

3. Program Adopted Unanimously.

As you examine the Committee's proposals, you will undoubtedly find, as I did, that they differ in some particulars from your own preferences. The Committee

itself recognizes this problem in its "Statement of Guiding Principles." After noting that the members of the Committee, starting from widely differing points of view, had arrived at a joint and unanimous set of conclusions and recommendations, the statement says: "Each one of us would differ with the form or content of one or another of the following recommendations." Then it goes on to say: "But the reader will find no minority report, no footnotes of dissent, since each one of us endorses the program as a whole. Give and take is the essence of democracy. It is our strong and unanimous conviction that the program as a whole will give Minnesota a vastly improved tax system. . ."

It is in the same spirit of give and take that I offer my vigorous endorsement of the Tax Study Committee's program and strongly commend it to you for consideration and adoption.

Since you have the Committee's report before you and later will get the lengthy staff report on which its findings and recommendations are based, I do not need to dwell on the details of the Committee's program in this message. But it may be helpful to call attention to some of the highlights of that program and to spell out its financial implications in terms of the various funds with which the legislature must deal.

The outstanding characteristic of the Committee's report, one which impressed me again and again as I went through it, is the insistent emphasis on equity in taxation--equity for the working man, the farmer and the businessman. At point after point in the structure or administration of our property tax, our personal income tax, and our business taxes, the Committee has called attention to inequities which must be removed to restore taxpayer morale and make Minnesota a better place in which to live, work, and invest.

4. Would Remove Major Inequities.

The Committee's program for improving Minnesota's tax environment for economic growth is a good case in point. It would provide some business tax relief, not in a blind rush for competitive advantage, but as part of a studied adjustment of the personal property tax designed to remove its major inequities. On the basis of staff research, the Committee recommends the removal of the worst offenders--the taxes on household goods, manufacturers' inventories and farmers' grain and livestock--and a 40 per cent reduction of the taxes on wholesale and retail inventories. Taking into account the total personal property of businessmen and farmers, including machinery and equipment, this recommendation would reduce personal property taxes for farmers by about 50 per cent and for manufacturers, wholesalers, and retailers by about 35 to 40 percent. The result: greater equity, plus removal of a tax penalty on Minnesota industry and agriculture.

5. Promises A Better Tax Future For All.

As you go through the point-by-point recommendations of the Committee, you will find that they hold out the following promises of a better tax future for Minnesota taxpayers:

- (1) To the householder, that he will no longer be plagued with the increasingly ridiculous and inefficient household goods tax.
- (2) To the farmer, that he will be relieved of the burdensome tax on his inventories of grain and his livestock.
- (3) To retailers and wholesalers, that they will get a substantial reduction of the taxes that have been bearing increasingly hard on their inventories.
- (4) To the manufacturer, that he will no longer be penalized by the tax on his inventories of raw materials, goods in process, and finished goods, a tax that bears little relation to his income in theory and, because of poor assessments, less in practice.

- (5) To individual income taxpayers, especially those with small and modest incomes, that they will no longer have to pay the onerous head tax which applies to every income tax filer regardless of the size of his income and family and that they will no longer have to pay a surtax which disregards their personal credits.
- (6) To the wage-earner, that his income tax will be collected in convenient installments by withholding on a pay-as-you-go basis, instead of being payable in lump sums that may force him into the hands of the loan sharks.
- (7) To the honest income taxpayer, that the chiselers and slackers will be brought to account by withholding, full checking of federal returns, and more widespread auditing.
- (8) To the small businessman, that he will be given inventory tax relief, that the minimum tax and filing fee will be removed, and that he can get a faster tax write-off on his machinery and equipment.
- (9) To married couples who are unable to split their incomes in two, that they will no longer have to pay a higher tax than other married couples with the same income divided between husband and wife.
- (10) To the working mother, that she can get a generous deduction for child care expenses.
- (11) To the businessmen seeking to locate or expand their operations in Minnesota, that the tax atmosphere in this state is fair and intelligent, one that is favorable to economic growth.

6. Certain Existing Revenues Continued.

The Tax Study Committee, acting in a responsible manner and recognizing that substantial increases in both the General Revenue and Income Tax School Funds are inevitable, has recommended a number of actions to continue or increase

existing revenues. It recommends continuation of the temporary taxes enacted in 1955, continuation of the bonus surtaxes with the adjustments noted, and a tightening up of the structure of the individual income tax, the corporate income tax, the insurance tax, and the cigarette and tobacco taxes. These actions, combined with the growth of revenues from our basic tax structure, will enable us to cover our expanding state expenditures, to enlarge our school aid program, and to make full restitution to local units of government for their revenue loss under the personal property tax relief program.

To get a comprehensive picture of how these measures fit together in the overall financial program for the next biennium, I refer you at this point to the large fold-out chart in the printed message. This chart brings together in one place the financial impact during the 1957-59 biennium of (1) my expenditure recommendations for that period; (2) the tax program and replacement financing recommended by the Governor's Tax Study Committee, and (3) my proposals, to be discussed below, for the use of certain non-recurring revenues to finance a Korean bonus and other non-recurring expenditures.

VI. Financing the General Revenue Fund

Without attempting to cover every point in this summary chart, I wish to highlight a few of the major points of the financing program, especially where changes from existing laws are involved. With respect to the General Revenue Fund, I call your attention to the following points:

(1) As noted, the Tax Study Committee's program includes reenactment of the temporary taxes payable into the General Revenue Fund.

(2) With respect to the taxes whose proceeds now go into the bonus fund, the Committee recommends repeal of the annual filing fee (head tax), conversion of the 5 per cent surtax from a before-credits to an after-credits basis and

continuation of the other surtaxes. The biennial revenues of \$16,745,000 remaining after the income tax reduction of \$13,000,000 would be divided as follows:

- (a) The revised surtaxes on income would be payable into the Personal Property Tax Replacement Account.
- (b) The surtaxes on liquor and iron ore royalties would be payable into the General Revenue Fund (\$3,240,000).
- (c) The 1 per cent iron ore occupation tax will be divided according to the formula applicable under Amendment No. 3, namely 50 per cent to the General Revenue Fund (\$2,238,000), 10 per cent to the University of Minnesota (\$447,600), and 40 per cent to the Income Tax School Fund (\$1,790,000). Although it is legally permissible to divide this 1 per cent occupation tax on iron ore in a different manner, since the proceeds of this tax are no longer needed for repayment of World War II bonus bonds, I believe it is desirable to abide by the spirit of Amendment No. 3.

(3) Another \$4,000,000 would accrue to the General Revenue Fund from the Committee's recommendations for bringing most exempt insurance premiums (except for non-commercial fraternal and town-mutuals) into the base of the 2 per cent gross premiums tax, for bringing the tax on tobacco products into alignment with the cigarette tax, and for eliminating cigarette stamping and distributors' 4 per cent discounts that go with it.

(4) The Committee recommendations to transfer the proceeds of the telephone gross earnings tax to the Personal Property Tax Replacement Account reduces the resources available to the General Revenue Fund by an estimated \$12,750,000 during the 1957-59 biennium.

(5) The Committee recommendation to transfer the financing of the Teachers Colleges to the Income Tax Fund relieves the General Revenue Fund of \$9,333,000 during the 1957-59 biennium.

(6) After the adjustments noted, the revenue available to the General Revenue Fund during the 1957-59 biennium will total \$189,631,000 or \$515,000 more than the total requested appropriations of \$189,116,000 for both budgeted and unbudgeted items.

VII. Financing the Income Tax School Fund

With respect to the Income Tax School Fund, I wish to call your attention to the following points:

(1) The Committee's program would add \$23,600,000 to this fund during the 1957-59 biennium, \$8,000,000 of which would be realized through improved collections resulting from income tax withholding (\$7,000,000) and full use of federal returns (\$1,000,000), and another \$7,200,000 through the combination of a joint return requirement for married couples and a liberal credit for working mothers.

(2) In spite of these increases and apart from the tax evaders who would be caught in the tighter enforcement net, the Committee's program as a whole, including removal of the head tax and other reliefs, would grant individuals a net reduction in income tax liabilities amounting to \$2,300,000 for the biennium.

(3) The estimated biennial improvement of \$7,000,000 in individual income tax collections as the result of the introduction of withholding of taxes from wages and salaries is a figure arrived at after careful study of the experience in the ten other states that have adopted income tax withholding. It represents roughly 5 per cent of our annual existing collections from this source, while several other states have experienced increases of 10 per cent or more.

(4) The Committee's recommendation to bring our medical expense and sick pay deductions into line with the federal allowances and to eliminate the 150-day loophole in non-resident earnings would bring in \$3,500,000 of additional revenue.

(5) Committee recommendations for adjustments in the structure of the corporate income tax would:

- (a) Eliminate the inequitable and ineffective property-payroll credit.
- (b) Abolish the alternative allocation formula by which a few corporations have been able to get an undue portion of their income removed from the tax base.
- (c) Allow less offsets and speedier write-offs of machinery and equipment to promote equity and stimulate investment.
- (d) Eliminate the \$500 credit and the \$10 minimum tax and \$5 filing fee.

On net balance, these changes will bring about a small increase in corporate tax liabilities in addition to the \$5,000,000 increase that will accrue to the Personal Property Tax Replacement Account from the 1 per cent additional tax on corporate income.

VIII. The Personal Property Tax Replacement Account

The following points concerning this account should be brought to your attention.

(1) To assure the hard-pressed municipalities and other local units of government that they will not be deprived of any revenue under the personal property tax adjustment program, the Tax Study Committee wisely provided for full replacement of the revenue losses under that program (except for one-half of the direct loss involved in the repeal of the household goods tax on grounds that this tax is so costly to administer that the net loss is much less than the gross loss).

(2) Each community would get a dollar-for-dollar replacement of its revenue losses (computed in terms of the 1957 levy on 1956 assessed valuations) in 1958 and 1959 and would get at least a dollar-for-dollar replacement in 1960

and 1961. However, to recognize differentials in growth of population and in the property tax base, the Committee recommends shifting to a formula basis for distributing the replacement revenues, moving gradually from the direct replacement basis to a formula basis incorporating such suggested factors as population and equalized assessed valuation.

(3) To finance the Replacement Account, the Committee recommended that the revenues from three specified sources be set aside:

- (a) A 10 per cent surtax on the individual income tax representing the two existing 5 per cent surtaxes combined into a single surtax of 10 per cent of the normal tax after personal credits.
- (b) The existing surtaxes and the recommended additional 1 per cent tax on corporate income.
- (c) The gross earnings tax on telephone companies. Since these three revenue sources have a far greater growth potential than the taxes on inventories and household goods they are replacing, the localities can look forward to a net addition to their revenues within the near future. During the past 10 years, for example, the revenues represented by these three sources have more than doubled.

(4) During the 1957-59 biennium, only $1\frac{1}{2}$ years' revenue loss to local units will be replaced (calendar year 1958 and the first half of calendar year 1959), with the result that the replacement taxes will yield approximately \$2,425,000 more than will be paid out during the biennium. This balance will be needed during the 1959-61 biennium, when a full two years' replacement payments will have to be made.

(5) While the replacement financing will protect the localities from revenue loss and will even supplement their revenues within a few years, I

recognize that this is only a small step toward meeting their serious financial problems. The increase in school aids is another step. The improvement in the distribution of highway funds under Constitutional Amendment Number 2 is a third step. These three steps offer some improvement in the fiscal position of local units.

IX. Non-Recurring Income and Activities

In the development of the overall financing program, we have segregated two substantial income items which will not recur in future bienniums. These are (1) the balance remaining in the Veterans Compensation Fund after payment of all bonus claims, which amounts to \$9,100,000, and (2) the income resulting from placing the individual income tax on a current payment basis, which will produce an estimated \$27,500,000, as shown in Table XIV. The total of non-recurring income available is \$36,600,000.

Table XIV	
Non-Recurring Income	
Balance in Veterans Compensation Fund	\$ 9,100,000
Current Payment of Individual Income Tax	<u>27,500,000</u>
Total	<u>\$36,600,000</u>

I believe we should use this money only for items that are non-recurring in character. The Committee report states "that if the legislature enacts withholding without tax forgiveness during the period of transition from our present system to the pay-as-you-go system, the windfall to the state resulting from the overlap of tax payments by individuals should be used only for non-recurring purposes, and in no event for current purposes." Further than this the Committee is silent on the question of tax cancellation (the so-called forgiveness problem).

By this stand they have recognized that the merits of withholding should not be confused with the issue of tax cancellation, and I believe the Committee was correct in sharply differentiating the two issues. The adoption of withholding is so vital to the integrity of the income tax and so important for easier budgeting of income tax payments by wage and salary earners that it should be adopted, with or without tax cancellation or forgiveness.

The cancellation issue is a difficult and delicate one, on both sides of which there is much to be said. On one hand, none of the other 10 states that have adopted withholding has granted any such so-called forgiveness. Furthermore, while there is some overlap of payments during the year of transition to a pay-as-you-go collection system, the taxpayer is later relieved of one year's liabilities at the time his income stops because of retirement, loss of his job, death, or by moving out of the state.

On the other hand, since taxpayers will still be paying part of their previous year's tax at the same time that they start paying on a current basis by withholding and quarterly payments, there will be a temporary bulge in their payments to the state.

The legislature must balance these considerations against the merits of non-recurring projects that can be financed with the proceeds of the payment overlap, amounting to \$27,500,000 (roughly 50 per cent of one year's liabilities).

I recommend to you the non-recurring items shown in Table XV.

TABLE XV	
Non-Recurring Items	
Korean Bonus	\$25,000,000
Bonus Administration	500,000
School Construction Revolving Fund	5,000,000
Aid for Nursing Home Construction	4,000,000
Duluth Port Authority	1,000,000
Student Loan and Scholarship Program	1,000,000
Centennial Veterans Commemoration	50,000
State Feasibility Study	50,000
Total	\$36,600,000

(1) The Korean Bonus. It is only fair and proper that the State of Minnesota recognize the sacrifices made by the veterans of the Korean War in the same fashion as was done for the veterans of World War II. I support the recommendation of your interim commission on the payment of the Korean bonus. I recommend \$25,000,000 for that purpose and \$500,000 for its administration.

(2) School Construction Revolving Fund. Minnesota faces no need for capital outlay more critically urgent than the construction of schools in many of our hard-pressed school districts. In order to provide essential aid to those districts that need it, I will continue to recommend measures to liberalize the borrowing restrictions on school districts and to make available more of our state funds from which they can borrow. In addition, I recommend that we set up a school construction revolving fund of at least \$5,000,000, to augment funds available for school construction.

(3) Aid for Nursing Home Construction. With a shortage at the present time of about 8,000 nursing home beds, an adequate program for the care of our aging citizens makes it imperative that state aid be extended to any county, city, or other political subdivision, as well as to qualifying non-profit associations, to encourage the construction of additional nursing homes. I recommend that \$4,000,000 be made available for such purposes during the coming biennium on a matching basis, as an outright grant with no obligation to repay, for the construction of facilities offering nursing care.

(4) Duluth Port Authority. I recommend the appropriation of \$500,000 per year for each of the next two years, for the purpose of planning the development of the Port of Duluth on a scale commensurate with the possibilities of that port as a great mid-continent outlet to the oceans of the world and, correspondingly, as a vital part of our program of economic development.

(5) Student Loan and Scholarship Program. The Governor's Committee on

Higher Education stresses the need for measures to make higher education available to young people, now unable to attend college because of inadequate finances.

In line with the recommendations of the committee, I recommend the appropriation of \$1,000,000 to create a scholarship and loan fund for Minnesota students. The fund will make possible both scholarships and low-interest loans to be repaid to the fund over a number of years after the student's education has been completed.

(6) Veterans Museum Centennial Commemoration. As one part of the state's participation in our centennial observance, I propose that special use be made of the new museum in the Veterans Service Building. An appropriate centennial program commemorating the participation of Minnesota men and women in the Armed Services of our country should be planned with the museum as its central point of development. I propose that this program be directed by the Adjutant General and that the Department of Military Affairs be authorized to equip the spacious facility for a proper program of commemoration. For this purpose I recommend an appropriation of \$50,000 for the biennium.

(7) Feasibility Study. Three of the functional task forces that participated in the Minnesota Self-Survey recommended that the State undertake what is known as a feasibility study of all administrative procedures which can be adapted to modern electronic high-speed machines at great ultimate savings to the state. This type of study is regularly conducted in private industry and is essential for basic improvement in our administrative procedures. For this purpose I recommend an appropriation of \$50,000.

These are important projects, and I hope you will give them serious and sympathetic consideration. I cannot conscientiously recommend that you cancel tax liabilities legally due the state in the face of such meritorious and necessary non-recurring programs as a bonus for Korean veterans, the construction of schools for our children, the providing of nursing homes for our senior citizens,

and the other projects I have mentioned, all of which would ~~not~~ be possible without such cancellation.

I believe these projects will contribute far more to the welfare and happiness of the people of Minnesota and to the future growth and development of our state than would the temporary benefits that would accrue--and these, in any substantial amount, only to a relatively small proportion of taxpayers--by the cancellation of tax obligations now due the state under existing law.

X. Conclusion

I should like to conclude this message with a final word of appreciation to you, to the members of the Governor's Tax Study Committee, and to the many others, both in and out of government, who have contributed to the development of this overall fiscal program.

It is a matter of personal pride to me that we face the financial problems of this session so fully prepared with sound information and carefully developed recommendations. This is possible because of the devoted and dedicated efforts of so many people.

By working together, I am confident we can meet the challenge presented by this program, the fulfillment of which will provide an appropriate launching for our second century of statehood. In this endeavor I pledge to you my full and wholehearted cooperation.

