POLICY BRIEF
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Use Tax Collection on Income Tax Returns in Other States

The use tax is a complement to the sales tax. Individuals owe the use tax on goods and services purchased outside their state of residence, by mail order, or over the Internet, but it is difficult for states to enforce compliance. Many states provide for individuals to report both state and local use tax liability on the individual income tax return. This policy brief explains the use tax, other states' efforts to collect it via the income tax return, and options for Minnesota to use the income tax return to increase use tax reporting and collections.

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The Use Tax and Collection Methods: A Summary

All states with a general sales tax have also enacted complementary use taxes. In general, a use tax is due on a transaction in which the sales tax is not collected and the good or service is used in the jurisdiction imposing the tax. The use tax equals the state sales tax rate plus the local sales tax rate, if any. For example, if a Minnesota resident travels to a jurisdiction that does not have a sales tax and purchases taxable items to bring home for use in Minnesota, or orders taxable items by mail or over the Internet, a use tax is due to Minnesota on those purchases. The tax equals the sales tax that would have applied if the purchase had been made in Minnesota, less sales tax actually paid where the purchase was made. The use tax is intended to discourage making purchases outside the state to avoid sales tax and to prevent erosion of the tax base. In addition, it helps to put in-state merchants on an equal competitive footing with merchants in lower tax jurisdictions and with merchants who are not required to collect sales tax on sales to Minnesota residents.

Minnesota allows individual taxpayers a de minimis exemption from the use tax. Individuals whose total purchases subject to use tax do not exceed $770 in a calendar year are not subject to use tax.[1] Minnesota is one of five states with some form of de minimis exemption for individuals.[2]

Of the 45 states with sales and use taxes, 38 also have an individual income tax. Of these 38 states, 25 provide for taxpayers to report use tax obligations on the individual income tax return, and another seven, including Minnesota, provide information about the use tax in the individual income tax booklets. The experience in other states and past Department of Revenue estimates suggest the following results for eliminating the de minimis exemption and/or providing for collection on the individual income tax return:

- Eliminate de minimis exemption and provide for individuals to pay use tax on the income tax return. Estimated revenue raised: between $0.4 million and $15.3 million per year[3]

- Eliminate de minimis exemption and require individuals with purchases of less than $770 to file use tax returns. Estimated revenue raised: $100,000 per year[4]

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[1] Minn. Stat. § 297A.67, subd. 21. When enacted in 1997, the $770 exemption equaled the amount of purchases necessary to generate $50 of use tax liability at the sales tax rate, which was then 6.5 percent. At the current statewide rate of 6.875 percent, $770 of purchases would result in $53 of use tax liability.

[2] California exempts $800 of purchases made in foreign countries and hand-carried into California (Cal. Rev. & Tax. Code § 6405). Michigan does not require taxpayers to pay use tax on purchases valued at less than $10 over the course of a month (Mich. Comp. Laws § 205.94). Missouri does not require a consumer use tax return if purchases total less than $2,000 during the year (Mo. Rev. Stat. § 144.655). Virginia has a de minimis exemption for mail-order catalog sales totaling $100 or less over the course of a year (Va. Code Ann. § 58.1-604(5)). Colorado had a de minimis exemption of $100 in purchases per year for individuals (Colo. Rev. Stat. § 39-26-203), but the exemption was repealed in 2004.

[3] Estimate based on other states' experience with collecting use tax on income tax returns.

[4] Minnesota Department of Revenue, Analysis of 1996 Tax Conference Committee Report, April 11, 1996; if this change were proposed now, the revenue estimate would likely increase because of population growth, inflation, and the increase in the sales tax rate from 6.5 percent to 6.875 percent.

- Retain de minimis exemption and provide for individuals with purchases greater than $770 to pay use tax on the income tax return. Estimated revenue raised: minimal[5]

The Use Tax and Minnesota's de Minimis Exemption

The use tax complements the general sales tax and is due on transactions in which the sales tax is not collected, but the good or service purchased is used in the jurisdiction imposing the sales tax.[6] Use tax typically applies to goods that an individual purchases in one state but uses in another, either by traveling to another state, or by purchasing the good remotely through mail order or over the Internet. The use tax rate equals the state sales tax rate plus the local sales tax rate in effect at the location where the item is used, if any.[7]

An alternative to the use tax would be to require businesses that make sales through catalogs or over the Internet to collect the use tax at the time a sale is made. However, several U.S. Supreme Court rulings, most recently *Quill Corp. v. Heitkamp* (1992), have prevented the states from requiring businesses to collect use tax unless the business has a physical presence in the state.[8] Because of the complexity of state sales tax laws, the court considered a collection requirement to be an undue burden on interstate commerce.

Twenty-one states are full members of the Streamlined Sales and Use Tax Agreement (SSUTA),[9] a voluntary compact that simplifies sales tax collections among the member states. The goal of the agreement is to persuade Congress to intervene and impose a duty on remote sellers to collect sales and use tax in member states. In the meantime, collecting the use tax directly from consumers of goods purchased while traveling, on-line, or through a catalog remains the states' only alternative to simply foregoing tax revenue owed on remote sales.

States have historically viewed the use tax on individuals as impractical to enforce—the tax typically involves small amounts owed on a large number of transactions for which the

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[5] Minnesota Department of Revenue, Analysis of House File 2682, January 29, 1998.

[6] In Minnesota, the use tax applies to taxable tangible personal property and taxable services that were not subject to the *Minnesota* sales tax. Minn. Stat. § 297A.63, subd. 1. Thus, even if sales tax is paid to the state in which the sale took place, the use tax still technically applies. However, the rate of the use tax is reduced to the difference between the Minnesota rate and sales tax rate in the state in which the tax was paid. Minn. Stat. § 297A.80. No tax is owed if the sales tax paid was as high or higher than the Minnesota sales (both state and any applicable local) tax. As a practical matter, most remote sales (catalog and Internet) are not subject to sales tax in the seller's state. Thus, the offset for taxes paid to another state rarely applies.

[7] In Minnesota, the city of Duluth and Cook County impose 1 percent local sales taxes; Albert Lea, Austin, Baxter, Bemidji, Brainerd, Clearwater, Fergus Falls, Hermantown, Hutchinson, Lanesboro, Mankato, Minneapolis, New Ulm, North Mankato, Owatonna, Proctor, Rochester, St. Augusta, St. Cloud, St. Joseph, St. Paul, Sartell, Sauk Rapids, Two Harbors, Waite Park, Willmar, and Worthington impose 0.5% local sales taxes; Hennepin County imposes a 0.15% local sales tax; and Anoka, Dakota, Hennepin, Ramsey and Washington counties impose a 0.25% local sales tax for transit improvement.

[8] *National Bellas Hess, Inc. v. Department of Revenue of the State of Illinois*, 386 U.S. 753 (1967) and *Quill Corp. v. Heitkamp*, 504 U.S. 298 (1992).

[9] Another three states are associate members, with delayed effective dates that have not yet been reached. For general background on SSUTA, see http://www.streamlinedsalestax.org.

individual has not kept records, and the costs of collection could easily exceed the revenues collected. In 1996, the Sales Tax Advisory Council recommended that Minnesota adopt a de minimis exemption from the use tax, recognizing that most taxpayers are unaware of the tax and the Department of Revenue is unlikely to collect the tax due to high administrative costs. The legislature adopted the council's recommendation, and the exemption took effect in 1997.

Individuals with less than $770 in purchases during a calendar year are exempt from the tax and are able to make incidental purchases by mail order, over the Internet, or while traveling without keeping records for the use tax. This amount, $770, is the amount of purchases necessary to generate $50 of tax at the 6.5 percent rate in effect when the exemption was enacted in 1997. Minnesota's statewide sales and use tax rate is now 6.875 percent, following passage of the constitutional amendment at the 2008 general election.

At the same time the de minimis exemption went into effect, Minnesota began including information on the use tax in the individual income tax instructions, directing individuals with purchases in excess of the de minimis exemption amount to file a use tax return. The box on the right reproduces some of the information provided in Minnesota's 2010 individual income tax form.

An excerpt from Form M-1 instructions for Minnesota income tax filers

If you purchased items for your own use without paying sales tax, you probably owe use tax. Here are some cases when use tax is due:

- You buy taxable items over the Internet, by mail order, from a shopping channel, etc., and the seller doesn't collect Minnesota sales tax from you.
- A seller in another state or country does not collect any sales tax from you on a sale of an item that is taxed by Minnesota.
- An out-of-state seller properly collects another state's sales tax at a rate lower than Minnesota's. In this case, you owe the difference between the two rates.

If your total purchases subject to use tax are less than $770 in a calendar year, you are not required to file a use tax return. This exemption applies only to items for personal use, not to items for business use.

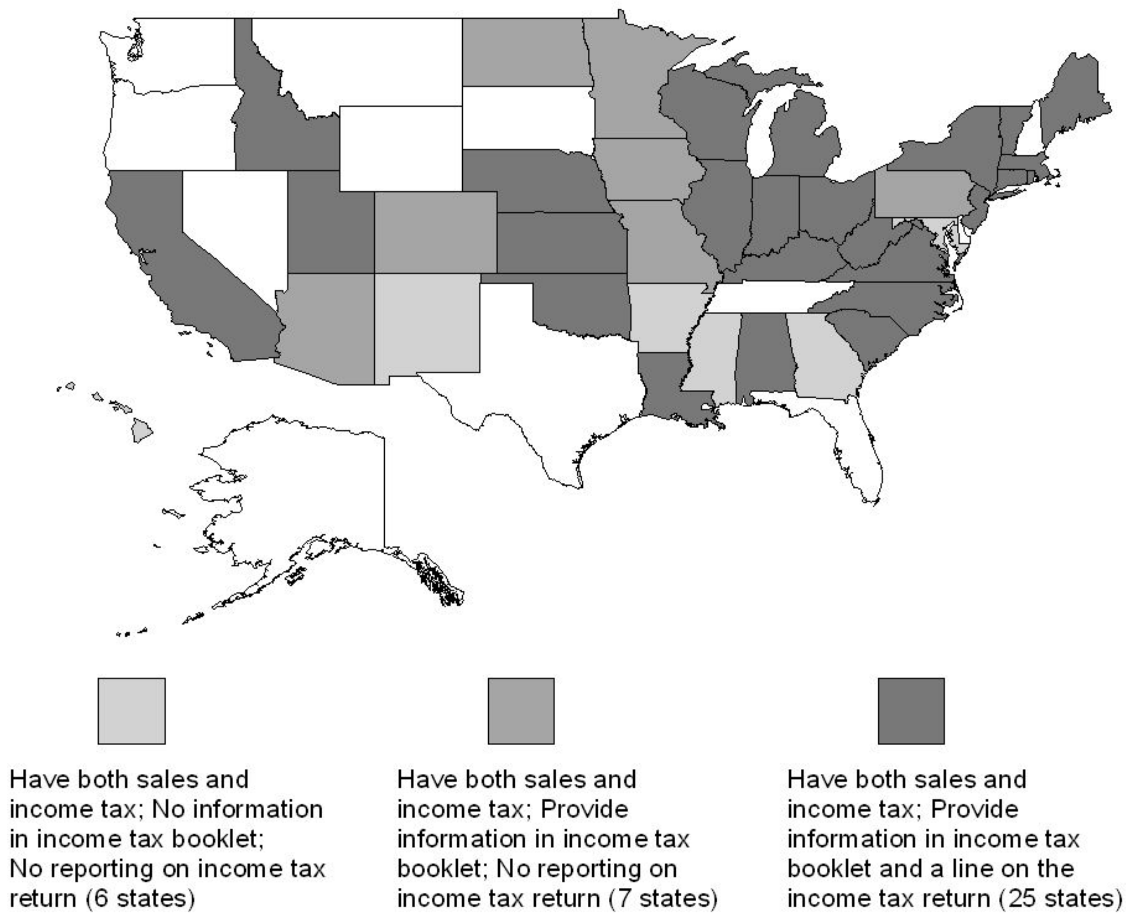
If your total purchases subject to use tax are $770 or more, you owe use tax on all taxable items purchased during the year.

Source: Form M-1 Instructions, Minnesota Department of Revenue, Tax Year 2011

State Reporting of Use Tax Liability

Many states have taken steps to make the use tax more visible. Thirty-eight states impose both a sales and use tax and a broad-based individual income tax. Seven of those 38 states (including Minnesota) provide information about the use tax in the income tax instruction booklet.[10] Twenty-five of the 38 states provide for use tax reporting on individual income tax returns. In 1974, Vermont added a line for use tax reporting to its income tax return, followed by a number of states, including Wisconsin, in the early 1980s. Illinois and Nebraska, which added the use tax reporting line on their 2010 returns, are the states that most recently provided for reporting on the personal income tax return. The map shows the states that impose both an income tax and a sales tax broken into three categories: those that provide neither information about the use tax nor use tax reporting (six states), those that provide information in their income tax booklet (seven states), and those that provide for use tax reporting on the income tax return (25 states).

States with Use Tax Reporting on Individual Income Tax Return



House Research Graphics

[10] The states that note use tax requirements in the income tax booklet but do not provide a reporting line are Arizona, Colorado, Iowa, Minnesota, Missouri, North Dakota, and Pennsylvania.

The map shows that most of the states that have an income tax and a sales tax are taking steps to make individual taxpayers aware of use tax obligations, either by providing for payment through the income tax or by providing information on how to file an individual use tax return.

Other States—Collections

The information in this section is based on tax year 2009 data obtained from 22 of the 25 states that collect use tax on the income tax return.[11] Table 1 shows 2009 use tax collections.

Table 1
Use Tax Collected on Income Tax Returns, Tax Year 2009

	Use tax reported (millions)	Percent of income tax returns reporting use tax	Average use tax reported per return reporting use tax
Alabama	$0.3	1.3%	$12
California	10.2	0.3	202
Idaho	0.9	1.2	101
Indiana	1.5	0.8	61
Kansas	1.0	1.8	36
Kentucky	0.9	0.6	73
Louisiana	0.8	0.6	70
Maine	3.1	9.8	49
Massachusetts	3.8	1.5	73
Michigan	5.0	2.3	49
New Jersey	2.0	0.3	142
New York	34.6	5.0	70
North Carolina	4.9	2.5	48
Ohio	2.7	0.9	57
Oklahoma	2.4	3.2	47
Rhode Island	0.1	0.2	93
South Carolina	0.9	0.5	79
Utah	0.5	0.7	57
Vermont	0.8	7.9	34
Virginia*	1.5	0.6	68
West Virginia	0.3	0.4	91
Wisconsin	1.7	1.0	59
* Virginia exempts annual mail-order catalog purchases of under $100 from use tax.			

[11] Illinois and Nebraska added the use tax line to their income tax returns in tax year 2010 and data are not yet available. Data from Connecticut were removed from the analysis. Connecticut reported large amounts of collections relative to the number of returns reporting collections not likely to be representative of a typical year's collections. Department of Revenue Services staff in Connecticut think it reasonably likely that a small number of returns had reported large purchases (such as artwork) or as a result of audit activity.

The amount of use tax collected in the states with use tax reporting varied depending on the participation rate and the size of the state. New York and California had the largest collections, at $34.6 and $10.2 million respectively, and New York also had a relatively high participation rate, with 5.0 percent of all income tax returns reporting use tax liability. Maine had the highest participation rate, perhaps stemming from a 2006 compliance campaign and also from an earlier practice, not long maintained, of assessing use tax liability for taxpayers who left the use tax line blank.

Some states that placed a use tax line on the income tax return reported significant increases in collections. Collections in Louisiana, Massachusetts, and Michigan all increased substantially in the year following implementation of use tax reporting on the income tax return; Louisiana and Michigan had previously included information on the use tax in their income tax booklets, while Massachusetts did not.

Michigan collections increased from $240,000 in 1998 to $2.9 million in 1999 and have increased since then, reaching $5.0 million in 2009.

Louisiana's collections via individual filings increased from about $20,000 per year prior to 2000, to over $500,000 reported on the income tax form in 2000, and nearly $640,000 for tax year 2004, and over $800,000 in 2009.

In Massachusetts, addition of a use tax line to the income tax return resulted in a sharp increase in the number of individuals reporting use tax, from 200 in 2001 to over 11,000 in 2002, the first year of reporting, and further increased to almost 40,000 in 2005. Revenues have increased sharply since the reporting line was first added, from about $1 million in 2001 to over $3 million per year since 2005.

Other states that have recently added use tax lines do not have data available on personal use tax collections for prior years.

The states that collect use tax on the income tax form use different techniques to try to maximize voluntary reporting by taxpayers. Some specifically require taxpayers to write in "zero" if they have no use tax liability. Others have combined use tax reporting with compliance initiatives, and several states provide tables in which taxpayers can "look up" their use tax liability based on their income.

Eleven states require taxpayers to clearly indicate if no use tax liability is owed.[12] States with the requirement and states without it collect use tax revenue from a slightly larger share of income tax returns (1.7 percent of returns compared to 1.4 percent of returns), but the states that do require the indication collect more use tax revenue per taxpayer: $1.22 compared to $0.74 per return for all income tax returns, and $73 compared to $52 for returns reporting use tax liability.

A small number of states combine reporting on the income tax return with compliance initiatives or education efforts. Two states have sent information about the use tax to a random

[12] States that require taxpayers to indicate when they have no use tax liability are: California, Connecticut, Kansas, Louisiana, Massachusetts, Michigan, New Jersey, New York, Ohio, Oklahoma, and Utah.

sample of taxpayers, resulting in higher collections in following years (Indiana[13] and Rhode Island[14]), and one state saw use tax collections peak in 1995 in conjunction with an individual compliance program (Kentucky). More recently, Massachusetts and Maine have experimented with compliance programs. Massachusetts sent letters to some taxpayers that resulted in unusually high use tax collections for tax year 2005, possibly due to a few taxpayers reporting large purchases. Maine legislators approved a compliance program that took place from July to December of 2006. The program included television commercials, letters sent to individuals and business owners, and interest-free payment of past unreported use tax liabilities.

Nine states with use tax reporting on the personal income tax return provide taxpayers with lookup tables for estimating their use tax liability.[15] Lookup tables provide estimates of use tax liability by taxpayer income. The tables typically consist of two columns. Taxpayers find their income in the left column and read across to the right column to find their estimated use tax liability. Use tax liability is assumed to represent a percentage of income. The percentage is intended to represent average use tax liability of taxpayers. The first states to use lookup tables did not have records of how the percentages they use were determined. The states that have subsequently provided lookup tables appear to have modeled their tables on those used in other states. The tables make compliance with the tax more convenient for taxpayers who know they have made untaxed purchases, either while traveling, through catalogs, or over the Internet, but have not maintained records of those purchases. Taxpayers with large purchases must report those separately from the use tax calculated using the lookup table, and those who did not make any purchases subject to use tax are not required to use the lookup table and may report liability equal to $0. Only one state (Kansas) allows taxpayers with purchases over $1,000 to use the lookup table to estimate liability.

As an example of how the lookup tables work, Michigan's lookup table gives estimated use tax liability by income ranges up to $100,000. Estimated liability equals 0.08 percent of the taxpayer's Michigan adjusted gross income. Taxpayers with incomes over $100,000 are instructed to multiply their income by 0.0008 to obtain an estimate of use tax liability.

Table 2 summarizes the characteristics of the various state lookup tables. Note that in four states, the percentages implicit in the tables vary with income. In Maine, New Jersey, and New York, the percentage decreases as income increases, while in Vermont it increases with income.

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[13] In 1993, Indiana identified taxpayers who had not reported use tax and had incomes above a certain level and sent educational letters explaining the use tax to a random sample of taxpayers identified, with the purpose of improving compliance.

[14] In 1995, Rhode Island sent letters explaining the use tax to about 15,000 taxpayers who had not reported use tax liability in 1994. This action was in response to low compliance with the use tax after the use tax line first appeared on the income tax return. The mailings resulted in negative publicity and have not been repeated.

[15] Kansas, Maine, Massachusetts, Michigan, New Jersey, New York, North Carolina, Oklahoma, and Vermont provide lookup tables for estimating use tax liability.

Table 2

Characteristics of State Use Tax Lookup Tables

State	Income base	Lookup table percentage	Use of lookup table limited to purchases less than $1,000
Kansas	State adjusted gross income	0.068%	No
Maine	State adjusted gross income	0.17% to 0.08%	Yes
Massachusetts	State adjusted gross income	0.05%	Yes
Michigan	State adjusted gross income	0.08%	Yes
New Jersey	State adjusted gross income	0.0933% to 0.0426%	Yes
New York	Federal adjusted gross income	0.1% to 0.041%	Yes
North Carolina	State taxable income	0.0675%*	Yes
Oklahoma	Federal adjusted gross income	0.056%	Yes
Vermont	Federal adjusted gross income	0.06% to 0.08%	Yes

* Note that while the percentage used is higher than in other states with lookup tables, it is applied to a narrower tax base—taxable income, which is income after all deductions and exemptions, rather than adjusted gross income, which is typically income before deductions and exemptions.

States that provide lookup tables for estimating liability have higher participation rates. About 1.6 percent of taxpayers report use tax across all states with use tax reporting on income tax returns. The participation rate is 3.1 percent for states with lookup tables and only 0.6 percent for those without. Seven states[16] have higher than average participation rates, led by Maine at 9.8 percent and Vermont at 7.9 percent. All of the states with higher participation rates provide taxpayers with the option of estimating use tax liability using a lookup table. Maine's exceptionally high participation rate in this and earlier years may be the result of its previous practice (through 1999) of assuming liability equal to 4 percent of income if none was reported. Maine has had a higher participation rate than other states since then. Maine's aggressive 2006 publicity program for the use tax may have also contributed to the high participation rate.

States with lookup tables collect slightly less use tax per return than do states without lookup tables.[17] Individuals who report use tax liability pay $72 on average across all states with use tax reporting on the income tax return. The amount collected per return reporting use tax is lower in states that provide a lookup table than in those that do not: $59 compared with $124. In past years it was also the case that states with lookup tables collected less per return, but from more returns, than did states without lookup tables.

Alabama, which does not provide a lookup table, collected $12 on average from returns reporting use tax, the lowest per return of any state. Vermont collected the lowest on average of states with lookup tables, at $34 per return. States with high per-return collections are led by

[16] Kansas, Maine, Michigan, New York, North Carolina, Oklahoma, and Vermont all have participation rates above the 1.6 percent average for all states.

[17] While states with lookup tables tend to have a higher share of returns reporting use tax and a lower average amount reported, the average amount reported will vary depending on the combined state and local sales/use tax rate and the state's sales/use tax base.

California, with $202 per return, New Jersey, with $149 per return, and Idaho, with $101 per return.[18]

Ten states collect local as well as state use tax on the income tax return (California, Kansas, Louisiana, New York, North Carolina, Ohio, Oklahoma, South Carolina, Utah, and Wisconsin). Most of these either provide listings of local rates or a table of combined state and local rates. Kansas and Oklahoma direct taxpayers to a web page showing local rates for various jurisdictions. Louisiana instructs taxpayers to multiply taxable purchases by 8 percent, of which 4 percent represents state use tax liability, and the remaining 4 percent is in lieu of the actual local rate, which varies.

Most states that collect local use tax on the income tax return distribute a portion of collections to the local jurisdictions. California, New York, North Carolina, Ohio, and Wisconsin distribute amounts collected to counties and other jurisdictions based on taxpayers' county of residence as reported on the income tax return.[19] Kansas distributes 50 percent of local use tax to cities and counties based on their proportional share of population, and 50 percent based on their share of property tax levies. Louisiana distributes the local share of use tax collections to all 64 parishes, including the one parish that does not impose a sales/use tax, on a per-capita basis. The parish tax collectors then distribute their share of use tax collections to tax-levying authorities within the parish, based on the previous year's pro-rata share of actual sales tax collections. Oklahoma distributes use tax collected on the income tax return to counties based on each county's proportionate share of sales tax collections. The local portion of South Carolina's use tax that is collected on the income tax is directed to a local option supplemental revenue fund, used to provide a minimum amount to all counties with local sales and use taxes. Utah distributes 50 percent of collections based on the taxpayer's place of residence, and 50 percent on the share of population in each local taxing jurisdiction relative to the state population.

[18] It's impossible to determine to what extent average amounts per return are skewed upward because of a small number of returns reporting very large liability, such as for purchases of artwork. In the case of Connecticut, which was omitted from the analysis, agency staff shared that their understanding was that reporting of a few big-ticket items resulted in high average results. Something similar may have occurred in California, New Jersey, and Idaho.

[19] Amounts for which North Carolina is unable to determine the taxpayer's county of residence are distributed to counties based on each county's proportionate share of sales tax collections.

Options for Minnesota

This section discusses three options that could increase use tax collections in Minnesota:

- Eliminate the $770 de minimis exemption and provide for use tax reporting on the income tax return (either with or without a lookup table)
- Eliminate the $770 de minimis exemption and require taxpayers with purchases below that amount to file use tax returns
- Retain the de minimis exemption and provide for use tax reporting on the income tax return

Option #1: Eliminate de minimis exemption and require reporting on the income tax return

Experience in other states suggests that Minnesota could increase use tax collections by repealing its de minimis exemption requirements and placing a use tax reporting line on the individual income tax return. Additional collections could equal about $4.6 million if Minnesota included a lookup table for taxpayers to use in estimating liability, and about $1.6 million without a lookup table. Estimates depend on Minnesota taxpayers reporting use tax liability at similar rates to taxpayers in other states. Use tax collected in other states was divided by the state's typical combined state and local sales/use tax rate to determine total purchases subject to use tax, and then the total from other states that apply the sales tax to clothing was adjusted to reflect Minnesota's exclusion of clothing from the sales tax base.[20]

Table 3 shows the participation rate and average purchases reported per return (adjusted for states that apply the sales/use tax to clothing) for each state collecting use tax on its income tax return, with the exception of Connecticut.[21] The final column shows the amount of use tax that Minnesota would collect through the income tax system if it experienced the same participation rate and average amount of purchases in each of the states listed. The estimated collections for Minnesota assume 2.6 million returns filed annually by resident taxpayers, the total for tax year 2009.

[20] Average purchases reported in states that tax clothing were adjusted downward by 11.1 percent, to reflect Minnesota's exclusion of clothing from the tax base. The adjustment was calculated based on the share that clothing makes up of e-commerce, as reported by U.S. Census Bureau's 2009 *E-Stats* report.

[21] See footnote 11, supra.

Table 3

Estimated Use Tax Collected on Income Tax Returns in Minnesota if de minimis exemption repealed and income tax reporting implemented

(based on data from other states)

	Participation rate	**Average purchases per return**	**Estimate of use tax collections for Minnesota** (in millions)
States without lookup tables			
Alabama	1.3%	$175	$0.4
California	0.3	1,978	1.0
Idaho	1.2	1,490	3.2
Indiana	0.8	773	1.2
Kentucky	0.6	1,077	1.2
Louisiana	0.6	739	0.8
Ohio	0.9	744	1.2
Rhode Island	0.2	1,334	0.4
South Carolina	0.5	999	0.9
Utah	0.7	763	1.0
Virginia*	0.6	1,218	1.3
West Virginia	0.4	1,352	0.9
Wisconsin	1.0	967	1.8
States with lookup tables			
Kansas	1.8%	$460	$1.5
Maine	9.8	869	15.3
Massachusetts	1.5	1,175	3.2
Michigan	2.3	733	3.0
New Jersey	0.3	2,029	1.3
New York	5.0	841	7.5
North Carolina	2.5	528	2.4
Oklahoma	3.2	494	2.9
Vermont	7.9	566	8.0
All states	**1.6%**	**$853**	**$2.4**
States without lookup table	**0.6%**	**$1,064**	**$1.1**
States with lookup table	**3.1%**	**$795**	**$4.4**
* Virginia exempts annual mail-order catalog purchases of under $100 from use tax.			

The final rows of Table 3 show the aggregate results for all states with use tax reporting on the income tax return, and the aggregates for states that do and do not provide a lookup table. While average purchases per return is higher in states without a lookup table—$1,064 compared with

$795—participation rates are higher in states that do provide a lookup table—3.1 percent of returns, compared with 0.6 percent.

Applying experience in other states to Minnesota gives a wide range of estimates. Use tax collections in Minnesota would equal $15.3 million if Minnesota's experience corresponded to Maine's with 9.8 percent of returns reporting average purchases of about $869. However, collections would only equal about $400,000 if Minnesotans behaved more like Alabamans with only 1.3 percent of returns reporting average purchases of $175. What would actually happen in Minnesota would depend on how many Minnesotans make purchases subject to use tax, how much they purchase, and how well they comply with reporting use tax liability on the income tax return. To the extent those factors vary with geography, Minnesota results might be expected to be similar to the experience in Michigan and Wisconsin. Applying participation rates and average purchases from these two states suggests collections of between $1.8 million and $3.0 million in Minnesota.

Repealing the de minimis exemption and placing a reporting line on the income tax return, but not providing a lookup table for estimating use tax liability, could result in an additional $1.1 million in use tax collections in Minnesota. The amount of revenue Minnesota would collect by repealing the use tax de minimis exemption and placing a use tax reporting line on its income tax return would depend on the participation rate and the average amount of use tax purchases reported by return.[22] If Minnesota's experience was like that of the 13 states listed in Table 2 without lookup tables, collections would be close to the estimated $1.1 million per year.

Use tax collections could be higher—up to $4.4 million—if Minnesota provided a lookup table for taxpayers to use in estimating liability. States with lookup tables tend to experience a higher participation rate and higher overall collections than states without lookup tables. If Minnesota were to employ a lookup table for use tax liability in the income tax instructions, collections could reach $4.4 million if Minnesota taxpayers behaved similarly to taxpayers in other states with lookup tables. The actual amount collected would depend on whether Minnesota taxpayers complied with the reporting requirement at a similar rate to taxpayers in other states.

Option #2: Eliminate the de minimis exemption and require taxpayers to file use tax returns

Simply repealing the exemption without requiring reporting on the income tax return could result in about $100,000 per year in additional use tax collections. This would be a return to individual use tax reporting requirements as they existed prior to enactment of the de minimis exemption. Each individual would be required to file a use tax return if he or she made any purchases subject to use tax—through a catalog, on-line, or while traveling out of state. Many taxpayers would remain unaware of the use tax obligation, though technically even those with only small amounts of purchases would owe the tax. At the time the exemption was

[22] Connecticut is omitted from the analysis (see footnote 11, supra).

enacted, the Department of Revenue estimated the loss of about $100,000 annually through exempting the first $770 of purchases from the tax.[23]

Option #3: Retain the de minimis exemption and allow for use tax payment on the income tax return

Minnesota would not be likely to collect much additional use tax by placing a line on the income tax return if the de minimis exemption provision were retained. House File 2682, introduced during the 1998 legislative session, proposed adding a line to the income tax return for use tax reporting, but left the exemption in place. The Department of Revenue estimate for this bill indicated that the revenue gain was "indeterminable, [but] it appears any impact would be small."[24] The same is likely to be true today.

Revenue gains from adding a use tax line to the income tax return would be offset by administrative costs to the Department of Revenue. Inclusion of the use tax line would require an additional line on the individual income tax return and additional instructions in the booklet. The change would also require programming changes to account for the amount of use tax paid via the income tax return.[25] Earlier estimates prepared by the department did not detail the amount of these administrative costs.

For more information about taxes, visit the income tax area of our website, www.house.mn/hrd/hrd.htm.

[23] Minnesota Department of Revenue, Analysis of 1996 Tax Conference Committee Report, April 11, 1996; see footnote 4, supra.

[24] Minnesota Department of Revenue, Analysis of House File 2682, January 29, 1998.

[25] Ibid.