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TAX EXPENDITURE BUDGET

FOR THE

STATE OF MINNESOTA

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FISCAL YEARS 1986 — 1989

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Business Office of 1880-1900
Minnesota Historical Society Museum Exhibit
East Gallery, August 1966

TAX EXPENDITURE BUDGET
FOR THE
STATE OF MINNESOTA

FISCAL YEARS 1986 - 1989

A REPORT TO THE 1987 MINNESOTA LEGISLATURE

STATUTORY REQUIREMENT: MINNESOTA STATUTES, SECTION 270.067

Commissioner of Revenue
St. Paul, Minnesota

January 1987

STATE OF MINNESOTA
DEPARTMENT OF REVENUE

January 1987

To the Honorable Rudy Perpich, Governor, and the Legislature of the State of Minnesota:

This report is the second comprehensive inventory of the tax expenditure provisions of Minnesota tax law. It contains an estimate of the revenue impact of each tax expenditure for fiscal years 1986 through 1989. This budget report was prepared and is submitted to you pursuant to the requirements of Minnesota Statutes, Section 270.067 (Laws of 1983, Chapter 301).

Sincerely,

Tom Triplett
Commissioner

AN EQUAL OPPORTUNITY EMPLOYER
155-C

PREFACE

This report is the second tax expenditure budget prepared for Minnesota as required by Minnesota Statutes, Section 270.067. The structure and purpose of the report have not changed from the one submitted to the 1985 Legislature. The report has been updated for law changes made during the 1985 and 1986 legislative sessions, and the fiscal impact estimates have been updated to cover fiscal years 1986 through 1989. The estimates for the individual and corporate income taxes do not take into account the impact of the federal Tax Reform Act of 1986.

In preparing this report, the assumptions, criteria, and methodology used in the first report were re-examined, resulting in some minor modifications. The assumptions, criteria, and methodology are explained in the main introduction (page 1) and in the chapter introduction for each tax.

The tax expenditure budget covers all state taxes and local taxes that are applied statewide. If a tax is currently not being paid by anyone or if it has no tax expenditures, it is listed in Appendix B or Appendix C, respectively. The taxes in the main body of the report are grouped by type of tax. Fees are not considered to be taxes and are not included in this report.

The tax expenditure budget was prepared by the Tax Research Division of the Minnesota Department of Revenue. The estimates for Chapter 17, Property Tax, were prepared by the Local Government Aids and Analysis Division. The assistance of people in other divisions of the Department of Revenue, in other state agencies, and in the federal government was invaluable in preparing this report and is gratefully acknowledged.

Questions or comments relating to this report may be directed to:

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TABLE OF CONTENTS

Page

INTRODUCTION TO THE TAX EXPENDITURE BUDGET

History and Purpose of the Tax Expenditure Budget

Minnesota Statutes, Section 270.067, enacted in 1983, requires the commissioner of revenue to prepare a tax expenditure budget which is to be submitted to the Legislature as a supplement to the governor's biennial budget. (The authorizing statute is reprinted at Appendix A.) This report is the second tax expenditure budget for Minnesota, the first one having been submitted to the 1985 Legislature.

The development of tax expenditure budgets began in the 1960's when the federal government started reviewing individual and corporation income tax expenditures. In 1974 a law was enacted which requires the federal Office of Management and Budget to prepare an annual report on tax expenditures. Tax expenditure budgets are also prepared by several states.

The purpose of a tax expenditure budget is to facilitate review of tax provisions in a manner similar to direct budget expenditures. By providing an inventory of tax expenditure provisions and an explanation and fiscal impact for each provision, the tax expenditure budget can be a useful tool in the decision-making process.

The purpose of a tax expenditure is to provide an economic incentive for a certain activity or to provide financial assistance in the form of tax relief to taxpayers in a certain situation. The tax expenditure concept recognizes that the fiscal impact of a tax provision is similar to the outlay of a direct expenditure. The same purpose could be accomplished through either a direct expenditure or a tax expenditure. For example, persons whose medical expenses are high in relation to their income could be assisted by the government through a direct expenditure (such as a grant or subsidy for medical expenses or medical care provided by government-funded agencies) or through a tax expenditure (such as an income tax deduction or credit for medical expenses).

The following section explains how the tax expenditure concept is specifically applied in this report.

Tax Expenditure Criteria

Criteria were established to determine what constitutes a tax expenditure, and these criteria are intended to be objective and consistent. No judgment is made relating to a provision's effectiveness or desirability. A provision must meet all the criteria in order to be considered a tax expenditure.

A provision is a tax expenditure if it:

- Has an impact on a tax that is applied statewide;
- Confers preferential treatment;
- Results in reduced tax revenue;
- Is included in the defined tax base;
- Is not subject to an alternative tax;
- Can be amended or repealed by a change in state law alone; and
- Is not an appropriation.

The first three criteria come directly from the definition portion of the statute that requires the preparation of the tax expenditure budget, Minnesota Statutes, Section 270.067, Subd. 6:

> (1) "Tax expenditure" means a tax provision which provides a gross income definition, deduction, exemption, credit, or rate for certain persons, types of income, transactions, or property that results in reduced tax revenue.
>
> (2) "Tax" means any tax of statewide application or any tax authorized by state law to be levied by local governments generally. It does not include a special local tax levied pursuant to a special law or to a special local tax levied pursuant to general authority that is no longer applicable to local governments generally.

A provision must confer preferential treatment for certain persons, types of income, transactions, or property in order to qualify as a tax expenditure. Therefore, a provision is not a tax expenditure if it provides general tax reductions for all persons, income, transactions, or property subject to the tax. For example, a graduated rate structure is not a tax expenditure if each taxpayer with the same amount of tax base pays at the same rate.

A provision may meet the other six criteria, but if it does not result in reduced tax revenue at any time during fiscal years 1986 through 1989, then it is not a tax expenditure. Some provisions would be tax expenditures except that they are not being used or are not likely to be used in the four fiscal years.

Some provisions exempt the state government from paying a tax that goes into the state treasury. Although technically the provision results in reduced tax revenue, the impact on the state treasury is zero because both revenues and expenditures are reduced by an equal amount. Therefore, these state government exemptions are not considered tax expenditures for taxes that are deposited in the state treasury. Likewise, an exemption for local governments is not a tax expenditure for a locally-collected tax.

A critical step in identifying the tax expenditures for a tax is defining the tax base. The defined tax base provides the framework of the tax for purposes of this study and is not necessarily what an ideal tax would cover. When the tax base is defined, then the tax expenditures can be determined. If something is outside the tax base, it cannot be a tax expenditure.

Each chapter introduction contains a definition of the tax base which explains the framework within which decisions for that tax were made. Answers to questions regarding why a provision is or is not a tax expenditure should be able to be found in the definition of the tax base for the tax and in the explanation of the other criteria found here.

When one tax is levied as an alternative to another tax, the exemption of an activity from the first tax is not considered a tax expenditure if the activity is subject to the alternative tax. This concept was applied more broadly in the preparation of the Tax Expenditure Budget submitted to the 1985 Legislature. For this study, the alternative taxes are limited to those listed here:

income tax - mining occupation tax
corporation income tax - bank excise tax
sales and use tax - motor vehicle excise tax
sales and use tax - charitable gambling tax
highway fuels excise taxes - compressed natural gas permit
property tax - taconite production tax
property tax - gross earnings taxes
airflight property tax - aircraft registration tax

The alternative tax concept applies when one tax is a replacement for another tax. If the taxpayer may choose between the lower of two taxes, that is not considered an alternative tax, and the option becomes a tax expenditure.

Because the tax expenditure budget is intended to be a tool for use by the governor and the Legislature in the budget-making process, only provisions within their jurisdiction are included as tax expenditures. Therefore, provisions that are found in the Minnesota Constitution, federal law, or the United States Constitution are not considered to be tax expenditures.

Finally, the basic purpose of a tax expenditure budget is to allow tax provisions to be reviewed in a manner similar to budget expenditures. Therefore, if a provision is funded through a direct or open appropriation, it is already included in the state budget, and it does not belong in the tax expenditure budget.

The Fiscal Impact of Tax Expenditures: Methodology and Limitations

In addition to understanding how the tax expenditure concept is applied in this study, it is important to understand how the fiscal impacts of the tax expenditures are measured and what the limitations of those measurements are.

Methodology

As the term "expenditure" implies, the estimate of a tax expenditure measures the amount that is being "spent" through the tax system due to a provision. In other words, it is the amount of tax relief provided. The intent of the estimate is not to measure the revenue that would be gained by the repeal of the provision.

When the impact of a tax expenditure is estimated, that provision is examined in isolation, and all other provisions in that tax and in other taxes are held constant. Therefore, the combined impact of two or more provisions are not considered simultaneously, and any secondary impact of one provision on another provision is not taken into account.

Another factor that is held constant is taxpayer behavior. Because the estimate measures the impact of the provision as it exists and not what would happen if it were repealed, no change in taxpayer behavior is assumed.

The precision of the estimates varies with the source of the data and with the applicability of the data to the tax expenditure provision. The sources of information used in the estimates include data from Minnesota tax returns, federal tax expenditure estimates, data from federal tax returns, and other data for Minnesota and the nation. The sources of data used for a tax expenditure estimate are not listed but are available upon request.

Any methodology that is specific to a certain tax is explained in the chapter introduction for that tax.

The term "minimal" is used when the impact is estimated to be less than $100,000 for that fiscal year.

Limitations

Two main points should be understood in using the tax expenditure estimates:

- The estimates do not measure the revenue that would be gained by repealing the provision; and

- The combined fiscal impact of two or more provisions may be very different from the total derived by adding together the fiscal impacts that were measured separately.

As explained under "methodology," the estimates measure the tax relief provided by a provision; they do not measure the impact of repealing the provision. To estimate the revenue to be gained by repealing a provision, other factors would have to be taken into account, including timing, interactions within a tax or between taxes, and changes in taxpayer behavior.

Each estimate is made separately and in isolation. If the combined impact of two or more provisions were to be estimated, the provisions should be considered together rather than making separate estimates and combining them. The results could be very different, especially in the situations described below.

For a tax with a graduated rate structure, such as the individual income tax, the amount of tax relief provided by a particular deduction is based on the average marginal rate that applies to taxpayers claiming that deduction. If that deduction were not available, taxable income and the marginal rate would be higher. The estimate for the combined impact of two or more deductions should take into account a higher level of marginal rates than is done when each item is treated separately. Therefore, the combined impact of two or more provisions would be underestimated by adding together the estimates that are made separately.

In some taxes two tax expenditures may overlap. In the sales and use tax, for example, a transaction may be exempt under two provisions, one which exempts the product and another which exempts the buyer or seller. When the impact of the first provision is estimated, it is assumed that all other tax provisions remain constant so that the transaction would still be exempt under the second provision. Likewise, when the impact of the second provision is estimated, the exemption under the first provision would still exist. Therefore, when a transaction is covered by two exemptions, it is not included in either estimate, and combining the fiscal impacts of the two tax expenditures would underestimate the combined impact of the two provisions.

The situations described here illustrate the problems in combining the estimates of two tax expenditures. The distortion could be much greater if a larger number of items were combined. Combining the estimates for tax expenditures in various taxes would also ignore the interactions between taxes, such as when one tax is a deduction or credit used in determining another tax.

Therefore, although a tax expenditure budget is similar to a direct expenditure budget in many ways, there is one major difference: any totals from a tax expenditure budget would not reflect total tax relief as accurately as the totals in a direct expenditure budget reflect total spending.

TAX EXPENDITURE SUMMARY LIST

	Fiscal Year Impact			
	1986	1987	1988	1989
INDIVIDUAL INCOME TAX				
Federal Exclusions				
1.01 Employer-Provided Meals and Lodging	$9,400,000	$10,300,000	$11,200,000	$12,100,000
1.02 Employer Educational Assistance (Repealed)	400,000	0	0	0
1.03 Employer-Provided Child Care	200,000	200,000	400,000	500,000
1.04 Value of Employer-Provided Commuter Vehicles (Repealed)	Minimal	0	0	0
1.05 Employer Contributions to Prepaid Legal Services Plans (Repealed)	200,000	0	0	0
1.06 Employer Pension Plans	356,500,000	398,000,000	435,000,000	475,200,000
1.07 Employer Contributions for Medical Insurance Premiums and Medical Care	174,400,000	200,900,000	226,200,000	254,100,000
1.08 Employer-Paid Accident and Disability Premiums	900,000	900,000	900,000	900,000
1.09 Employer-Paid Death Benefits	800,000	800,000	800,000	800,000
1.10 Employer-Paid Group Term Life Insurance Premiums	16,300,000	16,500,000	17,600,000	18,800,000
1.11 Cafeteria Plans	4,200,000	6,200,000	10,000,000	14,700,000
1.12 Employee Fringe Benefits (Other than Provisions Covered in Items 1.01 through 1.11)	22,400,000	24,300,000	25,900,000	27,800,000
1.13 Income Earned by Voluntary Employee Benefit Associations	2,800,000	2,800,000	2,800,000	3,300,000

	Fiscal Year Impact			
	1986	1987	1988	1989
1.14 Income Earned by Supplemental Unemployment Benefit Trusts	$200,000	$200,000	$200,000	$200,000
1.15 Income Earned Abroad by U.S. Citizens and Employer-Paid Foreign Housing Costs	700,000	700,000	700,000	800,000
1.16 Benefits and Allowances to Armed Forces Personnel	7,900,000	8,500,000	9,100,000	9,800,000
1.17 Veterans' Benefits Administered by the Veterans Administration	26,100,000	27,300,000	28,500,000	30,100,000
1.18 Military Disability Pensions	500,000	500,000	500,000	500,000
1.19 Workers' Compensation Benefits	46,700,000	51,600,000	56,900,000	62,900,000
1.20 Special Benefits for Disabled Coal Miners	Minimal	Minimal	Minimal	Minimal
1.21 Social Security Benefits	255,800,000	270,100,000	285,000,000	299,800,000
1.22 Cash Public Assistance	8,800,000	8,900,000	9,400,000	9,600,000
1.23 Certain Agricultural Cost-Sharing Payments	600,000	600,000	600,000	600,000
1.24 Interest on Life Insurance and Annuity Savings	40,600,000	42,900,000	45,200,000	47,400,000
1.25 Dividends	4,100,000	5,000,000	5,800,000	5,800,000
1.26 Reinvestment of Dividends in Public Utility Stock (Repealed)	2,100,000	0	0	0
1.27 Interest on General Purpose State and Local Government Debt	22,300,000	19,500,000	21,300,000	21,800,000
1.28 Interest on Nonguaranteed State and Local Government Debt	37,000,000	37,200,000	38,300,000	39,200,000

	Fiscal Year Impact			
	1986	1987	1988	1989
1.29 General Capital Gains Exclusion (Other than Special Provisions Covered in Items 1.30 through 1.35)	$208,400,000	$231,400,000	$265,200,000	$299,700,000
1.30 Capital Gains Treatment of Certain Agricultural Income	10,500,000	11,900,000	13,400,000	14,900,000
1.31 Capital Gains Treatment of Certain Timber Income	600,000	600,000	1,000,000	1,400,000
1.32 Capital Gains Treatment of Iron Ore Royalties	1,500,000	1,700,000	1,800,000	1,900,000
1.33 Capital Gains Treatment of Coal Royalties	Minimal	Minimal	Minimal	Minimal
1.34 Special Treatment of Capital Gains on Home Sales	54,500,000	58,700,000	63,600,000	69,100,000
1.35 Capital Gains at Death	33,600,000	37,000,000	42,000,000	46,200,000
1.36 Income from the Discharge of Debt	Minimal	Minimal	Minimal	Minimal
1.37 Permanent Exemptions from Imputed Interest Rules	1,400,000	1,400,000	1,400,000	1,400,000
1.38 Prizes and Awards	Minimal	Minimal	Minimal	Minimal
1.39 Scholarship and Fellowship Income	10,700,000	12,400,000	13,200,000	14,400,000
Federal Deductions				
1.40 Depreciation	81,800,000	77,400,000	73,700,000	73,500,000
1.41 Expensing Depreciable Business Property	500,000	500,000	500,000	200,000
1.42 Excess of Percentage Over Cost Depletion	1,200,000	1,200,000	1,200,000	1,200,000
1.43 Five-Year Amortization of Business Organizational and Start-Up Costs	1,400,000	1,400,000	1,400,000	1,400,000

	Fiscal Year Impact 1986	1987	1988	1989
1.44 Five-Year Amortization for Housing Rehabilitation (Repealed)	$400,000	$400,000	$400,000	$300,000
1.45 Five-Year Amortization of Trademark Expenses	Minimal	Minimal	Minimal	Minimal
1.46 Seven-Year Amortization for Reforestation Expenditures	Minimal	Minimal	Minimal	Minimal
1.47 Expensing of Research and Development Costs	1,300,000	1,300,000	1,300,000	1,300,000
1.48 Expensing of Magazine Circulation Expenditures	100,000	100,000	100,000	100,000
1.49 Expensing of Construction Period Interest and Taxes for Low Income Housing	700,000	700,000	700,000	700,000
1.50 Expensing for Removal of Barriers to the Handicapped and Elderly (Repealed)	100,000	0	0	0
1.51 Expensing of Exploration and Development Costs	2,100,000	2,100,000	2,100,000	2,300,000
1.52 Expensing of Certain Capital Outlays and Special Cash Accounting Rules for Farmers	1,600,000	1,600,000	1,600,000	1,600,000
1.53 Cash Accounting Other than Agriculture	200,000	200,000	200,000	200,000
1.54 Completed Contract Rules	2,400,000	2,400,000	2,400,000	2,400,000
1.55 Installment Sales	Minimal	Minimal	Minimal	Minimal
1.56 Bad Debt Reserves Other than Financial Institutions	300,000	300,000	300,000	300,000
1.57 Individual Retirement Accounts	113,200,000	125,800,000	140,000,000	154,000,000
1.58 Keogh Plans	17,300,000	19,100,000	21,000,000	22,700,000
1.59 Foreign Housing Costs Paid by Taxpayer	Minimal	Minimal	Minimal	Minimal

	Fiscal Year Impact 1986	1987	1988	1989
1.60 Deduction for Two-Earner Married Couples	$47,600,000	$48,900,000	$50,200,000	$51,700,000
Minnesota Subtractions				
1.61 Pension and Retirement Income (Other than Social Security)	75,200,000	86,400,000	99,500,000	116,200,000
1.62 Unemployment Compensation	36,500,000	36,200,000	35,100,000	35,900,000
1.63 Military Pay	12,800,000	13,900,000	15,000,000	16,200,000
1.64 Per Diem Amounts Paid to State Legislators	100,000	Minimal	100,000	Minimal
1.65 Disposition of Farm Property	Minimal	2,400,000	1,000,000	1,000,000
Personal Deductions				
1.66 Standard Deduction	96,600,000	101,600,000	107,700,000	115,200,000
1.67 Medical and Dental Expenses	28,500,000	29,100,000	29,800,000	30,600,000
1.68 Real Estate Taxes	60,100,000	63,900,000	69,100,000	74,700,000
1.69 General Sales Tax	30,000,000	30,600,000	31,400,000	32,200,000
1.70 Motor Vehicle Excise Tax	9,500,000	10,700,000	11,400,000	11,600,000
1.71 Motor Vehicle Registration Tax	5,500,000	5,800,000	5,900,000	6,200,000
1.72 Interest on Home Mortgages	184,400,000	200,200,000	219,900,000	246,500,000
1.73 Nonmortgage Interest	133,100,000	148,200,000	159,700,000	177,300,000
1.74 Charitable Contributions	80,400,000	82,000,000	84,100,000	86,400,000
1.75 Casualty and Theft Losses	1,300,000	1,400,000	1,400,000	1,400,000
1.76 Tax Return Preparation Fees	4,400,000	4,500,000	4,600,000	4,700,000
1.77 Adoption Expenses	Minimal	Minimal	Minimal	Minimal

	Fiscal Year Impact			
	1986	1987	1988	1989
1.78 Education Expenses for Dependent Children	$6,200,000	$6,300,000	$6,400,000	$6,600,000
Optional Deduction				
1.79 Federal Income Taxes	63,700,000	70,800,000	78,800,000	88,200,000
Preferential Computation				
1.80 Ten-Year Averaging of Lump Sum Distributions	17,300,000	20,100,000	23,300,000	27,000,000
Credits				
1.81 Personal Credits for Age 65 and Over, Blind, Deaf, and Quadriplegic	22,900,000	24,500,000	26,000,000	27,900,000
1.82 Personal Credits for Dependents	78,200,000	79,600,000	80,400,000	82,300,000
1.83 Credit for Income Tax Paid to Other States	6,600,000	7,500,000	8,500,000	9,600,000
1.84 Political Contribution Credit	4,000,000	6,300,000	4,500,000	6,700,000
1.85 Credit for Equity Investment in a Small Business (Repealed)	300,000	Minimal	Minimal	Minimal
1.86 Child and Dependent Care Credit	11,100,000	10,800,000	10,800,000	10,700,000
1.87 Construction Financing (Enterprise Zones)	Minimal	Minimal	Minimal	Minimal
1.88 Employer Tax Credits (Enterprise Zones)	700,000	2,300,000	600,000	600,000
CORPORATE INCOME AND BANK EXCISE TAXES				
Exempt Organizations				
2.01 Tax-Exempt Organizations	200,000	300,000	300,000	400,000
2.02 Credit Unions	2,300,000	2,300,000	2,300,000	2,300,000

	Fiscal Year Impact 1986	1987	1988	1989
Exclusions				
2.03 Deferral of Certain Foreign Dividends	$700,000	$900,000	$1,000,000	$1,100,000
2.04 Permanent Exemptions from Imputed Interest Rules	Minimal	Minimal	Minimal	Minimal
2.05 Income from the Discharge of Debt	Minimal	Minimal	Minimal	Minimal
2.06 Disposition of Farm Property	Minimal	300,000	100,000	100,000
2.07 Unrelated Income (Life Insurance Companies)	Minimal	Minimal	Minimal	Minimal
2.08 Underwriting Income (Life Insurance Companies)	Minimal	Minimal	Minimal	Minimal
2.09 Fee Income (Life Insurance Companies)	Minimal	Minimal	Minimal	Minimal
2.10 Royalties (Life Insurance Companies)	Minimal	Minimal	Minimal	Minimal
Deductions				
2.11 Foreign Source Dividends	0	3,400,000	3,800,000	4,300,000
2.12 Foreign Source Royalties	5,000,000	5,200,000	5,500,000	5,800,000
2.13 Sixty Percent Capital Gains Deduction	11,400,000	10,900,000	11,000,000	12,100,000
2.14 Depreciation	40,100,000	35,700,000	33,300,000	33,900,000
2.15 Expensing Depreciable Business Property	400,000	400,000	200,000	Minimal
2.16 Excess of Percentage Over Cost Depletion for Copper-Nickel Mining	Minimal	Minimal	Minimal	Minimal
2.17 Amortization of Organizational and Start-Up Costs	100,000	100,000	100,000	100,000
2.18 Expensing of Research and Development Costs	11,200,000	11,200,000	11,500,000	11,600,000

	Fiscal Year Impact			
	1986	1987	1988	1989
2.19 Expensing of Magazine Circulation Expenditures	$100,000	$100,000	$100,000	$200,000
2.20 Expensing of Construction Period Interest and Taxes for Low Income Housing	300,000	300,000	300,000	300,000
2.21 Expensing of Mineral Exploration and Development Costs	100,000	100,000	100,000	100,000
2.22 Expensing of Certain Capital Outlays and Special Cash Accounting Rules for Farmers	400,000	500,000	500,000	500,000
2.23 Cash Accounting Other than Agriculture	300,000	300,000	300,000	300,000
2.24 Completed Contract Rules	16,800,000	18,400,000	19,700,000	21,500,000
2.25 Installment Sales	700,000	700,000	700,000	700,000
2.26 Excess Reserves for Bad Debts (Banks)	2,600,000	2,600,000	2,100,000	1,500,000
2.27 Bad Debt Reserves Other than Financial Institutions	1,600,000	1,600,000	1,600,000	1,900,000
2.28 Nonrecognition of Gains on Property Distributions in Liquidation	11,500,000	14,000,000	16,400,000	18,600,000
2.29 Merger Rules for Thrifts	1,000,000	1,100,000	600,000	400,000
2.30 Employee Stock Ownership Plans	Minimal	Minimal	Minimal	Minimal
2.31 Weighted Apportionment	81,700,000	83,400,000	87,600,000	93,800,000
2.32 Single-Factor Apportionment for Mail Order Companies	600,000	600,000	600,000	600,000
2.33 Throwback Sales	25,500,000	25,500,000	25,500,000	25,500,000
2.34 Deductions Allowing Corporations to be Taxed as Partnerships	51,700,000	57,900,000	64,500,000	71,000,000
2.35 Charitable Contributions	10,200,000	11,200,000	12,300,000	13,400,000

	Fiscal Year Impact 1986	1987	1988	1989
2.36 Patronage Dividends (Cooperatives)	$5,400,000	$5,400,000	$5,400,000	$5,400,000
2.37 Dividend Received Deduction	22,500,000	23,000,000	24,200,000	25,900,000
2.38 Exempt Interest (Insurance Companies)	2,300,000	2,500,000	2,800,000	3,100,000
2.39 Sums Paid Out Other than Dividends (Mutual Insurance Companies)	Minimal	Minimal	Minimal	Minimal
2.40 Mean Reserves (Life Insurance Companies)	11,800,000	12,900,000	14,200,000	15,800,000
2.41 Reserves for Deferred Dividends (Life Insurance Companies)	100,000	100,000	100,000	100,000
Credits				
2.42 Research and Development Credit	18,300,000	19,000,000	19,800,000	20,700,000
2.43 Construction Financing (Enterprise Zones)	500,000	1,300,000	1,100,000	1,100,000
2.44 Employer Tax Credits (Enterprise Zones)	1,500,000	4,300,000	4,700,000	5,100,000
2.45 Credit for Technology Transfers to Small Businesses	Minimal	Minimal	Minimal	Minimal
2.46 Credit for Contributions to Small Business Assistance Offices	Minimal	Minimal	Minimal	Minimal
2.47 Credit for Equity Investment in a Small Business (Repealed)	Minimal	0	0	0
2.48 Credit for Gross Premiums Tax (Insurance Companies)	17,400,000	19,000,000	21,100,000	23,700,000

	Fiscal Year Impact			
	1986	1987	1988	1989
ESTATE TAX				
Preferential Valuations				
3.01 Alternate Valuation of Property	$100,000	Minimal	Minimal	Minimal
3.02 Special Use Valuation	800,000	$400,000	$200,000	$200,000
Exclusions				
3.03 Charitable Gifts	3,900,000	3,000,000	2,800,000	3,000,000
3.04 Pensions and Annuities	900,000	600,000	500,000	500,000
3.05 Social Security Benefits	Minimal	Minimal	Minimal	Minimal
3.06 Veterans' Burial Benefits (Repealed)	Minimal	Minimal	0	0
3.07 Life Insurance Proceeds	1,800,000	1,100,000	900,000	1,000,000
Deduction				
3.08 Marital Deduction	17,300,000	8,200,000	5,300,000	5,700,000
Credit				
3.09 Previously Paid Estate or Inheritance Tax (Repealed)	300,000	100,000	0	0
SALES AND USE TAX				
Exemptions - Particular Goods and Services				
4.01 Food	247,100,000	259,400,000	273,400,000	288,200,000
4.02 Clothing and Wearing Apparel	142,100,000	149,000,000	157,000,000	164,800,000
4.03 Publications	11,000,000	11,700,000	12,400,000	13,400,000
4.04 Drugs and Medicines	38,500,000	42,800,000	47,500,000	52,800,000
4.05 Prescription Eyeglasses	4,800,000	5,000,000	5,100,000	5,300,000
4.06 Therapeutic and Prosthetic Devices	3,400,000	3,900,000	4,500,000	5,100,000
4.07 Feminine Hygiene Items	1,600,000	1,600,000	1,700,000	1,800,000

	Fiscal Year Impact 1986	1987	1988	1989
4.08 Textbooks	$1,500,000	$1,600,000	$1,700,000	$1,800,000
4.09 Motor Fuels	148,800,000	133,500,000	136,100,000	141,900,000
4.10 Petroleum Products Used in the Improvement of Agricultural Land	100,000	100,000	100,000	100,000
4.11 Race Horses	600,000	800,000	1,000,000	1,400,000
4.12 Caskets and Burial Vaults	2,100,000	2,200,000	2,200,000	2,300,000
4.13 Accessory Tools	13,800,000	14,300,000	14,900,000	15,600,000
4.14 Capital Equipment Purchases (Distressed Counties)	0	2,000,000	4,800,000	4,100,000
4.15 Construction Materials and Supplies (Distressed Counties)	0	0	2,800,000	1,800,000
4.16 Construction Materials or Equipment (Enterprise Zones)	100,000	100,000	200,000	200,000
4.17 Repair and Replacement Parts for Farm Machinery	11,400,000	11,200,000	11,800,000	12,100,000
4.18 Personal Property Brought into Minnesota	4,900,000	5,100,000	5,300,000	5,500,000
4.19 Packing Materials	100,000	100,000	100,000	100,000
4.20 Out-of-State Leases of Vehicles	Minimal	Minimal	Minimal	Minimal
4.21 Goods Shipped or Transported Out of State	Minimal	Minimal	Minimal	Minimal
4.22 Resource Recovery Equipment	300,000	300,000	300,000	300,000
4.23 Club Dues	6,000,000	6,400,000	6,800,000	7,300,000
4.24 Services	503,300,000	551,200,000	604,700,000	665,400,000
4.25 Residential Sewer Services	5,200,000	5,400,000	5,600,000	5,900,000

	Fiscal Year Impact 1986	1987	1988	1989
4.26 Residential Water Services	$3,200,000	$3,400,000	$3,500,000	$3,700,000
4.27 Residential Heating Fuels	50,400,000	47,300,000	47,300,000	49,500,000
4.28 Interstate Telephone Service	22,900,000	24,000,000	25,200,000	26,500,000
Exemptions - Sales to Particular Groups				
4.29 Sales to Local Governments	41,100,000	43,100,000	45,300,000	47,500,000
4.30 Sales to Nonprofit Organizations	26,800,000	29,600,000	32,800,000	36,400,000
4.31 Sales to Veterans' Organizations	Minimal	Minimal	Minimal	Minimal
4.32 Sales of Building Materials to Disabled Veterans	Minimal	Minimal	Minimal	Minimal
4.33 New Satellite Broad-casting Facility	300,000	0	200,000	600,000
4.34 Telephone Central Office Equipment (Repealed)	4,200,000	2,200,000	0	0
4.35 Mill Liners and Grinding Rods and Balls	100,000	100,000	100,000	100,000
4.36 Railroad Rolling Stock	1,000,000	1,000,000	1,100,000	1,100,000
4.37 Airflight Equipment	14,200,000	23,300,000	20,700,000	20,800,000
Exemptions - Sales by Particular Groups				
4.38 Isolated or Occasional Sales	28,100,000	28,600,000	29,200,000	29,900,000
4.39 Sales by Auctioneers and Brokers	1,700,000	1,700,000	1,800,000	1,900,000
4.40 Institutional Meals	16,000,000	16,600,000	17,400,000	18,100,000
4.41 Admission Fees to Recreational Areas	800,000	900,000	900,000	1,000,000
4.42 Admission to Artistic Performances	1,100,000	1,100,000	1,200,000	1,200,000

		Fiscal Year Impact			
		1986	1987	1988	1989
4.43	Admission to School-Sponsored Events	$300,000	$300,000	$300,000	$300,000
4.44	Fundraising Sales by Nonprofit Organizations	1,900,000	2,000,000	2,100,000	2,200,000
4.45	Candy Sales by Organizations Which Provide Services to Minors	Minimal	Minimal	Minimal	Minimal
Special Rates / Reduced Sales Price					
4.46	Two Percent Rate for Farm Machinery	13,700,000	13,400,000	14,200,000	14,600,000
4.47	Two Percent Rate for Logging Equipment	200,000	200,000	200,000	200,000
4.48	Four Percent Rate for Capital Equipment Sold to New or Expanding Industries	5,200,000	4,400,000	3,200,000	3,900,000
4.49	Four Percent Rate for Special Tooling	100,000	100,000	100,000	100,000
4.50	Taxes Imposed by the United States Government	1,900,000	2,000,000	2,100,000	2,100,000
4.51	Tax Paid to Other States	600,000	600,000	600,000	600,000
4.52	Price Reduced by Value of Trade In	3,800,000	4,000,000	4,200,000	4,400,000
MOTOR VEHICLE EXCISE TAX					
Exemptions					
5.01	Vehicles Acquired by Inheritance	600,000	600,000	600,000	600,000
5.02	Out-of-State Acquisitions	1,000,000	1,100,000	1,100,000	1,200,000
5.03	Transfers Between Joint Owners	500,000	500,000	500,000	600,000
5.04	Transfers Between Spouses, Parents and Children, and Guardians and Wards	6,300,000	6,500,000	6,700,000	7,000,000
5.05	Transfers in Divorce Proceedings	200,000	200,000	200,000	200,000

	Fiscal Year Impact 1986	1987	1988	1989
5.06 Corporate and Partnership Transfers	Minimal	Minimal	Minimal	Minimal
5.07 Sales to Nonprofit Organizations	$1,000,000	$1,100,000	$1,100,000	$1,200,000
5.08 Sales to Local Governments	5,700,000	5,900,000	6,200,000	6,400,000
5.09 Sales to Disabled Veterans	Minimal	Minimal	Minimal	Minimal
Reduced Purchase Price				
5.10 Federal Excise Taxes	200,000	200,000	200,000	300,000
5.11 Price Reduced by Value of Trade In	31,800,000	32,900,000	34,300,000	35,700,000
Preferential Computation				
5.12 Flat Tax on Older Cars	4,300,000	4,400,000	4,600,000	4,800,000
Credit				
5.13 Credit for Taxes Paid to Other States	200,000	200,000	200,000	200,000
HIGHWAY FUELS EXCISE TAXES				
Exemptions				
6.01 Transit Systems Owned by Local Units of Government	1,600,000	1,600,000	1,700,000	1,700,000
6.02 Reciprocal Agreements for Out-of-State Purchases	500,000	500,000	500,000	500,000
6.03 Motor Vehicles Not Requiring Registration (Special Fuels)	200,000	200,000	200,000	200,000
Special Rates				
6.04 Border Rates	200,000	200,000	200,000	200,000
6.05 Gasohol (Other than for Governmental Units and Schools)	22,200,000	5,400,000	4,300,000	4,300,000
6.06 Gasohol for Governmental Units and Schools	200,000	200,000	200,000	200,000

	Fiscal Year Impact 1986	1987	1988	1989
6.07 Maximum Rate for High Mileage Vehicles (Compressed Natural Gas)	Minimal	Minimal	Minimal	Minimal
ALCOHOLIC BEVERAGE TAXES				
Exemptions				
7.01 Consumer Purchases Made Out of State	$1,400,000	$1,400,000	$1,400,000	$1,400,000
7.02 Home Fermentation (Wine and Beer)	100,000	100,000	100,000	100,000
7.03 Alcoholic Beverages Sold to Food Processors	Minimal	Minimal	Minimal	Minimal
7.04 Consumption on Brewery Premises (Beer)	Minimal	Minimal	Minimal	Minimal
7.05 Wine Used for Tasting and Testing	Minimal	Minimal	Minimal	Minimal
7.06 Wine for Sacramental Purposes	Minimal	Minimal	Minimal	Minimal
Credit				
7.07 Small Brewers' Credit (Beer)	200,000	200,000	200,000	200,000
CIGARETTE AND TOBACCO TAXES				
Exemptions				
8.01 Sales to Minnesota Correctional Institutions	215,000	235,000	255,000	277,000
8.02 Limited Quantities Exempt	520,000	520,000	520,000	520,000
MORTGAGE REGISTRY TAX				
Exemption				
9.01 Certain Persons and Organizations Exempt	100,000	100,000	100,000	100,000

	Fiscal Year Impact 1986	1987	1988	1989
DEED TRANSFER TAX				
Exemptions				
10.01 Transfers Between Co-Owners	Minimal	Minimal	Minimal	Minimal
10.02 Deeds of Distribution by Personal Representatives	Minimal	Minimal	Minimal	Minimal
10.03 Deeds for Cemetery Lots	Minimal	Minimal	Minimal	Minimal
10.04 Transfers Involving Government Agencies	$300,000	$300,000	$300,000	$300,000
CHARITABLE GAMBLING TAX				
Exemptions				
11.01 Bingo at a Nursing Home or Senior Citizen Organization	Minimal	Minimal	Minimal	Minimal
11.02 Bingo at Fairs and Civic Celebrations	Minimal	Minimal	Minimal	Minimal
11.03 Infrequent Bingo Occasions	Minimal	Minimal	Minimal	Minimal
11.04 Smaller Raffles	Minimal	Minimal	Minimal	Minimal
11.05 Lawful Gambling Under Certain Conditions	400,000	400,000	400,000	400,000
TELEPHONE GROSS EARNING TAX				
Exemptions				
12.01 Interstate Telephone Service	12,500,000	22,800,000	16,100,000	10,800,000
12.02 Cellular Radio	200,000	200,000	200,000	100,000
Reduced Rates				
12.03 Reduced Rate for Certain Business	10,000,000	9,200,000	6,700,000	5,000,000

	Fiscal Year Impact 1986	1987	1988	1989
INSURANCE PREMIUMS TAXES				
Exemptions				
13.01 Cooperative Life and Casualty Companies	Minimal	Minimal	Minimal	Minimal
13.02 Fraternal Beneficiary Societies	$2,300,000	$2,500,000	$2,700,000	$3,000,000
13.03 Nonprofit Health Service Plan Corporations	8,700,000	9,500,000	10,400,000	11,500,000
13.04 Health Maintenance Organizations	14,100,000	15,400,000	16,900,000	18,700,000
13.05 Domestic Mutual Insurance Companies Other than Life	4,700,000	6,100,000	5,800,000	5,900,000
13.06 Farmers' Mutual and Township Mutual Fire Insurance Companies (Fire Marshal Tax)	100,000	300,000	200,000	200,000
Preferential Computation				
13.07 Ocean Marine Profits Tax	200,000	300,000	300,000	300,000
Credit				
13.08 Credit for Payments to Minnesota Comprehensive Health Association	4,600,000	4,800,000	5,000,000	5,200,000
TACONITE PRODUCTION TAX				
Credit				
14.01 Water Filtration Plant Credit	250,000	250,000	0	0
MINING OCCUPATION TAX				
Credits				
15.01 Labor Credit	14,100,000	11,200,000	11,200,000	11,200,000
15.02 Pollution Control Credit	Minimal	Minimal	Minimal	Minimal
15.03 Research, Experimentation, and Exploration Credit	Minimal	Minimal	Minimal	Minimal

	Fiscal Year Impact 1986	1987	1988	1989
15.04 Loss Mine Credit (Iron Ore)	Minimal	Minimal	Minimal	Minimal
15.05 Discount Credit (Iron Ore)	Minimal	Minimal	Minimal	Minimal
MINERAL ROYALTY TAXES				
Credits				
16.01 Labor Credit	$4,200,000	$4,200,000	$4,200,000	$4,200,000
16.02 Loss Mine Credit	Minimal	Minimal	Minimal	Minimal
Note on Taconite Amendment				
16.03 Constitutional Limit on the Taxation of Taconite Mining Companies	N/A	N/A	N/A	N/A
PROPERTY TAX				
Exemptions				
17.01 Exempt Property	482,500,000	513,100,000	779,300,000	828,900,000
Preferential Valuations				
17.02 Classification System	N/A	N/A	N/A	N/A
17.03 Green Acres Treatment of Agricultural Land	6,300,000	5,400,000	5,100,000	5,800,000
17.04 Open Space Properties	2,600,000	3,200,000	4,000,000	5,000,000
Preferential Computations				
17.05 Auxiliary Forest Tax and Tree Growth Tax	1,300,000	1,000,000	800,000	700,000
Credits				
17.06 Taconite Homestead Credit	10,100,000	10,400,000	11,000,000	11,500,000
17.07 Power Line Credit	200,000	200,000	200,000	200,000

	Fiscal Year Impact			
	1986	1987	1988	1989
AIRFLIGHT PROPERTY TAX				
Preferential Computation				
18.01 Commuter Airlines	Minimal	Minimal	Minimal	Minimal
MOTOR VEHICLE REGISTRATION TAX				
Exemptions				
19.01 Government Vehicles	$2,900,000	$4,000,000	$4,200,000	$4,300,000
19.02 School Buses	100,000	100,000	100,000	100,000
19.03 Nonresident Military Personnel	Minimal	Minimal	Minimal	Minimal
19.04 Medal of Honor Recipients	Minimal	Minimal	Minimal	Minimal
19.05 Disabled Veterans	Minimal	Minimal	Minimal	Minimal
Credit				
19.06 Physically Handicapped Persons	200,000	200,000	200,000	200,000
AIRCRAFT REGISTRATION TAX				
Exemptions				
20.01 Local Government Aircraft	Minimal	Minimal	Minimal	Minimal
20.02 Civil Air Patrol Aircraft	Minimal	Minimal	Minimal	Minimal

CHAPTER 1: INDIVIDUAL INCOME TAX

Collections and History

The individual income tax is the largest single source of state revenue. For fiscal year 1986 net collections from this tax were $1.95 billion, which was 40.5% of total state revenue. All revenue from this tax goes into the state general fund.

The State of Minnesota enacted an income tax for both individuals and corporations in 1933, twenty years after the federal income tax had been adopted in 1913. The same graduated rate schedule applied to both taxes, and it was divided into $1,000 increments, with the lowest rate at 1% on the first $1,000 of taxable income and the highest rate at 5% on taxable income over $10,000.

Many changes have been made to the individual income tax since 1933, but the changes enacted in 1985 are among the most important with respect to the structure of the tax. These changes are effective beginning with the 1985 tax year.

Prior to 1985, the individual income tax was imposed primarily on the income of the individual. Although married couples could file joint returns, the choice between filing jointly or filing separately (on either a combined return or on separate returns) was not restricted. When both spouses had positive income, it was usually to their advantage to file separately. One rate schedule applied to all types of filers, and the same maximum standard deduction applied to each filer.

Beginning in 1985, the focus of the individual income tax for married persons shifted to the joint income of the couple. The election to file a joint return or separate returns is required to be the same as the election on the federal return. Because most couples benefit from filing joint federal returns, a great majority of married couples who had previously filed separately for Minnesota now file joint state returns. For the first time a different rate schedule applies to joint returns, and generally it confers preferential treatment on joint filing. The maximum standard deduction for a married person filing separately is half the amount allowed to a joint return or to an unmarried person.

The election of filing status and treatment of joint income were among several areas in which the Minnesota individual income tax structure was made more similar to the federal tax structure. Several modifications to federal adjusted gross income were eliminated, and the federal definition of dependent, which is more restrictive, was adopted. Continuing a trend of recent years, itemized deductions were brought into closer conformity with federal provisions. Several credits which were unique to Minnesota were repealed.

The other major change enacted in 1985 related to the deduction of the federal income tax. Federal income taxes have been deductible on the state return since 1933. When the standard deduction was enacted in 1949, the federal tax was made a deduction separate from the standard or itemized deductions. In 1985, the deduction of federal income taxes was made an option. If federal income taxes are deducted, one rate schedule is used, with a maximum rate of 14.0%. If federal income taxes are not deducted, a lower set of rates applies, with a maximum rate of 9.9%. The taxpayer computes his tax both ways and uses the lower tax.

Indexing was first adopted for the Minnesota individual income tax in 1979. The formula was modified in 1981 and was applicable through tax year 1984. The items that had previously been indexed--the tax rate brackets, the personal credit amount, and the maximum standard deduction--were set at specific amounts for tax year 1985.

Beginning with tax year 1986, indexing again applies to these three provisions. A new indexing formula, which is the same as used for the federal income tax, is adopted, and it is based on the annual increase in the United States Consumer Price Index. The impact of indexing is included in the tax expenditure estimates for the items and the years to which it applies.

Note: The impact of the federal Tax Reform Act of 1986 is not reflected in the estimates.

Tax Base

One criterion for determining if a provision is a tax expenditure is that it is included in the defined tax base. For this study, the tax base for the individual income tax is defined to be income from all sources less expenses that are reasonable and necessary to earn that income. If an expense is determined to be reasonable and necessary in earning income, it is not considered to be a tax expenditure.

For example, expenses related to the business use of a car are considered necessary in earning an income, and the deduction of these expenses is not considered to be a tax expenditure. However, expenses related to the personal use of a car are not considered necessary in earning an income. Therefore, the itemized personal deductions for the motor vehicle excise tax and the motor vehicle registration tax are defined as tax expenditures.

Computation of the Tax

The tax expenditures for the individual income tax, as for all other taxes, are shown in the order in which they occur in the computation of the tax. Beginning with tax year 1985, the Minnesota individual income tax is computed as follows:

		Income from all sources
	minus:	federal exclusions
	equals:	federal gross income
	minus:	federal deductions
	equals:	federal adjusted gross income
	plus:	Minnesota additions
	minus:	Minnesota subtractions
	equals:	Minnesota gross income
	minus:	personal deductions (standard or itemized)
	equals:	Minnesota taxable income
Option A	times:	graduated rates (top rate 9.9%)
	equals:	Minnesota gross tax
Option B	minus:	federal income tax liability
	equals:	taxable income
	times:	graduated rates (top rate 14.0%)
	equals:	Minnesota gross tax
	option:	the lower Minnesota gross tax under Option A or Option B
	minus:	personal and dependent credits
	minus:	other nonrefundable credits
	equals:	Minnesota net tax
	minus:	prior payments (withholding and estimated tax)
	minus:	refundable credits
	equals:	amount due or refund

The computation of the Minnesota individual income tax begins with federal adjusted gross income. Legislative action is required to adopt any federal provisions, or changes made to those provisions, which affect federal adjusted gross income. Such exclusions and deductions which Minnesota has adopted without adjustment are shown in the study as federal exclusions and federal deductions.

If Minnesota law requires that part of a federal exclusion or deduction be added back, the provision is shown as a federal exclusion or deduction, with the fiscal impact reflecting the net Minnesota exclusion. The two provisions for which this occurs are Items 1.27 and 1.28, the federal exclusions for state and municipal debt.

If Minnesota law allows a deduction for an item in addition to the federal exclusion or deduction, the item is shown as a Minnesota subtraction, reflecting the combined impact of the federal and state provisions. For example, Item 1.62, Unemployment Compensation, is shown in this way.

Minnesota subtractions also include provisions unique to Minnesota, such as Item 1.63, Military Pay.

Federal adjusted gross income is modified by the Minnesota adjustments to determine Minnesota gross income. The taxpayer then has the option of itemizing his personal deductions or of taking the standard deduction.

Beginning in 1985, the itemized deductions are the same as the federal itemized deductions, with two exceptions. State income taxes are not deductible on the Minnesota return, and specified dependent educational expenses are deductible. For the itemized deductions, the estimates measure the incremental cost of the deduction over the standard deduction for those taxpayers who would lose the benefit of itemizing by the loss of that one deduction. This methodology differs from that used for the itemized deductions in the Tax Expenditure Budget submitted to the 1985 Legislature. In that first study, the fiscal impact of each itemized deduction measured the cost of that deduction without any offset for those who would switch to the standard deduction.

Beginning in 1985, the standard deduction is 10% of Minnesota gross income, with a maximum deduction of $2,400 for married-joint returns and single persons and $1,200 for each married-separate filer. The maximum standard deduction is indexed annually, beginning with tax year 1986. For tax year 1986, the maximum deduction amounts are $2,500 and $1,200 respectively.

After personal deductions have been subtracted, the taxpayer has another option. He may deduct his federal income tax liability and use one rate schedule, or he may choose not to deduct his federal income tax liability and use a lower rate schedule. On the income tax return the taxpayer calculates his tax both ways and uses the lower of the two taxes.

The brackets and rates were established by law for the 1985 tax year, and beginning in 1986, the brackets are increased annually by the increase in the United States Consumer Price Index. The following are the brackets and rates for the 1986 tax year.

Married Couples Filing Joint Returns

Elect to Deduct Federal Taxes: Taxable Income			Rate	Elect Not to Deduct Federal Taxes: Taxable Income			Rate
$1	-	$910	1.5%	$1	-	$1,240	1.7%
911	-	1,810	2.0	1,241	-	1,760	2.1
1,811	-	3,630	2.9	1,761	-	2,800	2.3
3,631	-	5,570	4.8	2,801	-	5,810	3.3
5,571	-	7,260	5.9	5,811	-	9,440	5.3
7,261	-	7,390	6.1	9,441	-	13,070	6.8
7,391	-	9,200	7.2	13,071	-	18,460	8.5
9,201	-	12,830	8.3	18,461	-	31,940	9.3
12,831	-	14,520	9.3	31,941	and over		9.9
14,521	-	16,590	10.0				
16,591	-	22,300	11.0				
22,301	-	22,940	11.3				
22,941	-	26,440	12.3				
26,441	-	29,550	12.6				
29,551	-	32,920	13.7				
32,921	and over		14.0				

Single Persons and Married-Separate Returns

Elect to Deduct Federal Taxes: Taxable Income			Rate	Elect Not to Deduct Federal Taxes: Taxable Income			Rate
$1	-	$730	1.3%	$1	-	$310	1.0%
731	-	1,450	1.9	311	-	620	1.3
1,451	-	2,900	3.2	621	-	930	1.6
2,901	-	4,460	5.4	931	-	1,350	2.1
4,461	-	5,910	6.9	1,351	-	2,070	2.7
5,911	-	7,360	8.4	2,071	-	2,900	3.7
7,361	-	10,270	9.8	2,901	-	4,460	4.5
10,271	-	13,270	11.1	4,461	-	6,640	6.1
13,271	-	15,970	12.4	6,641	-	9,750	7.5
15,971	-	20,120	13.6	9,751	-	16,800	9.3
20,121	and over		14.0	16,801	and over		9.9

A nonrefundable personal credit against the tax is allowed to the taxpayer and to the spouse, and a credit is allowed for each qualifying dependent. Additional credits are allowed if the taxpayer and/or spouse is age 65 or over, or if a qualifying person is blind, deaf, or quadriplegic. For tax year 1985 the amount of each credit is $70, and the amount of the credit is indexed annually, beginning with tax year 1986. For tax year 1986, the amount of each credit is $73.

The personal credits and the other nonrefundable credits are subtracted from gross tax to determine net tax. The prior payments (withholding and estimated tax) and the refundable credits are then subtracted to arrive at the amount due or refund.

FEDERAL EXCLUSIONS

1.01 EMPLOYER-PROVIDED MEALS AND LODGING

Internal Revenue Code, Sections 119 and 107
Minnesota Statutes, Section 290.01, Subd. 20

Section 119 of the Internal Revenue Code allows an employee to exclude from federal gross income the value of meals and lodging furnished by the employer for the employer's convenience on his business premises. To qualify, the lodging must be required as a condition of employment, such as for a live-in housekeeper or an apartment resident manager. This provision does not cover those instances when an employee is reimbursed by his employer for amounts previously spent on meals and lodging.

Section 107 of the Internal Revenue Code allows a member of the clergy to exclude from gross income any housing allowance that is part of compensation, whether it is the rental value of a home furnished or a rental allowance paid, to the extent that it is used to rent or provide a home.

This exclusion was first allowed in 1918 by federal regulation. Section 119 was enacted in 1954 and last changed in 1981. Section 107 was enacted in 1954 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$9,400,000	$10,300,000	$11,200,000	$12,100,000

1.02 EMPLOYER EDUCATIONAL ASSISTANCE (REPEALED)

Internal Revenue Code, Section 127
Minnesota Statutes, Section 290.01, Subd. 20

Prior to 1978, only employer-provided educational assistance which was job related was excluded from federal gross income. In 1978, Section 127 of the Internal Revenue Code was enacted which removed the distinction between job-related and non-job-related educational expenditures and allowed all employer-provided educational assistance to be excluded if the assistance is not available only to management, highly-compensated employees, or to certain shareholders. Because costs incurred which are necessary in earning an income are not considered to be tax expenditures, only the exclusion for non-job-related educational expenses is considered a tax expenditure. Under this provision, all costs of an employee's tuition, fees, books, supplies and equipment paid for by an employer are excluded from the employee's gross income, up to a maximum of $5,000.

Section 127 of the Internal Revenue Code was enacted in 1978. In 1984 the exclusion was limited to $5,000, and the expiration date was extended for two years to December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$400,000	$0	$0	$0

1.03 EMPLOYER-PROVIDED CHILD CARE

Internal Revenue Code, Section 129
Minnesota Statutes, Section 290.01, Subd. 20

The value of employer-provided child or dependent care, not exceeding an employee's earned income, is excluded from federal gross income. Amounts exceeding earned income are taxed. If the taxpayer makes direct payments for child or dependent care, this exclusion does not apply, but the taxpayer may be eligible for the child and dependent care credit (Item 1.86).

This provision was enacted in 1981 and was first effective for tax year 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$400,000	$500,000

1.04 VALUE OF EMPLOYER-PROVIDED COMMUTER VEHICLES (REPEALED)

Internal Revenue Code, Section 124
Minnesota Statutes, Section 290.01, Subd. 20

The value to an employee of an employer-provided commuter vehicle which is used for transportation between an employee's residence and place of employment is excluded from the employee's gross income. However, a commuter vehicle must seat at least eight passengers to qualify. This provision is a tax expenditure only to the extent that the value of the vehicle received by the employee exceeds any fees or charges which the employee pays to the employer. In most cases employees are required to pay a per mile or monthly charge to at least partially compensate the employer for the cost of the commuting vehicle. On the average, 75% of an employer's costs are recovered in this way.

This provision was enacted in 1978 and expired for tax years beginning after December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	$0	$0	$0

1.05 EMPLOYER CONTRIBUTIONS TO PREPAID LEGAL SERVICES PLANS (REPEALED)

Internal Revenue Code, Sections 120 and 501(c)(20)
Minnesota Statutes, Section 290.01, Subd. 20

An employee may exclude from federal gross income the value of legal services or benefits received, if such services or benefits are from a qualified group prepaid legal services plan established by the employer. The exclusion applies only to plans that are prepaid by the employer; plans which reimburse employees for legal fees do not qualify. Also, the plan must provide legal services to all employees equally and not just to certain management personnel, highly-compensated employees, or certain shareholders.

This provision was enacted in 1976. Legislation enacted in 1984 extended the expiration date one year to December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$0	$0	$0

1.06 EMPLOYER PENSION PLANS

Internal Revenue Code, Sections 401-407, 410, 415, and 457
Minnesota Statutes, Section 290.01, Subd. 20

All employer contributions to an employee's qualified pension plan are excluded from the employee's federal gross income. The earnings derived from such contributions, as well as those from contributions made by the employee, are also excluded. The employee's contribution is excluded from income for specific types of plans, including 401(k) plans, certain government plans, tax-sheltered annuities, and deferred compensation.

Strictly speaking, this provision represents a deferral of income and not an exclusion, since all pension income which was not previously subject to taxation must be included in federal gross income when disbursements are received. The estimates show the fiscal impact of excluding current-year pension contributions and earnings from taxable income, net of all taxed pension income which is disbursed in that year.

Separate estimates are made for the fiscal impact of individual retirement accounts, Keogh plans, and the Minnesota subtraction for pension income (Items 1.57, 1.58, and 1.61, respectively).

This exclusion was enacted in 1921. Minnesota has allowed this exclusion since 1933, adopting the federal language in 1961. This provision was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$356,500,000	$398,000,000	$435,000,000	$475,200,000

1.07 EMPLOYER CONTRIBUTIONS FOR MEDICAL INSURANCE PREMIUMS AND MEDICAL CARE

Internal Revenue Code, Sections 105 and 106
Minnesota Statutes, Section 290.01, Subd. 20

An employee may exclude from federal gross income all employer contributions to health insurance plans which provide compensation for sickness and injury. Payments from such plans may be excluded to the extent that they are based on the nature of the injury or illness or the cost of medical care and not based on the period the employee is absent from work. A self-employed person is not an employee for the purpose of this exclusion.

Employer contributions for medical insurance premiums and medical care have never been taxed in the United States. In 1943, an Internal Revenue Service ruling made this previously unwritten rule explicit for employer contributions to group health insurance policies. The 1943 ruling did not cover contributions to individual health insurance policies, and a 1953 Internal Revenue Service ruling declared these to be taxable. Section 106 was enacted in 1954 to reverse the 1953 ruling; and, thereby, employer contributions to employee health and accident plans are excludable from an employee's gross income.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$174,400,000	$200,900,000	$226,200,000	$254,100,000

1.08 EMPLOYER-PAID ACCIDENT AND DISABILITY PREMIUMS

Internal Revenue Code, Section 106
Minnesota Statutes, Section 290.01, Subd. 20

Premiums paid by an employer to an employee accident and disability plan are excluded from the gross income of the employee.

Section 106 was enacted in 1954.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$900,000	$900,000	$900,000	$900,000

1.09 EMPLOYER-PAID DEATH BENEFITS

Internal Revenue Code, Section 101(b)
Minnesota Statutes, Section 290.01, Subd. 20

Benefits paid by an employer to a beneficiary upon the death of an employee may be excluded from federal gross income. The exclusion is limited to $5,000 and applies to a lump sum distribution from a profit-sharing plan, employee stock ownership plan, an annuity, or tax-sheltered annuity. It does not apply to a joint or survivor annuity.

This provision has been in effect since the 1930's and was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$800,000	$800,000	$800,000	$800,000

1.10 EMPLOYER-PAID GROUP TERM LIFE INSURANCE PREMIUMS

Internal Revenue Code, Section 79
Minnesota Statutes, Section 290.01, Subd. 20

An employee may exclude from federal gross income all group term life insurance premiums paid on his behalf by an employer. However, this exclusion applies only to premiums paid for insurance coverage of $50,000 or less; premiums for coverage in excess of $50,000 must be included in an employee's gross income. In order for the premiums to qualify for the exclusion, the plan must meet certain requirements including nondiscrimination in favor of certain employees, such as highly-compensated persons or senior management personnel.

In 1920 a federal administrative legal opinion was issued authorizing this exclusion. In 1954 when the Internal Revenue Code was revised, the provision was formally placed in the Code as Section 79. The last substantive change to this provision became effective beginning with tax year 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$16,300,000	$16,500,000	$17,600,000	$18,800,000

1.11 CAFETERIA PLANS

Internal Revenue Code, Section 125
Minnesota Statutes, Section 290.01, Subd. 20

Section 125 of the Internal Revenue Code allows an employee to choose to receive a combination of nontaxable fringe benefits or receive all or part of the value of the fringe benefits as taxable compensation. The value of a combination of fringe benefits chosen by the employee is excluded from federal gross income. In 1984 the nontaxable benefits that may be offered by a plan were restricted to the following: group life insurance; accident or health benefits; legal services; dependent care assistance; and 401(k), profit sharing or stock bonus plans.

This exclusion was first allowed in 1978. The last change was made in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,200,000	$6,200,000	$10,000,000	$14,700,000

1.12 EMPLOYEE FRINGE BENEFITS (OTHER THAN PROVISIONS COVERED IN ITEMS 1.01 THROUGH 1.11)

Internal Revenue Code, Section 132
Minnesota Statutes, Section 290.01, Subd. 20

In addition to the employee benefits covered in Items 1.01 through 1.11, certain other employee benefits may be excluded from gross income. The exempt benefits include: employee discounts, up to specified limits; no-additional-cost service, such as an airline pass for an otherwise empty seat; and de minimis fringe benefits for which the value of the property or service provided is so small as to make accounting for it unreasonable or administratively impracticable, such as meals in a subsidized cafeteria. Working condition fringe benefits are also excluded from gross income but are not considered tax expenditures because in general they are paid for expenses necessary in earning an income.

Prior to 1984, the status of employee benefits not specifically exempted by statute was uncertain. The Internal Revenue Code's definition of income appeared to include these benefits as taxable income; however, Congress prohibited the Internal Revenue Service from issuing any regulations defining these benefits as taxable income. The status of fringe benefits was made certain through the enactment of Section 132 of the Internal Revenue Code. This provision became effective January 1, 1985. Any benefit not specified as exempt by Section 132 or another section of the Internal Revenue Code is now considered taxable compensation.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$22,400,000	$24,300,000	$25,900,000	$27,800,000

1.13 INCOME EARNED BY VOLUNTARY EMPLOYEE BENEFIT ASSOCIATIONS

Internal Revenue Code, Section 501(c)(9)
Minnesota Statutes, Section 290.01, Subd. 20

Section 501 of the Internal Revenue Code provides an exemption for the earnings from money set aside in an entity called a voluntary employee benefit association. The money set aside and the earnings on the money are used to pay the cost of a variety of fringe benefits such as medical benefits.

The exemption was first allowed by the federal government in 1928. Minnesota statutes first allowed the exemption in 1941; the last change was in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,800,000	$2,800,000	$2,800,000	$3,300,000

1.14 INCOME EARNED BY SUPPLEMENTAL UNEMPLOYMENT BENEFIT TRUSTS

Internal Revenue Code, Section 501(c)(9) and 501(c)(17)
Minnesota Statutes, Section 290.01, Subd. 20

Section 501 of the Internal Revenue Code provides an exemption for the earnings from money set aside in an entity called a supplemental unemployment benefit trust. The money set aside and the earnings on the money are used to provide payments to separated employees. When benefits are distributed from the trust, the entire amount is taxable to the recipient.

The exemption of supplemental unemployment trust earnings was first allowed by Minnesota Statutes in 1941. The provision was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$200,000	$200,000

1.15 INCOME EARNED ABROAD BY U.S. CITIZENS AND EMPLOYER-PAID FOREIGN HOUSING COSTS

Internal Revenue Code, Sections 911 and 912
Minnesota Statutes, Section 290.01, Subd. 20

A United States citizen or resident whose principal residence is in a foreign country, and who is either present overseas for eleven out of twelve consecutive months or who is a bona fide resident of a foreign country may exclude from federal gross income the income which is earned in a foreign country up to a maximum amount. The maximum exclusion increases each year, with $80,000 being allowed through tax year 1987, $85,000 in 1988, $90,000 in 1989, and $95,000 thereafter. This exclusion does not apply to federal employees, including members of the Armed Forces. The taxpayer may also exclude from federal gross income employer-paid foreign housing costs. For a related discussion see Item 1.59.

Income earned abroad by United States citizens was first excluded from federal gross income in 1926. This provision was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$700,000	$700,000	$700,000	$800,000

1.16 BENEFITS AND ALLOWANCES TO ARMED FORCES PERSONNEL

Internal Revenue Code, Sections 112 and 113
Internal Revenue Service Regulation 1.61-2
Minnesota Statutes, Section 290.01, Subd. 20
Minnesota Rules, Part 8001.9000
Court Decisions

Under the authority of Internal Revenue Service Regulation 1.61-2 and several court decisions, the value of in kind meals and quarters given to military personnel is excluded from gross income. Also excluded are certain cash allowances provided in lieu of in kind benefits.

Specified combat pay and mustering-out pay are also excluded from income under Sections 112 and 113 of the Internal Revenue Code. However, it appears that no such payments are being made at this time.

The exclusion of benefits and allowances to Armed Forces personnel was first enacted in 1942, and the law remains substantially unchanged since then.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$7,900,000	$8,500,000	$9,100,000	$9,800,000

1.17. VETERANS' BENEFITS ADMINISTERED BY THE VETERANS ADMINISTRATION

38 United States Code 3101
Minnesota Statutes, Section 290.01, Subd. 20

All benefits administered by the Veterans Administration (VA) are excluded from a taxpayer's federal gross income. VA benefits may be divided into three categories:

1. compensation for service-connected disability or death;
2. pensions for non-service-connected disability or death; and
3. vocational rehabilitation, education, and training assistance (including what is commonly referred to as GI Bill benefits).

Compensation for service-related disability or death is based solely on the degree of impairment or injury, without regard to income or wealth. Pensions for non-service-related disabilities are determined according to how much income a veteran has; as income becomes larger, fewer benefits are awarded. Education and training benefits, including readjustment, rehabilitation, and educational assistance programs, are awarded according to the type of training received, time enrolled in the training program, marital status, and number of dependents.

VA benefits have never been taxed, having first been excluded from federal gross income by Congress in 1917.

	Fiscal Year Impact			
	1986	1987	1988	1989
Disability Compensation	$16,600,000	$17,600,000	$18,600,000	$19,800,000
Pensions	7,100,000	7,500,000	8,000,000	8,500,000
Education and Training	2,400,000	2,200,000	1,900,000	1,800,000
Total-State General Fund	$26,100,000	$27,300,000	$28,500,000	$30,100,000

1.18 MILITARY DISABILITY PENSIONS

Internal Revenue Code, Sections 104(a)(4) and 104(b)
Minnesota Statutes, Section 290.01, Subd. 20

Retired military personnel who have at least a 30% disability may receive a pension from the Department of Defense based on either the number of years in service or their percent disability, whichever would produce a larger pension. The amount of pension which would be awarded to the retiree based on percent disability is excluded from federal gross income.

The exclusion is restricted to qualified pensions. For retirees who had entered military service on or before September 24, 1975, qualified pensions include pensions awarded for personal injury and illness resulting from active service in the armed forces of any country. For retirees who had entered service after September 24, 1975, only pensions awarded for combat-related injuries qualify.

Military disability pensions were first excluded from federal gross income in 1942. The last major change to this provision occurred in 1976.

Approximately 1,200 Minnesota taxpayers use this provision.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$500,000	$500,000	$500,000	$500,000

1.19 WORKERS' COMPENSATION BENEFITS

Internal Revenue Code, Section 104(a)(1)
Minnesota Statutes, Section 290.01, Subd. 20

All workers' compensation benefits are excluded from federal gross income. The three basic types of workers' compensation benefits are: 1) payments for medical or rehabilitation expenses; 2) compensation for permanent disabilities; and 3) replacement of lost wages.

Workers' compensation benefits were first excluded from federal taxation in 1918 and from state taxation in 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$46,700,000	$51,600,000	$56,900,000	$62,900,000

1.20 SPECIAL BENEFITS FOR DISABLED COAL MINERS

Internal Revenue Code, Section 104(a)(1)
30 United States Code 801
Revenue Ruling 72-400
Minnesota Statutes, Section 290.01, Subd. 20
Minnesota Rules, Part 8001.9000

Benefits provided by certain federal programs to coal miners totally disabled as a result of pneumoconiosis (black lung disease), to widows of coal miners who died as a result of pneumoconiosis, and to their dependents are excluded from federal gross income.

Disability payments for black lung disease were first specifically excluded from federal gross income by the Black Lung Benefits Act of 1972. Payments received after December 31, 1972, were excluded from income by Revenue Ruling 72-400 because the benefits are classified as workers' compensation.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.21 SOCIAL SECURITY BENEFITS

Internal Revenue Code, Section 86
Minnesota Statutes, Section 290.01, Subd. 20

All social security benefits are excluded from income for a taxpayer with federal adjusted gross income at or below $32,000 for a married-joint return or $25,000 for a single filer. If a taxpayer's income is above the threshold, a portion of the benefits is excluded from income. The portion that is included in income is equal to the lesser of a) one-half of the benefits received or b) one-half of the excess over the income thresholds of the sum of the taxpayer's federal adjusted gross income plus interest on tax exempt obligations plus one-half of the social security benefits.

Prior to 1984, social security benefits had never been taxed by the federal or Minnesota income tax. The federal taxation of a portion of social security benefits was enacted in 1983, effective beginning in 1984. In 1984 Minnesota enacted a subtraction for benefits included in federal adjusted gross income so that no benefits were taxed. In 1985, Minnesota adopted the federal treatment, beginning with tax year 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$255,800,000	$270,100,000	$285,000,000	$299,800,000

1.22 CASH PUBLIC ASSISTANCE

Numerous Revenue Rulings
Minnesota Statutes, Section 290.01, Subd. 20
Minnesota Rules, Part 8001.9000

Public assistance benefits are excluded from federal gross income. The programs through which such benefits are paid include Aid to Families with Dependent Children, General Assistance, Emergency Assistance, Minnesota Supplemental Aid, and Supplemental Security Income.

Although all benefits, whether in cash or in kind, are excluded from income, only cash payments are included in the estimates. The estimates take into account that only a portion of the benefits would be subject to the income tax because the annual income of some recipients would be below the income tax filing requirements.

This exclusion has no direct statutory basis. During the 1930's the Internal Revenue Service issued a series of Revenue Rulings on the definition of federal gross income which explicitly exclude these benefits.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$8,800,000	$8,900,000	$9,400,000	$9,600,000

1.23 CERTAIN AGRICULTURAL COST-SHARING PAYMENTS

Internal Revenue Code, Sections 126 and 1255
Minnesota Statutes, Section 290.01, Subd. 20

Agricultural cost-sharing payments may be excluded from federal gross income if these three conditions are met:

1. The United States Secretary of Agriculture must certify that the payment serves to conserve soil and water resources, improve forests, or provide a habitat for wildlife.

2. A determination is made by the Internal Revenue Service that the improvement does not substantially increase the annual income from the property.

3. The cost-sharing payment must be for a capital expense.

No deductions, depreciation, amortization, or depletion may be claimed with respect to any such amount excluded from federal gross income. The estimates below represent the revenue impact of the exclusion provision over the alternative deduction allowed if improvements were capitalized.

This provision was enacted in 1978 and was last changed in 1980.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$600,000	$600,000	$600,000	$600,000

1.24 INTEREST ON LIFE INSURANCE AND ANNUITY SAVINGS

Internal Revenue Code, Sections 72 and 101(a)
Treasury Regulation 1.451-2
Minnesota Statutes, Section 290.01, Subd. 20
Minnesota Rules, Part 8001.9000

Interest earned on life insurance and annuity savings is not included in the recipient's gross income as the interest accumulates.

For a life insurance policy the exclusion applies to what is commonly referred to as "inside build-up" of investment income. When the premiums paid by the policyholder exceed the cost of insurance, the excess premiums are invested by the company, and interest is credited to the policy. This interest is excluded from the policyholder's income as it accumulates.

If the policy is surrendered before the death of the policyholder, only the excess of the cash surrender value over the premiums paid is included in income. Policy proceeds paid because of the death of the insured are excluded from the gross income of a beneficiary.

An annuity is an investment contract sold by a life insurance company in which the owner makes a deposit in either a lump sum or installment payments in exchange for regular payments for a lifetime or for a specified number of years. The interest is not included in the gross income of the owner as it accumulates but is deferred until payments are made from the contract to the annuitant.

These exclusions have been in effect since the income tax laws were enacted in 1933. The last change occurred in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$40,600,000	$42,900,000	$45,200,000	$47,400,000

1.25 DIVIDENDS

Internal Revenue Code, Section 116
Minnesota Statutes, Section 290.01, Subd. 20

A taxpayer may exclude from federal gross income the first $100 of qualifying dividends received during the tax year. A married couple filing a joint return may exclude up to $200. Qualifying dividends include those from taxable domestic corporations, cooperatives, and insurance companies. Nonqualifying dividends include those from foreign corporations, tax exempt organizations, and amounts paid or credited by mutual savings banks, building and loan associations, and similar institutions to the accounts of depositors as dividends on their deposits.

Separate rules apply to fiduciary taxpayers. An estate or trust may claim only that portion of the $100 exclusion equal to taxable income divided by gross income. Therefore, if only half of an estate's gross income is taxable, a maximum of $50 may be excluded from federal gross income.

This provision was first enacted in 1954. In 1964 the maximum exclusion amount was raised from $50 to $100. The provision remains substantially unchanged since then.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,100,000	$5,000,000	$5,800,000	$5,800,000

1.26 REINVESTMENT OF DIVIDENDS IN PUBLIC UTILITY STOCK (REPEALED)

Internal Revenue Code, Section 305(e)
Minnesota Statutes, Section 290.01, Subd. 20

A taxpayer who owns stock in a qualified domestic utility company and chooses to receive dividends in qualified common stock by means of an approved dividend reinvestment plan may exclude the dividends so received from federal gross income. The maximum exclusion is $750 per year ($1,500 on a joint return). Normally, dividends are included in gross income in the year in which they are received, but under this provision the inclusion in income is deferred until the stock is sold.

This provision was added to the Internal Revenue Code by the Economic Recovery Tax Act of 1981. It expired for distributions after December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,100,000	$0	$0	$0

1.27 INTEREST ON GENERAL PURPOSE STATE AND LOCAL GOVERNMENT DEBT

Internal Revenue Code, Section 103
Minnesota Statutes, Section 290.01, Subd. 20 and Subd. 20a(1)

Generally, all interest income is included in the taxpayer's federal gross income. However, Section 103 of the Internal Revenue Code allows a taxpayer to exclude from federal gross income interest received or accrued from all state and municipal general obligation bonds. This tax expenditure measures the impact of excluding the interest from bonds which are backed by the full faith and credit of the government which issues them. The impact of the interest exclusion for nonguaranteed bonds is estimated separately in Item 1.28.

In determining the Minnesota individual income tax, this exclusion is disallowed if the interest is derived from bonds of non-Minnesota governmental units. Interest from other states which was excluded from federal income is added back to arrive at Minnesota gross income. The result is that the exclusion is restricted to interest from bonds issued by the State of Minnesota or by local units of government in Minnesota.

The federal government first excluded the interest from state and local bonds from gross income in 1913. Minnesota first exempted interest from Minnesota state and local bonds in 1933. When the state began adopting the federal definition of gross income in 1961, the add-back provision was included in the statutes to maintain the intent and effect of the 1933 law.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$22,300,000	$19,500,000	$21,300,000	$21,800,000

1.28 INTEREST ON NONGUARANTEED STATE AND LOCAL GOVERNMENT DEBT

Internal Revenue Code, Section 103
Minnesota Statutes, Section 290.01, Subd. 20 and 20a(1)

Interest received from private activity tax-exempt bonds is excluded from federal gross income. For Minnesota income tax purposes, any interest from non-Minnesota state or local governments is added back to determine Minnesota gross income. Therefore, the net effect is that the exclusion is restricted to interest from private activity bonds issued by the State of Minnesota or by Minnesota local government units.

In contrast to Item 1.27 which shows the impact of the interest exclusion from bonds which are backed by the full faith and credit of the government which issues them, this provision covers the exclusion of interest from nonguaranteed bonds, also referred to as private activity tax-exempt bonds. These bonds are issued for one of three purposes:

1. owner-occupied housing;
2. private exempt entities and student loans; or
3. industrial development bonds.

The federal government first excluded interest from all forms of state and local bonds in 1913. Minnesota first exempted interest from Minnesota state and local bonds in 1933. When the state began adopting the federal definition of gross income in 1961, the add-back provision was included in the statutes to maintain the intent and effect of the 1933 law. A 1968 federal law restricted the tax-free status given interest of industrial revenue bonds to those issued for specific purposes. In 1984 a federal law was enacted which limits by state the total amount of certain types of state and local bonds which may be issued.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$37,000,000	$37,200,000	$38,300,000	$39,200,000

1.29 GENERAL CAPITAL GAINS EXCLUSION (OTHER THAN SPECIAL PROVISIONS COVERED IN ITEMS 1.30 THROUGH 1.35)

Internal Revenue Code, Sections 1201-1254
Minnesota Statutes, Section 290.01, Subd. 20

Sixty percent of a taxpayer's net long-term capital gains may be excluded from federal gross income. The 60% capital gains exclusion applies to the sale or exchange of capital assets, which are investment or personal property, and to certain property used in trade or business. The exclusion does not apply to inventory or to property held for sale in the ordinary course of business.

A net long-term capital gain occurs when sales or exchanges within a tax year result in an excess of long-term capital gains (net of any long-term capital losses) over short-term capital losses (net of any short-term capital gains). With some exceptions, the asset or property must be held a minimum of six months in order to receive the 60% exclusion.

The estimates below do not include the capital gains exclusions covered by the special provisions in Items 1.30 through 1.35.

Capital gains income was first given preferential treatment federally in 1921. In 1945 Minnesota first allowed an exclusion of 50% of net capital gains received from assets held more than six months. For tax year 1977, the minimum holding period was increased to nine months, and beginning in tax year 1978 it was raised to twelve months. For tax years beginning after October 31, 1978, the 50% deduction was expanded federally to the current 60% level. Minnesota raised the deduction to 60% in 1982 for long-term gains from all assets sold after December 31, 1982. In 1985 the minimum holding period was changed to six months for property acquired after June 22, 1984, and before January 1, 1988.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$208,400,000	$231,400,000	$265,200,000	$299,700,000

1.30 CAPITAL GAINS TREATMENT OF CERTAIN AGRICULTURAL INCOME

Internal Revenue Code, Sections 1201, 1202, 1221-1223, 1231, 1245, 1251, and 1252
Minnesota Statutes, Section 290.01, Subd. 20

Certain farm assets which normally would be defined as inventory are treated as long-term capital assets, and the proceeds from the disposition of these assets are granted the 60% capital gains exclusion if the assets have been held a specified minimum amount of time. This special capital gains treatment is granted to livestock used for breeding, draft, dairy, or sporting purposes and to land with unharvested crops. Generally, the minimum holding period for long-term gains is six months, but for horses and cows it is two years, and for other livestock it is one year.

This capital gains treatment for certain agricultural income was first enacted by Congress in 1951. The last changes affecting this tax expenditure were made in 1983. The minimum holding period applicable to most types of property was changed from twelve to six months in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$10,500,000	$11,900,000	$13,400,000	$14,900,000

1.31 CAPITAL GAINS TREATMENT OF CERTAIN TIMBER INCOME

Internal Revenue Code, Sections 631(a), 631(b), 1221, and 1231
Minnesota Statutes, Section 290.01, Subd. 20

The 60% capital gains exclusion applies to timber income from three sources:

1. Non-business occasional sales. Similar to other non-business sales, income from timber sales occurring outside the course of normal business is treated as a long-term capital gain.

2. Lease arrangements. Similar to the treatment of royalty payments for mineral rights, when a taxpayer leases the rights to cut timber on a tract of land, payments received (less any depletion allowance claimed) are considered long-term capital gains.

3. Timber used in trade or business. Timber which has appreciated in value may be treated as having been sold at the time it is cut down, even though the felling of the timber occurs in the normal course of business, and even though no sale or transaction takes place.

The 60% exclusion of income from non-business occasional sales is included in the estimate of Item 1.29, General Capital Gains Exclusion. This estimate covers the other two provisions.

The provisions allowing capital gains deductions for lease arrangements and timber used in trade or business were enacted by Congress in 1951. The last substantive change to these laws took place in 1983. In 1985 the minimum holding period for property to qualify for long-term capital gains treatment was changed from twelve months to six months.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	\$600,000	\$600,000	\$1,000,000	\$1,400,000

1.32 CAPITAL GAINS TREATMENT OF IRON ORE ROYALTIES

Internal Revenue Code, Sections 631(c) and 1231(b)
Minnesota Statutes, Section 290.01, Subd. 20

If an iron ore mineral interest is disposed of through a long-term lease arrangement, with royalty payments made to the owner based on the amount of ore mined per year, the 60% capital gains exclusion applies to the royalty income. Therefore, the transaction is treated as if it were an outright sale, even though the royalties are similar to rent.

Capital gains treatment for these lease arrangements was first allowed by federal law in 1964. The provision was last revised in 1976. In 1985 the minimum holding period for property to qualify for long-term capital gains treatment was changed from twelve months to six months.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	\$1,500,000	\$1,700,000	\$1,800,000	\$1,900,000

1.33 CAPITAL GAINS TREATMENT OF COAL ROYALTIES

Internal Revenue Code, Sections 631(c) and 1231(b)
Minnesota Statutes, Section 290.01, Subd. 20

Under certain circumstances an owner of coal mining rights may claim the 60% capital gains exclusion for income received from the disposal of those rights. This special treatment is allowed when the owner enters into a long-term lease agreement in which royalty payments are paid based on the amount of coal mined during the year. The capital gains eligible for the exclusion are equal to the royalty payments received less any depletion allowance claimed for the tax year. Without this provision royalty payments would be treated as rent payments and would be fully included in federal gross income.

This provision was first enacted into federal law in 1951. In 1985 the minimum holding period for property to qualify for long-term capital gains treatment was changed from twelve months to six months.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.34 SPECIAL TREATMENT OF CAPITAL GAINS ON HOME SALES

Internal Revenue Code, Sections 121 and 1034
Minnesota Statutes, Section 290.01, Subd. 20

The capital gains received from the sale of a taxpayer's principal residence may be excluded from federal gross income if a replacement residence of equal or greater value is purchased within two years of the sale.

This tax expenditure contains two distinct components: a deferral and an exclusion. A deferral occurs because eventually the capital gain will be subject to income taxation if the residence is sold and not replaced with a higher-priced home. Further, this deferral may be converted into a permanent exclusion in two different ways. One way occurs when the owner of the home dies. Estimates for the exclusion of capital gains at death are provided in Item 1.35. The second way in which a deferral may be converted into an exclusion is the once-in-a-lifetime exclusion of up to $125,000 of capital gains allowed on the sale of a principal residence by a taxpayer age 55 or over. Capital gains which were actually realized from previous home sales but deferred for tax purposes may thus be totally excluded from taxable income. Because the deferral and this exclusion are related, they are presented here together with separate estimates shown for each portion.

The fiscal impact estimates for both the deferral and the exclusion portion of this item measure the difference between current treatment and what would be the case if 100% of the gain from home sales were included in taxable income. The fiscal impact of the 60% capital gains exclusion from home sales not eligible for special treatment is included in Item 1.29, General Capital Gains Exclusion.

Congress enacted the deferral provision (Section 1034) in 1951. The exclusion provision (Section 121) was enacted by Congress in 1964. Both provisions were last revised in 1981. In 1985 the minimum holding period for property to qualify for long-term capital gains treatment was changed from twelve months to six months.

	Fiscal Year Impact			
	1986	1987	1988	1989
Deferral	$40,700,000	$44,200,000	$47,700,000	$51,800,000
Exclusion-Age 55+	13,800,000	14,500,000	15,900,000	17,300,000
Total - State General Fund	$54,500,000	$58,700,000	$63,600,000	$69,100,000

1.35 CAPITAL GAINS AT DEATH

Internal Revenue Code, Sections 1001, 1002, 1015, 1023, 1040, 1221, and 1222
Minnesota Statutes, Section 290.01, Subd. 20

When property is transferred at death, any accumulated gain is not subject to income tax. The decedent's capital gains are forgiven, with the recipient's basis being the value of the asset at the time of the decedent's death. The estimates of this tax expenditure measure the difference between the current special treatment and what would be the case if 100% of the decedent's accumulated gains were included in income at the time of death.

Congress first excluded capital gains at death from income taxation in 1921. A similar provision was also incorporated into the original Minnesota income tax law in 1933. In 1985 the minimum holding period for property to qualify for long-term capital gains treatment was changed from twelve months to six months.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$33,600,000	$37,000,000	$42,000,000	$46,200,000

1.36 INCOME FROM THE DISCHARGE OF DEBT

Internal Revenue Code, Sections 108 and 1017
Minnesota Statutes, Section 290.01, Subd. 20

In general, income from the cancellation of a debt is taxable. However, income which results from a taxpayer being allowed to pay off a debt for less than the originally agreed upon and legally required amount may be excluded from gross income under certain circumstances. The exclusion is the amount of income gained by the cancellation of the debt.

This provision was adopted in 1943 and last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.37 PERMANENT EXEMPTIONS FROM IMPUTED INTEREST RULES

Internal Revenue Code, Section 7872
Minnesota Statutes, Section 290.01, Subd. 20

Section 7872 of the Internal Revenue Code contains imputed interest rules designed to prevent the assignment of income through the use of below-market or interest-free loans. When the rules apply, a lender is deemed to have received interest payments, and a borrower is deemed to have paid interest payments. Exemptions from the imputed interest rules include loans of less than $10,000, and there is a special method for computing income from a gift loan of less than $100,000.

Imputed interest rules and exemption from the rules were first effective in 1984, and they were last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,400,000	$1,400,000	$1,400,000	$1,400,000

1.38 PRIZES AND AWARDS

Internal Revenue Code, Sections 74(b), 102, and 274(b)
Minnesota Statutes, Section 290.01, Subd. 20

Two types of prizes and awards are excluded by the Internal Revenue Code.

First, Internal Revenue Code Section 74(b) exempts from federal gross income prizes and awards received primarily in recognition of religious, charitable, scientific, educational, artistic, literary, or civic achievement. The recipient is prohibited from having to render substantial future services as a condition of the award.

Second, Internal Revenue Code Section 102 in combination with Section 274(b) allows certain employee awards to be classified as gifts. Limits on the size of the business deduction taken by the business giving the award determine the size of the award. The award must be tangible, personal property and given to an employee for one of the following reasons: length of service, productivity, or safety achievement. In general, the value of the award must not exceed $400 in value.

The exemption of prizes and awards by Section 74(b) was first allowed in 1954. The employee awards provision was first enacted in 1962 and last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.39 SCHOLARSHIP AND FELLOWSHIP INCOME

Internal Revenue Code, Section 117
Minnesota Statutes, Section 290.01, Subd. 20

Section 117 of the Internal Revenue Code exempts from federal gross income scholarships given to degree candidates to cover tuition, fees, and living expenses. A nondegree student may exclude up to $300 per month of scholarship or fellowship grants.

This exclusion was first allowed in 1954. The provision was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$10,700,000	$12,400,000	$13,200,000	$14,400,000

FEDERAL DEDUCTIONS

1.40 DEPRECIATION

Internal Revenue Code, Section 168
Minnesota Statutes, Section 290.01, Subd. 20 and Subd. 20f

Minnesota taxpayers are allowed a deduction for depreciation of property (other than land) used in a trade or business or held for the production of income. Depreciation is an attempt to measure an asset's decline in value due to use, wear, or decay within the tax year. Conceptually, the tax expenditure is the extent to which depreciation for tax purposes exceeds the actual decline in value of the asset during the applicable tax year. The estimates below measure the extent to which current depreciation allowances exceed actual declines in value as measured by 35 year straight line depreciation for real property and the midpoint in the class life asset depreciation ranges (CLADR) for personal property.

The depreciation deduction was a part of the original Minnesota income tax in 1933. Accelerated depreciation was first allowed through administrative practice by the federal government in 1946 and by law in 1954. Minnesota first enacted an accelerated depreciation provision in 1959. The last change to the Minnesota provision occurred in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$81,800,000	$77,400,000	$73,700,000	$73,500,000

1.41 EXPENSING DEPRECIABLE BUSINESS PROPERTY

Internal Revenue Code, Section 179
Minnesota Statutes, Section 290.01, Subd. 20

A taxpayer may elect to treat the cost of qualifying property as an expense and to deduct the cost in the year the property is placed in service. The deduction is taken instead of the depreciation deduction, and the maximum annual deduction is $5,000 for tax years 1983 through 1987, $7,500 for tax years 1988 and 1989, and $10,000 for tax year 1990 and thereafter.

Qualifying property is recovery property that would qualify for the federal investment credit and which is acquired by purchase for use in a trade or business. However, if the taxpayer elects to expense the property, the federal investment credit cannot be claimed.

The estimates measure the difference between expensing the property and a depreciation deduction which would reflect the actual useful life of the property.

This provision was adopted in 1982 and last amended in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$500,000	$500,000	$500,000	$200,000

1.42 EXCESS OF PERCENTAGE OVER COST DEPLETION

Internal Revenue Code, Sections 613 and 613A
Minnesota Statutes, Section 290.01, Subd. 20

Depletion allowances refer to the way in which investment costs are recovered for mining or other extractive operations. Depletion deductions are allowed on such diverse properties as oil and gas wells, mineral mines, peat bogs, clay mines, gravel quarries, and commercial stands of timber. In fact, depletion allowances may be taken for almost all exhaustible natural resources.

A taxpayer may choose from two forms of depletion: cost depletion and percentage depletion. Cost depletion is based on the taxpayer's basis in the property and is almost identical to depreciation in its application. Percentage depletion, on the other hand, is based on a percentage of the gross income received from the extractive operation and has little relationship to a taxpayer's basis. Because cost depletion is a normal and necessary cost of doing business, only the amount of percentage depletion in excess of cost depletion is considered a tax expenditure.

A deduction for cost depletion was first allowed in 1913 for the federal income tax, and percentage depletion was first allowed as an option in 1926. This provision was last changed in 1978.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,200,000	$1,200,000	$1,200,000	$1,200,000

1.43 FIVE-YEAR AMORTIZATION OF BUSINESS ORGANIZATIONAL AND START-UP COSTS

Internal Revenue Code, Sections 195 and 709
Minnesota Statutes, Section 290.01, Subd. 20

Under Section 195 of the Internal Revenue Code, taxpayers who pay or incur business investigatory start-up expenditures and subsequently enter the trade or business to which these costs relate may elect to amortize these expenses over a period of not less than sixty months, beginning with the month in which the business commences. In addition, Section 709 allows partnerships to similarly amortize organization fees.

Without these special provisions, these expenditures would be capitalized by adding them to the taxpayer's basis in the business. They would then be treated as nondepreciable intangible assets, with costs not being recoverable until the business is sold.

Section 709 was enacted in 1976, and Section 195 was enacted in 1980. The last change to these provisions took effect in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,400,000	$1,400,000	$1,400,000	$1,400,000

1.44 FIVE-YEAR AMORTIZATION FOR HOUSING REHABILITATION (REPEALED)

Internal Revenue Code, Section 167(k)
Minnesota Statutes, Section 290.01, Subd. 20

Capital expenditures for the rehabilitation of low-income rental housing may be amortized over five years rather than depreciated over a longer time. Qualifying expenditures must exceed a total of $3,000 per rental unit over two consecutive years, with a maximum of $20,000 per unit allowed ($40,000 per unit for certain projects).

This provision was enacted in 1969. Although it was previously set to expire after December 31, 1983, in 1985 it was extended to expenditures incurred before January 1, 1987.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$400,000	$400,000	$400,000	$300,000

1.45 FIVE-YEAR AMORTIZATION OF TRADEMARK EXPENSES

Internal Revenue Code, Section 177
Minnesota Statutes, Section 290.01, Subd.20

A taxpayer may elect to amortize over a period of sixty months capital expenditures for the acquisition, protection, expansion, registration, or defense of a trademark or trade name. This election relates to an expenditure properly chargeable to capital account and does not apply to the consideration paid for the purchase of an existing trademark or trade name.

This provision was enacted in 1956.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.46 SEVEN-YEAR AMORTIZATION FOR REFORESTATION EXPENDITURES

Internal Revenue Code, Sections 48 and 194
Minnesota Statutes, Section 290.01, Subd. 20

Beginning with tax year 1980, a taxpayer may elect to amortize over a seven-year period reforestation expenditures incurred in connection with the commercial production of timber. Prior to 1980, taxpayers were required to treat reforestation costs as capital expenditures which were not recoverable until the timber was harvested. The amortization deduction is limited to a maximum of $10,000 per year over the seven-year period. Qualifying expenditures include the cost of site preparation, seeds or seedlings, labor, and tools, including depreciation for equipment.

This provision was enacted in 1980, and it was last changed in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.47 EXPENSING OF RESEARCH AND DEVELOPMENT COSTS

Internal Revenue Code, Section 174
Minnesota Statutes, Section 290.01, Subd. 20

Generally, expenses incurred in creating or developing an asset must be capitalized, with recovery occurring over the life of the asset. However, a taxpayer may elect to expense in the current tax year all qualified research and development costs incurred in connection with a trade or business. If the asset resulting from the research or development expenditures has no determinable useful life (such as is the case with a process or formula), then the taxpayer may alternatively elect to amortize the costs over not less than sixty months.

No substantial changes have been made to this provision since it was adopted in 1955.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,300,000	$1,300,000	$1,300,000	$1,300,000

1.48 EXPENSING OF MAGAZINE CIRCULATION EXPENDITURES

Internal Revenue Code, Section 173
Minnesota Statutes, Section 290.01, Subd. 20

Generally, expenses incurred in creating or developing an asset must be capitalized, with recovery occurring over the life of the asset. However, a taxpayer may elect to deduct as an expense in the current year expenditures to establish, maintain, or increase the circulation of a newspaper, magazine, or other periodical. This treatment is restricted to certain types of deductions, and the election is binding for the current year and to similar expenditures in subsequent years.

Section 173 of the Internal Revenue Code was enacted in 1950 and was adopted by Minnesota in 1951. It was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

1.49 EXPENSING OF CONSTRUCTION PERIOD INTEREST AND TAXES FOR LOW INCOME HOUSING

Internal Revenue Code, Section 189
Minnesota Statutes, Section 290.01, Subd. 20

For property that qualifies as low income housing, property taxes and interest paid or accrued during the construction period may be deducted as an expense in the year incurred. Without this provision, these costs would be amortized over ten years.

This provision took effect in tax year 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$700,000	$700,000	$700,000	$700,000

1.50 EXPENSING FOR REMOVAL OF BARRIERS TO THE HANDICAPPED AND ELDERLY (REPEALED)

Internal Revenue Code, Section 190
Minnesota Statutes, Section 290.01, Subd. 20

A taxpayer may elect to expense qualifying barrier removal expenses in the year incurred instead of capitalizing them. To qualify, the removal of barriers must make a facility or public transportation vehicle, owned or leased by the taxpayer for use in his trade or business, more accessible to and usable by handicapped and elderly persons and must meet standards of the Architectural and Transportation Barriers Compliance Board. The maximum deduction per year is $35,000. The provision is repealed after December 31, 1985.

This provision was first effective for tax year 1977. In 1985, Minnesota adopted the federal extension of the sunset date to December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$0	$0	$0

1.51 EXPENSING OF EXPLORATION AND DEVELOPMENT COSTS

Internal Revenue Code, Sections 263(c), 465, 616, 617, 704(d), and 1254
Minnesota Statutes, Section 290.01, Subd. 20

Current year expensing is allowed for items such as labor costs, ground clearing, construction, and other site preparation costs in the exploration and development of oil, gas, other fuel, and non-fuel mineral deposits. Generally, amounts paid for permanent improvements or betterments to income-producing property are not deductible as current year expenses but are treated as capital expenses, which increase the taxpayer's basis in the property.

Current year expensing of development costs for oil and gas has been allowed federally since 1916. Expensing of development costs for other minerals and of exploration costs for all minerals, including oil and gas, was first allowed in 1951.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,100,000	$2,100,000	$2,100,000	$2,300,000

1.52 EXPENSING OF CERTAIN CAPITAL OUTLAYS AND SPECIAL CASH ACCOUNTING RULES FOR FARMERS

Internal Revenue Code, Sections 162, 175, 180, 182, 278, 447, 464, 465, and 704(d)
Internal Revenue Service, Regulations 1.61-4, 1.162-12, and 1.471-6
Minnesota Statutes, Section 290.01, Subd. 20
Minnesota Rules, Part 8001.9000

A taxpayer engaged in the business of farming may treat certain expenditures made during the tax year as expenses rather than as capital expenditures. Therefore, the expenditures are entirely deductible in the current year rather than throughout an asset's useful life. To qualify for this special treatment the expenditures must be for soil and water conservation, fertilizer purchases, land clearing, and land improvement projects.

Farmers are allowed to use cash accounting rather than the accrual system for income tax purposes. Therefore, costs attributable to goods not yet sold may be deducted in the current year. The accrual system is normally required under tax law when the sale of products is a material factor of the business.

Farmers have been allowed to use the cash accounting system for tax purposes since 1933. Minnesota began allowing the expensing of capital outlays in 1955.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,600,000	$1,600,000	$1,600,000	$1,600,000

1.53 CASH ACCOUNTING OTHER THAN AGRICULTURE

Internal Revenue Code, Section 446
Minnesota Statutes, Section 290.01, Subd. 20

Section 446 of the Internal Revenue Code allows a taxpayer to choose the cash method of accounting instead of the accrual method. The accrual method is considered a better measure of current-year income and expenses because it takes into account the income of receivables. This tax expenditure is the difference in net income measured by accrual accounting and cash accounting. Presently, accrual accounting is required in a limited form only for businesses that sell inventory directly.

Cash accounting has been permitted since 1933. The provision has remained unchanged since then.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$200,000	$200,000

1.54 COMPLETED CONTRACT RULES

P.L. 97-248, Section 248
Treasury Regulation 1.451-3
Minnesota Rules, Part 8007.0600, Subpart 2 B

Regulations issued by the U.S. Department of Treasury and Minnesota rules permit a method of accounting known as the completed contract method. One of two methods of accounting may be used to measure income from long-term contracts. The completed contract method measures income when income is received and when expenses are paid. In contrast, the percentage of completion method measures income when it is earned and expenses when they are incurred. The estimate is based on the difference between measuring income using the percentage of completion method and the completed contract method.

This tax expenditure also covers the lack of uniform capitalization rules for indirect costs. Under uniform capitalization rules a part of indirect costs, such as general and administrative expenses, must be capitalized and deducted in future years instead of being deducted as an expense in the current year. The lack of uniform capitalization rules applies not only to long-term contracts; it covers all types of business transactions.

The completed contract method of accounting dates back to 1918 and was permitted by Minnesota Regulations in 1934. The last change was in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,400,000	$2,400,000	$2,400,000	$2,400,000

1.55 INSTALLMENT SALES

Internal Revenue Code, Sections 453 and 453A
Minnesota Statutes, Section 290.01, Subd. 20

Section 453 of the Internal Revenue Code allows a method of accounting known as installment reporting. Instead of reporting the gain in the year the sale occurred, gains are reported when the cash from the sale is received. The estimate is based on the difference between measuring income without installment reporting and using installment reporting.

The installment method was first enacted in 1933 and was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.56 BAD DEBT RESERVES OTHER THAN FINANCIAL INSTITUTIONS

Internal Revenue Code, Section 166
Minnesota Statutes, Section 290.01, Subd. 20

Generally, a bad debt deduction is a necessary cost of doing business which arises when a taxpayer uses the accural method of accounting. Under the accrual method, a business includes as income all amounts that it has earned the right to receive. A bad debt deduction reduces accrued income that the taxpayer did not receive.

A taxpayer may choose the specific charge-off method or reserve method to compute its bad debt deduction. Under the specific charge-off method, a deduction is taken by the taxpayer when the debt becomes worthless. Under the reserve method the deduction is based on the interrelationship between a calculation of ending balance of the reserve and the amount of debts that become worthless. Given a growing balance of accounts receivable or a worsening loss experience, the bad debt reserve calculation allows a deduction for future losses. This tax expenditure is defined as the extent to which tax liability has been reduced beyond what it would have been using the specific charge-off method.

The reserve method has been permitted since 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$300,000	$300,000	$300,000

1.57 INDIVIDUAL RETIREMENT ACCOUNTS

Internal Revenue Code, Sections 219 and 408
Minnesota Statutes, Section 290.01, Subd. 20

An individual may take a deduction for contributions to an individual retirement account (IRA) up to a maximum of $2,000 or an amount equal to total wage income, whichever is less. Earnings on IRA funds are excluded from income until the funds are disbursed.

The net effect of this provision is the deferral of income because disbursements from an IRA are included in the recipient's gross income. The estimates show the fiscal impact of excluding current-year contributions and earnings, net of disbursements included in income that year.

A self-employed individual is eligible to open an IRA or a Keogh plan, which is available only to self-employed persons. Keogh plans are estimated separately in Item 1.58. Separate estimates are also made for employer plans and the Minnesota pension subtraction (Items 1.06 and 1.61).

This provision was enacted in 1974. From 1982 to 1984 the Minnesota deduction was more restrictive than the federal deduction. In 1985 Minnesota adopted the federally-allowed deduction.

In 1984 this deduction was claimed on 280,000 federal returns filed by Minnesota taxpayers.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$113,200,000	$125,800,000	$140,000,000	$154,000,000

1.58 KEOGH PLANS

Internal Revenue Code, Sections 219, 220, 401-405, and 408-415
Minnesota Statutes, Section 290.01, Subd. 20

A self-employed person may take a deduction for contributions made to a Keogh retirement plan of the lesser of 25% of self-employment income or $30,000.

The net effect of this provision is the deferral of income because disbursements from a Keogh plan are included in the recipient's gross income. The estimates show the fiscal impact of excluding current-year contributions and earnings, net of disbursements included in income that year.

This provision was originally enacted in 1962. From 1982 to 1984 the Minnesota deduction was more restrictive than the federal deduction. In 1985 Minnesota adopted the federally-allowed deduction.

In 1984 this deduction was claimed on 14,000 federal returns filed by Minnesota taxpayers.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$17,300,000	$19,100,000	$21,000,000	$22,700,000

1.59 FOREIGN HOUSING COSTS PAID BY TAXPAYER

Internal Revenue Code, Section 911(c)(3)
Minnesota Statutes, Section 290.01, Subd. 20

A deduction is allowed for foreign housing costs paid by the taxpayer, subject to certain limitations. If foreign housing costs exceed 16% of the federal employee salary at step 1 of grade GS-14 ($7,108 in 1985), a deduction is allowed equal to the excess housing costs up to a maximum amount. The maximum is the taxpayer's foreign earned income less any foreign earned income exclusion and/or employer-paid housing exclusion. These exclusions are explained in Item 1.15.

The deduction for foreign housing costs was enacted in 1979. This provision as it currently exists became effective with tax year 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.60 DEDUCTION FOR TWO-EARNER MARRIED COUPLES

Internal Revenue Code, Section 221
Minnesota Statutes, Section 290.01, Subd. 20

A deduction may be taken by a married couple if both spouses work and have qualified earned income and if they file a joint return. The deduction is equal to 10% of the lesser of a) the qualified earned income of the spouse with the lower earned income, or b) $30,000.

Earned income includes wages, salaries, commissions, other compensation, and net profit or loss from a proprietorship, partnership, or farm. The amount is reduced by any deductions taken for employee business expenses, contributions to an individual retirement account or Keogh plan, and repayment of supplemental unemployment benefits.

This provision was effective for the federal income tax beginning with tax year 1982 and was adopted for Minnesota income tax purposes beginning with tax year 1985.

This deduction is claimed on an estimated 450,000 married-joint returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$47,600,000	$48,900,000	$50,200,000	$51,700,000

MINNESOTA SUBTRACTIONS

1.61 PENSION AND RETIREMENT INCOME (OTHER THAN SOCIAL SECURITY)

Minnesota Statutes, Sections 290.01, Subd. 20b (6) and 290.08, Subd. 26

A Minnesota taxpayer may subtract from federal adjusted gross income pension and retirement income up to a maximum of $11,000 per year. This maximum is reduced dollar-for-dollar by any federal adjusted gross income in excess of $17,000. A married couple may take only one $11,000 subtraction, and the offset is based on their combined federal adjusted gross income. In general, the subtraction is available only to persons age 65 and over.

There are specified exceptions to the general rules. The age requirement does not apply to recipients of certain types of pensions, including public police and fire employees, state patrol, and state correctional employees. Persons age 65 and over who receive railroad retirement benefits may subtract the entire amount of such benefits. Involuntary lump sum retirement benefits paid to volunteer firemen are not subject to the age restriction, and the maximum $11,000 subtraction is not offset for federal adjusted gross income over $17,000.

This provision and the estimates below include distributions from public and private pension plans and annuities, railroad retirement benefits, individual retirement accounts, and Keogh plans. The exclusion of social security benefits is estimated separately in Item 1.21. The impact of ten-year averaging of lump sum distributions is found in Item 1.80. The exclusion of contributions and earnings to employer plans, individual retirement accounts, and Keogh plans are found in Items 1.06, 1.57, and 1.58 respectively.

Minnesota began excluding all government pension income in 1933. In 1978 the total subtraction of public employee pensions was changed to be a subtraction of any pensions, public or private, but it was limited to a maximum amount with qualifying offsets or reductions. Several changes were made to the provision when the current law was adopted in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$75,200,000	$86,400,000	$99,500,000	$116,200,000

1.62 UNEMPLOYMENT COMPENSATION

Internal Revenue Code, Section 85
Minnesota Statutes, Sections 290.01, Subd. 20 and 20b (8)

Minnesota does not tax any unemployment compensation benefits and thus allows any federally taxed benefits to be subtracted from federal adjusted gross income.

The fiscal impact totals shown below measure the total tax relief provided because Minnesota does not tax any of this income. The federal portion of the estimate measures what is not taxed by the federal government, and the Minnesota portion measures the additional tax relief provided because Minnesota does not tax the portion that is taxed by the federal government.

The federal government began excluding unemployment compensation benefits in 1938. In 1979 it began taxing a portion of unemployment compensation. Beginning with the 1983 tax year, the unemployment compensation included in federal adjusted gross income is equal to one-half of the amount of unemployment compensation combined with other income over $12,000 for a single filer and $18,000 for married-joint filers, up to the taxpayer's full amount of unemployment compensation. The Minnesota subtraction for unemployment compensation has been equal to the amount included in federal adjusted gross income for each year since 1979.

	Fiscal Year Impact			
	1986	1987	1988	1989
Federal Portion	$18,700,000	$15,100,000	$11,700,000	$10,500,000
Minnesota Portion	17,800,000	21,100,000	23,400,000	25,400,000
Total - State General Fund	$36,500,000	$36,200,000	$35,100,000	$35,900,000

1.63 MILITARY PAY

Minnesota Statutes, Section 290.01, Subd. 20b(7)

A Minnesota resident who is serving in the Armed Forces of the United States or of the United Nations may subtract from federal adjusted gross income the first $3,000 of military compensation received. The taxpayer may subtract an additional $2,000 of military compensation if the military service is performed wholly outside Minnesota.

This provision was first enacted in 1943 for tax year 1942. Although it was replaced by an income tax credit for the National Guard for tax year 1978, the provision was reinstated in 1979 and remains unchanged.

This subtraction is taken on approximately 34,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$12,800,000	$13,900,000	$15,000,000	$16,200,000

1.64 PER DIEM AMOUNTS PAID TO STATE LEGISLATORS

Internal Revenue Code, Section 162(h)
Minnesota Statutes, Sections 290.01, Subd. 20 and 290.09, Subd. 2(c)

Minnesota does not tax any per diem allowances received by Minnesota legislators and thus allows any federally taxed benefits to be subtracted from federal adjusted gross income.

The federal provision allows the exclusion only for legislators who reside more than fifty miles from the state capitol building and only for per diem allowances received for days that the Legislature is in session and for committee meetings that the legislator is required to attend. The additional amounts subtracted for the Minnesota income tax therefore include all per diem amounts for legislators who reside within fifty miles of the capitol building and interim per diem paid for days on official business for legislators who reside more than fifty miles from the capitol. For fiscal year 1986 the session per diem was $36 and the interim per diem was $48.

Minnesota first enacted this provision in 1959. The federal deduction became effective in 1976 and the fifty-mile restriction became effective in 1980. The provision was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	Minimal	$100,000	Minimal

1.65 DISPOSITION OF FARM PROPERTY

Minnesota Statutes Sections 290.01, Subd. 20b; 290.08, Subd. 27; 290.091, Subd. 2; and 290.491

A taxpayer may subtract from federal adjusted gross income the gain realized from the disposition of real or personal property used in a farm business if foreclosure is initiated or threatened in writing. The farm business must be owned and operated by the taxpayer as his principal business. The gain which may be subtracted is that which is realized upon termination of a contract for deed, foreclosure of a mortgage, or deed in lieu of foreclosure.

Also exempt is income realized on a sale or exchange of farm property if the taxpayer is insolvent at the time of the sale, and the proceeds are used solely to discharge indebtedness of the property sold.

The provision relating to insolvent farmers was enacted in 1985 and amended in 1986. The provision relating to farm foreclosure property was enacted in 1986. Both provisions were made retroactive to tax year 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	$2,400,000	$1,000,000	$1,000,000

PERSONAL DEDUCTIONS

1.66 STANDARD DEDUCTION

Minnesota Statutes, Section 290.089, Subd. 3

A taxpayer may either itemize his personal deductions or take the standard deduction, whichever is greater. The standard deduction is equal to 10% of Minnesota gross income, up to a specified maximum deduction. For tax year 1986, the maximum is $2,500 for married-joint returns and single persons and $1,200 for each married-separate return. The maximum standard deduction is increased annually based on the annual increase in the Consumer Price Index for the United States.

The itemized personal deductions are estimated separately in Items 1.67 through 1.78. The estimates for the standard deduction measure the cost of the deduction in total. No assumptions are made regarding the level of itemized deductions that would be claimed by the taxpayer if the standard deduction were not available.

The standard deduction was enacted in 1949 as 10% of Minnesota adjusted gross income up to a maximum deduction of $500. The maximum was increased to $1,000 in 1953 and to $2,000 in 1979. Indexing the maximum amount began in tax year 1981.

Several changes to the standard deduction were enacted in 1985 including the method of indexing, the different maximums for married-joint and married-separate returns, and the calculation and subtraction of the standard deduction before, instead of after, any federal income taxes are deducted.

The standard deduction is claimed on about 40% of the returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$96,600,000	$101,600,000	$107,700,000	$115,200,000

1.67 MEDICAL AND DENTAL EXPENSES

Internal Revenue Code, Sections 63(f) and 213
Minnesota Statutes, Section 290.089, Subd. 2

A deduction is allowed for expenses incurred for medical treatment, health care, health insurance, and transportation essential for medical care. The deduction is equal to the amount by which the sum of all qualified medical expenses exceeds 5% of federal adjusted gross income.

A deduction for medical expenses has been allowed by Minnesota since 1933. The state adopted the federal provisions for this deduction beginning with tax year 1982. The last change took effect in tax year 1984.

This deduction is claimed on an estimated 300,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$28,500,000	$29,100,000	$29,800,000	$30,600,000

1.68 REAL ESTATE TAXES

Internal Revenue Code, Sections 63(f) and 164
Minnesota Statutes, Section 290.089, Subd. 2

Real estate taxes paid during the taxable year, less any Minnesota property tax refund received, may be deducted in arriving at Minnesota taxable income. Special assessments are not considered real estate taxes and cannot be deducted. Business or trade-related real estate taxes are not included in the estimates because they are not itemized personal deductions. Furthermore, they are not considered tax expenditures because they are costs necessary for earning income.

Minnesota has allowed this itemized deduction since 1933. Upon enactment of the property tax refund, this deduction was reduced by the amount of that refund to determine the net property tax paid, beginning in 1976.

This deduction is claimed on approximately 750,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$60,100,000	$63,900,000	$69,100,000	$74,700,000

1.69 GENERAL SALES TAX

Internal Revenue Code, Sections 63(f) and 164
Minnesota Statutes, Section 290.089, Subd. 2

All sales taxes paid within the taxable year may be deducted from Minnesota gross income in arriving at Minnesota taxable income. The amount deductible is determined from either the taxpayer's records of the actual sales tax paid during the year or from the Optional State Sales Tax Tables in the federal income tax instruction booklet, which are based on income and family size. The estimates do not include the excise tax on motor vehicles, which is estimated separately in Item 1.70.

This provision allowing for sales taxes to be deducted was enacted in 1933 and last changed in 1983. The general Minnesota sales tax was enacted in 1967.

This deduction is claimed on about 830,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$30,000,000	$30,600,000	$31,400,000	$32,200,000

1.70 MOTOR VEHICLE EXCISE TAX

Internal Revenue Code, Sections 63(f) and 164
Minnesota Statutes, Section 290.089, Subd. 2

Minnesota taxpayers are allowed an itemized deduction equal to the amount of excise tax paid on the purchase of motor vehicles. The Minnesota motor vehicle tax rate is currently 6% of the purchase price and is applied to the sale or transfer of any motor vehicle required to be registered in Minnesota.

A deduction for several taxes, including those paid on motor vehicles, has been allowed in Minnesota since 1933. The Minnesota sales tax, enacted in 1967, included motor vehicles in the tax base until 1972, at which time the state motor vehicle excise tax was separately established.

This deduction was claimed on 250,000 returns in tax year 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$9,500,000	$10,700,000	$11,400,000	$11,600,000

1.71 MOTOR VEHICLE REGISTRATION TAX

Internal Revenue Code, Sections 63(f) and 164
Minnesota Statutes, Section 290.089, Subd. 2

Under federal provisions adopted by state law, an itemized deduction is allowed for the ad valorem portion of motor vehicle registration taxes paid during the tax year. The Minnesota motor vehicle registration tax is explained in Chapter 19.

This deduction was enacted in 1933. It was last changed in 1983.

In 1982, this deduction was claimed on 745,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,500,000	$5,800,000	$5,900,000	$6,200,000

1.72 INTEREST ON HOME MORTGAGES

Internal Revenue Code, Sections 63(f) and 163
Minnesota Statutes, Section 290.089, Subd. 2

A taxpayer may take an itemized deduction for all mortgage interest paid on his owner-occupied home, including traditional mortgages and contracts for deed. The deduction of nonmortgage interest is estimated separately in Item 1.73.

The deduction of home mortgage interest has been allowed since 1933.

This deduction was claimed on 600,000 returns in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$184,400,000	$200,200,000	$219,900,000	$246,500,000

1.73 NONMORTGAGE INTEREST

Internal Revenue Code, Sections 63(f) and 163
Minnesota Statutes, Section 290.089, Subd. 2

An itemized deduction is allowed for interest paid on nonbusiness indebtedness in addition to home mortgages (Item 1.72). This deduction includes interest paid on automobile loans, credit card purchases, and other personal loans.

Certain types of nonbusiness interest are not deductible, including: interest on a debt incurred in the purchase of certain life insurance policies; interest on a debt incurred in the earning of tax-exempt income, such as loans taken to buy government bonds; and interest on debt for which the taxpayer is not legally liable.

This deduction has been allowed since the Minnesota income tax was enacted in 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$133,100,000	$148,200,000	$159,700,000	$177,300,000

1.74 CHARITABLE CONTRIBUTIONS

Internal Revenue Code, Sections 63(f) and 170
Minnesota Statutes, Section 290.089, Subd. 2

A taxpayer may deduct contributions to organizations that are religious, charitable, educational, scientific, or literary in purpose. In general, the deduction is limited to a maximum of 50% of federal adjusted gross income, although other limitations apply to specific types of contributions. Excess contributions may be carried forward for up to five years.

A deduction for charitable contributions has been allowed since the Minnesota income tax was enacted in 1933. Until 1985, the deduction differed from the federally-allowed deduction, mainly in regard to the maximum deduction and carryforward provision. In 1985 Minnesota adopted the federal deduction.

This deduction is claimed on approximately 820,000 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$80,400,000	$82,000,000	$84,100,000	$86,400,000

1.75 CASUALTY AND THEFT LOSSES

Internal Revenue Code, Sections 63(f) and 165
Minnesota Statutes, Section 290.089, Subd. 2

A deduction is allowed for the uninsured portion of nonbusiness losses caused by theft, vandalism, fire, storm, and car, boat, and other accidents or similar causes. The deduction is allowed only to the extent that each separate casualty or theft loss exceeds $100 and that the total of all losses during the year exceeds 10% of federal adjusted gross income.

A deduction for casualty or theft loss was first authorized for the federal income tax in 1913 and for the state tax in 1933. This deduction is now the same as the federal deduction and was last changed in 1983.

This deduction is claimed on approximately 4,500 returns.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,300,000	$1,400,000	$1,400,000	$1,400,000

1.76 TAX RETURN PREPARATION FEES

Internal Revenue Code, Sections 63(f) and 212
Minnesota Statutes, Section 290.089, Subd. 2

A deduction is allowed for all the ordinary and necessary expenses paid during the year in connection with the determination, collection, or refund of any tax.

Since 1933, Minnesota has allowed a deduction for expenses ordinary and necessary in the production of income. In 1959, language specifically allowing the deduction for tax return preparation fees was first enacted. In 1983, Minnesota adopted the federal definition of this deduction, although no substantive change resulted.

This deduction is claimed on approximately 450,000 returns each year.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,400,000	$4,500,000	$4,600,000	$4,700,000

1.77 ADOPTION EXPENSES

Internal Revenue Code, Sections 63(f) and 222
Minnesota Statutes, Section 290.089, Subd. 2

Qualified expenses incurred in the adoption of a child with special needs are deductible, up to a maximum of $1,500 for each adopted child. Qualified expenses include adoption fees, court costs, and attorney fees. A child with special needs is one whom the state determines cannot or should not be returned to the parental home, who has a specific factor or condition that makes placement difficult, and who has been the subject of an unsuccessful placement effort.

The deduction of adoption expenses was enacted in 1969. Prior to 1985, the Minnesota deduction was for the adoption of any child, up to a given maximum amount. Beginning with tax year 1985, Minnesota adopted the federal provision which restricts the deduction to expenses incurred in the adoption of a child with special needs.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.78 EDUCATION EXPENSES FOR DEPENDENT CHILDREN

Minnesota Statutes, Section 290.089, Subd. 2(a)

A Minnesota resident may deduct certain education expenses for dependent children in public or private school. Qualifying expenses include those for tuition, transportation, and nonreligious textbooks or supplies required for a subject commonly taught in the public schools. The maximum deduction is $650 per child in kindergarten through sixth grade and $1,000 per child in seventh through twelfth grades.

This deduction has been allowed since 1955. From 1971 through 1973 Minnesota also provided a credit for tuition paid to private schools, but the credit was declared unconstitutional and repealed. In 1983 the United States Supreme Court ruled the deduction constitutional. This provision was last changed in 1984 when the maximum deduction amounts were increased to the current levels.

This deduction was claimed on 110,000 returns in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$6,200,000	$6,300,000	$6,400,000	$6,600,000

OPTIONAL DEDUCTION

1.79 FEDERAL INCOME TAXES

Minnesota Statutes, Sections 290.088; 290.10 (8)(c); and 290.18, Subd. 2

After subtracting the standard deduction or the itemized deductions from Minnesota gross income, the taxpayer has the option of deducting his federal income tax and using one rate schedule or of not deducting his federal income tax and using a schedule with lower rates. In completing the tax return, the taxpayer computes the tax under both options and uses the one which produces the lower tax.

The deduction includes the federal income tax liability plus 25% of any self-employment tax for tax year 1985 and 40% for tax years 1986 through 1989.

The deduction is limited to the proportion that Minnesota gross income is of federal adjusted gross income. If any pension income, railroad retirement, military pay, unemployment compensation, or United States bond interest is subtracted to arrive at Minnesota gross income, the deduction is reduced by the proportion that the subtracted income is of federal adjusted gross income.

Just under 40% of the individual income tax returns are estimated to benefit from this provision. The fiscal impact measures the difference between the tax computed with the federal income tax deducted and the higher rate schedule applied and the tax which would be computed using the lower, nondeductible rate schedule.

The deduction for federal income taxes was included in the Minnesota individual income tax when it was enacted in 1933. When the standard deduction was enacted in 1949, the deduction for the federal income tax was made separate from the standard or itemized deductions. The deduction was on a cash basis until 1981 when it was changed to the accrual basis. In 1985 the deduction was made an option.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$63,700,000	$70,800,000	$78,800,000	$88,200,000

PREFERENTIAL COMPUTATION

1.80 TEN-YEAR AVERAGING OF LUMP SUM DISTRIBUTIONS

Internal Revenue Code, Section 402(e)
Minnesota Statutes, Section 290.032

A lump sum distribution from a qualified pension, profit-sharing, or stock bonus plan is eligible for the special ten-year averaging provision. A separate tax is computed on the lump sum distribution. The tax is computed using ten-year averaging and is done in isolation of other income of the taxpayer. The estimates measure the difference between the lump sum distribution tax and the additional regular income tax that would be paid if the entire lump sum was added to the income of the taxpayer in the year received.

This provision was adopted by Minnesota in 1975, and it was last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$17,300,000	$20,100,000	$23,300,000	$27,000,000

CREDITS

1.81 PERSONAL CREDITS FOR AGE 65 AND OVER, BLIND, DEAF, AND QUADRIPLEGIC

Minnesota Statutes, Section 290.06, Subd. 3f and 3g

If a taxpayer or spouse is age 65 or over, blind, deaf, or quadriplegic, an additional nonrefundable personal credit may be claimed for each category that applies. An additional credit may also be claimed for each category that applies to a dependent who is blind, deaf, or quadriplegic. The amount of the credit is indexed annually. The amount of each credit is $70 for tax year 1985 and $73 for tax year 1986.

These credits were enacted in the following years: senior citizen and blind, 1951; deaf, 1975; quadriplegic, 1979. These credits were first indexed in tax year 1981, and the method of indexing was changed in 1985.

The number of credits claimed for tax year 1984 were: age 65 and over, 288,000; blind, 7,000; deaf, 4,000; and quadriplegic, 1,000.

	Fiscal Year Impact			
	1986	1987	1988	1989
Age 65 and Over	$21,900,000	$23,400,000	$24,800,000	$26,700,000
Blind	600,000	700,000	800,000	800,000
Deaf	300,000	300,000	300,000	300,000
Quadriplegic	100,000	100,000	100,000	100,000
Total - State General Fund	$22,900,000	$24,500,000	$26,000,000	$27,900,000

1.82 PERSONAL CREDITS FOR DEPENDENTS

Minnesota Statutes, Section 290.06, Subd. 3f and 3g

A taxpayer may claim a nonrefundable credit for each dependent. Beginning in 1985, the definition of dependent is the same as the definition used for the federal income tax and is somewhat more restrictive than that previously applicable for state income tax purposes. The amount of the credit is $70 for the 1985 tax year and $73 for tax year 1986. Additional credits may also be claimed for dependents who are blind, deaf, or quadriplegic. The impact of these additional credits is included in the estimate for Item 1.81.

Personal credits are also allowed for the taxpayer and spouse at the same dollar amount as the credit for dependents. However, because each taxpayer, or taxpayer and spouse, is given equal tax relief, these personal credits are not considered tax expenditures and are not included in the estimates.

Although a personal exemption, rather than a credit, was enacted as part of the original Minnesota individual income tax in 1933, the exemption was replaced with a $5 credit in 1937. The amount of the credit was increased several times over the years to $60 for the 1980 tax year and was first indexed for inflation in 1981. In 1985 the method of indexing was changed, and the federal definition of dependent was adopted.

Approximately 1,200,000 dependent credits are claimed annually.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$78,200,000	$79,600,000	$80,400,000	$82,300,000

1.83 CREDIT FOR INCOME TAX PAID TO OTHER STATES

Minnesota Statutes, Section 290.081

A resident taxpayer may claim a nonrefundable credit for the amount of income tax paid to another state or Canadian province to the extent that income taxed in the other state or province is included in Minnesota gross income. The credit is the lesser of the tax owed to the other state or province, or the amount computed by multiplying the Minnesota gross tax computed on all income, less personal credits, times the percentage that the income earned outside Minnesota is to Minnesota gross income.

The credit does not apply to wage and personal service income earned in a state with which Minnesota has a reciprocity agreement. Minnesota entered into such reciprocity agreements with Wisconsin in 1968, with North Dakota in 1969, and with Michigan in 1984. Under these agreements a taxpayer with wage and personal service income is required to file an income tax return only in the state of residency.

Since 1973 the Minnesota-Wisconsin reciprocity agreement has included a unique reimbursement provision. The state which experiences a net revenue loss due to reciprocity is reimbursed by the other state for the amount of that loss; and, therefore, this provision is not considered a tax expenditure. The reciprocity agreements with North Dakota and Michigan have no provisions for reimbursement. However, they are not considered tax expenditures because there is no estimated revenue loss for Minnesota.

This credit was enacted in 1959 and was last changed in 1983.

This credit was claimed on 11,700 returns in tax year 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$6,600,000	$7,500,000	$8,500,000	$9,600,000

1.84 POLITICAL CONTRIBUTION CREDIT

Minnesota Statutes, Section 290.06, Subd. 11

A taxpayer may take a nonrefundable credit against his Minnesota income tax for contributions made to qualifying candidates for elective state and federal public offices and to qualifying political parties. The amount of the credit is equal to 50% of the contributions made during the tax year, with a maximum credit of $50 for an individual and $100 for a married couple filing a joint return. Contributions to candidates for state offices, other than judgeships, qualify only if the candidate has signed an agreement with the Minnesota Board of Ethical Practices agreeing to limit campaign spending.

This credit first went into effect with the 1974 tax year. The maximum credit was raised to its current level in 1979. The last change made to this provision occurred in 1985.

The number of returns on which the credit is claimed varies from year to year and ranges from 100,000 to 150,000.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,000,000	$6,300,000	$4,500,000	$6,700,000

1.85 CREDIT FOR EQUITY INVESTMENT IN A SMALL BUSINESS (REPEALED)

Minnesota Statutes, Section 290.069, Subd. 4 and 6

A taxpayer may claim a credit equal to 30% of the net investment in excess of $25,000 in the equity stock of a qualified small business. The credit may not exceed $75,000, or 75% of the taxpayer's tax liability after the subtraction of all other credits, whichever is less. Additionally, the credit may not be taken if the taxpayer owns more than 49% of the small business's stock, or if the stock pays either fixed or variable interest rates. If the small business is located within an enterprise zone, credit may be taken for investments in excess of $10,000, up to a maximum credit amount of $100,000. Excess credit amounts may be carried forward for up to five years. No carryback is allowed.

This credit was enacted in 1983, to be effective for tax years 1984 and 1985. In 1985 the credit was repealed for qualified small businesses certified and for stock purchased after June 30, 1985.

This credit was claimed on approximately 350 returns filed for 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	Minimal	Minimal	Minimal

1.86 CHILD AND DEPENDENT CARE CREDIT

Internal Revenue Code, Section 21
Minnesota Statutes, Section 290.067

A Minnesota taxpayer may claim a refundable credit of from 23% to 30% of dependent care expenses, depending on income, provided that those expenses were necessary in order to hold or look for a job. The maximum credit is $720 for one dependent and $1,440 for two or more dependents. These maximum amounts and allowable percentages are reduced for taxpayers with incomes over $10,000, so that a taxpayer with federal adjusted gross income over $24,000 receives no credit. A dependent is defined as a child under age 15 or a person of any age who is disabled.

The dependent care credit was enacted in 1977. It was last revised in 1986.

This credit was claimed on 48,800 returns filed for tax year 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,100,000	$10,800,000	$10,800,000	$10,700,000

1.87 CONSTRUCTION FINANCING (ENTERPRISE ZONES)

Minnesota Statutes, Section 273.1314, Subd. 9(a)(3)

A taxpayer may apply for a credit equal to a percentage of the cost of debt financing for construction of new or expanded facilities in a designated enterprise zone. Each municipality determines the percentage of financing used in computing credit amounts within its zone. Credit amounts in excess of annual tax liability are refundable to the taxpayer.

The credit was enacted in 1983 and was last changed in 1984. It is scheduled to expire on December 31, 1996, when the enterprise zone program expires.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

1.88 EMPLOYER TAX CREDITS (ENTERPRISE ZONES)

Minnesota Statutes, Section 273.1314, Subd. 9(a)(2) and (f)(1)

Two separate refundable credits against the income tax are available to employers in designated enterprise zones.

1. An employer may claim a credit of up to $3,000 annually for each additional worker employed in a designated enterprise zone.

2. An employer in a designated border city zone may claim a credit of up to $1,500 annually for each worker employed in the zone who does not qualify for the $3,000 credit.

The employer job credit was enacted in 1983 and was last changed in 1984. It is scheduled to expire on December 31, 1996, when the enterprise zone program expires.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$700,000	$2,300,000	$600,000	$600,000

CHAPTER 2: CORPORATE INCOME AND BANK EXCISE TAXES

Collections and History

For fiscal year 1986 net revenues from the corporate income tax were $326 million and from the bank excise tax were $41 million, together equaling 7.6% of total state revenue. The revenue from both taxes goes into the state general fund.

The Minnesota corporate income tax was enacted in 1933, at the same time and at the same rates as the individual income tax. In 1937 the rates for both the individual and corporate income taxes were changed, and the corporate rate was no longer the same as the individual. The corporate rate was changed from a graduated rate schedule to a flat rate of 7% and remained basically a flat rate until tax year 1982 when it was changed to a two-step rate, although various rate changes, additional taxes, and surtaxes were enacted during the intervening years. Since tax year 1983, the rate has been 6% on the first $25,000 of taxable income apportioned to Minnesota and 12% on the remainder.

Banks are not subject to the corporate income tax, but a bank excise tax was first enacted in 1941 at a rate of 8%. The bank excise tax was at a rate different from the corporate income tax until 1973; since that time the rates for the two taxes have been the same. The deduction of federal income taxes for both taxes was eliminated in 1971.

In 1981 Minnesota adopted a domestic unitary method of taxation. A group of corporations is considered to be a unitary business when there is unity of ownership, operation, and use. Only domestic corporations, that is, those organized under United States federal or state law, are included in the unitary group. The Minnesota taxable income of a corporation that is part of a unitary group is determined by applying an apportionment formula to the combined net income of the unitary business.

Tax Base

For purposes of this study, the tax base for the corporate income tax and the bank excise tax is defined to be income from all sources less expenses that are reasonable and necessary to earn that income. Such reasonable and necessary expenses are, therefore, not considered to be tax expenditures.

A tax expenditure is created when a certain type of income is excluded or when a deduction or credit is allowed for expenses other than those considered reasonable and necessary. For example, when depreciation measures the actual decline in the value of an asset during the tax year, it is considered a necessary business expense and not a tax expenditure. However, when accelerated depreciation or expensing is allowed, the excess over the actual depreciation is considered to be a tax expenditure.

A tax expenditure is also created when a business or organization operates with all the rights and privileges of a corporation but is not subject to the tax. Items 2.01, 2.02, and 2.34 are tax expenditures for this reason. The exemption of banks from the corporate income tax is not considered a tax expenditure because they are subject to an alternative tax, the bank excise tax. Likewise, the exemption of mining companies from the income tax is not a tax expenditure because they are subject to the occupation tax (Chapter 15).

Computation of the Tax

The computation of the tax is as follows:

	Income from all sources
minus:	exclusions
equals:	gross income
minus:	deductions
equals:	total net income
times:	apportionment factor
equals:	Minnesota net income
minus:	dividends received and contributions deductions
equals:	taxable income
times:	tax rates (6% on the first $25,000, 12% on excess)
equals:	gross tax
minus:	nonrefundable credits
equals:	net tax
minus:	prior payments (estimated tax)
minus:	refundable credits
equals:	amount due or refund

The Minnesota corporate income tax is technically independent of federal law, although Internal Revenue Code provisions are referenced and followed in many instances. Insurance companies determine net income under the provisions of the Internal Revenue Code of 1936.

For most multi-state corporations, income is apportioned to Minnesota based on a three-factor formula of the Minnesota ratios of property, payroll, and sales. The corporation uses the lesser of the average of the three ratios or a weighted ratio of 15% property, 15% payroll, and 70% sales. With special permission, separate accounting or a single factor of sales may be used. For insurance companies, income is apportioned to Minnesota by the ratio that gross premiums collected in Minnesota is to total gross premiums collected for that year.

EXEMPT ORGANIZATIONS

2.01 TAX-EXEMPT ORGANIZATIONS

Subchapter F of the Internal Revenue Code
Minnesota Statutes, Section 290.05

Minnesota conforms to Subchapter F of the Internal Revenue Code in exempting certain types of organizations from taxation. However, while Minnesota totally exempts these organizations from income taxes, the federal government taxes them on their "unrelated business income" which is defined as income generated from sources substantially unrelated to the tax exempt goals of the organization.

Conceptually, the Minnesota tax expenditure is the revenue impact of exempting both related and unrelated business income. In practice, no data exists from which to derive what would be the taxable portion of related business income; and for many nonprofit organizations, applying the concept of taxable income to their related business income would be problematical.

The revenue impact of exempting unrelated business income from tax, however, can be estimated because federal data exists for that portion of this tax expenditure. The estimates below therefore are a measurement of exempting only that portion of income which is considered by the Internal Revenue Service to be unrelated to the goals of the organization.

The following is a list of the types of organizations which are exempt from the Minnesota corporate income tax:

IRC, Sec.	Type of Organization	Number of Organizations Nationally (1985)
501(c)(1)	Federal corporations created by federal law to act as instrumentalities of the United States. Example: Federal Deposit Insurance Corporation	24
501(c)(2)	Title-holding corporations for exempt organizations, necessary because certain states prohibit tax exempt organizations from holding property.	5,758
501(c)(3)	Religious, educational, charitable, scientific, and literary organizations testing for public safety, fostering certain national or international amateur sports competition, or prevention of cruelty to children or animals. This classification also includes private foundations.	366,071
501(c)(4)	Civic leagues, social welfare organizations, and local associations of employees which promote community welfare or contribute earnings to charitable, educational, or recreational purposes.	131,250
501(c)(5)	Labor, agricultural, and horticultural organizations which seek to improve working conditions, products, or efficiency through education or instruction.	75,623
501(c)(6)	Business leagues, chambers of commerce, real estate boards, and other similar organizations which seek to improve the common business of their members.	54,217
501(c)(7)	Clubs organized for the pleasure, recreation, or social activities of their members.	57,343
501(c)(8)	Fraternal beneficiary societies and associations. These organizations operate under the lodge system and provide life, sickness, and/or accident benefits to their members.	94,435
501(c)(9)	Voluntary employee benefit associations (including federal employee voluntary benefit associations formerly covered by Section 501(c)(10)). These organizations provide for payment of life, sickness, accident, or other benefits to members.	10,668

IRC, Sec.	Type of Organization	Number of Organizations Nationally (1985)
501(c)(10)	Domestic fraternal societies and associations. These organizations are similar to 501(c)(8) organizations but do not provide life, sickness, or accident payments to their members.	15,924
501(c)(11)	Teachers' retirement fund associations. These are organizations of a purely local character which provide for payment of retirement benefits.	11
501(c)(12)	Benevolent life insurance associations, mutual ditch or irrigation companies, and mutual or cooperative telephone companies among others.	5,244
501(c)(13)	Cemetery companies owned by and operated exclusively for the benefit of their members.	7,239
501(c)(14)	State chartered credit unions and mutual reserve funds. These organizations provide banking services to their members.	6,032
501(c)(15)	Mutual insurance companies or associations which provide insurance to members at cost. (Tax exempt status is limited to organizations with annual gross incomes of $150,000 or less).	967
501(c)(16)	Cooperative organizations which finance crop operations in conjunction with activities of a marketing or purchasing association.	18
501(c)(17)	Supplemental unemployment benefit trusts.	726
501(c)(18)	Employee funded pension trusts (founded prior to June 25, 1959).	3
501(c)(19)	Recognized posts or organizations of war veterans.	23,062
501(c)(20)	Trusts to provide for prepaid legal services for employees.	167
501(c)(21)	Black lung disease trusts.	15
501(c)(22)	Withdrawal liability payment funds. These organizations provide funds to meet the liability of employers withdrawing from a multi-employer pension fund.	-

IRC, Sec.	Type of Organization	Number of Organizations Nationally (1985)
501(c)(23)	Associations of past or present members of the Armed Forces, founded before 1880.	-
501(d)	Religious and apostolic associations. These organizations provide a common treasury of the regular business activities of a communal religious group.	82
501(e)	Cooperative hospital associations providing the following services for two or more exempt hospitals: data processing, purchasing, laboratory testing, printing, communications, records center, and personnel services.	82
501(f)	Cooperative educational service organizations. These perform collective investment services for educational organizations.	-
521(a)	Farmers cooperative associations. These organizations perform cooperative purchasing and marketing of agricultural products.	2,542

Most of these organizations have been exempt from Minnesota income tax since 1933. In 1981 Minnesota adopted the list of tax-exempt organizations found in Subchapter F of the Internal Revenue Code. The last change occurred in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$300,000	$300,000	$400,000

Note: Fiscal impact reflects only the income from unrelated business, as explained above.

2.02 CREDIT UNIONS

Minnesota Statutes, Section 290.05, Subd. 2

Credit unions, which are cooperative associations similar to savings banks, are exempt from both state and federal income taxation. The estimates are based on the assumption that credit unions would be taxed the same as building and loan associations if they were subject to the income tax.

Credit unions have been specifically excluded from state income taxation since 1937. In 1981, Minnesota adopted the language found in Subchapter F of the Internal Revenue Code which excludes numerous organizations, including credit unions, from income tax. The general topic of tax-exempt organizations is discussed in Item 2.01.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,300,000	$2,300,000	$2,300,000	$2,300,000

EXCLUSIONS

2.03 DEFERRAL OF CERTAIN FOREIGN DIVIDENDS

Internal Revenue Code, Sections 951-964
Minnesota Statutes, Section 290.52

A controlled foreign corporation (CFC) is a foreign corporation controlled by a domestic corporation. Dividends from a CFC, included in Subpart F income, are reported for federal income tax purposes when they are constructively received by the U.S. corporation. However, Minnesota does not recognize Subpart F income, and the dividends are not reported for Minnesota tax purposes until they are repatriated. This deferral in reporting the income is considered a tax expenditure.

The estimates measure the impact of the deferral and take into account the effect of the dividend received deduction (Item 2.37), which excludes from corporate income 85% of dividends received from another corporation.

Minnesota has always allowed parent corporations to defer dividends from CFC's until they are repatriated.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$700,000	$900,000	$1,000,000	$1,100,000

2.04 PERMANENT EXEMPTIONS FROM IMPUTED INTEREST RULES

Minnesota Statutes, Section 290.079, Subd. 1

Section 7872 of the Internal Revenue Code contains imputed interest rules designed to prevent the assignment of income through the use of below-market or interest-free loans. When the rules apply, a lender is deemed to have received interest payments, and a borrower is deemed to have paid interest payments. Exemptions from the imputed interest rules include loans of less than $10,000, and there is a special method for computing income from a gift loan of less than $100,000.

Imputed interest rules and exceptions to the rules were first effective in 1984, and they were last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.05 INCOME FROM THE DISCHARGE OF DEBT

Internal Revenue Code, Sections 108 and 1017
Minnesota Statutes, Section 290.08, Subd. 20

In general, income from the cancellation of a debt is taxable. However, income which results from a taxpayer being allowed to pay off a debt for less than the originally agreed upon and legally required amount may be excluded from gross income under certain circumstances. The exclusion is the amount of income gained by the cancellation of the debt.

This provision was adopted in 1957 and last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.06 DISPOSITION OF FARM PROPERTY

Minnesota Statutes, Sections 290.08, Subd. 27 and 290.491

A family farm corporation or an authorized farm corporation may exclude from gross income the gain realized from the disposition of real or personal property used in a farm business if foreclosure is initiated or threatened in writing. The farm business must be owned and operated by the taxpayer as his principal business. The gain is that which is realized upon termination of a contract for deed, foreclosure of a mortgage, or deed in lieu of foreclosure.

Also exempt is income realized on a sale or exchange of farm property if the taxpayer is insolvent at the time of the sale, and the proceeds are used solely to discharge indebtedness of the property sold.

The provision relating to insolvent farmers was enacted in 1985 and amended in 1986. The provision relating to farm foreclosure property was enacted in 1986. Both provisions were made retroactive to tax year 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	$300,000	$100,000	$100,000

2.07 UNRELATED INCOME (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Minnesota taxes life insurance companies on three types of income: interest, dividends, and rent. All other income, including income from non-insurance business activities, is excluded. The estimates below are for unrelated income only; other types of excluded income are estimated separately in Items 2.08, 2.09, and 2.10.

Unrelated income has been excluded from the corporate income tax since the state first taxed insurance companies in 1937.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.08 UNDERWRITING INCOME (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Life insurance companies may exclude from Minnesota taxable income all underwriting income earned in a taxable year. Underwriting income is defined as a life insurance company's total gain from operations minus the company's taxable investment income. Underwriting income is chiefly made up of the following two types of income: (1) mortality savings, which are realized when deaths occur at a rate less than was assumed when life insurance premiums and reserves were established; and (2) loading savings, which are realized when expenses incurred in placing insurance policies on the books and subsequently servicing them are lower than was anticipated.

Insurance companies were originally exempt from the Minnesota income tax when it was enacted in 1933. In 1937, the state adopted a portion of the Federal Revenue Act of 1936 dealing with the taxation of insurance companies. This act, which is still used by the state, imposed an income tax on insurance companies but excluded underwriting income. The federal government began including half of a company's underwriting income in taxable income in 1959.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.09 FEE INCOME (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Life insurance companies may exclude from taxable income any fees received during the taxable year. Examples of fees collected by life insurance companies are partial release fees, loan assumption fees, rent collection fees, mortgage loan commitment fees, and income cancellation mortgage loan commitment fees.

Fee income has been excluded since life insurance companies were first subject to the Minnesota corporate income tax in 1937.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.10 ROYALTIES (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Minnesota life insurance companies may exclude from taxable income all royalties received during the year.

The royalties of life insurance companies have been excluded from taxation since 1937.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

DEDUCTIONS

2.11 FOREIGN SOURCE DIVIDENDS

Minnesota Statutes, Section 290.21, Subd. 4(e)

Dividends may be excluded from gross income if they are received from a corporation organized under the laws of a foreign country or political subdivision. Excluded dividends must be paid from income arising from sources outside the United States, the Commonwealth of Puerto Rico, or the possessions of the United States.

The deduction is not allowed if the corporate stock on which the dividends are paid constitutes the stock in trade or inventory of the taxpayer or if the taxpayer is a holding company.

Since the bulk of foreign dividends may be deducted under the more general dividend received deduction (Item 2.37), the estimates measure the effect of excluding only the remaining portion of foreign dividends.

This exclusion was enacted in 1984 and became effective for tax years beginning after June 30, 1985. It was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$0	$3,400,000	$3,800,000	$4,300,000

2.12 FOREIGN SOURCE ROYALTIES

Minnesota Statutes, Section 290.21, Subd. 8

For tax years beginning after December 31, 1984, a corporation may deduct from taxable net income, prior to apportionment, amounts received from a foreign corporation as rentals, fees, and royalties. The payments received must be for the use or privilege of using outside the United States, patents, copyrights, secret processes and formulas, good will, know-how, trademarks, trade brands, franchises, and other like property. In order to claim this deduction, a corporation must receive at least 80% of its gross income from the above sources.

This provision was enacted in 1984 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,000,000	$5,200,000	$5,500,000	$5,800,000

2.13 SIXTY PERCENT CAPITAL GAINS DEDUCTION

Minnesota Statutes, Section 290.16, Subd. 4

Sixty percent of a taxpayer's net long-term capital gains may be deducted from gross income. The 60% capital gains deduction applies to the sale or exchange of capital assets, which are investment or personal property, and to certain property used in a trade or business. The deduction does not apply to inventory or to property used in a trade or business. The deduction does not apply to inventory or to property held for sale in the ordinary course of business.

A net long-term capital gain occurs when sales or exchanges within a tax year result in an excess of long-term capital gains (net of any long-term capital losses) over short-term capital losses (net of any short-term capital gains). With some exceptions, the asset or property must be held a minimum of six months in order to receive the 60% deduction.

This provision was enacted in 1945, with the last change occurring in 1982, when the deduction was increased from 50% to 60%.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,400,000	$10,900,000	$11,000,000	$12,100,000

2.14 DEPRECIATION

Internal Revenue Code, Section 168
Minnesota Statutes, Section 290.09, Subd. 7

Minnesota taxpayers are allowed a deduction for depreciation of property (other than land) used in a trade or business or held for the production of income. Depreciation is an attempt to measure an asset's decline in value due to use, wear, or decay within the tax year. Conceptually, the tax expenditure is the extent to which depreciation for tax purposes exceeds the actual decline in value of the asset during the applicable tax year. The estimates below measure the extent to which current depreciation allowances exceed actual declines in value as measured by 35 year straight line depreciation for real property and the midpoint in the class life asset depreciation ranges (CLADR) for personal property.

The depreciation deduction was a part of the original Minnesota income tax in 1933. Accelerated depreciation was first allowed through administrative practice by the federal government in 1946 and by law in 1954. Minnesota first enacted an accelerated depreciation provision in 1959. The last change to the Minnesota provision occurred in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$40,100,000	$35,700,000	$33,300,000	$33,900,000

2.15 EXPENSING DEPRECIABLE BUSINESS PROPERTY

Internal Revenue Code, Section 179
Minnesota Statutes, Section 290.09, Subd. 7(B)

A corporation may elect to treat the cost of qualifying property as an expense and to deduct the cost in the year the property is placed in service. The deduction is taken instead of the depreciation deduction, and the maximum annual deduction is $5,000 for tax years 1983 through 1987, $7,500 for tax years 1988 and 1989, and $10,000 for tax year 1990 and thereafter.

Qualifying property is recovery property that would qualify for the federal investment credit and which is acquired by purchase for use in a trade or business. However, if the taxpayer elects to expense the property, the federal investment credit cannot be claimed.

The estimates measure the difference between expensing the property and a depreciation deduction which would reflect the actual useful life of the property.

This provision was adopted in 1982 and last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$400,000	$400,000	$200,000	Minimal

2.16 EXCESS OF PERCENTAGE OVER COST DEPLETION FOR COPPER-NICKEL MINING

Internal Revenue Code, Sections 613 and 614
Minnesota Statutes, Section 290.09, Subd. 8 and 9

Minnesota corporate taxpayers may take a percentage depletion allowance, rather than a cost depletion allowance, for copper-nickel mining. Depletion allowance refers to the way in which investment costs are recovered for mining or other extractive operations. Cost depletion deductions are allowed for almost all exhaustible natural resources. Although the federal government allows percentage depletion for most exhaustible resources, Minnesota allows it only for copper-nickel mining.

Cost depletion is based on the taxpayer's basis in the property and is almost identical to depreciation in its application. Percentage depletion is based on a percentage of the gross income received from the extractive operation and has little relationship to a taxpayer's basis. Because cost depletion is a normal and necessary cost of doing business, only the amount of percentage depletion in excess of cost depletion is considered a tax expenditure.

Minnesota first allowed percentage depletion for copper-nickel mining in 1967. This provision was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.17 AMORTIZATION OF ORGANIZATIONAL AND START-UP COSTS

Internal Revenue Code, Sections 195 and 248
Minnesota Statutes, Section 290.09, Subd. 19

Corporations which incur certain expenses during their initial organization or start-up phase may elect to amortize those costs over a period of not less than sixty months, beginning in the month in which the corporation commences operations. Without this special provision, corporate taxpayers would be required to capitalize the costs, adding them to their basis.

Minnesota first adopted the deduction for organizational expenses in 1955, and the deduction for start-up costs was added in 1980. The provision was last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

2.18 EXPENSING OF RESEARCH AND DEVELOPMENT COSTS

Internal Revenue Code, Section 174
Minnesota Statutes, Section 290.09, Subd. 18

Generally, expenses incurred in creating or developing an asset must be capitalized, with recovery occurring over the life of the asset. However, a corporation may elect to expense in the current tax year all qualified research and development costs. If the asset resulting from the research or development expenditures has no determinable useful life (such as is the case with a process or a formula), then the taxpayer may alternatively elect to amortize the costs over not less than sixty months.

No substantial changes have been made to this provision since it was adopted in 1955.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,200,000	$11,200,000	$11,500,000	$11,600,000

2.19 EXPENSING OF MAGAZINE CIRCULATION EXPENDITURES

Internal Revenue Code, Section 173
Minnesota Statutes, Section 290.09, Subd. 16

Generally, expenses incurred in creating or developing an asset must be capitalized, with recovery occurring over the life of the asset. However, a taxpayer may elect to deduct as an expense in the current year expenditures to establish, maintain, or increase the circulation of a newspaper, magazine, or other periodical. This treatment is restricted to certain types of deductions, and the election is binding for the current year and to similar expenditures in subsequent years.

This provision was enacted by Minnesota in 1951 and was last amended in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$200,000

2.20 EXPENSING OF CONSTRUCTION PERIOD INTEREST AND TAXES FOR LOW INCOME HOUSING

Internal Revenue Code, Section 189
Minnesota Statutes, Section 290.09, Subd. 30

For property that qualifies as low income housing, property taxes and interest paid or accrued during the construction period may be deducted as an expense in the year incurred. Without this provision, these costs would be amortized over ten years.

This provision took effect in tax year 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$300,000	$300,000	$300,000

2.21 EXPENSING OF MINERAL EXPLORATION AND DEVELOPMENT COSTS

Internal Revenue Code, Sections 616 and 617
Minnesota Statutes, Section 290.09, Subd. 25

Current-year expensing is allowed for items such as labor costs, ground clearing, construction, and other site preparation costs incurred in the exploration and development of mineral deposits except oil and gas. Generally, amounts paid for permanent improvements or betterments to income-producing property are not deductible as current year expenses but are treated as capital expenses, which increase the taxpayer's basis in the property.

Expensing of exploration and development costs for all minerals was first allowed by Minnesota in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

2.22 EXPENSING OF CERTAIN CAPITAL OUTLAYS AND SPECIAL CASH ACCOUNTING RULES FOR FARMERS

Internal Revenue Code, Section 175
Minnesota Statutes, Section 290.09, Subd. 21
Minnesota Rules, Parts 8001.0500, Subp. 7 and 8009.1300

A corporate taxpayer engaged in the business of farming may treat expenditures made during the tax year for soil and water conservation for farm land as expenses rather than as capital expenditures. Therefore, these expenditures are entirely deductible in the current year rather than throughout an asset's useful life.

Family farm corporations and certain nurseries are allowed to use cash accounting rather than the accrual system for income tax purposes. Therefore, costs attributable to goods not yet sold may be deducted in the current year. The accrual system is normally required under tax law when the sale of products is a material factor of a corporation's business and is required for most agricultural corporations other than nurseries and family farm corporations.

Certain agricultural corporations have been allowed to use the cash accounting system for tax purposes since 1933. Minnesota began allowing the expensing of capital outlays in 1955.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$400,000	$500,000	$500,000	$500,000

2.23 CASH ACCOUNTING OTHER THAN AGRICULTURE

Internal Revenue Code, Section 446
Minnesota Statutes, Section 290.07

Section 446 of the Internal Revenue Code allows a taxpayer to choose the cash method of accounting instead of the accrual method. The accrual method is considered a better measure of current-year income and expenses because it takes into account the income of receivables. This tax expenditure is the difference in net income measured by accrual accounting and cash accounting. Presently accrual accounting is required in a limited form only for corporations that sell inventory directly.

Cash accounting has been permitted since 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$300,000	$300,000	$300,000

2.24 COMPLETED CONTRACT RULES

P. L. 97-248, Section 229
Treasury Regulation 1.451-3
Minnesota Rules, Part 8007.0600, Subp. 2B

Regulations issued by the U.S. Department of Treasury and Minnesota Rules permit a method of accounting known as the completed contract method. One of two methods of accounting may be used to measure income from long-term contracts. The completed contract method measures income when income is received and when expenses are paid. In contrast, the percentage of completion method measures income when it is earned and expenses when they are incurred. The estimate is based on the difference between measuring income using the percentage of completion method and the completed contract method.

This tax expenditure also covers the lack of uniform capitalization rules for indirect costs. Under uniform capitalization rules a part of indirect costs, such as general and administrative expenses, must be capitalized and deducted in future years instead of being deducted as an expense in the current year. The lack of uniform capitalization rules applies not only to long-term contracts; it covers all types of business transactions.

The completed contract method of accounting dates back to 1918 and was permitted by Minnesota Regulations in 1934. The last change was in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$16,800,000	$18,400,000	$19,700,000	$21,500,000

2.25 INSTALLMENT SALES

Internal Revenue Code, Sections 453 and 453A
Minnesota Statutes, Section 290.07, Subd. 5

Section 453 of the Internal Revenue Code allows a method of accounting known as installment reporting. Instead of reporting the gain in the year the sale occurred, gains are reported when the cash from the sale is received. The estimate is based on the difference between measuring income without installment reporting and using installment reporting. Revolving credit plans are the largest user of installment reporting.

The installment method was first enacted in 1933 and was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$700,000	$700,000	$700,000	$700,000

2.26 EXCESS RESERVES FOR BAD DEBT (BANKS)

Internal Revenue Code, Sections 585, 593, and 596
Minnesota Statutes, Section 290.09, Subd. 6(c)
Minnesota Rules, Parts 8009.2100 and 8009.2400

Generally, bad debt deductions are a necessary cost of doing business which arise when a taxpayer uses the accrual method of accounting. Under the accrual method, a taxpayer includes as income all amounts that it has earned the right to receive. A bad debt deduction reduces accrued income that the taxpayer did not receive.

A bank may choose the charge-off method or the reserve method to compute its bad debt deduction. Under the charge-off method, a deduction is taken by a bank at the time a debt becomes worthless. There is no overstatement of the bad debt deduction and no tax expenditure. Under the reserve method, the deduction is based on the interrelationship between a calculation of ending balance of the reserve and the amount of debt that becomes worthless. Given a growing balance of account receivables or a worsening loss experience, the bad debt reserve calculation gives a deduction for future losses. This tax expenditure is defined as the extent to which tax liability has been reduced beyond what it would have been using the charge-off method.

Both the state and federal governments place ceilings on the amount a financial institution may add to its bad debt reserves. Ceilings are based on such things as the type of institution, the type of loans the institution has outstanding, and the past history of the institution. The ceilings serve to limit the tax expenditure but do not eliminate it.

Banks were first allowed to use the reserve method in 1947. This provision was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,600,000	$2,600,000	$2,100,000	$1,500,000

2.27 BAD DEBT RESERVES OTHER THAN FINANCIAL INSTITUTIONS

Minnesota Statutes, Section 290.09, Subd. 6
Minnesota Rules, Parts 8009.2100 and 8009.2400

Generally, a bad debt deduction is a necessary cost of doing business which arises when a taxpayer uses the accrual method of accounting. Under the accrual method, a taxpayer includes as income all amounts that it has earned the right to receive. A bad debt deduction reduces accrued income that the taxpayer did not receive.

A taxpayer may choose the specific charge-off method or reserve method to compute its bad debt deduction. Under the specific charge-off method, a deduction is taken by the taxpayer when the debt becomes worthless. Under the reserve method the deduction is based on the interrelationship between a calculation of ending balance of the reserve and the amount of debts that become worthless. Given a growing balance of accounts receivable or a worsening loss experience, the bad debt reserve calculation gives a deduction for future losses. This tax expenditure is defined as the extent to which tax liability has been reduced beyond what it would have been using the specific charge-off method.

The reserve method has been permitted since 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,600,000	$1,600,000	$1,600,000	$1,900,000

2.28 NONRECOGNITION OF GAINS ON PROPERTY DISTRIBUTIONS IN LIQUIDATION

Internal Revenue Code, Sections 336-346 and 386
Minnesota Statutes, Section 290.135

Minnesota Statutes adopt Internal Revenue Code provisions that exclude the recognition of gains a corporation realizes when a corporation is liquidated. The basis for this exclusion is a 1935 court case, General Utilities Operating Company vs. Helvering. Through a series of court rulings and subsequent codification of court rulings, the exclusion of corporate gains on liquidation has been labeled the General Utilites Doctrine.

This exclusion was first codified by the Internal Revenue Code in 1954 and by Minnesota statute in 1957. This provision was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,500,000	$14,000,000	$16,400,000	$18,600,000

2.29 MERGER RULES FOR THRIFTS

Internal Revenue Code, Sections 368 and 382
Minnesota Statutes, Sections 290.136 and 290.138, Subd. 3

Minnesota Statutes adopt Internal Revenue Code Sections 368 and 382 that classify the merger of insolvent thrifts as a tax-free reorganization. A thrift is one of the following: a mutual savings bank, a coopertive bank, or a building and loan association. Even though the shareholders of the thrift being merged do not maintain a meaningful ownership interest in the merged corporation, the merger is classified as a tax-free reorganization. Under tax-free reorganization rules, the new thrift is able to carryover net operating losses of the thrift being merged.

Tax-free reorganization rules for insolvent thrifts were first effective in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,000,000	$1,100,000	$600,000	$400,000

2.30 EMPLOYEE STOCK OWNERSHIP PLANS

Internal Revenue Code, Sections 404(k)(j) and 1042
Minnesota Statutes, Sections 290.13, Subd. 1 and 290.26, Subd. 2

Minnesota Statutes adopt two provisions of the Internal Revenue Code that allow a corporation to take a deduction and defer income from certain transactions connected with an employee stock ownership plan (ESOP).

A corporation is allowed to deduct from its income dividends paid to an ESOP. The deduction is allowed if the dividends are paid in cash and distributed to the ESOP's participants or beneficiaries.

A corporation is allowed to defer income on the sale of stock to an ESOP provided that a buyer and seller meet certain conditions. The stock must be stock that has no really tradable stock outstanding. One of the main conditions the seller must meet is a requirement to reinvest the proceeds in another domestic corporation. One of the main conditions the buyer must meet is the buyer must own 30% of the company stock.

Corporations were first allowed to use the above provisions in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.31 WEIGHTED APPORTIONMENT

Minnesota Statutes, Section 290.19

Minnesota allows a corporation to apportion its income to Minnesota by using a three-factor formula of the Minnesota ratios of property, payroll, and sales. The corporation uses the lesser of the average of the three ratios or a weighted ratio of 15% property, 15% payroll, and 70% sales.

For purposes of this study, the extent to which the weighted apportionment formula reduces the tax as compared to the tax that would be paid under the average ratio formula is considered a tax expenditure.

Minnesota first allowed manufacturing firms the option to choose between the two formulas in 1939. Nonmanufacturing firms were given the same option in 1953. This provision was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$81,700,000	$83,400,000	$87,600,000	$93,800,000

2.32 SINGLE-FACTOR APPORTIONMENT FOR MAIL ORDER COMPANIES

Minnesota Statutes, Section 290.19, Subd. 1(3)

A business which consists exclusively of selling tangible personal property and services by mail order or telephone and has all of its property and payroll in Minnesota may apportion its income to Minnesota based only on the percentage of sales delivered in Minnesota. Without this provision, the business would use the weighted apportionment formula (Item 2.31).

This provision was enacted in 1985, effective for tax years beginning after December 31, 1984, and before January 1, 1989.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$600,000	$600,000	$600,000	$600,000

2.33 THROWBACK SALES

Minnesota Statutes, Section 290.19, Subd. 1a

Multi-state corporate taxpayers are not required to include throwback sales in their Minnesota sales when apportioning income to Minnesota for tax purposes. "Throwback sales" are defined as sales of goods from Minnesota offices, stores, warehouses, and factories to either the federal government or to a purchaser in another state if the other state does not impose an income tax on the seller. Although this provision could reduce the tax for any multistate corporation, its impact is even more significant for a corporation using the weighted apportionment formula (Item 2.31).

Prior to 1973 Minnesota used an origin-of-sale basis for corporate apportionment. In 1973, when Minnesota switched to a destination-of-sale basis, throwback was not adopted. This provision was changed last in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$25,500,000	$25,500,000	$25,500,000	$25,500,000

2.34 DEDUCTIONS ALLOWING CORPORATIONS TO BE TAXED AS PARTNERSHIPS

Internal Revenue Code, Sections 851, 856-860, and 1362
Minnesota Statutes, Sections 290.09, Subd. 28; 290.21, Subd. 6; and 290.9725

The Minnesota corporate income tax is imposed by statute "... for the privilege of existing as a corporation ..." However, certain types of corporations have the characteristics of a corporation but are allowed deductions which, in effect, cause them to be taxed as partnerships. Income earned by a partnership is normally not taxable to the partnership but instead is taxable to the partners under the individual income tax. Electing to be taxed as a partnership is a tax expenditure to the extent that it allows corporations to deduct from gross income amounts distributed to shareholders, which would otherwise be subject to the corporate income tax. The following three types of organizations may elect to receive this special tax treatment.

S Corporations (also known as subchapter S or small business corporations): A corporation must meet certain requirements in order to qualify for the preferential tax status including: only one class of stock; domestic corporations only; only individuals as shareholders; no more than 35 shareholders; and all shareholders unanimously elect special status. Termination of special status will occur if the corporation fails to meet the standards above, or if those controlling more than 50% of the voting shares agree to revocation.

Regulated Investment Companies: A regulated investment company engages primarily in the business of investing, reinvesting, or trading of stocks and securities. A regulated investment company may elect to be treated as a partnership for tax purposes provided that at least 90% of the corporation's gross earnings are from dividends, interest, or are gains from the sale of stocks or securities, and provided that less than 30% of the corporation's income is derived from securities held less than three months. By electing special status, a regulated investment company is able to deduct from gross income all amounts distributed to shareholders. However, income retained by the regulated investment company is subject to the corporate income tax. Once this election is made, it is irrevocable for the current and all succeeding taxable years.

Real Estate Investment Trusts: A real estate investment trust is involved in a number of activities, including operation of rental property and the granting of loans. A qualified real estate investment trust may deduct from gross income all amounts distributed to shareholders. Any income retained by the real estate investment trust is subject to the corporate income tax.

Special tax status was first allowed for regulated investment companies in 1941, S corporations in 1961, and real estate investment trusts in 1971. The last change affecting any of these provisions took place in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
S Corporations	$8,600,000	$9,600,000	$10,700,000	$11,800,000
Regulated Investment Companies	42,400,000	47,500,000	52,900,000	58,200,000
Real Estate Investment Trusts	700,000	800,000	900,000	1,000,000
Total - State General Fund	$51,700,000	$57,900,000	$64,500,000	$71,000,000

2.35 CHARITABLE CONTRIBUTIONS

Minnesota Statutes, Section 290.21, Subd. 3

Minnesota banks and corporations may deduct from taxable net income charitable, public purpose, religious, scientific, literary, artistic, or educational contributions made in a taxable year. The contribution deduction is limited to 15% of the taxpayer's net income less the deduction allowed for dividends received; no carryovers are allowed. If contributions are made to non-Minnesota recipients, a taxpayer may deduct only a portion of contributions equal to the portion that Minnesota taxable net income is of total U.S. net income.

This deduction was enacted in 1933 and last changed in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$10,200,000	$11,200,000	$12,300,000	$13,400,000

2.36 PATRONAGE DIVIDENDS (COOPERATIVES)

Minnesota Statutes, Section 290.08, Subd. 12

Cooperative buying, selling, or producing associations may exclude from gross income amounts which are distributed to customers (patrons) in the form of patronage dividends. This exclusion applies to both cash and noncash dividends. Cooperatives may retain earnings beyond the end of the tax year in this manner. This provision results in cooperatives paying very little or no corporate income tax. However, both cash and noncash dividends are treated as taxable income to the patron.

Minnesota has excluded patronage dividends from the income of cooperatives since 1933.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,400,000	$5,400,000	$5,400,000	$5,400,000

2.37 DIVIDEND RECEIVED DEDUCTION

Minnesota Statutes, Section 290.21, Subd. 4

Under certain conditions a corporation or bank may deduct from its taxable net income either 85% or 100% of dividend income it receives from other corporations. Generally the conditions relate to the nature or type of corporation receiving the dividends, the purpose for which the stocks are held, and the relationship between the dividend recipient and the dividend paying company.

Effective for tax years beginning after July 1, 1985, all dividends received from a corporation organized under the laws of a foreign country may be excluded from income (see Item 2.11). The estimates below reflect the exclusion of foreign source dividends to the extent that they qualify for exclusion under this provision. The estimates for Item 2.11 reflect the balance of foreign source dividends which are not already excluded by this provision.

The dividend received deduction was enacted in 1947 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$22,500,000	$23,000,000	$24,200,000	$25,900,000

2.38 EXEMPT INTEREST (INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Insurance companies may take a deduction for interest income which they receive by virtue of holding interest-bearing debt obligations of a state, territory, possession of the United States, or of any political subdivision thereof.

This provision was enacted in 1937 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,300,000	$2,500,000	$2,800,000	$3,100,000

2.39 SUMS PAID OUT OTHER THAN DIVIDENDS (MUTUAL INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Mutual insurance companies may take a deduction from net income for all sums paid out other than dividends. Certain sums paid out, such as payments on claims, are deemed to be ordinary and necessary business expenses, and their deduction is not viewed as a tax expenditure. Other sums paid out represent special treatment, and their deduction is considered a tax expenditure. Examples of the latter include liabilities for unearned premiums and company surplus. Current-year liability is affected when these sums are held for more than one tax year before being refunded to the policyholders. Therefore, they constitute a form of retained earnings which are not taxed, and their deduction is considered a tax expenditure.

This provision was enacted in 1937 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.40 MEAN RESERVES (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Depending on certain conditions, life insurance companies are allowed a deduction from gross income of either 3.75% or 4% of the mean of reserve funds held at the beginning and end of the taxable year. Reserve funds are required by state law for most types of life insurance policies in order to protect policyholders. The conditions affecting the deduction involve interest rates, the types of policies issued, and determinations made by the commissioner of revenue.

The provision was enacted in 1937 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,800,000	$12,900,000	$14,200,000	$15,800,000

2.41 RESERVES FOR DEFERRED DIVIDENDS (LIFE INSURANCE COMPANIES)

Minnesota Statutes, Section 290.35

Life insurance companies may take a deduction, in addition to the deduction allowed for all business expenses, equal to 2% of all qualified funds held at the end of a taxable year as a reserve for payment of deferred dividends. Qualifying funds must be for dividend payments which are deferred for not less than five years from the date of the policy contract.

This provision was enacted in 1937 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

CREDITS

2.42 RESEARCH AND DEVELOPMENT CREDIT

Minnesota Statutes, Section 290.068

A corporate taxpayer may claim a nonrefundable credit against the income tax based on qualified expenditures for research and development performed solely within Minnesota. Expenditures include such things as wages paid to researchers, costs of supplies used in conducting research, rental costs of personal property used in research, 65% of contract costs paid to others for doing research, and certain contributions to nonprofit organizations engaged in research and development within Minnesota. Current year expenditures must exceed the average yearly research and development expenditures for the three preceding years to qualify. This average of the preceding three years is referred to as the base-year expenditure.

The credit is equal to 12.5% of the first $2 million of current-year expenditures over the base-year expenditure. A credit equal to 6.25% is allowed for amounts in excess of $2 million over the base year. The credit claimed may not exceed the taxpayer's current tax liability. However, credit in excess of current tax liability may be carried forward fifteen years and back three years.

The research and development credit was enacted in 1981 and was last changed in 1986.

This credit was claimed on 410 returns filed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$18,300,000	$19,000,000	$19,800,000	$20,700,000

2.43 CONSTRUCTION FINANCING (ENTERPRISE ZONES)

Minnesota Statutes, Section 273.1314, Subd. 9(a)(3)

A corporation may apply for a credit equal to a percentage of the cost of debt financing for construction of a new or expanded facility in a designated enterprise zone. Each municipality determines the percentage of financing used in computing credit amounts within its zone. Credit amounts in excess of annual tax liability are refundable to the taxpayer.

The credit was enacted in 1983 and was last changed in 1984. It is scheduled to expire on December 31, 1996, when the enterprise zone program expires.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$500,000	$1,300,000	$1,100,000	$1,100,000

2.44 EMPLOYER TAX CREDITS (ENTERPRISE ZONES)

Minnesota Statutes, Section 273.1314, Subd. 9(a)(2) and (f)(1)

Two separate refundable credits against the income tax are available to employers in designated enterprise zones.

1. An employer may claim a credit of up to $3,000 annually for each additional worker employed in a designated enterprise zone.

2. An employer in a designated border city zone may claim a credit of up to $1,500 annually for each worker employed in the zone who does not qualify for the $3,000 credit.

The employer job credit was enacted in 1983 and last changed in 1984. It is scheduled to expire on December 31, 1996, when the enterprise zone program expires.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,500,000	$4,300,000	$4,700,000	$5,100,000

2.45 CREDIT FOR TECHNOLOGY TRANSFERS TO SMALL BUSINESSES

Minnesota Statutes, Section 290.069, Subd. 2 and 6

A Minnesota corporate taxpayer may claim a nonrefundable credit against the income tax equal to 30% of the net value of technology transferred to a qualified small business, up to a maximum credit of $300,000. Technology is defined as ". . . a proprietary process, formula, pattern, device, or compilation of scientific or technical information unless it (1) is in the public domain; or (2) cannot be accurately valued."

Beginning with tax year 1986, the credit is allowed only if the transferee is located in the designated technology corridor project area in Minneapolis. Other restrictions apply, including that the transferee cannot be a subsidiary or affiliate of the transferor and that the transferee makes a substantial investment in acquiring or developing the technology.

This credit was enacted in 1983. In 1985 the credit was restricted to the technology corridor project area in Minneapolis, and the expiration date was extended so that it expires for contributions made after December 31, 1988.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.46 CREDIT FOR CONTRIBUTIONS TO SMALL BUSINESS ASSISTANCE OFFICES

Minnesota Statutes, Section 290.069, Subd. 3 and 6

A Minnesota corporate taxpayer may claim a credit for contributions to a small business assistance office or to an innovation center public corporation. The credit is equal to 50% of the contribution up to a maximum credit of $25,000.

A small business assistance office is a nonprofit corporation which provides assistance and training to individuals who are financing, developing, or establishing qualified small businesses. In order to qualify for this provision, the small business assistance office must meet certain requirements and be certified by the Minnesota Department of Energy and Economic Development. An innovation center public corporation is a nonprofit public corporation located at a Minnesota state university that has as its purpose encouraging and assisting Minnesota high-technology small businesses.

This credit was enacted in 1983. In 1985 the expiration date was extended to December 31, 1988.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

2.47 CREDIT FOR EQUITY INVESTMENT IN A SMALL BUSINESS (REPEALED)

Minnesota Statutes, Section 290.069, Subd. 4 and 6

A taxpayer may claim a credit equal to 30% of the net investment in excess of $25,000 in the equity stock of a qualified small business. The credit may not exceed $75,000, or 75% of the taxpayer's tax liability after the subtraction of all other credits, whichever is less. Additionally, the credit may not be taken if the taxpayer owns more than 49% of the small business's stock, or if the stock pays either fixed or variable interest rates. If the small business is located within an enterprise zone, credit may be taken for investments in excess of $10,000, up to a maximum credit amount of $100,000. Excess credit amounts may be carried forward for up to five years. No carryback is allowed.

This credit was enacted in 1983, to be effective for tax years 1984 and 1985. In 1985 the credit was repealed for qualified small businesses certified and for stock purchased after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	$0	$0	$0

2.48 CREDIT FOR GROSS PREMIUMS TAX (INSURANCE COMPANIES)

Minnesota Statutes, Section 290.06, Subd. 3f(6)

Minnesota insurance companies may take a credit against the corporate income tax for the amount of Minnesota gross insurance premiums tax paid during the tax year.

This credit was enacted in 1937.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$17,400,000	$19,000,000	$21,100,000	$23,700,000

CHAPTER 3: ESTATE TAX

Collections and History

Revenues from the Minnesota estate tax were $14.8 million in fiscal year 1986. All revenues from this tax go into the state general fund.

In 1905 the Minnesota Legislature first enacted a tax on the estates of decedents in the form of an inheritance tax. Minnesota had an inheritance tax until 1979 when it was repealed and an estate tax was adopted. The inheritance tax was imposed on each individual who received property from an estate, and the amount of tax depended upon the amount of property received and the relationship of the recipient to the decedent. The estate tax is imposed on the taxable estate before it is distributed.

Major changes in the federal estate tax were enacted in 1981, and Minnesota adopted conforming legislation to remove the limit on the marital deduction and to increase, over a six-year period, the minimum filing requirement and the general estate deduction.

In 1985 a major change was made in the estate tax. Prior to the effective date of the 1985 legislation, the Minnesota estate tax was equal to the greater of: a) the tax computed from the Minnesota rate schedule on the Minnesota taxable estate; or b) the Minnesota portion of the federal estate tax credit for state taxes. The 1985 law eliminated the first computation and adopted the Minnesota portion of the federal tax credit for state taxes, known as the "pick-up tax," as the Minnesota estate tax, effective for estates of decedents dying after December 31, 1985.

Tax Base

The tax base for the estate tax is defined for this study as the net estate transferred. In other words, it is gross estate less administrative costs and other necessary and reasonable expenses paid before the estate is distributed. Therefore, a tax expenditure is created in the estate tax when a certain component of the estate is exempted or excluded because of its source, such as pensions and annuities (Item 3.04) or when a distribution is excluded from taxable estate because of the identity of the recipient, such as the deduction for charitable gifts (Item 3.03) or the marital deduction (Item 3.08). Preferential valuations and credits are also considered to be tax expenditures.

Computation of the Tax

Prior to the 1985 law changes, that is, for estates of decedents dying before January 1, 1986, the estate tax is the greater of the tax computed according to the Minnesota rate schedule or the Minnesota portion of the maximum federal credit for state taxes, known as the "pick-up tax."

Minnesota Rate Schedule Tax	
	Gross estate
minus:	federal exclusions
equals:	federal gross estate
minus:	non-Minnesota property
equals:	Minnesota gross estate
minus:	exemptions and deductions
equals:	Minnesota taxable estate
times:	graduated rates
equals:	gross tax
minus:	credits
equals:	Minnesota rate schedule tax

Pick-up Tax	
	Gross estate
minus:	federal exclusions
equals:	federal gross estate
minus:	federal exemptions and deductions
equals:	federal taxable estate
minus:	$60,000
equals:	federal adjusted taxable estate
times:	graduated rates
equals:	maximum state tax credit
times:	proportion of Minnesota gross estate to federal gross estate
equals:	pick-up tax

Estate tax equals: the greater of the rate schedule tax or the pick-up tax.

For estates of decedents dying after December 31, 1985, the computation of the rate schedule tax is eliminated, and the tax is the pick-up tax. For the estate of a resident decedent, an alternate computation is used if it results in a tax larger than the pick-up tax. The alternate tax is equal to the maximum state tax credit minus the death tax paid to the other state. Therefore, the alternate computation would be used only when the other state's tax was less than its share of the pick-up tax.

An estate tax return must be filed if the decedent's federal gross estate exceeds $500,000 for persons dying in 1986 and $600,000 for persons dying in 1987 and later.

The 1985 law changes affect how the fiscal impacts of the tax expenditures are measured over the four years of this study. Because the estate tax is required to be paid by nine months after the death of the decedent, the estate tax law as it existed prior to the 1985 legislative changes is reflected in the estimates for fiscal year 1986 and the first quarter of fiscal year 1987. The effects of the law as enacted in 1985 are shown in the estimates for the remainder of fiscal year 1987 and for fiscal years 1988 and 1989.

The methodology used to measure the fiscal impact of the estate tax items in this study has been corrected from that used for the Tax Expenditure Budget submitted to the 1985 Legislature. In that first study, only the impact of the provision on the computation of the rate schedule tax was measured. For this study, however, the impact of the provision on the pick-up tax is also measured when applicable. The correction in methodology recognizes that these items pass through to the Minnesota pick-up tax in a manner similar to the way in which the provisions affecting federal adjusted gross income pass through to the Minnesota individual income tax.

PREFERENTIAL VALUATIONS

3.01 ALTERNATE VALUATION OF PROPERTY

Internal Revenue Code, Section 2032
Minnesota Statutes, Section 291.215, Subd. 1

As a general rule, property included in a decedent's gross estate is valued at its fair market value as of the date of death. However, the decedent's personal representative may choose an alternate valuation which is the value of the property six months after death. Property which is sold, distributed, or otherwise disposed of during the six month period is valued at its fair market value at the time of disposition. When the alternate valuation is used, it must be used for all property. The tax expenditure in this provision is the difference between the tax liability using the valuation on the date of death and the tax liability using the alternate valuation.

Minnesota enacted this provision adopting Section 2032 of the Internal Revenue Code in 1980, and it was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	Minimal	Minimal	Minimal

3.02 SPECIAL USE VALUATION

Internal Revenue Code, Section 2032A
Minnesota Statutes, Section 291.075

Property is generally included in the estate at its fair market value. Fair market value is a property's value based on its best possible use. However, certain property which is used in a farm or other closely-held business may be valued at its farm or business use value, even though it is less than the market value. The total decrease in the value of the property for which the special use valuation applies cannot be more than $750,000. The estimates below measure the difference between tax liability using the highest use market value and tax liability using the special use valuation.

The special use valuation option was included in Minnesota's estate tax when it was enacted in 1979. The last change occurred in 1985.

The special use valuation was claimed on 75 returns in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$800,000	$400,000	$200,000	$200,000

EXCLUSIONS

3.03 CHARITABLE GIFTS

Internal Revenue Code, Section 2055
Minnesota Statutes, Section 291.05 (1)

Gifts from an estate to certain persons or organizations are excluded from the gross estate for tax purposes. Qualifying recipients include: charitable, scientific, literary, and educational organizations; public cemeteries; religious organizations; members of the clergy; employee stock ownership trusts; and federal, state, or local governments.

This provision was enacted in 1911 as part of the inheritance tax and exempted gifts to charitable, religious, and educational organizations and units of government. Scientific and literary groups were added to the list in 1919, public cemeteries in 1927, members of the clergy in 1963, and employee stock ownership trusts in 1974. In 1979 when the inheritance tax was repealed, this exemption was carried over to the estate tax. In 1985 the application of this provision to the Minnesota rate schedule tax was repealed, along with that tax, effective for estates of decedents dying after December 31, 1985. (See the introduction to Chapter 3 for further explanation.)

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$3,900,000	$3,000,000	$2,800,000	$3,000,000

3.04 PENSIONS AND ANNUITIES

Internal Revenue Code, Section 2039
Minnesota Statutes, Section 291.065

The value of pensions and annuities paid to survivors is excluded from gross estate. Because the revenue impact of exempting pensions and annuities paid to a surviving spouse is measured as a part of the marital deduction (Item 3.08), that impact is not included here.

This exemption was enacted in 1959 as part of the inheritance tax. When the inheritance tax was repealed in 1979, this provision was carried over to the estate tax. In 1985 the application of this provision to the Minnesota rate schedule tax was repealed, along with that tax, effective for estates of decedents dying after December 31, 1985. (See the introduction to Chapter 3 for further explanation.)

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$900,000	$600,000	$500,000	$500,000

3.05 SOCIAL SECURITY BENEFITS

Revenue Ruling 55-87
Minnesota Statutes, Section 291.05(4)

Social security lump sum death benefits which are paid to surviving spouses and dependents are exempt from the Minnesota estate tax. The amount of the lump sum benefit is fixed at $255.

This exemption was enacted in 1963 under the inheritance tax laws and was carried over to the estate tax without change when the inheritance tax was repealed in 1979. The last change occurred in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

3.06 VETERANS' BURIAL BENEFITS (REPEALED)

Minnesota Statutes, Section 291.05(4)

The amount of veterans' burial benefits paid by the Veterans Administration is excluded from gross estate. This benefit is typically $300, unless a veteran dies from service-related injuries, in which case benefits may be as high as $1,100.

This exemption was enacted in 1979 and was repealed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	$0	$0

3.07 LIFE INSURANCE PROCEEDS

Internal Revenue Code, Section 2042
Minnesota Statutes, Section 291.005, Subd. 1(1)

Generally, death benefits from a life insurance policy paid to a named beneficiary and not to the estate itself are excluded from federal gross estate. The estimates below do not include death benefits paid to a spouse because such benefits would also be exempt under the marital deduction (Item 3.08).

This provision was originally enacted in 1951 under the inheritance tax. With some modification, it was carried over to the estate tax in 1979. It was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,800,000	$1,100,000	$900,000	$1,000,000

DEDUCTION

3.08 MARITAL DEDUCTION

Internal Revenue Code, Section 2056
Minnesota Statutes, Section 291.051

The net value of all property passing from a decedent to a surviving spouse may be deducted from gross estate. The net value of the property is the gross value reduced by the amount of exemptions and deductions associated with the property being passed to the spouse.

This deduction was enacted in 1911 as a $10,000 inheritance tax deduction. In 1979, when the inheritance tax was repealed, the marital deduction was continued for estate tax purposes, with a maximum deduction of $250,000 or one-half the adjusted gross estate, whichever was greater. An unlimited marital deduction was enacted in 1981. In 1985 the application of this provision to the Minnesota rate schedule tax was repealed, along with that tax, effective for estates of decedents dying after December 31, 1985. (See the introduction to Chapter 3 for further explanation.)

The marital deduction was claimed on approximately 1,100 returns filed in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$17,300,000	$8,200,000	$5,300,000	$5,700,000

CREDIT

3.09 PREVIOUSLY PAID ESTATE OR INHERITANCE TAX (REPEALED)

Minnesota Statutes, Section 291.06

A credit against the Minnesota estate tax may be claimed for any Minnesota estate or inheritance tax paid on property which was inherited by the decedent from a person who died up to five years before the decedent. The credit is limited to the lesser of: 1) prior Minnesota estate or inheritance taxes paid on the property if assessed within those five prior years, or 2) current Minnesota estate taxes attributable to the property or traceable assets acquired by exchange.

The credit may be applied only to a tax computed under the Minnesota rate schedule. If the tax paid is the federal credit amount for state death taxes, this credit may not be taken.

This credit was enacted in 1939, as part of the inheritance tax law. In 1979, when the inheritance tax was repealed, this provision was continued as part of the estate tax. The credit is repealed, along with the Minnesota rate schedule tax, for returns filed for deaths after December 31, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$100,000	$0	$0

CHAPTER 4: SALES AND USE TAX

Collections and History

Revenues from the general sales and use tax totaled $1.36 billion in fiscal year 1986, making it the second largest source of state revenue with 28.3% of the total. All revenues from the sales and use tax are deposited in the state general fund.

The Minnesota general sales and use tax was enacted in a special session of the 1967 Legislature and became effective on August 1, 1967, at a rate of 3%. The rate has been increased three times since enactment of the tax: to 4% on November 1, 1971; to 5% on July 1, 1981; and to 6% on January 1, 1983.

A separate motor vehicle excise tax (Chapter 5) was enacted, effective January 1, 1972. Prior to that time, motor vehicles were subject to the general sales and use tax, but, with the enactment of the motor vehicle excise tax, they were exempted from the general sales and use tax.

Many exemptions have been added since 1967, including accessory tools in 1973, residential heating fuels in 1978, residential water in 1979, and repair and replacement parts for farm machinery in 1985. Exemptions were removed from cigarettes and from candy and soft drinks in 1982 and from over-the-counter magazines and periodicals in 1983.

With the exception of vending machines, one sales and use tax rate applied to all taxable sales from 1967 until 1981. When the rate was increased from 4% to 5%, the rate on farm machinery was kept at 4%. In 1984, when the general rate was 6%, the rate for certain capital equipment and special tooling was reduced to 4%, and the farm machinery rate remained at 4%. In 1985, the rate for farm machinery was reduced from 4% to 2%.

Tax Base

For purposes of this study, the tax base for the general sales and use tax is defined to be the sale of tangible personal property or services to the final consumer. However, this fairly simple definition requires some explanation.

This definition is a working definition for this study and should not be interpreted as defining what the ideal tax base should be. Although services could properly be considered outside the tax base, they are included in the tax base for this study because currently some services are taxed.

Sales for resale in the regular course of business are not included in the tax base. Because only the sale to the final consumer, which is normally at retail, is included in the tax base, the exemption of the sale to the wholesaler or other distributor is not a tax expenditure. In agricultural and industrial production, the sales of raw materials, component parts, and products consumed directly in the process are considered to be for resale, and therefore the exemption of these items is not a tax expenditure. However, the sale of machinery, equipment, and tools used in agricultural or industrial production is not considered a sale for resale. Therefore, a tax expenditure is created when a certain type of machinery, equipment, or tools is exempt from the sales tax or is taxed at a reduced rate.

Although the tax base would include motor vehicles, the exemption of motor vehicles from the sales tax is not considered a tax expenditure because motor vehicles are subject to an alternative tax, the motor vehicle excise tax.

Computation of the Tax

The sales tax is imposed on the gross receipts from taxable sales made by any person in Minnesota. The complementary use tax is imposed on the storage, use, or consumption in Minnesota of taxable personal property unless the Minnesota sales tax was paid on the sales price. The rate for both the sales tax and the use tax is 6%, with lower rates applicable to certain items (Items 4.46 through 4.49).

Generally, a retail sale is subject to the tax unless it is specifically exempted by law. Taxable sales also include: selling, leasing, or renting tangible personal property; the furnishing of meals or drinks for a consideration; the furnishing for a consideration of lodging for less than thirty days; the admission to places of amusement or athletic events; the furnishing for a consideration of electricity, gas, water, or steam; and local exchange telephone service and intrastate toll service.

The tax is imposed on the sales price of the item, which is defined as the total consideration valued in money, whether paid in money or otherwise. Exclusions from the sales price include: property taken in trade for resale; cash discounts; certain federal excise taxes; and separately-stated interest, finance, or carrying charges.

The sales tax is paid by the purchaser to the seller; the seller collects and remits the tax to the state. The use tax is paid directly by the purchaser to the state.

EXEMPTIONS - PARTICULAR GOODS AND SERVICES

4.01 FOOD

Minnesota Statutes, Sections 297A.01, Subd. 3(c) and 297A.25, Subd. 1(a)

Generally, food purchased for home consumption is exempt from the sales tax, and food that is prepared and served, such as in a restaurant, is taxable, as is all food sold in vending machines. Taxable items also include candy, chewing gum, soft drinks and other carbonated beverages, ice, heated food and drinks, hand-prepared ice cream or ice milk products, and sandwiches and party trays prepared by the retailer.

Food items that would otherwise be taxable but are exempt because of the identity of the seller are estimated separately. See Items 4.40, 4.44, and 4.45.

The exemption granted sales of food was included when the sales and use tax was enacted in 1967. It was last changed in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$247,100,000	$259,400,000	$273,400,000	$288,200,000

4.02 CLOTHING AND WEARING APPAREL

Minnesota Statutes, Section 297A.25, Subd. 1(g)

Generally, all clothing, whether new or used, is exempt from the sales and use tax. The exemption includes inner and outer wear, footwear, headwear, gloves and mittens, neckwear, hosiery, and similar items customarily worn for general use. Also exempted are fabrics, thread, buttons, zippers, and similar items which are to be directly incorporated into wearing apparel. This exemption does not apply to jewelry, articles made of fur or pelt, perfume, luggage, handbags, billfolds, or sports clothing sold for exclusive use in a sporting activity.

The exemption granted for clothing was included in the sales and use tax statutes enacted in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$142,100,000	$149,000,000	$157,000,000	$164,800,000

4.03 PUBLICATIONS

Minnesota Statutes, Section 297A.25, Subd. 1(i)

Publications regularly issued at least once every three months, such as newspapers, journals, and magazines, are exempt from the sales and use tax. As of July 1, 1983, this exemption does not apply to magazines and periodicals sold over the counter (non-subscription).

This provision was included in the original sales and use tax enacted in 1967. It was last changed in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,000,000	$11,700,000	$12,400,000	$13,400,000

4.04 DRUGS AND MEDICINES

Minnesota Statutes, Section 297A.25, Subd. 1(b)
Minnesota Rules, Part 8130.4800

Prescription and nonprescription drugs and medicines used for human beings are exempt from the sales and use tax. The exemption applies to products used in the cure, mitigation, treatment, or prevention of illness and in the preservation of health. Cosmetics or toiletries are not exempt. Minnesota Rules, Part 8130.4800 contains lists of exempt and taxable products.

This provision was enacted in 1967 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$38,500,000	$42,800,000	$47,500,000	$52,800,000

4.05 PRESCRIPTION EYEGLASSES

Minnesota Statutes, Section 297A.25, Subd. 1(b)

Sales of prescription eyeglasses and contact lenses are exempt from the sales and use tax.

This provision was enacted in 1967 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,800,000	$5,000,000	$5,100,000	$5,300,000

4.06 THERAPEUTIC AND PROSTHETIC DEVICES

Minnesota Statutes, Section 297A.25, Subd. 1(b)
Minnesota Rules, Part 8130.4800

Minnesota Rules, Part 8130.4800 specifies the requirements that a therapeutic or prosthetic device must meet in order to be exempt from the sales tax.

A therapeutic device must not only be useful in the preservation of health, but it must also serve to cure or heal. It must serve to alleviate human injury, illness, or disease, either directly or by administering a curative agent. Examples of exempt items are hypodermic syringes, oxygen tents, vaporizers, resuscitators, hospital beds, and equipment and supplies necessary for dialysis treatment.

A prosthetic device must be used to replace an injured, diseased, or missing part of the human body, either temporarily or permanently.

This provision was enacted in 1967 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$3,400,000	$3,900,000	$4,500,000	$5,100,000

4.07 FEMININE HYGIENE ITEMS

Minnesota Statutes, Section 297A.25, Subd. 1(y)

Consumer purchases of all feminine hygiene items, including sanitary napkins, tampons, and similar products, are exempt from the sales and use tax.

This exemption became effective July 1, 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,600,000	$1,600,000	$1,700,000	$1,800,000

4.08 TEXTBOOKS

Minnesota Statutes, Section 297A.25, Subd. 1(t)

Sales of textbooks to students are exempt from the sales and use tax, provided that the books are required for a course of study at a public or private school, college, university, business, or trade school.

This provision was enacted in 1973.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,500,000	$1,600,000	$1,700,000	$1,800,000

4.09 MOTOR FUELS

Minnesota Statutes, Section 297A.25, Subd. 1(f)

The gross receipts from the sale of and storage, use, or consumption of petroleum products taxed under the motor fuels tax (Minnesota Statutes, Chapter 296) are exempt from the sales and use tax. The exemption applies whether or not any part of the motor fuels tax is subsequently refunded.

The exemption applies to gasoline and special fuel for highway, aviation, motorboat, or snowmobile use.

This exemption was enacted in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$148,800,000	$133,500,000	$136,100,000	$141,900,000

4.10 PETROLEUM PRODUCTS USED IN THE IMPROVEMENT OF AGRICULTURAL LAND

Minnesota Statutes, Section 297A.25, Subd. 1(f)

Gross receipts from the sale of petroleum products used in the improvement of agricultural land are exempt from the sales and use tax. Products qualifying for exemption are those used in constructing, maintaining, and repairing drainage ditches, tile drainage systems, grass waterways, water impoundment, and other erosion control structures.

This provision was enacted in 1985, effective for sales made after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

4.11 RACE HORSES

Minnesota Statutes, Section 297A.01, Subd. 3(h)

Sales of race horses born and bred in Minnesota are exempt from the sales and use tax. The exemption also extends to certain fees associated with sales, such as claiming fees and breeding fees.

Sales of Minnesota race horses became exempt from the sales and use tax on April 1, 1984, approximately six months after voters had ratified an amendment to the Minnesota Constitution which made pari-mutuel betting on horse races legal in this state.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$600,000	$800,000	$1,000,000	$1,400,000

4.12 CASKETS AND BURIAL VAULTS

Minnesota Statutes, Section 297A.25, Subd. 1(p)

The gross receipts from the sale of caskets, burial vaults, and urns used for human burial or cremation purposes are exempt from the Minnesota sales and use tax.

This provision was enacted in 1967 and has not been changed.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,100,000	$2,200,000	$2,200,000	$2,300,000

4.13 ACCESSORY TOOLS

Minnesota Statutes, Section 297A.25, Subd. 1(h)

As a general rule, machinery, equipment, tools, and implements used in industrial production are subject to the Minnesota sales and use tax. This provision exempts accessory tools, equipment, and other short-lived items which meet three criteria: are separate units detachable from machinery; are used to produce a direct effect on a product; and have an ordinary useful life of less than twelve months.

Items exempt under this provision include drill bits, grinding and abrasive wheels, saw blades, printing plates, dies, jigs, taps, patterns, and molds.

The exemption for accessory tools became effective January 1, 1974.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$13,800,000	$14,300,000	$14,900,000	$15,600,000

4.14 CAPITAL EQUIPMENT PURCHASES (DISTRESSED COUNTIES)

Minnesota Statutes, Sections 297A.15 and 297A.257

The purchase of capital equipment placed in service in connection with the construction of a new or expanded manufacturing facility in a distressed county is exempt from the sales tax if certain conditions are met. Only purchases in excess of $100,000 in a calendar year are exempt. To qualify as an expansion, either the production must be increased by at least 20% or the capital investment made within a twelve-month period must exceed $25 million.

A county may be designated annually as distressed by the commissioner of energy and economic development if it has a one-year unemployment rate of 10% or more, or, if 20% or more of the county's economy is dependent upon agriculture, it has an unemployment rate greater than 110% of the state average.

Capital equipment in a new or expanding manufacturing facility is normally subject to a special 4% rate, as explained in Item 4.48. Therefore, the estimates measure the difference between the exemption and the 4% rate.

This provision was enacted in 1985, effective for sales made after August 1, 1985. The authority of the commissioner of energy and economic development to designate distressed counties expires June 30, 1989.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$0	$2,000,000	$4,800,000	$4,100,000

4.15 CONSTRUCTION MATERIALS AND SUPPLIES (DISTRESSED COUNTIES)

Minnesota Statutes, Sections 297A.15, Subd. 5 and 297A.257, Subd. 2a

The purchase of construction materials and supplies used in constructing a new or expanding an existing manufacturing facility in a distressed county is exempt from the sales tax if the total capital investment made within a three-year period exceeds $75 million.

A county may be designated annually as distressed by the commissioner of energy and economic development if it has a one-year unemployment rate of 10% or more, or, if 20% or more of the county's economy is dependent upon agriculture, it has an unemployment rate greater than 110% of the state average.

This exemption was enacted in 1986, effective for purchases made after May 1, 1986. However, no refunds can be paid due to this exemption before July 15, 1987. The authority of the commissioner of energy and economic development to designate distressed counties expires June 30, 1989.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$0	$0	$2,800,000	$1,800,000

4.16 CONSTRUCTION MATERIALS OR EQUIPMENT (ENTERPRISE ZONES)

Minnesota Statutes, Section 273.1314, Subd. 9(a)

An exemption from the sales and use tax may be authorized by the commissioner of revenue for sales of construction materials or equipment used in a designated enterprise zone. Only those sales made after an approved application for the enterprise zone was made may qualify for the exemption.

This provision was enacted in 1983 and was last changed in 1985. This exemption, along with the enterprise zone program, is scheduled to expire on December 31, 1996.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$200,000	$200,000

4.17 REPAIR AND REPLACEMENT PARTS FOR FARM MACHINERY

Minnesota Statutes, Section 297A.25, Subd. 1(bb)

Repair and replacement parts, except tires, used for maintenance or repair of farm machinery are exempt from the sales and use tax. To qualify, the part must replace a farm machinery part assigned a specific or generic part number by the manufacturer of the machinery.

This exemption was enacted in 1985, effective for sales made after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$11,400,000	$11,200,000	$11,800,000	$12,100,000

4.18 PERSONAL PROPERTY BROUGHT INTO MINNESOTA

Minnesota Statutes, Section 297A.25, Subd. 3

When individuals, businesses, or corporations move into Minnesota, all articles of tangible personal property they bring with them are exempt from the Minnesota use tax. Unless the Minnesota sales tax had previously been levied on them, these items would normally be subject to the use tax when brought into the state. The estimates are reduced by the amount of sales tax paid to other states as explained in Item 4.51.

This provision was enacted in 1967 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,900,000	$5,100,000	$5,300,000	$5,500,000

4.19 PACKING MATERIALS

Minnesota Statutes, Section 297A.25, Subd. 1(e)

Sales of packing materials used to pack and ship household goods are exempt from the sales and use tax. The packing materials must be used to ship goods to an out-of-state destination and must not be returned to Minnesota except as to pass through the state in the course of interstate commerce.

This exemption was enacted in 1973.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

4.20 OUT-OF-STATE LEASES OF VEHICLES

Minnesota Rules, Part 8130.0400, Subp. 2

In general, payments made pursuant to leases of tangible personal property are subject to the sales and use tax if the property is used in Minnesota. However, the tax is not imposed upon lease payments made in Minnesota pursuant to a lease executed in another state for a drive-it-yourself automobile, trailer, or other vehicle.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

4.21 GOODS SHIPPED OR TRANSPORTED OUT OF STATE

Minnesota Statutes, Section 297A.25, Subd. 1(d)

Goods which are sold in Minnesota, delivered to a purchaser in Minnesota, transported outside Minnesota by the purchaser without intermediate use, and used in a trade or business outside Minnesota are exempt from the sales and use tax if one of the following conditions is met:

1. the property is not subject to the sales tax in the state or country to which it is transported; or
2. the property is to be used in the other state or country as part of a maintenance contract; or
3. the other state allows a similar exemption for taxable property purchased there and transported to Minnesota for use.

If the state to which the property is transported imposes a use tax, then that state's use tax rate applies. If the rate is lower than the Minnesota rate, a revenue loss occurs. If the other state imposes no use tax, then the Minnesota rate applies.

Although property used in interstate commerce is also exempt from the sales and use tax, it is not included in the estimates because the federal government prohibits the state from taxing interstate commerce.

This provision was enacted in 1967 and last changed in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

4.22 RESOURCE RECOVERY EQUIPMENT

Minnesota Statutes, Section 297A.25, Subd. 1(aa)

The gross receipts from the sale of equipment used to process solid or hazardous waste at a qualifying resource recovery facility are exempt from the sales and use tax.

This provision was enacted in 1984 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$300,000	$300,000	$300,000

4.23 CLUB DUES

Minnesota Rules, Part 8130.0900, Subp. 5

Generally taxable under the Minnesota sales and use tax are the sales of admissions to amusements and athletic events and the use of amusement devices or athletic facilities. This provision grants an exemption for membership dues paid to country clubs, curling clubs, tennis clubs, and other similar clubs where a portion of the dues payments may represent fees for the use of or admission to an athletic or amusement facility.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$6,000,000	$6,400,000	$6,800,000	$7,300,000

4.24 SERVICES

Minnesota Statutes, Section 297A.01, Subd. 3 and 4

Services could properly be considered outside the tax base of the sales and use tax, and therefore the exemption of services would not be a tax expenditure. For purposes of this study, however, services are included in the tax base because some services are taxed.

It should be noted that the exemption of some services, such as sewer, water, and long-distance telephone service, are dealt with as separate tax expenditures because they are dealt with separately in the law. The total fiscal impact for this item includes only those services found in the list below.

Although there is no statutory provision which specifically excludes services from the sales and use tax, services as a class have not been subject to taxation since the sales tax was imposed in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$503,300,000	$551,200,000	$604,700,000	$665,400,000

The following is a breakdown of services into eleven categories based on the Standard Industrial Classification. The totals above and the various subtotals below may not add due to rounding. It should also be noted that all estimates have been adjusted so they do not include services which would remain exempt from tax, even if services in general were subject to the sales and use tax. Services provided to the federal government or to nonprofit organizations are examples of services which would remain exempt due to other provisions of the law.

		Fiscal Year Impact			
		1986 (000's)	1987 (000's)	1988 (000's)	1989 (000's)
A.	Personal Services (total)	$31,300	$33,800	$36,500	$39,400
	1. Laundry, Cleaning and Garment Services	10,400	11,200	12,100	13,100
	2. Beauty Shops	9,100	9,800	10,600	11,400
	3. Barber Shops	2,100	2,200	2,400	2,600
	4. Shoe Repair	300	400	400	400
	5. Funeral Services and Crematories	5,200	5,600	6,100	6,600
	6. Miscellaneous Personal Services	4,200	4,600	4,900	5,300
B.	Legal Services (total)	$41,500	$45,900	$50,800	$56,300
C.	Engineering, Architectural, and Surveying Services (total)	$27,200	$30,100	$33,300	$37,000
D.	Business Services (total)	$78,500	$87,700	$97,200	$107,800
	1. Advertising	17,700	19,800	21,900	24,300
	2. Management, Consulting, and Public Relations Services	21,200	23,700	26,300	29,100
	3. Tax Exempt Research Services	800	900	1,000	1,100
	4. Services to Dwellings and Other Buildings	7,900	8,800	9,800	10,900
	5. Computer and Data Processing	17,200	19,200	21,300	23,600
	6. Other Business Services	13,700	15,300	16,900	18,800
E.	Accounting (total)	$27,100	$30,300	$33,600	$37,200
F.	Auto Services (total)	$17,400	$19,000	$20,800	$22,500
	1. Parking Lots and Structures	1,500	1,600	1,800	1,900
	2. Automotive Repair Services	13,200	14,400	15,700	17,100
	3. Automotive Services Other Than Repair	2,700	3,000	3,300	3,500

		Fiscal Year Impact			
		1986 (000's)	1987 (000's)	1988 (000's)	1989 (000's)
G.	**Miscellaneous Repair Services (total)**	**$4,400**	**$4,700**	**$5,200**	**$5,500**
	1. Electrical and Electronic Repair	300	300	400	400
	2. Watch, Clock, and Jewelry Repair	100	100	100	100
	3. Reupholstery and Furniture Repair	400	400	500	500
	4. Other Miscellaneous Repair Services	3,600	3,900	4,200	4,500
H.	**Health Services (total) - Except Hospitals**	**$178,100**	**$194,000**	**$211,900**	**$232,000**
	1. Physicians	58,400	63,600	69,400	76,100
	2. Optometrists	2,600	2,800	3,000	3,300
	3. Dentists	23,800	25,900	28,300	31,000
	4. Osteopathic Physicians	100	100	200	200
	5. Chiropractors	3,900	4,300	4,700	5,100
	6. Nursing and Personal Care Facilities	15,000	16,300	17,800	19,500
	7. Other Health Services	8,000	8,800	9,600	10,400
	8. Tax Exempt Health Services	64,900	70,700	77,200	84,600
	9. Veterinarians	1,400	1,500	1,700	1,800
I.	**Selected Educational Services (total)**	**$28,400**	**$31,000**	**$35,100**	**$41,200**
	1. Private Elementary and Secondary Schools	5,800	6,300	7,100	8,400
	2. Colleges, Universities, Professional Schools, and Junior Colleges	19,000	20,800	23,600	27,600
	3. Libraries, Vocational, Others	2,700	2,900	3,300	3,900
	4. Tax Exempt Educational Services	900	1,000	1,100	1,300
J.	**Social Services (total)**	**$62,200**	**$67,100**	**$72,300**	**$78,000**
	1. Child Day Care Services	3,300	3,600	3,900	4,200
	2. Individual and Family Social Services, Job Training and Rehabilitation Services, Residential Care, and Social Services Not Classified Elsewhere	16,100	17,400	18,700	20,200
	3. Tax Exempt Social Services	41,300	44,500	48,000	51,800
	4. Other Services	1,500	1,600	1,700	1,800
K.	**Transportation (total)**	**$7,200**	**$7,600**	**$8,000**	**$8,500**
	1. Taxi Services	2,900	3,100	3,300	3,500
	2. Intercity Bus Services	1,300	1,400	1,400	1,500
	3. Other Local Transit Services	3,000	3,100	3,300	3,500

4.25 RESIDENTIAL SEWER SERVICES

Minnesota Statutes, Section 297A.01, Subd. 3(f)

The furnishing of sewer services to residential customers is exempt from the Minnesota sales and use tax.

This exemption was enacted in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,200,000	$5,400,000	$5,600,000	$5,900,000

4.26 RESIDENTIAL WATER SERVICES

Minnesota Statutes, Section 297A.01, Subd. 3(f)

The furnishing of water services to residential customers is specifically exempt from the Minnesota sales and use tax.

This provision was enacted in 1979 and has remained unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$3,200,000	$3,400,000	$3,500,000	$3,700,000

4.27 RESIDENTIAL HEATING FUELS

Minnesota Statutes, Section 297A.25, Subd. 1(v)

Generally, sales of electricity, gas, water, steam, or other energies for use or consumption within Minnesota are taxable. This provision, however, exempts from the sales and use tax any fuel oil, coal, wood, steam, hot water, propane gas, or L.P. gas sold to residential customers for residential use. Additionally, purchases of natural gas or electricity by residential customers who use natural gas or electricity for their primary source of residential heat are exempt from November 1 through April 30.

This provision was enacted in 1978 and was expanded in 1984 to include hot water heat sold for residential use.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$50,400,000	$47,300,000	$47,300,000	$49,500,000

4.28 INTERSTATE TELEPHONE SERVICE

Minnesota Statutes, Section 297A.01, Subd. 3(f)

Although local exchange telephone service and intrastate toll service are subject to the sales tax, interstate long distance service is exempt from the tax.

This provision was enacted in 1967 and last changed in 1977.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$22,900,000	$24,000,000	$25,200,000	$26,500,000

EXEMPTIONS - SALES TO PARTICULAR GROUPS

4.29 SALES TO LOCAL GOVERNMENTS

Minnesota Statutes, Sections 297A.25, Subd. 1(j) and 297A.258

The sale of tangible personal property to the United States or to a state, or their agencies, instrumentalities, or political subdivisions, is exempt from the Minnesota sales and use tax. This exemption is a tax expenditure to the extent that it costs the state money and to the extent that the state could tax the transaction if it chose to do so. Therefore, the estimates measure only the fiscal impact of exempting Minnesota's local and regional governments. This exemption also applies to a private vendor treated as a municipality under a service contract. It should be noted that these estimates do not include items such as food, motor vehicles, and motor fuels which would remain exempt due to other provisions even if local government purchases were generally subject to taxation.

This exemption was enacted in 1967 and last revised in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$41,100,000	$43,100,000	$45,300,000	$47,500,000

4.30 SALES TO NONPROFIT ORGANIZATIONS

Minnesota Statutes, Section 297A.25, Subd. 1(o)
Minnesota Rules, Part 8130.6200

According to Minnesota Statutes, Section 297A.25, Subd. 1(o), ". . .the sale of tangible personal property to, and storage, use, or other consumption of such property by, any corporation, society, association, foundation, or institution organized and operated exclusively for charitable, religious, or educational purposes. . ." is exempt from the sales and use tax. The property purchased must be used in the performance of the charitable, religious, or educational function of the organization.

It should be noted that the estimates below do not include: sales to governments, which are discussed in Item 4.29; sales to veterans' organizations, discussed in Item 4.31; or sales of items such as food and services which are exempt due to other provisions of this tax.

This provision was included in the sales and use tax when it was enacted in 1967. In 1979 the definition of nonprofit organizations was broadened to include senior citizens' groups operated for nonprofit purposes. The most recent change was in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$26,800,000	$29,600,000	$32,800,000	$36,400,000

4.31 SALES TO VETERANS' ORGANIZATIONS

Minnesota Statutes, Section 297A.25, Subd. 1(x)

Purchases of tangible personal property and the storage, use, or consumption of such property by an organization of military service veterans or an auxiliary unit are exempt from taxation provided:

1. the group is organized in Minnesota and is exempt from income taxes under federal law; and
2. the property is used for charitable, civic, educational, or nonprofit uses and not for social, recreational, pleasure, or profit uses.

This provision was enacted in 1980.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

4.32 SALES OF BUILDING MATERIALS TO DISABLED VETERANS

Minnesota Statutes, Section 297A.25, Subd. 1(s)

Building materials used in constructing or remodeling a disabled veteran's residence are exempt from the sales and use tax if the project is financed in whole or in part by the U.S. Government in accordance with Title 38, United States Code, Sections 801 to 805. This exemption is provided in the form of a refund to the veteran for sales tax paid.

This exemption was enacted in 1971.

Fewer than ten claims for refund are filed annually under this provision.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

4.33 NEW SATELLITE BROADCASTING FACILITY

Minnesota Statutes, Section 297A.253

All materials, supplies, and equipment used or consumed in the construction and equipping of a new, FCC licensed, direct satellite broadcasting facility within Minnesota are exempt from the sales and use tax.

This exemption was enacted in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$0	$200,000	$600,000

4.34 TELEPHONE CENTRAL OFFICE EQUIPMENT (REPEALED)

Minnesota Statutes 1984, Section 297A.25, Subd. 1(n)

The gross receipts from the sale of telephone central office telephone equipment used in furnishing intrastate and interstate telephone service to the public are exempt from the Minnesota sales and use tax.

This exemption was enacted in 1971. In 1985 it was repealed for sales made after December 31, 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,200,000	$2,200,000	$0	$0

4.35 MILL LINERS AND GRINDING RODS AND BALLS

Minnesota Statutes, Section 297A.25, Subd. 1(n)

The gross receipts from the sale of and the storage, use, or consumption by taconite mining companies of mill liners, grinding rods, and grinding balls are exempt from the sales and use tax. To qualify, the items must be substantially consumed in the production of taconite, the material of which primarily is added to and becomes a part of the material being processed.

The estimates do not include items that would qualify under the exemption for accessory tools (Item 4.13).

This exemption was enacted in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

4.36 RAILROAD ROLLING STOCK

Minnesota Statutes, Sections 270.89 and 297A.25, Subd. 1 (l)
Minnesota Rules, Part 8130.5900

The gross receipts from the sales of rolling stock to railroads are exempt from the sales and use tax. Rolling stock is defined as the portable or moving apparatus and machinery of a railroad which are intended for use on railroad tracks. Exempted property includes engines, cars, tenders, coaches, and the parts necessary for the repair and maintenance of such property.

This exemption was enacted in 1967 and last changed in 1979.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,000,000	$1,000,000	$1,100,000	$1,100,000

4.37 AIRFLIGHT EQUIPMENT

Minnesota Statutes, Section 297A.25, Subd. 1 (m)
Minnesota Rules, Part 8130.6000

The gross receipts from the sales of airflight equipment to airline companies taxed under the airflight property tax are exempt from the sales and use tax. Airflight equipment includes airplanes, communications and navigational equipment, flight simulators, and parts necessary for the repair and maintenance of airflight equipment.

This exemption was enacted in 1967 and last changed in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$14,200,000	$23,300,000	$20,700,000	$20,800,000

EXEMPTIONS - SALES BY PARTICULAR GROUPS

4.38 ISOLATED OR OCCASIONAL SALES

Minnesota Statutes, Section 297A.25, Subd. 1(k)

Although sales of tangible personal property in Minnesota are generally subject to the sales and use tax, isolated or occasional sales made by persons not engaged in selling such property in the normal course of business are exempt. The following singular or infrequent sales are examples of those qualifying for exemption:

- the sale of a used lawn mower to a neighbor;
- sales made by a fiduciary in the liquidation of an estate;
- the sale of an entire business by the owner (except that the transfer of stock or inventory is taxable); and
- garage sales, where the items sold have not been specifically gathered for resale.

This provision was enacted in 1967 and last revised in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$28,100,000	$28,600,000	$29,200,000	$29,900,000

4.39 SALES BY AUCTIONEERS AND BROKERS

Minnesota Statutes, Section 297A.25, Subd. 1(k)
Minnesota Rules, Part 8130.5800, Subp. 2B

When an auctioneer or broker sells items for someone who is not in the business of selling that type of merchandise, the gross receipts from the sale are exempt from the sales tax as an isolated or occasional sale. However, the sale is taxable if the items would have been taxable if they had been sold by the owner or if the auctioneer or broker purchases the items to sell at an auction.

Isolated or occasional sales have been exempt since the sales tax was enacted in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,700,000	$1,700,000	$1,800,000	$1,900,000

4.40 INSTITUTIONAL MEALS

Minnesota Statutes, Section 297A.01, Subd. 3(c)
Minnesota Rules, Part 8130.0800

As a rule, prepared meals offered for sale are subject to the sales and use tax. This provision exempts from the sales tax meals and drinks furnished, prepared, or served by: hospitals, nursing homes, sanitariums, and senior citizens' homes; and meals and drinks served at public and private schools, universities, and colleges.

This provision was enacted as part of the sales and use tax law in 1967 and was last changed in 1975 when it was expanded to include congregate dining, the home delivery of meals, and other programs which provide meals to senior citizens or the handicapped.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$16,000,000	$16,600,000	$17,400,000	$18,100,000

4.41 ADMISSION FEES TO RECREATIONAL AREAS

Minnesota Rules, Part 8130.0900, Subp. 8

Although an admission charge to any place of amusement is taxable, recreational areas which provide no facilities other than parking lots, fire pits, docks, tables, and equipment necessary for the preservation of the area are not considered amusement areas. Admission charges to certain campgrounds and other recreational areas are therefore exempt from the sales and use tax.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$800,000	$900,000	$900,000	$1,000,000

4.42 ADMISSION TO ARTISTIC PERFORMANCES

Minnesota Statutes, Section 297A.25, Subd. 1(w)

In general, an admission charge is a taxable sale. Taxable admission charges include those for concerts, stage plays, and dances. This provision exempts from taxation the sale of tickets or admissions to events which provide opportunities for participation in the creation, performance, or appreciation of the arts. Only those artistic events sponsored by organizations which are exempt from income taxes, for example churches and charities, qualify under this provision.

This exemption was enacted in 1980 and remains substantially unchanged since then.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,100,000	$1,100,000	$1,200,000	$1,200,000

4.43 ADMISSION TO SCHOOL-SPONSORED EVENTS

Minnesota Statutes, Section 297A.25, Subd. 1(cc)

The gross receipts from the sale of tickets or admissions to regular season school games, events, and activities of elementary and secondary schools are exempt from the sales and use tax.

This exemption was enacted in 1985, effective for sales made after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$300,000	$300,000	$300,000	$300,000

4.44 FUNDRAISING SALES BY NONPROFIT ORGANIZATIONS

Minnesota Statutes, Section 297A.256

Certain fundraising sales by nonprofit organizations are exempt from the Minnesota sales tax.

The exemption applies to:

1. Fundraising sales by an organization that: a) is an educational or social organization for people age eighteen and under or is a senior citizen group that is exempt from the sales tax; and b) has gross annual receipts from fundraising that do not exceed $10,000.

2. Sales, including personal property, admission charges, and meals, at fundraising events sponsored by a nonprofit organization when the entire proceeds, except necessary expenses, go exclusively for charitable, religious, or educational purposes. This exemption does not apply to bingo or other gambling activities. The exemption is limited to no more than 24 days a year.

This provision was enacted in 1985, effective for sales made after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,900,000	$2,000,000	$2,100,000	$2,200,000

4.45 CANDY SALES BY ORGANIZATIONS WHICH PROVIDE SERVICES TO MINORS

Minnesota Statutes, Section 297A.25, Subd. 1(a) (i)

Candy and candy products are exempt from the sales tax when sold for fundraising purposes by a nonprofit organization which provides educational and social activities for young people age eighteen and under.

This exemption was enacted in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

SPECIAL RATES / REDUCED SALES PRICE

4.46 TWO PERCENT RATE FOR FARM MACHINERY

Minnesota Statutes, Sections 297A.01, Subd. 15; 297A.02, Subd. 2; and 297A.14

New or used farm machinery is taxed at a 2% sales and use tax rate rather than the general 6% rate. Farm machinery is defined by statute as ". . . machinery, equipment, implements, accessories and contrivances used directly and principally in the production for sale, but not including the processing, of livestock, dairy animals, dairy products, poultry and poultry products, fruits, vegetables, forage, grains and bees and apiary products."

The exemption of farm machinery repair and replacement parts is estimated separately in Item 4.17.

The special rate for farm machinery was enacted in 1981 when the general sales and use tax rate was raised from 4% to 5%. In 1985 the rate was reduced to 2%, effective for sales made after June 30, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$13,700,000	$13,400,000	$14,200,000	$14,600,000

4.47 TWO PERCENT RATE FOR LOGGING EQUIPMENT

Minnesota Statutes, Sections 297A.01, Subd. 15; 297A.02, Subd.2; and 297A.14

New and used logging equipment is subject to a 2% sales and use tax rate, rather than the general 6% rate. Included in the exemption are chain saws used only for logging if the engine displacement equals or exceeds five cubic inches.

The reduced rate for logging equipment was enacted in 1984 at 4% and was reduced to 2% in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$200,000	$200,000

4.48 FOUR PERCENT RATE FOR CAPITAL EQUIPMENT SOLD TO NEW OR EXPANDING INDUSTRIES

Minnesota Statutes, Sections 297A.01, Subd. 16; 297A.02, Subd. 2; and 297A.15, Subd. 5

Certain capital equipment and machinery purchases are subject to a 4% sales and use tax rate rather than the general 6% rate. In order to qualify, the capital equipment, or the materials necessary to construct and install it, must be used by the purchaser or lessee to establish or expand a manufacturing, fabricating, or refining facility in the state. This reduced rate does not extend to: 1) equipment purchased as replacements; 2) replacement or repair parts; or 3) machinery or equipment used to extract, receive, or store raw materials.

Capital equipment which is exempt from the sales and use tax because it is used in a distressed county is not included in the estimates below, but it is estimated separately in Item 4.14.

This provision was enacted in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,200,000	$4,400,000	$3,200,000	$3,900,000

4.49 FOUR PERCENT RATE FOR SPECIAL TOOLING

Minnesota Statutes, Sections 297A.01, Subd. 17; 297A.02, Subd. 2; and 297A.14

Special tooling, defined as "tools, dies, jigs, patterns, gauges, and other special tools which have value and use only for the buyer and for the use for which it is made", is subject to a 4% sales and use tax rate rather than the general 6% rate. To qualify for the reduced rate, items must be special ordered and produced in accordance with buyer specifications. Some special tools are also classified as accessory tools, in which case they are exempt from any sales tax, and they are included in Item 4.13.

The reduced rate for special tooling was enacted in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

4.50 TAXES IMPOSED BY THE UNITED STATES GOVERNMENT

Minnesota Statutes, Section 297A.01, Subd. 8

When computing the Minnesota sales and use tax, the retail sales price of a good is reduced by any federal tax imposed upon the consumer or retailer. The reduction does not apply to a manufacturers' or importers' excise tax. The federal excise tax on communications (telephone and teletype) is excluded from the taxable sales price under this provision. Because long distance telephone service is exempt from the sales and use tax, the estimates include only intrastate and local exchange telephone services.

This provision was enacted in 1967 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,900,000	$2,000,000	$2,100,000	$2,100,000

4.51 TAX PAID TO OTHER STATES

Minnesota Statutes, Section 297A.24

If a sales or use tax has previously been paid on an article of tangible personal property to another state at a rate lower than the Minnesota rate, then the Minnesota rate applicable to that article is the difference between the Minnesota rate and the other state's rate. In practice, the reduced rate is the equivalent of providing a credit to taxpayers for taxes paid to other states. If the other state's rate is equal to or higher than Minnesota's rate, no Minnesota sales and use tax is imposed.

The estimates below are based on actual use tax returns filed. No attempt was made to estimate those cases technically subject to the reduced rate for which no Minnesota use tax return was filed.

This provision was enacted in 1967 and was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$600,000	$600,000	$600,000	$600,000

4.52 PRICE REDUCED BY VALUE OF TRADE IN

Minnesota Statutes, Section 297A.01, Subd. 8
Minnesota Rules, Part 8130.1500

The sales price is reduced by any amount allowed as credit for tangible personal property taken in trade for resale. To qualify for the exclusion, the property must be taxable under the sales and use tax law or the motor vehicle excise tax law and of the type of property normally sold in the regular course of the retailer's business.

This provision was enacted in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$3,800,000	$4,000,000	$4,200,000	$4,400,000

CHAPTER 5: MOTOR VEHICLE EXCISE TAX

Collections and History

Total revenues from the motor vehicle excise tax were $207.6 million in fiscal year 1986. Prior to fiscal year 1985, all revenues from this tax went into the state general fund. The distribution of the receipts has been modified as follows:

Fiscal Years	General Fund	Highway User Tax Distribution Fund	Transit Assistance Fund
1985	75%	18.75%	6.25%
1986 - 1987	100	0	0
1988 - 1989	50	37.50	12.50
1990 - 1991	25	56.25	18.75
1992 and after	0	75.00	25.00

The motor vehicle excise tax was enacted during the 1971 legislative session in lieu of the general sales tax on motor vehicles. Motor vehicles were exempted from the sales tax at the same time.

When the tax became effective on January 1, 1972, the rate was 4%. The rate was increased to 5% on July 1, 1981, and to the current 6% rate on July 1, 1983.

Tax Base

The tax base for the motor vehicle excise tax is the purchase price of a motor vehicle when ownership is transferred and the motor vehicle is required to be registered under the laws of Minnesota. The transfer of a motor vehicle to a dealer for resale in the regular course of business is not within the base. Regardless of the number of times a vehicle is sold, each transfer of ownership is in the tax base. For a vehicle transferred by gift or for a nominal or no monetary consideration, the purchase price is deemed to be the average value of similar motor vehicles.

Computation of the Tax

The motor vehicle excise tax is imposed when a motor vehicle required to be registered in Minnesota is purchased or acquired, either in or outside Minnesota. The 6% rate is applied to the purchase price, which is defined as the total consideration valued in money, whether paid in money or otherwise. When one motor vehicle is taken in trade on another vehicle, the trade-in value is deducted in arriving at the purchase price. In the case of a gift or a transfer for a nominal or no monetary consideration, the average value of similar motor vehicles is used as the purchase price.

The tax is paid to the motor vehicle registrar, and it must be paid before registration plates or certificate can be issued.

EXEMPTIONS

5.01 VEHICLES ACQUIRED BY INHERITANCE

Minnesota Statutes, Section 297B.01, Subd. 7(a)

When any vehicle is transferred by inheritance or by bequest of a decedent, the transfer is exempt from the motor vehicle excise tax.

This provision was enacted in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$600,000	$600,000	$300,000	$300,000
Highway User Tax Distribution Fund	0	0	225,000	225,000
Transit Assistance Fund	0	0	75,000	75,000
Total - All Funds	$600,000	$600,000	$600,000	$600,000

5.02 OUT-OF-STATE ACQUISITIONS

Minnesota Statutes, Section 297B.03 (2)

When a person moves to Minnesota and establishes residency, any motor vehicle owned by that person which was purchased and titled in another state more than sixty days prior to the move is exempt from the Minnesota motor vehicle excise tax.

This provision was enacted in 1971 and remains substantially unchanged since that time.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,000,000	$1,100,000	$550,000	$600,000
Highway User Tax Distribution Fund	0	0	412,500	450,000
Transit Assistance Fund	0	0	137,500	150,000
Total - All Funds	$1,000,000	$1,100,000	$1,100,000	$1,200,000

5.03 TRANSFERS BETWEEN JOINT OWNERS

Minnesota Statutes, Section 297B.01, Subd. 7(b)

When the joint owner of a motor vehicle gratuitously transfers his or her interest to the other joint owner(s) of the vehicle, the transaction is exempt from the motor vehicle excise tax.

Enacted in 1971, this provision remains unchanged.

	Fiscal Year Impact 1986	1987	1988	1989
State General Fund	$500,000	$500,000	$250,000	$300,000
Highway User Tax Distribution Fund	0	0	187,500	225,000
Transit Assistance Fund	0	0	62,500	75,000
Total - All Funds	$500,000	$500,000	$500,000	$600,000

5.04 TRANSFERS BETWEEN SPOUSES, PARENTS AND CHILDREN, AND GUARDIANS AND WARDS

Minnesota Statutes, Section 297B.01, Subd. 7(c) and 8

Any transfer of a vehicle in the form of a gift (where no monetary consideration is involved) between spouses, a parent and a child, or a guardian and a ward is exempt from the motor vehicle excise tax. Since other transfers of vehicles by gift are taxed on the basis of the fair market value of the vehicle, this provision is a tax expenditure.

This exemption was enacted in 1971 and last changed in 1974.

	Fiscal Year Impact 1986	1987	1988	1989
State General Fund	$6,300,000	$6,500,000	$3,350,000	$3,500,000
Highway User Tax Distribution Fund	0	0	2,512,500	2,625,000
Transit Assistance Fund	0	0	837,500	875,000
Total - All Funds	$6,300,000	$6,500,000	$6,700,000	$7,000,000

5.05 TRANSFERS IN DIVORCE PROCEEDINGS

Minnesota Statutes, Section 297B.01, Subd. 7(d)

The transfer of a motor vehicle between husband and wife in a divorce proceeding, whether the transfer is voluntary or involuntary, is exempt from taxation. Because transfers between joint owners are exempt under another provision (Item 5.03), the estimates below include only those transfers involving vehicles previously registered to one person.

This provision was enacted in 1974.

	Fiscal Year Impact 1986	1987	1988	1989
State General Fund	$200,000	$200,000	$100,000	$100,000
Highway User Tax Distribution Fund	0	0	75,000	75,000
Transit Assistance Fund	0	0	25,000	25,000
Total - All Funds	$200,000	$200,000	$200,000	$200,000

5.06 CORPORATE AND PARTNERSHIP TRANSFERS

Minnesota Statutes, Section 297B.03 (4)

When an individual transfers a vehicle to a corporation in exchange for stock or securities, or to a partnership in exchange for an interest in the partnership, the transfer is exempt from the motor vehicle excise tax.

This provision was enacted in 1975.

	Fiscal Year Impact			
	1986	1987	1988	1989
Total - All Funds	Minimal	Minimal	Minimal	Minimal

5.07 SALES TO NONPROFIT ORGANIZATIONS

Minnesota Statutes, Section 297B.03 (1)

The purchase or use of a motor vehicle by a qualifying charitable, religious, or educational organization is exempt from the motor vehicle excise tax. Included in this exemption is use under a lease purchase agreement or installment sales contract.

This exemption was enacted in 1971 and last amended in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$1,000,000	$1,100,000	$550,000	$600,000
Highway User Tax Distribution Fund	0	0	412,500	450,000
Transit Assistance Fund	0	0	137,500	150,000
Total - All Funds	$1,000,000	$1,100,000	$1,100,000	$1,200,000

5.08 SALES TO LOCAL GOVERNMENTS

Minnesota Statutes, Section 297B.03 (1)

All motor vehicles purchased by the U.S. government, state governments, their agencies, instrumentalities, or political subdivisions are exempt from the Minnesota motor vehicle excise tax. Because the state is restricted from imposing taxes on the federal government, and because tax-exempt sales to Minnesota state agencies do not represent a net revenue loss to the state, their exemption from tax is not deemed a tax expenditure. The estimates below therefore measure only the impact of exempting vehicles purchased by all local governments and states other than Minnesota. This provision exempts automobiles, school and transit buses, trucks, and public safety vehicles such as ambulances and fire trucks.

This provision was enacted in 1971 and last changed in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$5,700,000	$5,900,000	$3,100,000	$3,200,000
Highway User Tax Distribution Fund	0	0	2,325,000	2,400,000
Transit Assistance Fund	0	0	775,000	800,000
Total - All Funds	$5,700,000	$5,900,000	$6,200,000	$6,400,000

5.09 SALES TO DISABLED VETERANS

Minnesota Statutes, Section 297B.03 (1)

Disabled veterans who purchase motor vehicles with funds provided, either in whole or in part, by the Veterans Administration under the provisions of 38 United States Code, Section 1901, are not required to pay any motor vehicle excise tax.

This provision was enacted in 1971 and has not been revised since that time.

	Fiscal Year Impact			
	1986	1987	1988	1989
Total - All Funds	Minimal	Minimal	Minimal	Minimal

REDUCED PURCHASE PRICE

5.10 FEDERAL EXCISE TAXES

Minnesota Statutes, Section 297B.01, Subd. 8

When computing the Minnesota motor vehicle excise tax, any federal taxes imposed on the retail sale of a vehicle may be eliminated from the purchase price. At the present time two federal excise taxes are levied upon new motor vehicles, both at a rate of 12% of retail price. The first is levied upon trucks in excess of 33,000 pounds gross vehicle weight, and the second is levied upon trailers or semitrailers in excess of 26,000 pounds gross vehicle weight.

This provision was enacted in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$100,000	$150,000
Highway User Tax Distribution Fund	0	0	75,000	112,500
Transit Assistance Fund	0	0	25,000	37,500
Total - All Funds	$200,000	$200,000	$200,000	$300,000

5.11 PRICE REDUCED BY VALUE OF TRADE IN

Minnesota Statutes, Section 297B.01, Subd. 8

When a motor vehicle is taken in trade as a credit or as part payment on another motor vehicle, the selling price is reduced by the amount of credit or trade-in value allowed. The 6% motor vehicle excise tax is applied to the reduced price. This provision applies to dealer sales and to sales between individuals.

The provision was enacted, along with the motor vehicle excise tax, in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$31,800,000	$32,900,000	$17,150,000	$17,850,000
Highway User Tax Distribution Fund	0	0	12,862,500	13,387,500
Transit Assistance Fund	0	0	4,287,500	4,462,500
Total - All Funds	$31,800,000	$32,900,000	$34,300,000	$35,700,000

PREFERENTIAL COMPUTATION

5.12 FLAT TAX ON OLDER CARS

Minnesota Statutes, Sections 297B.02, Subd. 2 and 297B.025

In lieu of the 6% motor vehicle excise tax, a flat tax of $10 is imposed on the transfer of a passenger automobile that is in at least its tenth year of vehicle life and has a resale value of less than $3,000. An automobile registered under the special provisions for collectors' vehicles does not qualify.

This provision was enacted in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,300,000	$4,400,000	$2,300,000	$2,400,000
Highway User Tax Distribution Fund	0	0	1,725,000	1,800,000
Transit Assistance Fund	0	0	575,000	600,000
Total - All Funds	$4,300,000	$4,400,000	$4,600,000	$4,800,000

CREDIT

5.13 CREDIT FOR TAXES PAID TO OTHER STATES

Minnesota Statutes, Section 297B.08

Minnesota allows a credit against the motor vehicle excise tax due at the time of vehicle registration for any sales, use, or excise tax paid on a vehicle to another state. The credit is allowed only if the other state has a similar provision allowing a credit for excise taxes paid in Minnesota.

Because vehicles purchased by nonresidents more than sixty days prior to moving into Minnesota are exempt (Item 5.02), this provision affects only purchases by nonresidents that occurred within the sixty days prior to the move and purchases by residents for any tax paid to another state.

This exemption was enacted in 1971 and was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$100,000	$100,000
Highway User Tax Distribution Fund	0	0	75,000	75,000
Transit Assistance Fund	0	0	25,000	25,000
Total - All Funds	$200,000	$200,000	$200,000	$200,000

CHAPTER 6: HIGHWAY FUELS EXCISE TAXES

Collections and History

The net revenues from the taxes on highway gasoline, special fuels, and compressed natural gas were $334 million in fiscal year 1986. All revenues from these taxes go into the highway user tax distribution fund.

Minnesota first imposed an excise tax on highway fuels in 1925 at a rate of 2¢ per gallon. Ten rate increases have occurred since then. The current rate of 17¢ per gallon has been in effect since January 1, 1984.

In 1985 an annual user permit fee was enacted for vehicles using compressed natural gas, to be imposed in lieu of the gasoline and special fuels taxes.

Tax Base

The tax base for the highway gasoline and special fuels taxes is motor fuel used in vehicles on Minnesota highways. Therefore, it is not considered a tax expenditure when the tax does not apply to off-road usage, such as for farming, or to out-of-state usage.

The tax base for the compressed natural gas user permit fee is the number of miles driven annually, based on the weight of the vehicle. Because the permit fee is imposed in place of the gasoline and special fuels taxes, the exemption of compressed natural gas vehicles from the gasoline and special fuels taxes is not considered a tax expenditure.

Computation of the Tax

The highway fuel tax rate is 17¢ per gallon and is imposed on gasoline and special fuels used on Minnesota highways. Motor carriers based in states other than Minnesota pay the road tax which is 17¢ per gallon for gasoline or special fuel used on Minnesota highways.

Lower rates may apply in areas bordering other states (Item 6.04) and lower effective rates apply to gasohol (Items 6.05 and 6.06). A person who purchases gasoline or special fuel in Minnesota and regularly drives in another state(s) may claim a refund for the tax paid on the fuel used in another state.

For gasoline, the distributor collects and remits the tax; for special fuel, the seller collects and remits the tax. A special fuel is defined as all combustible gases and liquid petroleum products or substitutes therefore, except gasoline.

Beginning October 1, 1985, vehicles using compressed natural gas pay an annual user permit fee in lieu of gasoline or special fuels taxes. The fee is based on the vehicle's weight and mileage in the preceding year as follows:

Gross Vehicle Weight	Fee per 1,000 Miles
Under 12,000 pounds	$9
12,001 - 18,000 pounds	$16
18,001 - 26,000 pounds	$23
26,001 - 36,000 pounds	$27
Over 36,000 pounds	$34

The maximum fee cannot exceed the fee charged for 22,000 miles. If the mileage figures are not available, the fee is based on 15,000 miles.

The fee is paid annually to the Department of Public Safety.

EXEMPTIONS

6.01 TRANSIT SYSTEMS OWNED BY LOCAL UNITS OF GOVERNMENT

Minnesota Statutes, Sections 296.02, Subd. 1a and 296.025, Subd. 1a

The highway fuel excise taxes are not imposed on gasoline and special fuel purchased by a transit system owned by one or more cities or towns.

This exemption was enacted in 1977 and has not been changed since that time.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$1,600,000	$1,600,000	$1,700,000	$1,700,000

6.02 RECIPROCAL AGREEMENTS FOR OUT-OF-STATE PURCHASES

Minnesota Statutes, Section 296.17, Subd. 6

In general, all gasoline and special fuels used in vehicles on Minnesota highways are subject to the Minnesota highway fuels excise taxes. Motor carriers based in states other than Minnesota pay the road tax for gasoline or special fuel purchased in another state and used on Minnesota highways.

This provision exempts motor carriers based in another state from paying the Minnesota road tax if the other state exempts Minnesota-based motor carriers from paying the road tax in that state. The only state with which Minnesota has this type of reciprocity agreement is North Dakota.

This exemption was enacted in 1961 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$500,000	$500,000	$500,000	$500,000

6.03 MOTOR VEHICLES NOT REQUIRING REGISTRATION (SPECIAL FUELS)

Minnesota Statutes, Sections 168.012, Subd. 1 and 296.18, Subd. 1

The highway special fuels tax is imposed on licensed motor vehicles, which are those requiring registration. Vehicles not requiring registration and therefore exempt from the special fuels tax include municipal fire apparatus, police patrols, and ambulances, the appearance of which is unmistakable. For example, an unmarked police car must be registered and is therefore not exempt.

This provision was enacted in 1951 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$200,000	$200,000	$200,000	$200,000

SPECIAL RATES

6.04 BORDER RATES

Minnesota Statutes, Section 296.02, Subd. 1

When the excise tax on highway fuel sold at a Minnesota service station located within 7.5 miles of a service station in a contiguous state is more than 3¢ higher than the tax levied on the same fuel in the bordering state, the Minnesota excise tax is reduced to 3¢ over the bordering state's rate for the affected Minnesota service station. The current excise tax rates for border states are:

	Highway Fuels Taxes - Rate Per Gallon	
State	Gasoline	Diesel
Minnesota	17.0¢	17.0¢
Iowa	16.0¢	18.5¢
North Dakota	13.0¢	13.0¢
South Dakota	13.0¢	13.0¢
Wisconsin	17.5¢	17.5¢

This provision was enacted in 1981 and last revised in 1983.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$200,000	$200,000	$200,000	$200,000

6.05 GASOHOL (OTHER THAN FOR GOVERNMENTAL UNITS AND SCHOOLS)

Minnesota Statutes, Section 296.02, Subd. 7

Agricultural alcohol gasoline, commonly referred to as "gasohol," is a gasoline blend of up to 10% agriculturally derived fermentation ethanol. Gasohol is taxed lower than gasoline, although the means of providing the preferential treatment changes over the four fiscal years covered in this report.

In fiscal year 1986, the tax rate for gasohol was 4¢ less than the rate for gasoline, or 13¢ per gallon instead of 17¢. In fiscal year 1987, the reduced rate is replaced by a credit. The credit is 25¢ per gallon of ethanol blended with gasoline to produce gasohol. This credit is the equivalent of a 2.5¢ reduced rate for gasohol because the blend nearly always contains 10% ethanol. The credit is reduced to 20¢ per gallon of ethanol, beginning in fiscal year 1988.

Preferential treatment for gasohol was first enacted in 1980 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$22,200,000	$5,400,000	$4,300,000	$4,300,000

6.06 GASOHOL FOR GOVERNMENTAL UNITS AND SCHOOLS

Minnesota Statutes, Section 296.02, Subd. 8

The tax on gasohol which is sold to governmental units and to schools is lower than the tax on gasoline. It is also lower than the tax on gasohol sold to the general public, as explained in Item 6.05.

In fiscal year 1986, the tax rate for gasohol sold to governmental units and to schools was 8¢ per gallon less than the rate for gasoline. Beginning in fiscal year 1987, the reduced rate is replaced by a credit of 80¢ per gallon of ethanol blended with gasoline to produce gasohol. The fiscal impact of the credit is virtually the same as the reduced rate because the blend is nearly always 10% ethanol.

This provision was enacted in 1983 and last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$200,000	$200,000	$200,000	$200,000

6.07 MAXIMUM RATE FOR HIGH MILEAGE VEHICLES (COMPRESSED NATURAL GAS)

Minnesota Statutes, Section 296.026, Subd. 2

The owner of a vehicle using compressed natural gas pays an annual user permit fee in lieu of the highway fuels excise tax. The fee is based on the vehicle's weight and its mileage in the preceding year. The maximum fee cannot exceed the fee charged for 22,000 miles. Therefore any annual usage above 22,000 miles is exempt from the fee.

This provision was enacted in 1985 along with the compressed natural gas permit fee.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	Minimal	Minimal	Minimal	Minimal

CHAPTER 7: ALCOHOLIC BEVERAGE TAXES

Collections and History

In fiscal year 1986, the revenues from the alcoholic beverage taxes were: $36.5 million from distilled spirits; $11.4 million from beer; and $3.6 million from wine. The total of $51.5 million was 1.1% of total state revenues. All revenues from these taxes are deposited in the state general fund.

An excise tax was first imposed on alcoholic beverages in Minnesota in 1934. The initial rates were: 60¢ per gallon for distilled spirits; $1 per barrel for 3.2% beer and $2 per barrel for strong beer; and wine rates ranging from 10¢ to 60¢ per gallon.

The tax rates were increased at various times from 1934 through 1971. Generally, the current rates were adopted in 1971, although the rates for distilled spirits and for sparkling wines have been lowered since then. Lower rates for wine produced by a Minnesota farm winery were enacted in 1980 but were repealed in 1985.

A credit for beer produced in Minnesota was enacted in 1973 and was amended in 1976 to equal $2 per barrel on the first 75,000 barrels of beer produced and sold in Minnesota each year. This Minnesota brewers' credit was repealed, effective August 1, 1985, and at the same time a credit for small brewers, regardless of location, was put into effect. (Item 7.07).

Tax Base

The base for the alcoholic beverages taxes is alcoholic beverages for human consumption which are manufactured, imported, sold, or possessed in Minnesota. Therefore, the exemptions for alcohol used for purposes other than human consumption are not tax expenditures, such as the exemption for alcohol used in industrial production.

Computation of the Tax

The tax is paid by the wholesaler, distributor, or manufacturer upon acquisition for sale within Minnesota. The tax is based on volume, not price. Alcoholic beverages are also subject to a sales tax of 8.5% of the purchase price.

The current rates are:

Beer: Alcohol by Weight	Tax per Barrel of 31 Gallons
3.2% or less	$2.00
More than 3.2%	$4.00

	Tax	
	Per Liter	Per Gallon
Distilled Spirits	$1.16	$4.39
Wine: Alcohol by Volume		
Less than 14%	$.07	$.27
14% to 21%	.21	.79
21% to 24%	.42	1.58
More than 24%	.81	3.08
Sparkling Wine	.40	1.50

EXEMPTIONS

7.01 CONSUMER PURCHASES MADE OUT OF STATE

Minnesota Statutes, Section 297C.09

Any person who may legally consume alcohol in Minnesota may bring into this state specified quantities of alcoholic beverages from another state or country without paying the appropriate Minnesota excise tax. A person may bring into Minnesota from another state one liter of distilled spirits or wine or nine quarts of beer without paying the excise tax. A person entering Minnesota from another country may have in possession four liters of distilled spirits or wine or ten quarts of beer without paying the Minnesota excise tax.

This provision was enacted in 1947 and last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
Distilled Spirits	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Wine	100,000	100,000	100,000	100,000
Beer	300,000	300,000	300,000	300,000
Total - State General Fund	$1,400,000	$1,400,000	$1,400,000	$1,400,000

7.02 HOME FERMENTATION (WINE AND BEER)

Minnesota Statutes, Section 297C.07(3)

No excise tax is placed upon beer or wine made in the home for family use.

This exemption was first authorized by statute in 1957 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$100,000	$100,000	$100,000

7.03 ALCOHOLIC BEVERAGES SOLD TO FOOD PROCESSORS

Minnesota Statutes, Section 297C.03

Alcoholic beverages sold to food processors are exempt from the alcoholic beverage taxes. This provision primarily affects liquor sold to bakeries for use in fruit cakes and other such specialty items.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

7.04 CONSUMPTION ON BREWERY PREMISES (BEER)

Minnesota Statutes, Section 297C.07(4)

Beer that is served by a brewery at no charge for on-premise consumption or is distributed to brewery employees for on-premise consumption under a labor contract is exempt from the Minnesota excise tax.

This provision was enacted in 1941 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

7.05 WINE USED FOR TASTING AND TESTING

Minnesota Statutes, Section 297C.03

The excise tax imposed on the production of wine in Minnesota exempts wine which is used for tasting and testing purposes.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

7.06 WINE FOR SACRAMENTAL PURPOSES

Minnesota Statutes, Sections 297C.07 (2) and 340A.316

Sales of wine exclusively for sacramental purposes by a manufacturer or wholesaler to a minister, rabbi, or priest of a church or established religious organization are not subject to the Minnesota excise tax.

This provision was adopted in 1937 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

CREDIT

7.07 SMALL BREWERS' CREDIT (BEER)

Minnesota Statutes, Section 297C.02, Subd. 3

A credit is allowed to a brewer who manufactures less than 100,000 barrels of beer in the calendar year preceding the year for which the credit is claimed. The credit is $4 per barrel on

25,000 barrels sold in a fiscal year, with a maximum credit of the lesser of the brewer's tax liability or $100,000.

The credit was enacted in 1985, effective August 1, 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$200,000	$200,000

CHAPTER 8: CIGARETTE AND TOBACCO TAXES

Collections and History

In fiscal year 1986, the net revenues from the cigarette tax were $97.7 million and from the tobacco products tax were $3.9 million. Of the 23¢ per pack cigarette tax, the revenues are distributed as follows: the tax on 16¢ per pack goes to the state general fund; 4¢ goes to the state water pollution control fund; 2¢ goes to the Minnesota resources fund; and 1¢ to the public health fund. Of the tobacco products tax, 80% goes to the state general fund and 20% to the state water pollution control fund.

The cigarette tax was enacted in 1947 at a rate of 3¢ per pack. Several rate increases have occurred since then, with the most recent being to 18¢ in 1971 and to 23¢ on July 1, 1985. Cigarettes were first subject to the general sales tax in 1982.

The tobacco products tax was enacted in 1955 at a rate of 15% of the wholesale price. The rate was increased to 20% in 1959 and to 25% on July 1, 1985. Tobacco products have been subject to the general sales tax since it was enacted in 1967.

Tax Base

The tax base is essentially the same for both the cigarette tax and the tobacco products tax. It is the sale of cigarettes or tobacco products in Minnesota. Also included in the tax base is the use or storage in Minnesota of cigarettes or tobacco products if the tax was not paid previously.

Computation of the Tax

The cigarette tax is 23¢ per pack of twenty cigarettes or little cigars. The tax is paid by the distributor by purchasing stamps that are affixed to the packages. The distributors receive a discount of 2% for the first $1 million of stamps purchased and 1.25% for stamps over $1 million purchased each year.

A complementary use and storage tax of 23¢ per pack is imposed on cigarettes or little cigars that are used or stored in Minnesota, on which the tax had not previously been paid (unstamped packages).

The tobacco products tax is 25% of the wholesale price. The tax is imposed on all tobacco products except cigarettes and little cigars and includes cigars, smoking tobacco, and chewing tobacco. The tax is paid by the distributor, who receives a discount of 2% of the tax.

A complementary use and storage tax of 25% of the cost is imposed on tobacco products that are used or stored in Minnesota, on which the tax had not previously been paid.

For both the cigarette and tobacco products taxes, the statutes state the tax "... shall not be construed as a cost of doing business or an overhead expense ...". In all cases, the taxes are passed on to the consumer.

EXEMPTIONS

8.01 SALES TO MINNESOTA CORRECTIONAL INSTITUTIONS

Minnesota Statutes, Sections 297.02, Subd. 6 and 297.32, Subd.8

Institutions under the control and management of the commissioner of corrections are specifically exempt from the cigarette tax and the tobacco products tax. This tax expenditure occurs when prisons and other correctional institutions buy cigarettes and other tobacco products on a regular basis to sell to inmates. Consequently the inmates do not pay the tax. No other state agencies or institutions are granted this exemption.

This exemption was authorized in 1965 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
Cigarettes				
State General Fund	$140,000	$151,000	$163,000	$176,000
State Water Pollution Control Fund	35,000	38,000	41,000	44,000
Minnesota Resources Fund	17,000	19,000	20,000	22,000
Public Health Fund	8,000	9,000	10,000	11,000
Total - Cigarettes	$200,000	$217,000	$234,000	$253,000
Tobacco Products				
State General Fund	$12,000	$14,000	$17,000	$19,000
State Water Pollution Control Fund	3,000	4,000	4,000	5,000
Total - Tobacco Products	$15,000	$18,000	$21,000	$24,000
Grand Total	$215,000	$235,000	$255,000	$277,000

8.02 LIMITED QUANTITIES EXEMPT

Minnesota Statutes, Sections 297.22, Subd. 3 and 297.32, Subd.2

A use and storage tax equal to the cigarette tax is imposed on consumers in possession of cigarettes or little cigars which were not previously subject to the Minnesota cigarette excise tax. Likewise, a use and storage tax equal to the tobacco products tax is imposed on consumers in possession of tobacco products not previously subject to the tobacco products tax.

For both taxes, limited quantities in the possession of a consumer are exempt from the tax. The exemption applies to: not more than 200 cigarettes; not more than fifty cigars; not more than ten ounces of snuff or snuff powder; and not more than one pound of smoking or chewing tobacco or other tobacco products not specifically mentioned in the statutes.

Although this exemption could be viewed as an incentive for consumers to purchase cigarettes and tobacco products in bordering states with lower tax rates, only North Dakota has a lower cigarette tax rate.

State	Cigarette Tax Rate Per Pack
Minnesota	23¢
Iowa	26¢
North Dakota	18¢
South Dakota	23¢
Wisconsin	25¢

The exemption for cigarettes was enacted in 1949 and was last changed in 1973. The exemption for tobacco products was enacted in 1957 and revised in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
Cigarettes				
State General Fund	$348,000	$348,000	$348,000	$348,000
State Water Pollution Control Fund	87,000	87,000	87,000	87,000
Minnesota Resources Fund	43,000	43,000	43,000	43,000
Public Health Fund	22,000	22,000	22,000	22,000
Total-Cigarettes	$500,000	$500,000	$500,000	$500,000
Tobacco Products				
State General Fund	$16,000	$16,000	$16,000	$16,000
State Water Pollution Control Fund	4,000	4,000	4,000	4,000
Total-Tobacco Products	$20,000	$20,000	$20,000	$20,000
Grand Total	$520,000	$520,000	$520,000	$520,000

CHAPTER 9: MORTGAGE REGISTRY TAX

Collections and History

In fiscal year 1986, revenues from the mortgage registry tax were estimated to be $17.7 million. Beginning July 1, 1985, all revenues from this tax go to the county revenue fund of the county in which the tax is collected. However, 95% of the tax is used as a deduction from welfare expenditures and results in a reduction of state welfare aid payments equal to that amount.

Minnesota first enacted a mortgage registry tax in 1907 at a rate of 50¢ for each $100 of principal debt secured by a mortgage of real property. Since 1945 the rate has been 15¢ for each $100, or fraction thereof, of such debt.

Tax Base

The tax base is the amount of principal debt secured by a mortgage of real property within Minnesota. Only registered mortgages are within the tax base. Although similar to a mortgage in some respects, a contract for deed is not a mortgage because the debt is not secured by real property. Therefore, the exemption of registered contracts for deed is not considered a tax expenditure.

Computation of the Tax

The mortgage registry tax is 15¢ for each $100, or fraction thereof, of principal debt which is or may be secured by any mortgage of real property within Minnesota and which is recorded or registered. If the real estate used to secure the debt includes property outside Minnesota, the tax is applied to a proportion of the entire debt, the proportion being the value of the Minnesota real estate to the value of the entire real estate described in the mortgage.

The statutes do not specify who pays the mortgage registry tax. Generally, the lender records or registers the mortgage and pays the tax. The tax is paid to the county treasurer at or before the time of filing the mortgage for record or registration.

EXEMPTION

9.01 CERTAIN PERSONS AND ORGANIZATIONS EXEMPT

Minnesota Statutes, Section 287.06

Organizations which are exempt from the property tax, such as municipalities, churches, and school districts, are exempt from the mortgage registry tax when they are the mortgage lender. This exemption is based on the identity of the lender because it is the lender who pays the tax in order to officially register its security interest in the affected property.

This provision was enacted in 1907 and was last revised in 1965.

	Fiscal Year Impact			
	1986	1987	1988	1989
County Welfare Fund	$100,000	$100,000	$100,000	$100,000

CHAPTER 10: DEED TRANSFER TAX

Collections and History

Total revenues from the deed transfer tax were estimated to be $17.8 million in fiscal year 1986. Beginning July 1, 1985, all revenue from the deed transfer tax goes to the county revenue fund of the county in which the tax is collected. However, 97% of the tax is used as a deduction from welfare expenditures and results in a reduction of state welfare aid payments equal to that amount.

Minnesota enacted a deed transfer tax in 1961 at a rate of $1.10 for consideration of $1,000 or less plus 55¢ for each $500 in excess of $1,000. The current rates were adopted in 1967, and they are $2.20 for consideration of $1,000 or less plus $1.10 for each $500 in excess of $1,000.

Tax Base

The tax base for the deed transfer tax is the granting, assigning, transferring, or otherwise conveying of real estate by deed, instrument, or writing. The most common situation is the transferring of real estate by deed.

Computation of the Tax

A tax of $2.20 is imposed in these situations:

1. transfers made by instruments pursuant to mergers, consolidations, sales, or transfers of substantially all of the assets of corporations pursuant to plans of reorganization; or
2. transfers made with no consideration; or
3. transfers made with consideration of $1,000 or less.

When the consideration is in excess of $1,000, the tax is $2.20 plus $1.10 for each $500, or fractional part of $500, in excess of $1,000.

The person who grants, assigns, tranfers, or conveys real estate is liable for the tax. The deed, instrument, or writing cannot be recorded or registered unless the tax is paid or unless the transaction is exempt. The tax is paid to the county at the time of transfer.

EXEMPTIONS

10.01 TRANSFERS BETWEEN CO-OWNERS

Minnesota Statutes, Section 287.22

Deeds transferred between co-owners in order to partition a commonly-held piece of land are exempt from the deed transfer tax.

This provision became effective August 1, 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
County Welfare Fund	Minimal	Minimal	Minimal	Minimal

10.02 DEEDS OF DISTRIBUTION BY PERSONAL REPRESENTATIVES

Minnesota Statutes, Section 287.22

Deeds of distribution by personal representatives are exempt from the deed transfer tax.

This provision was enacted in 1975 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
County Welfare Fund	Minimal	Minimal	Minimal	Minimal

10.03 DEEDS FOR CEMETERY LOTS

Minnesota Statutes, Section 287.22

Deeds or other instruments transferring cemetery lots are exempt from the deed transfer tax.

This provision was enacted in 1961.

Approximately 30,000 cemetery lots are sold in Minnesota each year.

	Fiscal Year Impact			
	1986	1987	1988	1989
County Welfare Fund	Minimal	Minimal	Minimal	Minimal

10.04 TRANSFERS INVOLVING GOVERNMENT AGENCIES

Minnesota Statutes, Section 287.22

This provision exempts from tax any deed, instrument, or writing in which a governmental body or agency is the grantor, assignor, transferor, conveyor, grantee, or assignee. In other words, any time a government agency is one of the parties involved in a deed transfer, no deed transfer tax is imposed.

This provision was enacted in 1961 and remains substantially unchanged since then.

	Fiscal Year Impact			
	1986	1987	1988	1989
County Welfare Fund	$300,000	$300,000	$300,000	$300,000

CHAPTER 11: CHARITABLE GAMBLING TAX

Collections and History

Fiscal year 1986 was the first year that the charitable gambling tax was collected, and the total receipts were $6.4 million. The proceeds from this tax are deposited in the state general fund.

The 10% charitable gambling tax was enacted in 1984 and became effective June 1, 1985. The enactment of the tax was part of legislation which created the Charitable Gambling Control Board and gave the board jurisdiction over charitable gambling. Previously, licensing was the responsibility of the local government units. The provisions of the charitable gambling law specify the requirements for all phases of lawful gambling activity.

The charitable gambling tax is imposed in lieu of the 6% sales and use tax on lawful gambling covered under the charitable gambling law.

Effective January 1, 1987, a separate tax on pull-tabs is established, and pull-tabs are exempt from the charitable gambling tax.

Tax Base

The tax base is gross receipts from lawful gambling less prizes.

Computation of the Tax

The charitable gambling tax covers lawful gambling, which is defined by statute as "... the operation, conduct or sale of bingo, raffles, paddlewheels, tipboards, and pull-tabs." Lawful gambling is allowed only by qualifying organizations which are licensed by the Charitable Gambling Control Board or which are exempt from licensing by statute. The organization must be a fraternal, religious, veterans, or other nonprofit organization. The profits from the lawful gambling must be used only for the purposes specified by statute.

The tax is 10% of the gross receipts of a licensed organization from lawful gambling less prizes actually paid out. Organizations which are exempt from licensing are also exempt from the tax (Items 11.01 to 11.05). The tax is paid by the organization to the Charitable Gambling Control Board.

Pull-tabs are exempt from the charitable gambling tax beginning January 1, 1987, when a separate pull-tab tax goes into effect. The tax is 10% of the face resale value of all the pull-tabs in each deal less the total prizes which may be paid out for that deal. A "deal" is defined as each separate package, or series of packages, consisting of one game of pull-tabs. The tax is paid to the commissioner of revenue.

EXEMPTIONS

11.01 BINGO AT A NURSING HOME OR SENIOR CITIZEN ORGANIZATION

Minnesota Statutes, Section 349.214, Subd. 1a

An exemption from the charitable gambling tax is allowed for bingo conducted within a nursing home or a senior citizen housing project or by a senior citizen organization if the prizes for a single bingo game do not exceed $10, total prizes awarded at a single bingo occasion do not exceed $200, no more than two bingo occasions are held each week, and specified other conditions are met.

This provision was enacted in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

11.02 BINGO AT FAIRS AND CIVIC CELEBRATIONS

Minnesota Statutes, Section 349.214, Subd. 1 (1)

The 10% charitable gambling tax is not imposed on bingo conducted in connection with a county fair, the state fair, or a civic celebration if conducted twelve or fewer consecutive days in a calendar year.

This exemption was enacted in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

11.03 INFREQUENT BINGO OCCASIONS

Minnesota Statutes, Section 349.214, Subd. 1 (2)

An exemption from the charitable gambling tax is allowed for bingo conducted by an organization which holds four or fewer bingo occasions in a calendar year.

This exemption was enacted in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

11.04 SMALLER RAFFLES

Minnesota Statutes, Section 349.214, Subd. 2 (a)

If the value of all raffle prizes awarded by an organization in a calendar year does not exceed $750, then the raffles of that organization are exempt from the charitable gambling tax.

This provision was enacted in 1984 and amended in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

11.05 LAWFUL GAMBLING UNDER CERTAIN CONDITIONS

Minnesota Statutes, Section 349.214, Subd. 2(b)

Lawful gambling is exempt from the charitable gambling tax if certain conditions are met, including that the organization conducts lawful gambling on five or fewer days in a calendar year and the organization does not award more than $50,000 in prizes for lawful gambling in a calendar year.

This exemption was enacted in 1986, effective June 1, 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$400,000	$400,000	$400,000	$400,000

CHAPTER 12: TELEPHONE GROSS EARNINGS TAX

Collections and History

The revenue from the telephone gross earnings tax was $55.5 million in fiscal year 1986. All revenue from this tax goes to the state general fund.

Minnesota first enacted a gross earnings tax on telephone companies in 1887 at a rate of 2%. Although replaced by a property tax between 1891 and 1897, the gross earnings tax was re-enacted in 1897 at a rate of 3%. The rate was increased to 4% in 1921, and in 1937 the rates that were in existence through 1986 were adopted.

Legislation enacted in 1985 phases out the gross earnings tax and replaces it with the property tax, which will go into effect beginning with property taxes payable in 1988. Prior to that legislation, the gross earnings tax had been in lieu of all other taxes, except the income tax.

Tax Base

The tax base is the gross earnings of telephone companies from business within Minnesota.

Computation of the Tax

The gross earnings tax is paid by each telephone company that owns or operates a telephone line or telephone exchange for hire wholly or partly within Minnesota.

The rate of the gross earnings tax depends upon the source of the business. Beginning in 1990 the tax is repealed, and the rates are reduced from 1986 through 1989, as follows:

	Percent of Gross Earnings				
Type of Telephone Service	Through 1986	1987	1988	1989	After 1989
Service to rural subscribers and to cities of the fourth class	4.0%	3.0%	1.5%	1.0%	Exempt
Service to all others	7.0%	5.5%	3.0%	2.5%	Exempt

EXEMPTIONS

12.01 INTERSTATE TELEPHONE SERVICE

Minnesota Statutes, Section 295.34, Subd. 1

Business originating or terminating outside Minnesota is exempt from the telephone gross earnings tax.

This exemption was enacted in 1985, effective January 1, 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$12,500,000	$22,800,000	$16,100,000	$10,800,000

12.02 CELLULAR RADIO

Minnesota Statutes, Section 295.01, Subd. 10

Cellular radio is exempt from the telephone gross earnings tax.

This exemption was enacted in 1985, effective January 1, 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$200,000	$200,000	$100,000

REDUCED RATES

12.03 REDUCED RATE FOR CERTAIN BUSINESS

Minnesota Statutes, Section 295.34, Subd. 1

Telephone companies having gross earnings of more than $1,000 for the calendar year are taxed at a percentage of their gross earnings. Gross earnings received from rural subscribers and from exchange business in cities of the fourth class (those having a population of 10,000 or less) are taxed at a lower rate than all other types of business.

In 1985, the following schedule of rates was adopted, so that the telephone gross earnings tax is repealed, beginning in 1990. The gross earnings tax is replaced by a property tax which will go into effect beginning with property taxes payable in 1988.

	Percent of Gross Earnings				
Type of Telephone Service	Through 1986	1987	1988	1989	After 1989
Service to rural subscribers and to cities of the fourth class	4.0%	3.0%	1.5%	1.0%	Exempt
Service to all others	7.0%	5.5%	3.0%	2.5%	Exempt

The gross earnings tax on telephone companies was enacted in 1887 at a flat 2% rate. The preferential rate for gross earnings received from rural or small city customers was introduced in 1937. In 1985 the phase-out of the gross earnings tax was enacted.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$10,000,000	$9,200,000	$6,700,000	$5,000,000

CHAPTER 13: INSURANCE PREMIUMS TAXES

Collections and History

In fiscal year 1986 the revenues from the insurance premiums taxes totaled $97.2 million. The proceeds from these taxes are deposited in the state general fund.

A tax on insurance premiums was first enacted in Minnesota in 1868 at a rate of 2% of the premiums received by foreign (non-Minnesota) insurance companies. In 1872 the tax was extended to domestic (Minnesota) companies. The basic rate remains at 2%.

In 1913 the fire marshal tax was enacted at a rate of 0.375%, and the rate was increased to the current 0.5% rate in 1937. This tax is in addition to the 2% gross premiums tax and is imposed only on fire premiums.

In 1934 a surcharge was enacted at a rate of 2% on fire, lightning, and sprinkler leakage premiums on property located in cities of the first class (Minneapolis, St. Paul, and Duluth). The rate remains at 2%, and the surcharge is in addition to other taxes.

In 1953 the ocean marine profits tax was enacted at a rate of 5% on taxable underwriting profit from marine insurance written in Minnesota. This tax replaced the 2% gross premiums tax for this type of insurance. The rate remains at 5%.

A tax on surplus lines insurance premiums was enacted in 1963 at a rate of 2%, and the rate was increased to the current 3% rate in 1978. This tax applies to insurance placed with an insurer not licensed in Minnesota when coverage is not available from a Minnesota-licensed insurer.

Tax Base

For purposes of this study, the tax base is defined as gross premiums less return premiums on all direct business received in Minnesota by domestic and foreign insurance companies.

Computation of the Tax

The 2% premiums tax is imposed on the gross premiums less return premiums received by domestic and foreign insurance companies on all direct business in Minnesota. A domestic company is one which is incorporated or organized in Minnesota, and a foreign company is one which is incorporated in another state or country. Domestic mutual insurance companies other than life pay the 2% tax on only fire, lightning, and sprinkler leakage premiums, except for auto and ocean marine fire business (Item 13.05).

The 0.5% fire marshal tax is imposed on the gross fire premiums and assessments less return premiums received by the company in Minnesota. Every insurance company must pay this tax, with the exception of farmers' and township mutual fire insurance companies (Item 13.06).

The 2% surcharge is imposed on the fire, lightning, and sprinkler leakage gross premiums less return premiums on all direct business received by domestic and foreign fire insurance companies on property in cities of the first class. The cities of the first class are Minneapolis, St. Paul, and Duluth.

The 3% surplus lines insurance tax is imposed on total written premiums less cancellations for insurance placed with an insurer not licensed in Minnesota when coverage is not available from a

Minnesota licensed insurer. The tax is paid by the Minnesota agent or broker who has a surplus lines license.

The ocean marine profits tax is not based on the amount of premiums but is 5% of the average of the taxable underwriting profits or losses of marine insurance written in Minnesota in the three preceding years. The computation of the taxable underwriting profit or loss is specified by statute.

The amount of premiums tax paid, except for the surcharge, is allowed as a credit against the corporation income tax (Item 2.48).

EXEMPTIONS

13.01 COOPERATIVE LIFE AND CASUALTY COMPANIES

Minnesota Statutes, Section 61A.49

Although cooperative companies perform the same function as other life and casualty insurers, all cooperative life and casualty insurance companies are exempt from the Minnesota gross premiums tax.

This exemption was enacted in 1907 and was last changed in 1967.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

13.02 FRATERNAL BENEFICIARY SOCIETIES

Minnesota Statutes, Section 64B.24

Fraternal beneficiary societies or associations are exempt from the Minnesota gross premiums tax. These societies are nonprofit, charitable organizations which provide life, sickness, and/or accident benefits for their members.

This exemption dates back to 1907 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$2,300,000	$2,500,000	$2,700,000	$3,000,000

13.03 NONPROFIT HEALTH SERVICE PLAN CORPORATIONS

Minnesota Statutes, Section 62C.01, Subd. 3

Medical and hospital service associations organized and controlled by state law under the Minnesota Nonprofit Health Service Plan Corporations Act are exempted from the gross premiums tax.

This provision was enacted in 1971 and has remained unchanged since that time.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$8,700,000	$9,500,000	$10,400,000	$11,500,000

13.04 HEALTH MAINTENANCE ORGANIZATIONS

Minnesota Statutes, Section 62D.01, Subd. 2

Health maintenance organizations qualifying under the Health Maintenance Act of 1973 are exempt from the Minnesota gross premiums tax.

This provision was enacted in 1973.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$14,100,000	$15,400,000	$16,900,000	$18,700,000

13.05 DOMESTIC MUTUAL INSURANCE COMPANIES OTHER THAN LIFE

Minnesota Statutes, Section 60A.15, Subd. 1 and 2

Domestic mutual insurance companies other than life insurance companies pay the 2% gross premiums tax only on their fire, lightning, and sprinkler leakage premiums; these companies are exempt from paying the gross premiums tax on all other types of premiums.

This exemption was enacted in 1905 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,700,000	$6,100,000	$5,800,000	$5,900,000

13.06 FARMERS' MUTUAL AND TOWNSHIP MUTUAL FIRE INSURANCE COMPANIES (FIRE MARSHAL TAX)

Minnesota Statutes, Section 299F.21

Insurance companies doing business in Minnesota are required to pay an annual fire marshal tax on their fire insurance premiums. The tax is equal to 0.5% of gross fire insurance premiums and assessments received annually on all direct business in Minnesota. Farmers' mutual insurance companies and township mutual insurance companies are exempt from this tax.

This exemption was enacted in 1915 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$100,000	$300,000	$200,000	$200,000

PREFERENTIAL COMPUTATION

13.07 OCEAN MARINE PROFITS TAX

Minnesota Statutes, Section 60A.15, Subd. 6

The ocean marine profits tax is based not on the amount of premiums but is 5% of the average of the taxable underwriting profits or losses of marine insurance written in Minnesota in the three preceding years. The estimates measure the difference between the 5% ocean marine profits tax and the tax that would be paid if the 2% gross premiums tax were applied to ocean marine premiums.

The ocean marine profits tax was enacted in 1953.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$200,000	$300,000	$300,000	$300,000

CREDIT

13.08 CREDIT FOR PAYMENTS TO MINNESOTA COMPREHENSIVE HEALTH ASSOCIATION

Minnesota Statutes, Section 62E.11, Subd. 8

Insurance companies may take a credit aganist the gross premiums tax in an amount equal to their contributions during the tax year to the Minnesota Comprehensive Health Association (MCHA). The MCHA was established by state law to provide insurance for high risk individuals. By law, membership in the association consists of all insurers, self-insurers, and fraternal and health maintenance organizations licensed or authorized to do business in the state. All members subject to the Minnesota gross premiums tax must make an annual contribution to the association based on their gross premium income.

This provision was enacted in 1979 as a credit against either the corporate income or the gross premiums tax, at the taxpayer's election. In 1984 the credit was changed so that effective for tax years beginning after December 31, 1983, the credit may be applied only against the gross premiums tax.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,600,000	$4,800,000	$5,000,000	$5,200,000

CHAPTER 14: TACONITE PRODUCTION TAX

Collections and History

Collections from the taconite production tax were $65.1 million in fiscal year 1986. Beginning with taxes payable in 1986, the tax is paid directly to the counties and to the Iron Range Resources and Rehabilitation Board. The statutes specify the distribution to local units of government and for other purposes in northeastern Minnesota. The state general fund no longer receives any portion of this tax.

The taconite production tax was enacted in 1941 at a rate of 5¢ per ton plus 0.1¢ per ton for each 1% that the iron content exceeded 55%.

The tax rate was increased three times, and then in 1977 it was set at $1.25 per gross ton of merchantable iron ore concentrate produced. The rate was increased annually from 1977 to the 1984 production year by the steel mill products index. The rate applicable to the 1984 and 1985 production years was $2.05 per ton, and it is $1.90 per ton for production year 1986. Beginning in 1987, the rate is increased annually by the implicit price deflator unless certain conditions exist. Beginning in 1985, the additional tax for iron content was eliminated.

Tax Base

The tax base for the taconite production tax is tonnage of merchantable iron ore concentrate produced from taconite.

Computation of the Tax

The tax rate of $1.90 per ton applies to production year 1986 and is increased annually thereafter by the implicit price deflator. However, the increase will not go into effect in 1987 if production is more than 33 million tons or in 1988 if production is more than 34 million tons.

For the 1985 production year, the tax applied to the average of the production for 1984 and 1985. Beginning with the 1986 production year, the tax applies to the average production of the current year and the previous two years.

Although the tax is now collected locally, the mining companies still file the production tax returns with the Minnesota Department of Revenue. The Department of Revenue determines the amount of tax and the distribution of the tax.

The production tax is in lieu of the property tax on the land, buildings, and equipment used in connection with taconite mining, quarrying, or production. The production tax does not apply to the property involved in iron ore mining, quarrying, and production; that property is subject to the property tax (Chapter 17).

CREDIT

14.01 WATER FILTRATION PLANT CREDIT

Minnesota Statutes, Section 298.24, Subd. 4

A credit of $250,000 per year is allowed to a taconite producer that built a water filtration and treatment plant in 1984 at a cost of more than $1 million. The plant must have been built to alleviate the contamination of water resulting from the disposal of taconite tailings on land. The credit may be applied against production taxes paid in 1985, 1986, and 1987.

This credit was enacted in 1984 and last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
Taconite Environmental Protection Fund	$250,000	$250,000	$0	$0

CHAPTER 15: MINING OCCUPATION TAX

Collections and History

In fiscal year 1986, revenues from the occupation tax were $5.4 million. The Minnesota Constitution mandates the distribution of the tax: 50% to the state general fund, 40% for the support of elementary and secondary schools, and 10% for the general support of the university. Of the general fund portion, an amount equal to the yield of a 1¢ per ton production tax is appropriated to the Iron Range Resources and Rehabilitation Board to be used for specified purposes.

The occupation tax was enacted in 1921 at a rate of 6%. Several rate changes have been enacted since then, including increases and decreases, surtaxes and additional taxes. Although the rates for taconite and for iron ore have not always been the same, the rate for both types of ore is 15% for production year 1985, 14.5% for production year 1986, and 14% for production years 1987 and after.

In 1964 the Minnesota Constitution was amended to limit for 25 years the taxation of taconite companies. (See Item 16.03.)

Tax Base

The tax base for the occupation tax is the taxable value of the ore, defined as the value of the ore less necessary and reasonable expenses incurred in mining, producing, and transporting that ore. For purposes of this study, all the deductions that are currently allowed, either by statute or by administrative practice, are considered to define the tax base rather than to be exceptions to that base. Therefore, none of the deductions are considered to be tax expenditures.

Computation of the Tax

The occupation tax is imposed on mining companies in lieu of the income tax and is somewhat similar to an income tax.

Minnesota statutes specify that the computation of the occupation tax begins with the value of the ore at the mouth of the mine. Because no published market price exists for ore at the mouth of a Minnesota mine, the determination of this valuation has been established by administrative practice and court decisions. The value at the mouth of the mine is determined by taking the Lake Erie value less certain deductions, including stockpiling and loading costs, transportation costs, and processing costs.

After the value at the mouth of the mine is determined, certain deductions are allowed by statute to determine the taxable value of the ore. These deductions include mining costs, plant and equipment depreciation, and other expenses.

The tax rate applied to the taxable value of the ore for both taconite and iron ore is 15% for ore produced in calendar year 1985, 14.5% for calendar 1986, and 14% for ore produced in calendar year 1987 and thereafter.

Certain credits are allowed against the tax, the most important of which is the labor credit (Item 15.01). The labor credit can reduce the effective rate of tax to a minimum of 6.75% for 1985, 6.25% for 1986, and 5.75% for 1987 and subsequent years. The other credits allowed are also included in this report (Items 15.02 through 15.05).

The Taconite Amendment to the Minnesota Constitution limits the combined occupation, royalty, and excise taxes of a taconite company to the greater of: a) the amount of these taxes as computed under 1963 laws; or b) the income and sales tax that the company would pay if it were a manufacturing corporation. The amendment was adopted in 1964 and will expire in 1989.

The fiscal impacts shown in this chapter do not take the constitutional limit into account. The effects of the limitation and a further explanation of it can be found on in Item 16.03.

CREDITS

15.01 LABOR CREDIT

Minnesota Statutes, Section 298.02

A credit may be claimed against the occupation tax for high labor cost ores. The credit is determined by a formula based on the cost of labor per ton of processed iron ore or concentrate. The credit cannot exceed 8.25% of the valuation of the ore used in computing the occupation tax. Therefore, the effective rate of the tax can be reduced to a minimum of 6.75% for 1985, 6.25% for 1986, and 5.75% for 1987 and subsequent years.

The labor credit was enacted in 1939 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$14,100,000	$11,200,000	$11,200,000	$11,200,000

(Computed without regard to constitutional limitation. See Item 16.03.)

15.02 POLLUTION CONTROL CREDIT

Minnesota Statutes, Section 298.028

A company engaged in mining taconite or other iron bearing ores in Minnesota may take a credit against the occupation tax equal to 5% of the net cost of equipment used primarily to abate or control pollutants in order to meet or exceed state laws, rules, or standards. The credit amount is limited to $75,000 for any single tax year. Excess credit amounts may be carried forward for up to four successive years.

The pollution control credit was enacted in 1979 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

(Computed without regard to constitutional limitation. See Item 16.03.)

15.03 RESEARCH, EXPERIMENTATION, AND EXPLORATION CREDIT

Minnesota Statutes, Section 298.026

An occupation tax credit is allowed each Minnesota mining operation for the cost of all research, experimentation, pilot plant tests, and exploration work performed in Minnesota for the express purpose of furthering the discovery, development, or beneficiation (concentration) of Minnesota ores. Credit amounts exceeding current tax liability may be carried forward up to two years.

This provision was enacted in 1963 and was last changed in 1976.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

(Computed without regard to constitutional limitation. See Item 16.03.)

15.04 LOSS MINE CREDIT (IRON ORE)

Minnesota Statutes, Section 298.027

An occupation tax credit may be claimed by iron ore mining operations when allowable costs of a mine's operation exceed the value of the ore at the place where the ore is brought to the surface of the earth. The credit is limited to a specified percentage of the loss, depending on the type of mining operation. The credit is allowed only for the year in which the excess occurs.

The loss mine credit was enacted in 1963 and was last changed in 1976.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

15.05 DISCOUNT CREDIT (IRON ORE)

Minnesota Statutes, Section 298.031

A tax credit is allowed to iron ore mining companies for iron ore which is sold at a discount. The credit amount is determined by multiplying the number of tons of ore sold at a discount by the amount of the discount as determined by the commissioner of revenue. The credit is subject to several limitations.

The discount credit was enacted in 1961 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

CHAPTER 16: MINERAL ROYALTY TAXES

Collections and History

In fiscal year 1986, a total of $4.1 million in royalty taxes was collected. The proceeds from this tax are deposited in the state general fund.

The royalty tax was first enacted in 1923 at a rate of 6%. Since that time the rates have been the same as the occupation tax rates. The rate for taconite and iron ore is 15% for 1985, 14.5% for 1986, and 14% for 1987 and after. The rate for copper-nickel royalties is 1% plus an additional 1% of the royalties paid on gold, silver, platinum, and other precious metals.

In 1964 the Minnesota Constitution was amended to limit the taxation, including the royalty tax, of taconite companies. (See Item 16.03.)

Tax Base

The tax base is all royalty received in money or in value of property for permission to explore, mine, take out, and remove ore from land in Minnesota.

Computation of the Tax

Royalty is defined by statute as ". . . the amount in money or value of property received by any person having any right, title, or interest in or to any tract of land in this state for permission to explore, mine, take out and remove ore therefrom."

The tax rate is applied to the amount of the royalty. The rate for taconite and iron ore is 15% for royalty received in calendar 1985, 14.5% for calendar year 1986, and 14% for calendar year 1987 and thereafter. A labor credit is allowed against the tax which reduces the effective rate of tax to a minimum of 6.75% in 1985, 6.25% in 1986, and 5.75% in 1987 and thereafter. These rates and effective rates for the royalty tax on iron ore and taconite are the same as for the occupation tax (Chapter 15).

The tax rate on copper-nickel royalties is 1%. An additional 1% tax is imposed on the royalties paid on gold, silver, platinum, and other precious metals.

Although the terms of the lease between the mining company and the owner of the land determine who is liable for the tax, the tax is remitted by the mining company to the Department of Revenue.

The amount of royalty tax paid by taconite companies is limited by the Taconite Amendment to the Minnesota Constitution. The fiscal impacts of the tax expenditures in this chapter were computed without taking into account that limitation. The overall impact of the constitutional limitation is shown in Item 16.03.

CREDITS

16.01 LABOR CREDIT

Minnesota Statutes, Section 299.012, Subd. 1

Taxpayers receiving royalties from a taconite or other ore operation may claim a labor credit in an amount which will cause the net effective tax rate to equal the net effective mining occupation tax rate for the same operation. See Item 15.01 for a discussion of the occupation tax labor credit.

This provision was enacted in 1959 and was last amended in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$4,200,000	$4,200,000	$4,200,000	$4,200,000

(Computed without regard to constitutional limitation. See Item 16.03.)

16.02 LOSS MINE CREDIT

Minnesota Statutes, Section 299.012, Subd. 1

A credit is allowed against the royalty tax when the allowable costs of a mine operation exceed the value of the ore at the place where the ore is brought to the surface of the earth. The credit is equal to 8.25% of the royalty for taconite and iron ore operations.

This provision was enacted in 1959 and was last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	Minimal	Minimal	Minimal	Minimal

(Computed without regard to constitutional limitation. See Item 16.03.)

NOTE ON TACONITE AMENDMENT

16.03 CONSTITUTIONAL LIMIT ON THE TAXATION OF TACONITE MINING COMPANIES

Minnesota Constitution, Article X, Section 6
Minnesota Statutes, Section 298.40

The Minnesota Constitution places a ceiling on the total amount of occupation, royalty, and excise taxes to be paid annually by each taconite mining company.
The ceiling is the greater of a) the total amount of occupation, royalty, and excise taxes which would be payable by the company under the laws of 1963, or b) the amount of income and excise taxes which would be payable if the company were a manufacturing corporation.

If a company's computed occupation, royalty, and excise taxes are at or above its ceiling, no fiscal impact from the tax expenditures in these taxes can be attributed to that company because the state is constitutionally prohibited from taxing the company above its ceiling.

If a company's occupation, royalty, and excise taxes are below its ceiling, the total of the tax expenditures attributed to that company is limited to the amount by which its ceiling exceeds its current taxes.

For those companies below their ceilings in 1986, the amount by which their ceilings exceeded their current taxes was $6,500,000. This amount was not adjusted for fiscal years 1987 through 1989 because of the difficulty and uncertainty that would be involved in projecting all the variables for each company.

The Taconite Amendment to the Minnesota Constitution was passed by the Legislature in 1963 and adopted by the voters in 1964. It is set to expire in 1989.

	Fiscal Year Impact			
	1986	1987	1988	1989
State General Fund	$6,500,000	$6,500,000	$6,500,000	$6,500,000

(Maximum possible fiscal impact for all occupation, royalty, and sales tax expenditures relating to taconite mining companies.)

CHAPTER 17: PROPERTY TAX

Collections and History

Net property tax collections were $2.4 billion for property taxes payable in 1986. The property tax is collected by the counties and is distributed to the local units of government which impose the tax--counties, cities, townships, school districts, and special taxing districts. The state does not levy a general property tax.

Although the property tax is entirely a local source of revenue, nearly all aspects of the tax are controlled by state statute.

The property tax was already in place when the first book of statutes was compiled for the Territory of Minnesota in 1851. Numerous changes have been made to the property tax since that time, a few of which are highlighted here.

The classification system was first enacted in 1913 with four classes of property. In 1933 the number of classes was expanded to provide preferential treatment for homestead property, both platted and unplatted. The number of classes of property has continued to increase over time.

Many important changes to the property tax system were enacted in 1967. The state property tax levy was eliminated, and a portion of the revenues from the newly-enacted sales tax was distributed to local units of government. Enacted that year were the homestead credit, the rent credit, and the senior citizen credit. These credits have been expanded in coverage and increased in amount since 1967.

A number of changes in the taxation of the personal property of business began in 1967. In that year, livestock and agricultural machinery were exempted from the tax, and businesses were given the option to have either their inventories or their tools and machinery exempted. In 1971 the exemption for business property was expanded to include both inventories and tools and machinery. Whereas the previously-enacted exemptions pertained to personal property, in 1973 an exemption was also enacted for commercial and industrial equipment attached to and considered as real property, known as attached machinery.

In 1971 levy limitations and local government aids were enacted which are important in determining the amount of the property tax levy. Modifications have been made to both of these programs since that time.

Tax Base

For purposes of this study, the tax base for the property tax is the market value of real and personal property in Minnesota. Generally, market value is the estimated selling price of the property. Other approaches to determining market value are considered to be substitutes for selling price and therefore are not tax expenditures.

Because all property is included in the tax base, any property exempted by Minnesota statutes is a tax expenditure (Item 17.01). However, any property exempted by the Minnesota Constitution or by federal law is not included as a tax expenditure because one of the criteria for determining if an item is a tax expenditure is that it could be amended or repealed by a change in state law alone.

The working definition of the tax base assumes that all types of property are treated the same, and therefore the classification system is considered to be a tax expenditure (Item 17.02).

Computation of the Tax

The computation of the property tax is different from the computation of other types of taxes in Minnesota with regard to how the total yield of the tax is determined. This difference is important in understanding how the fiscal impacts of the property tax expenditures are different from the fiscal impacts of other tax expenditures.

The impact of a property tax expenditure affects the distribution of the tax rather than the total yield of the tax.

For the other taxes, the taxable amount (income, sales price, volume sold, etc.) is multiplied by a rate or set of rates specified by statute to yield the total tax. A preferential provision has an impact on the total yield of the tax. Any redistribution of that impact would require legislative action.

For the property tax, the taxable amount (assessed value, which is market value times the assessment ratio) is determined by statute. The total yield of the tax (the property tax levy) is not the result of a computation but is determined by the unit of government which imposes the tax. The governing body of the local unit, such as the school board, the county board, or the city council, determines the amount of the levy and in doing so must take into account many factors, including the level of services provided, mandated programs, debt service, levy limitations, and other sources of revenue such as local government aids.

The levy is divided by the total assessed value of the taxing district to determine the rate of tax (mill rate). For each parcel of property, the assessed value is multiplied by the aggregate mill rate of the county, city or township, school district, and any special taxing districts to determine the gross tax. An exemption, assessment ratio, or other preferential provision lowers the total assessed value and results in a higher mill rate that is applicable to all taxable property. Therefore, although the total yield from the tax is not affected, the tax is shifted from preferential to nonpreferential property.

Net tax is determined by subtracting from gross tax the applicable credit(s), if any. With the exception of the taconite homestead credit and the power line credit (Items 17.06 and 17.07), all these credits are reimbursed by the state to the local government units. They are included in the state budget as open and standing appropriations of the general fund; and, therefore, they are not included in this study as tax expenditures. The credits, listed in the order in which they are subtracted from gross tax, are as follows:

1. Disaster Credit
2. Wetlands Credit
3. Native Prairie Credit
4. Powerline Credit
5. Agricultural Preserves Credit
6. Enterprise Zone Credit
7. School Agricultural Credit
8. State Paid Homestead Credit
9. Taconite Homestead Credit
10. Supplemental Homestead Credit

Additional tax relief is provided to qualifying homeowners and renters through the property tax refund. The property tax refund is based on the net homestead tax or the tax attributable to the rental unit and on household income, with the amount of refund phasing out as income increases. The property tax refund is paid directly by the state to the claimant.

Acknowledgement: The estimates for the tax expenditures in the property tax were prepared by the Local Government Aids and Analysis Division of the Department of Revenue.

EXEMPTIONS

17.01 EXEMPT PROPERTY

Minnesota Statutes, Sections 272.02, Subd. 1 and 273.18

Certain types of property are exempt from the property tax by statute, and they are included in the estimates below. Certain other types of property are exempt under either the Minnesota Constitution or federal law, and their exemption is not included in the tax expenditure estimates. These properties are churches, academies, colleges, universities, and Indian reservations.

Since 1926 the county assessors have been required to value exempt property every six years, and the most recent valuations of exempt property took place in 1980 and 1986. The fiscal year 1986 and 1987 estimates are based on the 1980 values, and the 1988 and 1989 estimates are based on the 1986 values. The values were multiplied by a 43% assessment rate and a statewide average mill rate computed or estimated for each year to arrive at the estimated net property tax figures shown below. In computing the estimates, the mill rates were adjusted to take into account the additional taxable value which would result if the property were not exempt.

Certain types of property have been exempt from taxation since at least 1851 when the first book of statutes was compiled for the Territory of Minnesota. The statute was last changed in 1985.

	Net Property Tax - Fiscal Year Impact			
Type of Property	1986	1987	1988	1989
Real Property:				
Elementary and secondary schools	$161,600,000	$171,900,000	$241,500,000	$256,900,000
Public burying grounds	3,800,000	4,000,000	5,400,000	5,700,000
Hospitals	48,900,000	52,000,000	82,700,000	88,000,000
Charitable institutions	19,200,000	20,400,000	32,100,000	34,100,000
Federal and state forests, parks, and wildlife refuges	30,200,000	32,100,000	43,400,000	46,100,000
Public property used for public purposes	176,100,000	187,300,000	325,900,000	346,700,000
Total Real Property	$439,800,000	$467,700,000	$731,000,000	$777,500,000
Total Personal Property*	$42,700,000	$45,400,000	$48,300,000	$51,400,000
Total Exempt Property	$482,500,000	$513,100,000	$779,300,000	$828,900,000

* Personal property includes iron ore stockpiles, direct products of furnaces, agricultural products, attached machinery, commerical and industrial personal property.

PREFERENTIAL VALUATIONS

17.02 CLASSIFICATION SYSTEM

Minnesota Statutes, Section 273.13

Each parcel of taxable property is classified by type, and the market value is multiplied by the appropriate assessment ratio(s), depending upon the type of property. Due to the classification system, some types of property are treated preferentially compared to other types of property, the extent of the preferential treatment varying by property type. The classification system is considered a tax expenditure because each dollar of market value is not treated the same.

Although there are some seventy different classes of property, the estimates are summarized by twelve major groups. The estimates assume that, instead of having many different assessment ratios, one ratio applies to all types of property. However, no new revenue is generated because the mill rates are adjusted to reflect the new assessed values.

The fiscal impacts therefore reflect shifts in tax burdens. A positive figure indicates a tax increase and a negative figure a tax decrease for a group. When the gross tax is computed, the total of the differences between the groups is zero. When the net tax is computed, the differences between groups do not equal zero due to an increase in tax credits for some types of property.

The property tax classification system was enacted in 1913 and last changed in 1986.

	Fiscal Year Impact			
Type of Property	1986	1987	1988	1989
1. Farm	$52,300,000	$44,900,000	$43,200,000	$43,100,000
2. Seasonal Recreational Residential	300,000	300,000	300,000	300,000
3. Seasonal Recreational Commercial	700,000	700,000	800,000	900,000
4. Residential	153,400,000	161,700,000	181,800,000	202,200,000
5. Apartments	-36,800,000	-40,900,000	-44,300,000	-47,700,000
6. Vacant Land	-17,700,000	-18,200,000	-20,000,000	-21,500,000
7. Commercial	-133,300,000	-152,400,000	-170,800,000	-188,200,000
8. Industrial	-56,600,000	-62,200,000	-66,700,000	-70,600,000
9. Public Utility	-17,000,000	-17,800,000	-18,800,000	-19,600,000
10. Mineral	-1,500,000	-1,400,000	-1,500,000	-1,500,000
11. Railroad	-3,800,000	-4,300,000	-4,500,000	-4,800,000
12. Personal	-30,400,000	-33,300,000	-35,900,000	-37,900,000

(Changes in net property taxes by major groups due to elimination of the classification system.)

17.03 GREEN ACRES TREATMENT OF AGRICULTURAL LAND

Minnesota Statutes, Section 273.111

In 1967 the Minnesota Agricultural Property Tax Law, commonly referred to as "green acres," was enacted. The law provides for preferential and deferred assessment of qualifying agricultural land consisting of ten or more acres.

A qualifying parcel is valued according to its agricultural use only. A higher value that would result from nonagricultural use is not used for property tax purposes. For example, farm land that is near a commercial development would be valued according to its agricultural use and not according to its potential value for commercial development.

When green acres property no longer qualifies as such or is sold, a tax is due equal to the amount by which the preferential assessment has reduced the property tax for the previous three years.

The estimates below show the increase in net property tax that would result from valuing the green acres property at its highest and best use, as opposed to its agricultural use, at the statewide average mill rate computed or estimated for each year.

This provision was enacted in 1967 and last revised in 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
Green Acres	$6,300,000	$5,400,000	$5,100,000	$5,800,000

17.04 OPEN SPACE PROPERTIES

Minnesota Statutes, Section 273.112

Private outdoor recreational, open space, and park land is given preferential valuation and tax deferment as long as it meets certain criteria.

For property tax purposes, the property is valued at its current use rather than at a higher value that would reflect its potential use. For example, a golf course would be valued at its current use rather than at its potential use for commercial, industrial, or residential development.

When the open space property no longer qualifies for preferential valuation, taxes are due equal to the amount by which the preferential assessment reduced the tax for the previous seven years.

The Minnesota Open Space Property Tax Law was enacted in 1969 and was first effective for property taxes payable in 1971. It was last amended in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
Open Space Properties	$2,600,000	$3,200,000	$4,000,000	$5,000,000

PREFERENTIAL COMPUTATIONS

17.05 AUXILIARY FOREST TAX AND TREE GROWTH TAX

Minnesota Statutes, Sections 88.47 to 88.53 and 270.31 to 270.39

Forest land is taxed under one of three taxes--the general property tax, the auxiliary forest tax, or the tree growth tax. The estimates reflect the amount by which the auxiliary forest tax or the tree growth tax is lower than the general property tax that would be paid for those properties. Both taxes are payable and distributed in the same manner as the general property tax.

Qualifying land is designated an auxiliary forest upon application by the owner and approval by the county board. The auxiliary forest tax applies for the duration of the contract. When the contract expires, the land automatically qualifies for the tree growth tax. A law enacted in 1974 prohibits new auxiliary forest contracts from being issued or existing contracts from being extended after June 30, 1974.

The auxiliary forest tax is 10¢ per acre of land plus a yield tax of from 40% to 10% of the value of the timber, the rate determined by the year of the harvest in relation to the contract period. To be classified as an auxiliary forest, the property must be either a minimum of 35 acres suitable for forestation or a wood lot of from five to forty acres.

To qualify for the tree growth tax, the property must be a minimum of five acres of forest lands used exclusively for the growing of continuous forest crops. The owner must apply to and receive approval from the county board to have qualifying property taxed under the tree growth tax.

The tax rates for the tree growth tax depend upon the type of property involved. Commercial forests pay an annual tax of 30% of the value of annual growth. Temporarily nonproductive forests are taxed at 5¢ per acre or 15¢ per acre for noncompliance with a reforestation agreement. Permanently nonproductive forest lands are taxed at 5¢ per acre annually.

The auxiliary forest tax was enacted in 1927. The tree growth tax was enacted in 1957.

	Fiscal Year Impact			
	1986	1987	1988	1989
Auxiliary Forest Tax	$500,000	$400,000	$300,000	$300,000
Tree Growth Tax	800,000	600,000	500,000	400,000
Total	$1,300,000	$1,000,000	$800,000	$700,000

CREDITS

17.06 TACONITE HOMESTEAD CREDIT

Minnesota Statutes, Section 273.135

Homestead property within the defined taconite tax relief areas of Minnesota receives a credit against the property tax of either 57% or 66% of the net tax, the higher percentage applicable to property located in qualifying municipalities. The credit is limited to specified maximums and is calculated on the net tax after the regular homestead credit has been subtracted.

The taconite homestead credit was enacted in 1969 and last changed in 1985.

	Fiscal Year Impact			
	1986	1987	1988	1989
Taconite Homestead Credit	$10,100,000	$10,400,000	$11,000,000	$11,500,000

17.07 POWER LINE CREDIT

Minnesota Statutes, Sections 273.42, Subd. 2 and 273.425

The owner of qualifying property, such as a residence or a farm, receives a property tax credit if the property is crossed by an electric transmission line of 200KV or more which was constructed after July 1, 1974. The credit is limited to 20% of the gross property tax for any forty acre parcel of property. No credit is paid if it is less than $10. The credit is financed by a portion of the property taxes paid by the transmission lines giving rise to the credit.

The power line credit was enacted in 1979 and became effective for property taxes payable in 1982. It was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
Power Line Credit	$200,000	$200,000	$200,000	$200,000

CHAPTER 18: AIRFLIGHT PROPERTY TAX

Collections and History

Revenues from the airflight property tax were $4.8 million in fiscal year 1986. The proceeds from this tax go to the state airports fund of the state treasury.

The airflight property tax was enacted in 1945, and the structure of the tax has changed very little since then. Originally the assessment ratio was 40%, but it was reduced to 33 1/3% in 1953.

Tax Base

The tax base is the value of airflight property of airline companies engaged in air commerce. The apportionment formula and the 33 1/3% assessment ratio apply uniformly to all airflight property, and therefore they are not considered to be tax expenditures.

Computation of the Tax

The property subject to the tax is the aircraft and flight equipment, including spare flight equipment, of airline companies. Airline companies are defined as those that engage in the business of air commerce, and air commerce is defined as the transportation by aircraft of persons or property for hire on flights by airline companies operating under authorization of the United States Civil Aeronautics Board.

Privately-used aircraft are subject to the aircraft registration tax (Chapter 20) in lieu of the airflight property tax. A privately-used aircraft that is used occasionally in transportation for hire is not subject to the airflight property tax if the person furnishing the transportation is not in the business of transportation for hire.

The value of the airflight property is determined by the Department of Revenue. The value is apportioned to Minnesota by a three-factor formula. The apportioned value is multiplied by an assessment ratio of 33 1/3% to compute the assessed value which is then multiplied by the statewide average mill rate to determine the tax. The tax is paid by the airline company to the Department of Revenue.

Under a provision in the Minnesota Constitution, the airflight property tax is in lieu of other property taxes on airflight property. Therefore, airflight property is exempt from the local property tax. However, the property tax does apply to the other property of an airline company.

PREFERENTIAL COMPUTATION

18.01 COMMUTER AIRLINES

Minnesota Statutes, Section 360.521

Generally, commercial aircraft are taxed under the airflight property tax, and non-commercial aircraft are taxed under the aircraft registration tax. However, commuter airlines have the option of having their aircraft taxed under one tax or the other, whichever is lower.

Because commuter airlines could be considered commercial, the exemption of commuter airlines from the airflight property tax because they pay the aircraft registration tax is considered a tax expenditure. The estimates reflect the difference between the aircraft registration tax paid and the airflight property tax that would be paid if they were subject to that tax.

This provision was enacted in 1969.

	Fiscal Year Impact			
	1986	1987	1988	1989
State Airports Fund	Minimal	Minimal	Minimal	Minimal

CHAPTER 19: MOTOR VEHICLE REGISTRATION TAX

Collections and History

In fiscal year 1986, a total of $223.3 million in motor vehicle registration tax was collected. All the proceeds from this tax are deposited in the highway user tax distribution fund.

A motor vehicle registration tax was first enacted in 1911 at a rate of $1.50 per vehicle. In 1921 a tax of 2% of value was enacted, with the minimum tax determined by the weight category of the passenger car or truck.

From 1921 to 1949 the tax was based primarily on value. In 1949 a tax based only on weight was adopted, and for trucks the tax continues to be determined by weight. For passenger cars, however, a tax of $10 plus 1.25% of the base value was adopted in 1971 and remains in effect.

Tax Base

The tax base for the motor vehicle registration tax is motor vehicles that use the public streets and highways in Minnesota. The exemption of off-road vehicles, such as farm machinery, is therefore not considered to be a tax expenditure.

Historically, the tax has been based on weight, value, or a combination of the two, and currently passenger cars are taxed on value and trucks and buses are taxed on weight. Although arguments could be made for using either the weight system or the value system in the definition of the tax base, for purposes of this study one system is considered to be a replacement for the other. Therefore, neither the weight system nor the value system is considered to be a tax expenditure.

Computation of the Tax

The tax on passenger cars, pick-up trucks, and vans is $10 plus 1.25% of the base value. Base value is the manufacturer's suggested retail price, including destination charges but excluding separately-stated options. The percentage of base value used to compute the tax decreases with the age of the vehicle, from 100% in the first year of vehicle life to 10% for the tenth year. The flat tax for vehicles over ten years old and the minimum tax for all vehicles are both $35 ($10 plus $25 minimum additional tax).

The tax on trucks, tractors, and buses is based on the type, weight, and age of the vehicle. A minimum tax applies, the amount of which is determined by the type of the vehicle.

The tax is paid when the vehicle is first registered and annually thereafter when it is reregistered.

EXEMPTIONS

19.01 GOVERNMENT VEHICLES

Minnesota Statutes, Section 168.012, Subd. 1, 6, and 10

Vehicles owned or leased by a political subdivision of the state are exempt from the motor vehicle registration tax. Exempt vehicles include ambulances, fire equipment, utility fleets, police vehicles, and buses owned by city transit companies. Publicly owned or leased school buses are included in the estimate for Item 19.02.

The exemption for government vehicles was enacted in 1921 and was last changed in 1986.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$2,900,000	$4,000,000	$4,200,000	$4,300,000

19.02 SCHOOL BUSES

Minnesota Statutes, Section 168.012, Subd. 1 and 10

Vehicles which are used by Minnesota educational institutions for the sole purpose of transporting students to and from those institutions are exempt from the motor vehicle registration tax. Publicly owned or leased buses other than school buses are included in the exemption for government vehicles (Item 19.01).

This exemption was enacted in 1933 and was extended to leased vehicles in 1982.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$100,000	$100,000	$100,000	$100,000

19.03 NONRESIDENT MILITARY PERSONNEL

Minnesota Statutes, Section 168.04, Subd. 1

Vehicles of nonresident military personnel stationed in Minnesota are exempt from the motor vehicle registration tax if they meet the following four conditions:

1. the vehicle is properly registered in another state;
2. the owner is a resident of the state in which the vehicle is registered;
3. the vehicle is used only for the owner's personal transportation; and
4. the vehicle is subject to all other provisions of law applicable to vehicles owned by Minnesota residents.

This provision was enacted in 1967 and was last changed in 1981.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	Minimal	Minimal	Minimal	Minimal

19.04 MEDAL OF HONOR RECIPIENTS

Minnesota Statutes, Section 168.124

Congressional medal of honor recipients may obtain special license plates with the inscription "MEDAL OF HONOR" on them. The recipient is issued these plates as well as all subsequent tabs, stickers, or replacement plates free of any charges or tax.

This provision was enacted in 1983 and became effective beginning with calendar year 1984.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	Minimal	Minimal	Minimal	Minimal

19.05 DISABLED VETERANS

Minnesota Statutes, Section 168.031

Any motor vehicle which has been furnished either free of charge or at reduced cost by the United States government to a disabled war veteran is exempt from the motor vehicle registration tax.

This provision was enacted in 1941 and was last changed in 1971.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	Minimal	Minimal	Minimal	Minimal

CREDIT

19.06 PHYSICALLY HANDICAPPED PERSONS

Minnesota Statutes, Section 168.021, Subd. 2

Physically handicapped persons may obtain special license plates bearing the internationally accepted wheelchair symbol. Although these plates are subject to the full motor vehicle registration tax, a one dollar credit is allowed for each month the vehicle is registered.

This provision was enacted in 1975 and last changed in 1976.

In fiscal year 1986, this credit was allowed for 17,300 vehicles.

	Fiscal Year Impact			
	1986	1987	1988	1989
Highway User Tax Distribution Fund	$200,000	$200,000	$200,000	$200,000

CHAPTER 20: AIRCRAFT REGISTRATION TAX

Collections and History

In fiscal year 1986, the revenues from the aircraft registration tax were $1.3 million. All the proceeds from this tax go into the state airports fund of the state treasury. Expenses incurred in administering the tax are reimbursed to the general fund each year.

The aircraft registration tax was enacted in 1945, and the basic structure and rate of the tax have remained the same since that time.

Tax Base

The tax base for the aircraft registration tax is the value of non-commercial aircraft which regularly use the airspace over and the airports in Minnesota. Technically, the base applies to aircraft operating without a certificate of convenience and necessity issued by the United States Civil Aeronautics Board.

Computation of the Tax

Aircraft subject to the aircraft registration tax are those which are used privately and which use the airspace over Minnesota or the airports in Minnesota.

The value used in the computation of the tax begins with the base price of the aircraft, which is the manufacturer's list price, or, if the list price is not available, the commissioner of transportation's estimate of such. After the first year, the base price is reduced for depreciation--10% in the second year and 15% for the third and each succeeding year, subject to the minimum tax.

The tax is 1% of the value. The minimum tax is the greater of: a) 25% of the tax computed on the original base price; or b) $10.

The tax is paid when the aircraft is first registered and annually thereafter.

EXEMPTIONS

20.01 LOCAL GOVERNMENT AIRCRAFT

Minnesota Statutes, Section 360.55, Subd. 2

Aircraft owned and used solely in the transaction of official business by local govenment units are exempt from the aircraft registration tax.

This provision was enacted in 1945 and last amended in 1965.

	Fiscal Year Impact			
	1986	1987	1988	1989
State Airports Fund	Minimal	Minimal	Minimal	Minimal

20.02 CIVIL AIR PATROL AIRCRAFT

Minnesota Statutes, Section 360.55, Subd. 3

Aircraft owned and used solely in the transaction of offical business by the Civil Air Patrol are exempt from the aircraft registration tax.

This exemption was enacted in 1957 and remains unchanged.

	Fiscal Year Impact			
	1986	1987	1988	1989
State Airports Fund	Minimal	Minimal	Minimal	Minimal

APPENDIX A: MINNESOTA STATUTE REQUIRING THE TAX EXPENDITURE BUDGET

270.067 TAX EXPENDITURE BUDGET.

Subdivision 1. **Statement of purpose.** State governmental policy objectives are sought to be achieved both by direct expenditure of governmental funds and by the granting of special and selective tax relief or tax expenditures. Both direct expenditures of governmental funds and tax expenditures have an effect on the ability of the state and local governments to lower tax rates or to increase expenditures. As a result, tax expenditures should receive a regular and comprehensive review by the legislature as to (a) their total cost, (b) their effectiveness in achieving their objectives, (c) their effect on the fairness and equity of the distribution of the tax burden, and (d) the public and private cost of administering tax expenditure financed programs. This section is intended to facilitate a regular review of the state and local tax expenditure budget by the legislature by providing for the preparation of a regular biennial tax expenditure budget.

Subd. 2. **Preparation; submission.** The commissioner of revenue shall prepare a tax expenditure budget for the state. The tax expenditure budget report shall be submitted to the legislature as a supplement to the governor's budget and at the same time as provided for submission of the budget pursuant to section 16A.11, subdivision 1.

Subd. 3. **Period covered.** The report shall include estimates of annual tax expenditures for, at a minimum, a three-year period including the two-year period covered in the governor's budget submitted in the preceding January pursuant to section 16A.11.

Subd. 4. **Contents.** The report shall detail for each tax expenditure item the amount of tax revenue foregone, a citation of the statutory or other legal authority for the expenditure, and the year in which it was enacted or the tax year in which it became effective. The report may contain additional information which the commissioner considers relevant to the legislature's consideration and review of individual tax expenditure items. This may include, but is not limited to, statements of the intended purpose of the tax expenditure, analysis of whether the expenditure is achieving that objective, and the effect of the expenditure device on the distribution of the tax burden and administration of the tax system.

Subd. 5. **Revenue estimates; legislative bills.** Upon reasonable notice from the chairman of the house or senate tax committee that a bill is scheduled for hearing, the commissioner of revenue shall prepare an estimate of the effect on the state's tax revenues which would result from the passage of a legislative bill establishing, extending, or restricting a tax expenditure. These revenue estimates shall contain the same information as provided in subdivision 4 for expenditure items contained in the tax expenditure budget, as appropriate.

Subd. 6. **Definitions.** For purposes of this section, the following terms have the meanings given:

(1) "Tax expenditure" means a tax provision which provides a gross income definition, deduction, exemption, credit, or rate for certain persons, types of income, transactions, or property that results in reduced tax revenue.

(2) "Tax" means any tax of statewide application or any tax authorized by state law to be levied by local governments generally. It does not include a special local tax levied pursuant to special law or to a special local tax levied pursuant to general authority that is no longer applicable to local governments generally.

History: 1983 c 301 s 176

APPENDIX B: INACTIVE TAXES

Express Companies Gross Earnings Tax. Minnesota Statutes, Section 295.21

Freight Line Companies Gross Earnings Tax. Minnesota Statutes, Section 295.24

Sleeping Car Companies Gross Earnings Tax. Minnesota Statutes, Section 295.29

Taconite Tailing Tax. Minnesota Statutes, Section 298.24

Copper-Nickel Occupation Tax. Minnesota Statutes, Section 298.52

Copper-Nickel Production Tax. Minnesota Statutes, Section 298.61

Semi-Taconite Production Tax. Minnesota Statutes, Section 298.35

Agglomerating Facilities Production Tax. Minnesota Statutes, Section 298.393

Iron Bearing Materials Other Than Taconite and Semi-Taconite Production Tax. Minnesota Statutes, Section 298.405

APPENDIX C: TAXES WHICH CONTAIN NO TAX EXPENDITURE PROVISIONS

Hazardous Waste Generator Tax. Minnesota Statutes, Section 115B.22

Pari-Mutuel Betting Tax. Minnesota Statutes, Section 240.15

Severed Mineral Interests Tax. Minnesota Statutes, Section 273.13

Rural Electric Cooperative Membership Tax. Minnesota Statutes, Section 273.41

Taconite Railroad Gross Earnings Tax. Minnesota Statutes, Section 294.22

Telegraph Companies Gross Earnings Tax. Minnesota Statutes, Section 295.32

Trust Companies Gross Earnings Tax. Minnesota Statutes, Section 295.37

Aviation Fuels Excise Taxes. Minnesota Statutes, Section 296.02 and 296.025

Marine Gasoline Excise Tax. Minnesota Statutes, Section 296.02

Controlled Substances Tax. Minnesota Statutes, Section 297D.08

Unmined Taconite Tax. Minnesota Statutes, Section 298.26

INDEX