Minnesota Biennial Budget

FY 2012 - 2013

2012 - 2013

State Taxes and Local Aids and Credits

Governor's Budget

February 15, 2011

STATE TAXES AND LOCAL AIDS AND CREDITS

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A summary of the Governor's recommendation on State taxes and appropriations for aid and credit programs. Also included: more detailed descriptions about tax aid and credit programs, including purpose, funding source, 2009-2013 financial information, legal citation and program contacts.

MINNESOTA · REVENUE

February 15, 2011

The 2011 Minnesota Legislature:

Today we are transmitting to you Governor Dayton's recommendations for tax revenue and tax policy changes. The recommendations provide for tax revenue increases that, coupled with proposed spending reductions, will help close the large and persistent structural budget deficits and will increase the overall progressivity of Minnesota's state and local tax system.

The recommendations reflect the Governor's priorities for achieving a balanced budget; increasing tax fairness by reversing the trend toward an increasingly regressive tax system; and protecting individuals from regressive property tax increases.

As described in the 2009 Minnesota Tax Incidence Study, the individual income tax is the only progressive tax in Minnesota's portfolio of statewide taxes. The 2009 study found that while most middle-income Minnesotan's paid about 12.3 percent of their income in state and local taxes, the top ten percent paid 10.1 percent, the top five percent paid 9.7 percent, and the top one percent paid 8.8 percent. Consistent with the goals of tax fairness and increased progressivity, the Governor recommends that the Legislature:

- Increase individual income tax revenues by $1.9 billion with a new top marginal rate of 10.95%. The new rate would increase taxes for the top 5.4 percent of income tax filers; over 90% of Minnesotan's would pay no additional income tax.
- Adopt a temporary surtax on taxable incomes over $500,000—the top one percent of income tax filers—to address the immediate budget challenge.
- Eliminate corporate tax preferences and adopt nexus and economic substance rules that make it more difficult for some corporations to avoid Minnesota taxes while profiting from sales to Minnesota customers.
- Adopt a state property tax on residences valued over one million dollars; the tax would be about one-percent of the value above $1 million.

In addition, the Governor recommends changes to increase tax fairness among consumers by adopting nexus rules that capture tax from remote sellers of products that are already taxable in Minnesota. Other provisions that modernize statutory definitions to ensure that products or services already taxable for most Minnesotans will be taxable even if they are acquired through newer technologies or business models.

Governor Dayton also recommends:

- No reductions in aids for local governments in order to minimize pressure to further increase regressive local property taxes.
- No increase in the effective property tax burdens of homeowners and renters from reductions in property tax refunds that are paid renters and homeowner.

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Recommendations to expand tax compliance efforts will help ensure that those who owe taxes, pay taxes. The compliance initiative will increase tax collections $43.5 million in FY 2012-13, a net gain of $32.1 million after an $11.2 million investment in increased audit staff.

We look forward to working with you to help solve the serious budget deficit and achieve a balanced budget that will enhance confidence in Minnesota as a great place to live, work, and recreate.

Respectfully,

Dan Salomone
Acting Commissioner

Matt Massman
Assistant Commissioner for Tax Policy

STATE TAXES AND LOCAL AIDS AND CREDITS BUDGET PRESENTATION

Summary

The Governor's tax initiatives for the FY 2012 – 2013 biennium include revenue increases reflective of the need to find a permanent, responsible solution to the state's structural deficits and improve the progressivity of the overall state and local tax system. No reductions are made to property tax aid and credit programs to reduce the pressure for increases in the regressive property tax to fund local services. Over one-quarter of the proposed new tax revenues are temporary. The elimination of corporate tax preferences and loopholes, and the modernization of selected sales tax definitions, will help promote fairness among the businesses and consumers subject to those taxes.

The revenue proposals include:

- a new 4^{th} tier marginal income tax rate of 10.95% that provides needed ongoing resources; the new rate will increase income tax for 5.4 percent of tax filers.
- a temporary surtax on income over $500,000 that will provide immediate budget deficit relief;
- proposals to close corporate tax loopholes, ensure that corporations that profit from sales to Minnesota also pay tax in Minnesota, modernize statutory definitions to ensure the collectability of certain taxes; and
- conformity to most federal law changes and other tax policy adjustments that promote tax fairness, simplicity and understandability.

As summarized in the table below, the Governor's tax initiatives are expected to meet several tax policy and budget objectives. The negative numbers represent expenditures or revenue losses.

Governor's FY 2012-13 Tax Policy, Aids and Credits Budget Summary

Expenditure/Revenue Type (dollars in 000s)	Gov's Rec. FY 2012	Gov's Rec. FY 2013	Gov's Rec. FY 2014	Gov's Rec. FY 2015
Tax Fairness, Structural Budget Balance	$1,046,845	$953,829	$930,974	$1,000,929
Temporary Budget Deficit Relief	$483,800	$434,600	$248,400	$0
Corporate Loopholes, Tax Fairness	$199,300	$156,100	$158,600	$163,100
Sales Tax Fairness	$14,517	$16,883	$18,284	$19,815
Other Tax Simplifications	$5,969	$8,812	$8,812	$9,493
Federal Conformity, Simplification	($23,765)	$5,500	$12,535	($28,815)
Local Aids and Credits	$0	$0	$0	$0
Tax Changes from Other Budget Areas	*$2,600*	*$7,613*	*$7,713*	*$7,913*
Total Changes (General Fund)	**$1,729,266**	**$1,583,337**	**$1,385,144**	**$1,172,435**

STATE TAXES AND LOCAL AIDS AND CREDITS BUDGET PRESENTATION

The table below and the succeeding narratives describe the Governor's recommended tax changes and their fiscal impact. Some of the tax-related items affect other policy areas and more information on them can be found in other parts of the state budget presentation.

Governor's Recommended Tax Initiatives for the 2012-13 Biennium (dollars in '000s)

Governor's Recommendations	Fund	FY 2012 Gov Rec	FY 2013 Gov Rec	FY 2012-13 Gov Rec
Individual Income Tax				
New Bracket and Marginal Rate for Higher Incomes	General	1,003,900	886,400	1,890,300
Temporary Surtax on Income over $500,000	General	483,800	434,600	918,400
Part-Year Residents Maintaining a Minnesota Abode	General	15,000	15,000	30,000
Repeal Section 125 Health Insurance Credit	Other	0	55	55
Simplify the Non-Resident Entertainer Tax	General	0	28	28
Subtotal	General	**1,502,700**	**1,336,028**	**2,838,728**
	Other	-	55	55
Corporate Franchise Tax				
Repeal Foreign Royalties Subtractions and FOC Preferences	General	155,500	116,700	272,200
Unitary Business Sales Attributable to Minnesota	General	26,000	20,000	46,000
Repeal Exemption for Insurance Companies	General	9,700	7,300	17,000
Index Minimum Fees	General	8,000	8,000	16,000
Misc. Corporate Franchise Tax Items	General	100	4,100	4,200
Subtotal	General	**199,300**	**156,100**	**355,400**
Sales and Use Tax				
Affiliate Nexus	General	4,800	5,750	10,550
	Other	280	330	
Misc Sales Tax Items	General	9,717	11,133	20,850
	Other	533	621	
Subtotal	General	**14,517**	**16,883**	**31,400**
	Other	813	951	1,764
Federal Conformity				
Federal Tax Law Conformity	General	**(23,765)**	**5,500**	**(18,265)**
Subtotal	General	**(23,765)**	**5,500**	**(18,265)**
Other Tax Areas				
Estate Tax- Pass Through Entity (non-resident)	General	5,400	7,600	13,000
Motor Vehicle Sale Tax-Exemption of Emergency Response Vehicles	Other	(15)	(15)	(30)
Statewide Property Tax- Residential Tax on Homes Valued Over $1 Million	General	27,945	52,401	80,346
Misc. Special Taxes	General	569	1,212	1,781
	Other	21	76	97
Informational Tax Items Carried in Other Budget Areas	General	2,600	7,613	10,213
	Other	-	21,720	21,720
Subtotal	General	**36,514**	**68,826**	**105,340**
	Other	6	21,781	21,787
Total Tax Changes				
	General	**1,729,266**	**1,583,337**	**3,312,603**
	Other	819	22,787	23,606

Program: Individual Income Tax
Change Item: New Bracket and Marginal Rate for Higher Incomes

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$1,003,900	$886,400	$862,800	$931,100
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(1,003,900)	$(886,400)	$(862,800)	$(931,100)

Recommendation

The Governor recommends creating a new 4th bracket for upper incomes at a marginal income tax rate 10.95%. This change will generate $1.890 billion of additional revenue for the General Fund in FY 2012-13. The new bracket would begin at $150,000 taxable income for joint filers, $130,000 for head-of-household filers, and $85,000 for single filers. The new bracket would be effective beginning with tax year 2011. It would not be indexed for inflation.

Rationale

The Department of Revenue's Tax Incidence Study illustrates that the state and local tax system in Minnesota is regressive. In particular, the top ten percent of households measured by annual income pay a smaller share of their income to support state and local services than do households at lower incomes. Among the major tax types, the income tax is the only progressive tax and the property tax is the most regressive. The new marginal rate on higher income households reflects the Governor's priorities to increase state revenues to support general fund programs in a way that makes the overall tax system more progressive.

As shown in the table below, the tax burden as a percent of income is less for those with highest incomes than for the rest of the population. This pattern has become more pronounced in recent years.

Portion of the Population	Total Income	State and Local Tax Burden as Percent of Income (projected to 2011)
Lowest 90 percent	Less than $137,000	12.3%
Top 10 percent	$137,000 or more	10.1%
Top 5 percent	$194,000 or more	9.7%
Top 1 percent	$481,000 or more	8.8%

The additional tax bracket will raise taxes on 5.5 percent of those who file tax returns (9.6 percent of married filers and 2.3 percent of single filers). Those with incomes over $500,000 (0.8% of total filers) would pay 70 percent of the additional tax. The percentage of taxpayers affected would be even smaller if non-filers were included.

Program: Individual Income Tax
Change Item: New Bracket and Marginal Rate for Higher Incomes

Impact of 4th Tier (Tax Year 2011)

Income Range	Tax Returns	Returns with Tax Increase	Percent with Tax Increase	Average Tax Increase for Those with an Increase*	Increase in Tax as Percent of AGI*
Less than $75,000	1,864,063	-	0.0%	0	0.00%
$ 75,000 to $ 99,999	265,491	2,228	0.8%	1	0.00%
$100,000 to $199,999	309,785	50,903	16.4%	87	0.07%
$200,000 to $499,999	69,150	65,173	94.2%	2,720	1.05%
$500,000 or more	20,557	19,974	97.2%	24,801	2.48%
Total	2,529,046	138,278	5.5%	287	0.48%

* Federal deductability will reduce average tax change and effective tax increase by about 1/3rd.

The average income tax increase for the 5.5% of filers that will pay more income tax under this proposal is 0.5% of adjusted gross income. For those above $500,000, the average state tax increase is $24,801 or about 2.48% of income before reductions in federal tax due to increased deductions for state income tax paid. After federal deductions, the average income tax increase would be about 1.7% of income for taxpayers with incomes over $500,000.

Key Goals and Measures

State income tax receipts are a key component of Minnesota's state-local finance system and the resources collected through this change will fund other key goals and objectives of state and local government. The Governor's proposal to create a new 4th tier income tax rates for fewer than the top 10 percent will make the overall tax system more fair by increasing the income tax, which is the only progressive tax Minnesota has, and avoiding regressive local property tax increases, the most regressive tax.

The 2009 Tax Incidence Study found that the top 10 percent of Minnesotans—those with incomes over $137,000--paid 10.1 percent of their income in Minnesota state and local taxes while the bottom 90 percent paid about 12.3 percent. The Governor's recommendation for a new tax bracket will increase income tax for fewer than 10 percent of Minnesotans, about 5.4 percent of tax returns. Though it affects only about half of them, the Governor's proposed 4th tier rate would raise the average tax burden for the top 10 percent of taxpayers from 10.1 percent to about 11 percent; progressivity would be improved, but the top 10 percent will still pay a lower share of their income in tax than the bottom 90% of households.

Minnesota Milestone Indicator 33 (Price of Government) states that "government in Minnesota will be cost-efficient" and uses as an indirect measure of efficiency the amount of revenue collected by state and local governments as a share of Minnesota personal income, citing a historic range of 15% to 16.2%. With the adoption of the Governor's tax revenue changes, resources will be available to fund other key public priorities identified in the milestones and the price-of-government will continue to fall within the historic range.

Statutory Change: Minn. Stat. § Amends Minnesota Statutes Section 290.06.

Program: Individual Income Tax
Change Item: Temporary Surtax on Income Over $500,000

Preliminary Budget Option

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$483,800	$434,600	$248,400	$0
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(483,800)	$(434,600)	$(248,400)	$0

Recommendation

The Governor recommends a temporary surtax on income over $500,000. The surtax would be equal to an additional three-percent marginal rate on the income above $500,000 regardless of filing status. The temporary rate would apply to tax years 2011 through 2013 and generate $918.4 million in FY 2012-13.

Rationale

Under current law, Minnesota faces a significant structural deficit. However, the gap between general fund revenue and spending projected for the FY 2014-15 planning biennium is somewhat smaller than the immediate budget deficit projected for FY 2012-13. The surtax is proposed to be in place for tax years 2011, 2012, and 2013 only and then expire in recognition of the smaller projected deficit in future years and anticipated return to a stronger, more stable Minnesota economy.

The surtax will apply only to income over $500,000. The surtax will increase tax for an estimated 17,200 returns (0.7 percent of all filers) by an average of $20,300 for tax year 2011. When combined with the permanent addition of a new 4th tier, the average income tax increase for filers with annual income exceeding $500,000 per year would be $41,546, or about 4.15% of income, for taxpayers with incomes over $500,000 before reductions in federal tax due to increased deductions for state income tax paid. After federal deductions, the average income tax increase would be about 2.7% of income for taxpayers with incomes over $500,000.

Combined Impact of 4th Tier and Income Tax Surcharge (Tax Year 2011)

Income Range	Tax Returns	Returns with Tax Increase	Percent with Tax Increase	Average Tax Increase for Those with an Increase*	Increase in Tax as Percent of AGI*
Less than $75,000	1,864,063	-	0.0%	0	0.00%
$ 75,000 to $ 99,999	265,491	2,228	0.8%	1	0.00%
$100,000 to $199,999	309,785	50,903	16.4%	87	0.07%
$200,000 to $499,999	69,150	65,173	94.2%	2,723	1.05%
$500,000 or more	20,557	20,006	97.3%	41,546	4.15%
Total	2,529,046	138,310	5.5%	421	0.70%

* Federal deductability will reduce average tax change and effective tax increase by about 1/3rd.

Program: Individual Income Tax
Change Item: Temporary Surtax on Income Over $500,000

Key Goals and Measures

The 2009 Tax Incidence Study found that the top 1 percent of Minnesotans—those with incomes over about $481,000--had paid 8.8 percent of their income in state and local taxes while the bottom 90 percent paid 12.3 percent of their income in state and local taxes. The Governor's recommendation for a temporary tax surtax targeted at incomes over $500,000 is needed to balance the state budget and to increase the progressivity of the overall tax system. If the income tax burden for the top 1% had increased by a percentage similar to the Governor's proposal, the average state and local tax burden for the top 1% would increase to 12.3%, the same as the state and local tax burden for the bottom 90% of households. Without the temporary surtax, the new 4th tier would make the state and local tax system more progressive than current law but the overall tax burden for the top 1% would be about 11%.

Minnesota Milestone Indicator 33 (Price of Government) states that "government in Minnesota will be cost-efficient" and uses as an indirect measure of efficiency the amount of revenue collected by state and local governments as a share of Minnesota personal income, citing a historic range of 15% to 16.2%. With the adoption of the Governor's tax revenue changes, resources will be available to fund other key public priorities identified in the milestones and the price-of-government will continue to fall within the historic range.

Statutory Change: Minn. Stat. § 290.06 is amended by adding a section.

Program: Individual Income Tax
Change Item: Part-Year Residents Maintaining a Minnesota Abode

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$15,000	$15,000	$15,000	$15,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(15,000)	$(15,000)	$(15,000)	$(15,000)

Recommendation
The Governor recommends extending the income tax to persons who are present in the state for more than 60 days but less than 183 and who maintain an abode in Minnesota for at least six months. An exception is made for days an individual is in the state for the purpose of receiving medical services. The provision will generate $30 million a biennium beginning in FY 2012-13.

Rationale
Under current law, an individual is a Minnesota resident for income tax purposes if they are domiciled in Minnesota or if they maintain an abode in Minnesota and are present in the state for 183 days or more. The 183-day bright line test allows for individuals who spend substantial portions of the year in Minnesota (up to 182 days), and maintain an abode in Minnesota, to avoid paying Minnesota income tax but continue to benefit from public services, natural resources and arts and cultural opportunities in Minnesota.

Under the change proposed by the Governor, individuals will continue to make lifestyle choices about where to live and vacation but will no longer be able to avoid Minnesota income taxes simply by being physically present in the state for fewer than 183 days.

Individuals who maintain an abode in Minnesota and are physically present in the state for more than 60 days, but less than 183, will be considered “part-year residents.” Part-year residents will be subject to tax on their Minnesota-sourced income (as they are now) and a pro-rata share of all other income based on the number of days they are present in the state. A credit will be granted for income taxes paid on the same income to other states if the other state does not allow a credit for tax paid to Minnesota. Days an individual is in the state receiving, or caring for a close family member who is receiving medical services will be excluded from determination of part-year resident.

The proposed change will be effective beginning with tax year 2011.

Key Goals and Measures

The Governor’s recommendation will make the overall tax system more fair by requiring those who benefit from Minnesota’s state and local public services for a substantial portion of the year to also contribute to the cost of providing those services.

Statutory Change: Amends Minn. Stat. § 290.01, subd. 7; 290.06, subd. 22; and 290.17, subd 1.

Program: Individual Income Tax
Change Item: Repeal Section 125 Health Insurance Credit

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Transfer In	0	$(55)	$(60)	$(65)
Revenues	0	55	60	65
HCAF Fund				
Transfer Out	0	(55)	(60)	(65)
Revenues	0	0	0	0
Net Fiscal Impact	0	$(55)	$(60)	$(65)

Recommendation
The Governor recommends repealing Minnesota Statutes Section 290.0678, which provides for a tax credit equal to 20 percent of the health insurance premiums paid for a plan under I.R.C. Section 125. Under current law, the Health Care Access Fund (HCAF) reimburses the general fund for any lost income tax revenue attributable to this credit. With the repeal, there will be no net effect on the general fund as the tax revenue change will be offset by the repeal of the transfer from the HCAF; the HCAF will no longer make a transfer to the general fund.

Rationale
Consistent with the objectives of the Federal Patient Protection and Affordable Care Act of 2010, the Governor recommends ongoing efforts to improve access to affordable health care for all Minnesotans. The section 125 credit is a narrow and inefficient incentive for promoting access to health care. The income ranges eligible for the credit are narrow and it is unlikely a taxpayer could be certain they would fall into an eligible range until the tax year is over. The provisions are complicated to administer, both for the state and the taxpayer and participation is low.

- As of October 1, 2010, this credit was claimed by only 122 taxpayers on tax year 2009 returns, for a total amount of $44,140, or an average of $362 per return.

The credit is available to taxpayers who pay health insurance premiums for the first twelve months of coverage under a Section 125 plan administered by their employers, who did not have health insurance for at least a year prior to Section 125 coverage, and who meet certain income restrictions.

Effective beginning with tax year 2012.

Key Goals and Measures
The elimination of the tax preference will contribute to making state government more efficient by eliminating a complicated tax expenditure that benefits few individuals who will be more effectively and efficiently served by a reformed health care delivery system. The elimination of the tax preference will eliminate the need for an entire Minnesota income tax form (M1H).

Statutory Change: Repeal Minn. Stat. § 290.0678

Program: Individual Income Tax
Change Item: Simplify the Non-Resident Entertainer Tax

Preliminary Budget Option

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$0	$28	$30	$31
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$0	$(28)	$(30)	$(31)

Recommendation
The proposed change revises how the current law non-resident entertainer tax is administered to make it more transparent and efficient for both taxpayers and tax administrators. The change is designed to be largely revenue neutral but does have a modest revenue gain of $28,000 in FY 2012-13.

Rationale
Under current law, non-resident entertainers are not subject to Minnesota income tax but are subject to a 2 percent tax on their gross compensation. Current law requires promoters to withhold two percent from all compensation paid to those entertainers from the first dollar. All nonresident entertainers are then allowed a $120 nonrefundable credit against the tax, which they take when they file their nonresident entertainer tax return.

The proposed change would repeal the $120 credit, require a promoter to withhold 2 percent only on the amounts above $600 that the promoter pays the nonresident entertainer in a year (the same as the federal informational return requirement for this kind of income), and exempt entertainers who receive total compensation less than the individual filing requirements ($9,350 in 2010).

Effective beginning with tax year 2012.

Key Goals and Measures
The revisions to the non-resident entertainer tax further the goal of making Minnesota state government more efficient and more accessible for citizens and customers by simplifying compliance with this tax for taxpayers, promoters and entertainers, and tax administrators.

Statutory Change: Amends Minn. Stat. § 290.9201.

Program: Corporate Franchise Tax
Change Item: Repeal Foreign Royalties Subtractions and FOC Preferences

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$155,500	$116,700	$118,500	$122,500
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(155,500)	$(116,700)	$(118,500)	$(122,500)

Recommendation
The Governor recommends repealing the current law subtraction for foreign royalties and provisions for foreign operating corporations (FOC's). The change will increase general fund revenues by $272.2 million in FY 2012-13.

Rationale
The current law phase-in to 100 percent sales factor apportionment by 2014 promotes a competitive tax climate for Minnesota corporations by ensuring that Minnesota corporations will only be taxed on that portion of their income allocated to Minnesota based on their percentage of sales in Minnesota. As a result, sales apportionment addresses many of the competitive disadvantages that the royalties subtraction and FOC provisions were originally intended to address.

The foreign royalties subtraction was originally designed to give tax relief to domestic corporations with foreign royalties at a time when those royalties were not included in the income apportionment calculation. While the original objective was to exclude income from outside the United States in the determination of Minnesota taxable income, amendments to the apportionment provisions to include royalties in determining the sales factor have now nullified the original objective for the subtraction. Likewise, the original justification for the FOC provision has also diminished because the move to 100% sales apportionment eliminates disadvantages that existed between companies that had overseas operations relative to those that owned overseas corporate subsidiaries.

While the foreign royalties subtraction and FOC provisions continue to provide real benefits to non-Minnesota corporations, those tax preferences can no longer be afforded given the importance of returning stability to the state budget and economy and funding the programs essential to providing a highly educated and productive workforce.

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund Revenues				
Foreign Operating Corps (FOC)	42,300	31,900	32,500	33,400
Foreign Royalties Subtraction	111,200	82,800	84,000	87,100
Interaction	2,000	2,000	2,000	2,000
Net Fiscal Impact	(155,500)	(116,700)	(118,500)	(122,500)

Under current law, the subtraction of 80% of royalties, fees, or other like income accrued or received from a foreign operating corporation (FOC) or a foreign corporation which is part of the same unitary business as the receiving corporation, is a subtraction against income. Under the change:

- all domestic and foreign royalties will be treated in a consistent manner and conform to the Internal Revenue Code treatment of this income; and
- the disparity with similarly situated sellers of tangible property to a FOC or foreign affiliate, for which there is no similar subtraction, will be eliminated;

- The elimination of both provisions will also enhance compliance by simplifying the tax code and allowing corporate tax audits to focus on compliance issues instead of verifying that the taxpayer has complied with the foreign royalties or the complicated FOC tax regime.

Program: Corporate Franchise Tax
Change Item: Repeal Foreign Royalties Subtractions and FOC Preferences

Key Goals and Measures
The Goal of Minnesota Milestones 2010 Indicator 30: Price of Government is that "Government in Minnesota will be cost-efficient, and services will be designed to meet the needs of the people who use them." By repealing the royalties subtraction and FOC provisions, tax administration resources will be available to identify and insure compliance in the other aspects of the corporate tax law.

This recommended change is consistent with the Department of Revenue strategy that "We will identify and recommend changes to align the revenue system with economic activity." The repeal of the royalties subtraction aligns the revenue system with current economic activities and helps the department to be more cost-efficient in administering the corporate tax. Audits, appeals, and litigation pertaining to royalties subtraction and FOC provisions will be eliminated for tax audit years after 2010.

Statutory Change: Amend Minn. Stat. § 290.01, Subd. 19d(10); 290.0921, Subd. 3(13); 290.095, Subd. 2(a); 290.17, Subd. 4(g)(2) and (i); and 290.191, Subd. 5(a)(6)

Program: Corporate Franchise Tax
Change Item: Unitary Business Sales Attributable to Minnesota

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$26,000	$20,000	$20,000	$20,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(26,000)	$(20,000)	$(20,000)	$(20,000)

Recommendation
The Governor recommends amending statutes to require that all sales to this state of a unitary business to be included in the sales factor for this state. The proposal will increase general fund revenues by $46.0 million in FY 2012-13.

Rationale
As more states have moved closer to full single sales apportionment for corporate tax purposes, some companies have attempted to avoid taxation by restructuring their business to locate all their sales in a company that is in the unitary group but has no nexus in Minnesota. Current law only requires members of a unitary business to include their sales in the numerator of the sales factor if they have Minnesota nexus. The proposed revision to our definition of Minnesota sales would require that sales by members of the unitary business be included even if they have no Minnesota nexus.

The basis for unitary filing is to ensure that the income of the unitary business subject to Minnesota corporate tax reflects the income attributable to Minnesota based on the market provided to the unitary business. When sales to customers in Minnesota by a member of a unitary business are not included in the numerator of the sales factor the net income of the unitary business allocated to Minnesota is understated. Requiring that all Minnesota sales of the unitary business are included in the numerator of the sales factor ensures that the appropriate net income of the unitary business is allocated to Minnesota. By enacting this recommendation Minnesota will be allocated the proper income of the unitary business. This will maintain an even playing field for all businesses benefiting from the Minnesota marketplace.

Effective for taxable years beginning after December 31, 2010. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures
The recommended change promotes tax compliance and tax fairness by limiting the ability of corporate taxpayers to benefit from sales to the Minnesota marketplace by structuring its unitary businesses to avoid Minnesota corporate franchise tax. Further, the proposal levels the playing field by promoting the equal treatment of business competitors for corporate tax purposes.

Statutory Change: Minn. Stat. § 290.191, Subd. 5.

Program: Corporate Franchise Tax
Change Item: Repeal Exemption for Insurance Companies

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$9,700	$7,300	$7,600	$7,800
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(9,700)	$(7,300)	$(7,600)	$(7,800)

Recommendation
The Governor recommends repealing the current law allowing insurance companies an exemption from the corporate franchise tax. The change will increase general fund revenues by $17.0 million in FY 2012-13.

Rationale
Under current law, unlike other corporations conducting business in Minnesota, insurance company income is exempt from determination of corporate tax liability for the activities it conducts in Minnesota. The exemption was enacted in 2001 leaving insurance companies subject to only the tax based on insurance premiums. This exemption was enacted after the federal 1999 Gramm-Leach-Bliley Act (GLB) was passed which allowed banks, security firms, and insurance companies to consolidate but before the effects of GLB were reflected on the corporate franchise tax returns. For years before 2001, insurance companies were subject to the corporate franchise tax and were allowed a credit for taxes paid based on insurance premiums.

Repealing the exemption will put insurance companies on par with other corporations subject to the Minnesota corporate franchise tax. A subtraction will be allowed for taxes paid on premiums sold in Minnesota and exemptions will be granted to insurance companies based in states with retaliatory tax provisions to ensure that Minnesota based insurance companies are not disadvantaged relative to their competitors in other states.

The change will be effective for taxable years ending after December 31, 2010. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures
This recommended change is the result of the Department of Revenue strategy to “identify and recommend changes to align the revenue system with economic activity.” The repeal of the exemption for insurance companies aligns the revenue system with current economic activities.

Statutory Change: Minn. Stat. § 290.05, Subd. 1(c)

Program: Corporate Franchise Tax
Change Item: Index Minimum Fees

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$8,000	$8,000	$8,000	$8,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(8,000)	$(8,000)	$(8,000)	$(8,000)

Recommendation
The Governor recommends indexing the minimum fee brackets and tax amounts for inflation since 1990. The minimum fee was established in 1990 and has not been adjusted since that time. The change will increase general fund revenues by $16.0 million in FY 2012-13.

Rationale
The minimum fee was established to assess a minimum tax on the opportunity to do business in Minnesota. As adopted in 1990, the minimum fee is based on the sum of property, payroll and sales in Minnesota with six brackets and fees ranging from $0 to $5,000. A total of $60 million is paid annually by S-corporations, partnerships, and C-corporations. The brackets and fee amounts have not been adjusted to reflect changes in the economy since 1990. The proposal increases both brackets and minimum fees for inflation since 1990.

Indexing the minimum fee brackets will prevent taxpayers from being subject to the next higher bracket based solely on economy changes while updating the brackets and amounts since 1990 will ensure that corporations benefiting from sales to the Minnesota market place will pay a minimum tax to support the public investments that sustain that marketplace.

The change will be effective for taxable years ending after December 31, 2010. The indexing of the minimum fee brackets and tax amounts is facilitated as part of the annual updates to publications and computer systems. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures
This recommended change is the result of the Department of Revenue strategy to "identify and recommend changes to align the revenue system with economic activity." Indexing the minimum fee brackets and tax amounts aligns the revenue system with current economic activities.

Statutory Change: Minn. Stat. § 290.0922 Minimum fee;

Current Law Minimum Fee

Sum of Minnesota Property, Payroll, and Sales	Annual Fee
Less than $ 500,000	$0
$ 500,000 to $ 999,999	$100
$ 1,000,000 to $ 4,999,999	$300
$ 5,000,000 to $ 9,999,999	$1,000
$ 10,000,000 to $19,999,999	$2,000
$ 20,000,000 or more	$5,000

Proposed Minimum Fee

Sum of Minnesota Property, Payroll, and Sales	Annual Fee
Less than $870,000	$0
$870,000 to $1,739,999	$170
$1,740,000 to $8,689,999	$520
$8,690,000 to $17,369,999	$1,740
$17,370,000 to $34,749,999	$3,470
$34,750,000 or more	$8,690

Program: Corporate Franchise Tax
Change Item: Foreign Partnership Income

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	0	$3,000	$3,000	$3,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	0	$(3,000)	$(3,000)	$(3,000)

Recommendation

The Governor recommends amending the statutes to conform to the federal law treatment of foreign entities in Section 701 of the Internal Revenue Code. Under federal law, the distributive share of income from all domestic and foreign partnerships flows to its domestic owners. In contrast, current Minnesota law excludes the net income and apportionment factors of foreign partnerships in calculating net income and apportionment factors for a unitary business. The change will increase general fund revenues by $3.0 million in FY 2012-13.

Rationale

- Under current law, income that a domestic corporation recognizes from these foreign entities is not included in the taxpayer's Minnesota taxable income.
- The recommendation treats the recognized income in a manner that is consistent with federal treatment under the Internal Revenue Code.
- The taxpayer's Minnesota taxable income will include the portion attributed to income that the taxpayer recognizes from all sources.
- Treating income recognized by the Internal Revenue Code in a consistent manner for Minnesota tax purpose will result in greater tax compliance by simplifying the tax treatment of this income. Corporate audits will focus on other compliance issues instead of verifying that the taxpayer has excluded the proper foreign entities.
- This change would be effective for the taxable years ending after December 31, 2011. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures

The Goal of Minnesota Milestones 2010 Indicator 30: Price of Government is that "Government in Minnesota will be cost-efficient, and services will be designed to meet the needs of the people who use them." Removing the foreign entities exclusion simplifies taxpayer reporting requirements and tax administration resources will be available to identify and ensure compliance in the other aspects of the corporate tax law.

This recommended change is the result of the Department of Revenue to "identify and recommend changes to align the revenue system with economic activity." The treatment of foreign entities in a manner consistent with the Internal Revenue Code helps the department to be more cost-efficient in administering the corporate tax. The number of audits, appeals, and litigation pertaining to exclusion of foreign entities will be reduced for tax audit years after 2010.

Statutory Change: Minn. Stat. § 290.17, Subd. 4(f) and (h)

Program: Corporate Franchise Tax
Change Item: Exclude REIT Dividends from the Dividend Received Deduction

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	0	$1,000	$1,000	$1,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	0	$(1,000)	$(1,000)	$(1,000)

Recommendation
The Governor recommends eliminating an unintended double-deduction by excluding dividends received from a real estate investment trust (REIT) in calculating the deduction allowed to a corporation for dividends received deduction (DRD) from another corporation. The DRD allowed for dividends received from a REIT affords the receiving corporation a tax benefit not intended by the DRD provision. The change will increase general fund revenues by $1 million in FY 2012-13.

Rationale
Under current law, unlike other corporations, a REIT is allowed a deduction for the dividends it pays to shareholders. The DRD was enacted to reduce the perception of double taxation on income. The paying corporation's dividends are usually the product of the corporation's profit which is subject to corporate tax. Relief from possible double taxation is afforded corporations receiving a dividend through the DRD. The dividends paid by a REIT are not the product of income that has been subject to the corporate tax.

The proposed change would remove the tax benefit afforded corporations receiving dividends from REITs that is not consistent with the intent of the DRD provision. As a result, dividends received from a REIT would be treated in a manner consistent with the treatment provided under the Internal Revenue Code.

This change is effective for the taxable years ending after December 31, 2011. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures
This recommended change is the result of the Department of Revenue strategy to "identify and recommend changes to align the revenue system with economic activity." The exclusion of dividends received from a REIT in calculating the DRD aligns the revenue system with current economic activities and helps the Department to be more cost-efficient in administering the corporate tax.

Statutory Change: Minn. Stat. § 290.21(c)

Program: Corporate Franchise Tax
Change Item: Clarify Research Credit Base Period Documentation

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$0	$(200)	$(200)	$(200)
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$0	$200	$200	$200

Recommendation
The Governor recommends modifying documentation requirements so that taxpayers may benefit from the current law research and development credit when limited base period documentation is available. The change will decrease general fund revenues by $200,000 in FY 2012-13.

Rationale
Under current law, Minnesota businesses may earn a Research and Development Credit (R&D Credit) equal to 10% of the first $2 million and 2.5% of the excess over $2 million of qualifying research and development expenses in Minnesota. Qualifying expenses are calculated relative to a base amount. Some taxpayers lack documentation on R&D spending in the base years of 1984-1988. Without this information, no base year percentage can be computed and no R &D tax credit can be computed. Establishing such documentation would be burdensome for the businesses and difficult to audit and verify for the state.

The recommendation allows the taxpayer to use a base year percentage of 16% when the taxpayer no longer has documentation for 1984 through 1988. Taxpayers that identify that they may be allowed the credit may no longer have documentation from 1984 through 1988.

- The credit provision currently requires that 1984 through 1988 base period documentation must be provided to establish the base year percentage. The maximum base year percentage by statute is 16 %. It is to the benefit of the taxpayer to have the lowest base year percentage. Allowing the maximum base year percentage affords taxpayers the credit when the documentation is no longer available.
- Taxpayers will be allowed the credit when documentation of old years is no longer available.

This change is effective for taxable years ending after December 31, 2010. The department will notify the taxpayers and tax preparation community through the normal publications and internal tax return processing systems will be modified to reflect this change.

Key Goals and Measures
The Goal of Minnesota Milestones 2010 Indicator 30: Price of Government is that “Government in Minnesota will be cost-efficient, and services will be designed to meet the needs of the people who use them.” By affording this documentation relief taxpayers are afforded the credit while reducing their documentation requirements.

This recommended change is the result of the Department of Revenue strategy to “identify and recommend changes to align the revenue system with economic activity.” It is not economically for taxpayers to retain old year documentation. This provision aligns the credit provisions with economic reality allowing additional taxpayers to avail themselves to the tax benefits of the credit.

Statutory Change: Minn. Stat. § 290.068, Subd 2

Program: Corporate Franchise Tax
Change Item: Adoption of Economic Substance Test

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$100	$300	$700	$1,000
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(100)	$(300)	$(700)	$(1,000)

Recommendation
The Governor recommends adopting statutory language requiring that business transactions meet an economic substance test to be allowed in determining Minnesota taxable income in conformance with federal case law. This tax policy change will have a modest revenue gain of $400,000 in FY 2012-13 but will foreclose the opportunity for businesses to structure themselves solely to avoid taxes.

Rationale
Unlike most states, Minnesota has not adopted an economic substance test. Such a provision requires that transactions have an objective and appreciable net effect on the taxpayer's economic position apart from tax effects. Adoption of this provision is not anticipated to affect businesses other than circumstances in which a business is structuring itself simply to avoid taxes.

Currently, the tax laws have been administered with the understanding the national case law requiring economic substance was required to allow transactions that affect Minnesota taxable income. However, the Minnesota Supreme Court recently held in *HMN Financial, Inc*. that the Minnesota Commissioner of Revenue does not have the authority to attribute income and assess taxes to a business on the grounds that the business structured itself to comply with the relevant tax statutes and was motivated to do so solely by tax avoidance.

The proposed change will apply the standards held in federal case law, which are a well understood and accepted standard for establishing economic substance of business structures and transactions, to all transactions that affect Minnesota taxable income. While the federal case law has been codified in federal law, the recent Minnesota Supreme Court decision in *HMN Financial, Inc*. demonstrates the importance of adopting an economic substance standard that will apply to transactions only affecting the determination of Minnesota income.

This change will be effective for taxable years ending after December 31, 2010. The department will notify the taxpayers and tax preparation community through the normal publications.

Key Goals and Measures
The Goal of Minnesota Milestones 2010 Indicator 30: Price of Government is that "Government in Minnesota will be cost-efficient, and services will be designed to meet the needs of the people who use them." By enacting the economic substance provision taxpayers will avoid schemes designed solely to reduce their tax liability which will allow tax administration resources to be available for identifying and insuring compliance in the other aspects of the corporate tax law.

Statutory Change: Minn. Stat. § 270C.01; 270C.03; 270C.33, Subd. 6; 289A.122; and 289A.60 (if an accompanying civil penalty is enacted)

Fiscal Impact ($000s)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
General Fund					
Expenditures	0	0	0	0	0
Revenues—Income Tax	$(16,815)	$(37,415)	$(18,610)	$7,095	$(8,305)
Revenues—Corporate Tax	(6,425)	13,650	24,110	5,440	(20,510)
Other Fund					
Expenditures	0	0	0	0	0
Revenues	0	0	0	0	0
Net Fiscal Impact	$23,240	$23,765	$(5,500)	$(12,535)	$28,815

Recommendation

The Governor recommends conforming Minnesota's income tax law to most federal changes made after March 18, 2010. The changes proposed by the Governor will reduce general fund revenues by $23.2 million in FY 2011 and by $18.3 million in FY 2012-13, or a total of $41.5 million for the three years. The proposed changes affect both individual income and corporate tax filers, including many provisions relevant to tax year 2010.

Rationale

Federal taxable income is the starting point for determining Minnesota taxable income and both Minnesota's individual income tax and corporate franchise tax use federal tax definitions. While full conformity generally promotes tax system transparency and simplicity for taxpayers, partial conformity has sometimes been pursued when budget constraints or state-federal tax policy differences exist and workable alternatives can be found. For example, in recent years Minnesota has not fully conformed to federal changes related to Section 179 expensing and bonus depreciation deduction provisions.

The Governor proposes to conform to almost all provisions in four federal bills: the Patient Protection and Affordability Care Act of 2010 (P.L. 111-148, enacted March 2010); the Health Care and Education Reconciliation Act of 2010 (P.L. 111-152, enacted March 2010); the Small Business Jobs Act of 2010 (P.L. 111-240, enacted September 2010), and the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312, enacted December 2010).

Fiscal Impact ($000s)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Income Tax					
Health Care Bills	(2,280)	(4,110)	(4,260)	3,840	2,940
Small Business Jobs Act	(230)	6,450	3,630	(2,795)	(5,780)
Tax Relief, UI, Job Creation	(14,305)	(39,755)	(17,980)	6,050	(5,465)
Income Tax Total	(16,815)	(37,415)	(18,610)	7,095	(8,305)
Corporate Tax					
Small Business Jobs Act	(1,225)	11,800	3,100	(4,700)	(8,200)
Tax Relief, UI, Job Creation	(5,200)	1.850	21,010	10,140	(12,310)
Corporate Tax Total	(6,425)	13,650	24,110	5,440	(20,510)
Net Fiscal Impact	23,240	23,765	(5,500)	(12,535)	28,815

The Governor proposes not to conform to the federal changes listed below:

- increased Section 179 expensing and bonus depreciation, which the Governor proposes be treated as in past years (80 percent add-back with that amount subtracted over the following 5 years);
- the additional standard deduction for married filers;
- the limit on itemized deductions and phase-out of personal exemptions; and
- the exception under Subpart F for active financing.

The provisions for which the Governor does propose conforming to federal provisions include the following:

- deduction for tuition and expenses;
- deduction for K-12 educator classroom expenses (up to $250);
- Working Family Credit, increase the phase-out range for married filers by $5000.
- Dependent Care Credit, increase eligible amounts and credit rates;
- exclusion of employer-provided education assistance;
- tax-free IRA distributions to charities (individuals age 70 ½ and over);
- enhanced charitable deduction for food, books, and computers donated from business inventories;
- deduction for mortgage insurance premiums; and
- exclusion of employer-provided insurance for children up to age 26.

Key Goals and Measures

Federal conformity will simplify income tax filing, eliminate the need for businesses to keep two sets of books for tax purposes (one for federal tax and one for Minnesota tax), and provide benefits to many Minnesota residents. Conforming to the remaining provisions is either too costly (additional standard deduction for married couples, adoption of federal Section 179 expensing limits) or would benefit only a limited number of high-income Minnesotans (repeal of limit on itemized deductions and phase-out of personal exemptions).

Statutory Change: Amends Minn. Stat. § 289A.02, 290.01, subds. 19, 19a, 19c, 19d, and 31 and 290A.03.

Program: Sales and Use Tax
Change Item: Affiliate Nexus

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$4,800	$5,750	$6,320	$6,960
Other Fund				
Expenditures	0	0	0	0
Revenues - Legacy Funds	280	330	370	400
Net Fiscal Impact	$(5,080)	$(6,080)	$(6,690)	$(7,360)

Recommendation

The Governor proposes amending statutes for sales tax nexus to create a rebuttable presumption that a retailer maintains a place of business in the state if they enter into an agreement with a solicitor for the referral of Minnesota customers for a fee and the retailer's gross receipts are at least $10,000 over a 12-month period. The proposal will result in an additional $10.6 million of sales tax collections in FY 2012-13 on the sale of products that are already subject to the sales and use tax.

Rationale

The proposed change will promote fairness and compliance with the sales and use tax by clarifying the expectation that remote sellers of taxable products to Minnesota purchasers should collect and remit taxes as do storefront retailers selling the same products.

Under current law, taxable purchases for use and consumption in Minnesota are already subject to sales and use tax. However, it is difficult to collect the tax on purchases made from remote sellers who are not required to collect the tax for Minnesota because they do not have a physical presence in Minnesota. Many of these remote sellers sell their products over the Internet. This change would require remote sellers who sell to Minnesota purchasers that are referred under an agreement by a business that has nexus (physical presence) in Minnesota to collect the sales and use tax on those purchases. This situation typically occurs when a purchaser goes to a Minnesota seller's web-site and then is directed to a remote seller's web-site to purchase products.

Several states have taken steps to ensure the collectability of tax by remote sellers in recent years and more states are considering such action in current legislative sessions. The current proposal is similar to the approach adopted by the state of New York a few years ago.

Effective for sales and purchases made after June 30, 2011.

Key Goals and Measures

This change would create fairness by leveling the playing field between brick and mortar businesses located within Minnesota and out-of-state sellers who do not have a physical presence in Minnesota. This change would also reduce the burden on purchasers to file Individual Use Tax returns to remit their use tax on their purchases.

Statutory Change: Minn. Stat. § 297A.66 is amended by adding a subdivision.

Program: Sales and Use tax
Change Item: Exempt Ring Tones

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$(200)	$(210)	$(200)	$(190)
Other Fund				
Expenditures	0	0	0	0
Revenues -- Legacy fund	(10)	(12)	(10)	(10)
Net Fiscal Impact	$210	$222	$210	$200

Recommendation
The Governor recommends repeal of the sales and use tax on ring tones to maintain Minnesota's compliance with the Streamlined Sales and Use Tax Agreement (SSUTA). The change will result in a general fund revenue loss of $410,000 in FY 2012-13.

Rationale
Under current law, ring tones are a taxable service but downloads of other digital audio works are not. In order to be in compliance with the Streamlined Sales and Use Tax Agreement, Minnesota's statutes need to be amended to either impose the sales tax on all digital audio works (which includes ring tones) or repeal the tax on ring tones.

Effective July 1, 2011.

Key Goals and Measures
This would put Minnesota into compliance with the Streamlined Sales and Use Tax Agreement.

Statutory Change – Amends Minn. Stat. § 297A.61, subd. 3.

Program: Sales and Use Tax
Change Item: Parallel Taxation of Direct Satellite Services

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$1,070	$1,240	$1,310	$1,390
Other Fund				
Expenditures	0	0	0	0
Revenues-Legacy Funds	60	70	75	80
Net Fiscal Impact	$(1,130)	$(1,310)	$(1,385)	$(1,470)

Recommendation
The Governor recommends expanding the definition of "direct satellite service" to include digital video recorder (DVR) services and programming services requiring subscriber interaction, such as pay-per-view. Those services are already taxable when provided by a cable TV provider. The proposal will increase general fund revenue by $2.3 million in FY 2012-13.

Rationale
As the economy and technology continue to evolve, statutory definitions related to the applicability of the sales tax often need to be adjusted to keep pace and to ensure a level playing field with taxation of similar products and services.

Under current law, DVR services and programming services are taxable when sold by a cable TV service provider but are not taxable when sold by a direct satellite service provider. The proposal would treat similar services equally by having the sales tax apply to all DVR and programming services, whether they are sold by a cable TV or direct satellite provider.

Effective July 1, 2011.

Key Goals and Measures
This promotes fairness and creates ease of administration. This is an instance where the law has not kept up with technology.

Statutory Change – Amends Minn. Stat. § 297A.61, subds. 25 and 27.

Program: Sales and Use Tax
Change Item: On-line Lodging Reservations

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$4,000	$4,550	$4,700	$4,800
Other Fund				
Expenditures	0	0	0	0
Revenues – Legacy Funds	200	250	300	300
Net Fiscal Impact	$(4,200)	$(4,800)	$(5,000)	$(5,100)

Recommendation
The Governor recommends clarifying statutes to confirm the original intent of the sales tax on lodging and related services that the tax is applicable to the full price and charges paid by the consumer for the occupancy, including any reservation or similar ancillary services that are part of the transaction. The clarification will increase General Fund collections by $8.6 million in FY 2012-13 from transactions already presumed to be taxable by consumers.

Rationale
The proposed statutory clarification ensures the collectability of sales tax on lodging services that have been taxable in the past remain taxable despite changes in industry business models.

Historically, when an individual made a reservation for lodging services through an intermediary such as a travel agent, the individual paid nothing to the travel agent. Instead, the consumer paid the hotel for the full amount of lodging services plus sales tax and the hotel then paid the travel agent a percentage of the amount collected from the consumer for lodging services after the individual checked out of the hotel. With changes in travel industry business models, consumers often make hotel reservations through agents and pay the agents for the lodging services at the time of reservation. Agents then pay the hotel for the accommodations based on agreements between the agent and the hotel. Typically the amount paid to the hotel is net of a fee retained by the agent that is similar to fee the hotel would have paid to the agent under the former business model, as well as possible discounts the agent may get for purchasing blocks of rooms from the hotel. Currently, intermediaries are not charging tax on this additional fee so the consumer pays less tax if they reserve a room through an intermediary as compared to the amount of tax that would be paid if the consumer made the reservation directly with the hotel even though in both situations the price of the room is the same. This change would make the tax the same in both situations.

Statutes will be clarified to define any person or entity, other than an accommodations provider (i.e., other than the hotel), that facilitates the sale of lodging as defined in section 297A.61, subdivision 3, paragraph (g), clause (2), and that charges a room charge to the customer as an “accommodations intermediary.” Accommodations intermediaries will be required to collect and remit sales tax on the full amount charged for lodging services. The term "facilitates the sale" includes brokering, coordinating, or in any way arranging for the purchase of or the right to use accommodations by a customer.

Effective day is day after final enactment.

Key Goals and Measures
To create fairness by leveling the playing field between hotels and accommodations providers who sell the same product and to reduce erosion of the sales and use tax base.

Statutory Change: Amends Minn. Stat. § 297A.61 and creates new statutory language.

Program: Sales and Use Tax
Change Item: Event Admissions

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$3,400	$3,500	$3,600	$3,700
Other Fund				
Expenditures	0	0	0	0
Revenues-Legacy Fund	200	200	210	210
Net Fiscal Impact	$(3,600)	$(3,700)	$(3,810)	$(3,910)

Recommendation
The Governor recommends that the sales and use tax be imposed on admissions to suite rentals at stadiums and to admissions to exhibitions and selling events. The change will increase general fund sales tax collections by $6.9 million in FY 2012-13.

Rationale
Under current law, admission charges to any places of amusement or athletic events such as admissions to musical concerts, dances, motion picture theaters or theaters presenting stage shows and plays, and admissions to golf courses, tennis courts, skating rinks, swimming pools, and to state, county and other fairs are taxable, but admissions to other events and venues are not taxed. This proposal would modify the definition of taxable admissions to include admissions to home and garden, boat, auto, and similar shows, and on rental of box seats and suites at stadiums.

While current law statutes could be interpreted to allow for the imposition of sales tax on the rental of box seats and suites at stadiums, Minnesota currently treats these facilities as exempt rental of real property rather than as admissions.

By including admissions to rental of box seats and suites at stadiums as well as other venues, such as admissions to product event shows at convention centers, the playing field will be leveled between consumption of these admissions and admissions that are already being taxed under current law.

Effective July 1, 2011.

Key Goals and Measures
This would provide consistency and support ease of administration.

Statutory Change – Amends Minn. Stat. § 297A.61, subd. 3 (g)(1).

Program: Sales and Use Tax
Change Item: Parallel Taxation of Remote Access Software

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$1,400	$2,000	$2,500	$3,100
Other Fund				
Expenditures	0	0	0	0
Revenues-Legacy Funds	80	110	140	180
Net Fiscal Impact	$(1,480)	$(2,110)	$(2,640)	$(3,280)

Recommendation
The Governor recommends that the sales tax apply to charges for the access and use of remote access (web-based) software maintained by the seller or a third-party. Remote access models may also be known as "software as a service" (SaaS), application service provider (ASP), or cloud computing. The sales tax already applies to other software purchases or leases. The provision will increase general fund revenues by $3.4 million in FY 2012-13.

Rationale
As the economy and technology continue to evolve, statutory definitions related to the applicability of the sales tax often need to be adjusted to keep pace and to ensure a level playing field with taxation of similar products and services. This modification will ensure that the purchase or rental of computer services that are hosted remotely will be subject to sales tax the same as would be the case if a customer purchased computer equipment or purchased software for installation on a computer.

Under current law, the sales and use tax applies to charges for a license to use prewritten computer software but does not apply to the access charges for the use of similar software if provided by the seller because the customer does not have title to or control over the prewritten computer software they are using. Minnesota Rule 8130.0500 states that the making available of a computer on a time-share basis for use by customers securing access by remote facilities is a nontaxable service, not the granting of a "license to use" which is taxable. Also, Minnesota Rule 8130.9700 states that the use of equipment on a time-sharing basis, where access to the equipment is only by means of remote access facilities, is not a taxable leasing of such equipment. This makes the applicability of the sales tax more fair by leveling the playing field by making the time-sharing of hardware and the time-sharing of software the same for tax purposes. This proposal would tax the use of prewritten computer software as a license to use prewritten computer software and the use of computer equipment by remote access as a taxable lease of tangible personal property.

Effective July 1, 2011.

Key Goals and Measures
This would provide clarification and consistency and promote ease of administration.

Statutory Change – Amends Minn. Stat. § 297A.61, subd. 3 (f); repeals Minn. Rules 8130.0500, subp. 2; and deletes a portion of Minn. Rules part 8130.9700, subp. 3, item B.

Program: Sales and Use Tax
Change Item: Sourcing Rules for Florist Sales

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$47	$53	$54	$55
Other Fund				
Expenditures	0	0	0	0
Revenues -- Legacy fund	3	3	3	3
Net Fiscal Impact	$(50)	$(56)	$(57)	$(58)

Recommendation

The Governor recommends a change to the sourcing rules for florist sales. This change is neutral for most sellers and consumers but will result in a modest revenue increase of $100,000 in FY 2012-13.

Rationale

The proposed change will make application of the sales tax more consistent for all floral sales and simplify tax administration for businesses and tax administrators. Allowing multiple sourcing options for florists creates inconsistencies and confusion for both taxpayers and auditors which would be resolved by requiring telefloral orders to be sourced to the location of the florist (origin-based sourcing) consistent with Minnesota Rule 8130.8900.

The sale of florist products and services includes floral sales that originate within the state for customers that may be located either in or out of Minnesota, as well as sales that originate outside the state for delivery in Minnesota, such as telefloral orders. Since adopting the Streamlined Sales and Use Tax Agreement (SSUTA) sourcing rules, the state has administratively allowed florists two options: (1) use destination-based sourcing for telefloral orders (i.e., tax according to where the order is sent), which follows sourcing rules under M.S. 297A.668, subd. 2, or (2) use origin-based sourcing (i.e., tax according to the location of the florist), which follows the sourcing rules in Minnesota Rule 8130.8900.

While the SSUTA initially had a delayed effective date for requiring destination-based sourcing on telefloral sales, the Streamlined Sales Tax Governing Board eventually adopted an amendment which would allow states to continue to tax telefloral sales using the origin-based sourcing rules the industry had negotiated with all 50 states. All other member SSUTA states have chosen to use origin-based sourcing for telefloral orders, which is consistent with their past practice and with Minnesota Rule 8130.8900. The proposal would amend statutes to require origin-based sourcing for Minnesota.

Most florists already use origin-based sourcing but florists that have chosen to use destination-based sourcing would be required to change their procedures.

Effective July 1, 2011.

Key Goals and Measures

The change affirms Minnesota's approach to taxing florist sales consistent with SSUTA, provides clarification and consistency, and creates ease of administration.

Statutory Change — Amend Minn. Stat. § 297A.668, adding a new subdivision.

Agency: Tax Policy, Tax Aids and Credits

Program: Estate Tax

Change Item: Pass-through entity (Non-residents)

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$5,400	$7,600	$7,900	$8,300
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(5,400)	$(7,600)	$(7,900)	$(8,300)

Recommendation

The Governor recommends that real and tangible personal property located in Minnesota and held by a nonresident decedent in a pass-through entity (partnership, S corporation, limited liability company, or trust) be part of the Minnesota taxable estate for estate tax purposes. The change will increase general fund revenue $13.0 million in FY 2012-13.

Rationale

Under current law, ownership interests in a pass-through entity are treated as intangible assets and are assigned to a decedent's domicile at death. Real and tangible personal property located in Minnesota is assigned to Minnesota. As a result, while real or tangible personal property located in Minnesota and owned outright by a nonresident decedent is assigned to Minnesota for estate tax purposes, the value of that same property is not assigned to Minnesota for estate tax purposes if it is held in a pass-through entity.

The Governor recommends expanding the nexus rules under the estate tax so that real and tangible personal property located in Minnesota is assigned to Minnesota when it is owned outright by a nonresident decedent and when it is held in a pass-through entity. This change will ensure equitable tax treatment for real and tangible personal property.

Key Goals and Measures

Ensure the revenue system works well for Minnesota and similarly situated taxpayers are taxed the same.

Statutory Change: Minn. Stat. § 291.005, subd. 1.

Program: Sales and Use Tax and Motor Vehicle Sales Tax
Change Item: Exemption of Emergency Response Vehicles

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Other Fund				
Expenditures	0	0	0	0
Revenues – Highway User Distribution and Transit Assistance Funds	$(15)	$(15)	$(15)	$(15)
Net Fiscal Impact	$15	$15	$15	$15

Recommendation
As proposed by the Governor, the purchase of emergency response vehicles by an ambulance service will be exempt from the motor vehicle sales tax and the lease of this type of vehicle will also be exempt from the sales and use tax. A modest revenue loss is anticipated for the Transit Assistance and HUTD Funds.

Rationale
Current law exempts the purchase of ambulances owned by a licensed ambulance service from the sales tax on motor vehicles, and leases for ambulances are exempt from the general sales and use tax. Ambulances also have an exemption from the sales and use tax for their repair and replacement parts and their medical supplies and equipment, and they are exempt from the motor vehicle registration tax.

In 2008, emergency response vehicles owned by a licensed ambulance service were exempted from the motor vehicle registration tax and the repair and replacement parts for these vehicles were exempted from the sales and use tax. Under the proposal, M.S. 297B.03 will specify that emergency response vehicles, that are equipped and specifically intended for emergency response, purchased by a licensed ambulance service are exempt from the motor vehicle sales tax. In addition, M.S. 297A.70, subd. 6, will specify that the lease of this type of vehicle will also be exempt from the sales and use tax.

- In recent years, there have been approximately 275 municipal and private ambulance services in Minnesota, with 750 ambulances owned by these ambulance services. Most ambulance services have only one or two vehicles. There are 13 services with eight or more ambulances and 32 services that have four or more vehicles.
- Based on information from the Emergency Medical Services Regulatory Board (EMSRB), about 10% of ambulance services would have a vehicle affected by the proposal.

Effective for sales and purchases made after June 30, 2011 for the exemption from the sales and use tax on leased vehicles. The exemption from the motor vehicle sales tax is effective day following final enactment.

Key Goals and Measures
This change would provide clarification and consistency, and create ease of administration by correcting an oversight.

Statutory Change: Amends Minn. Stat. § 297A.70, subd. 6 and 297B.03.

Program: State Residential Property Tax
Change Item: Residential Tax on Homes Valued Over $1 Million

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues – Property Tax	$27,945	$56,293	$57,249	$58,467
Revenues – Income Tax	0	(3,893)	(4,106)	(3,669)
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(27,945)	$(52,401)	$(53,144)	$(54,798)

Recommendation
The Governor recommends implementing a statewide tax on residential single-unit property valued over $1,000,000. The tax would only apply to the incremental value over $1,000,000 and will generate $80.3 million for FY 2012-13. The FY 2012 revenue from this recommendation is approximately half of what would be generated in subsequent years because only the first of the two 2012 tax payments will occur within the state's 2012 fiscal year.

Rationale
The proposal will reduce the overall regressivity of the property tax by applying the new tax only to value in excess of $1,000,000; owners of these extremely high valued homes typically have the greatest ability-to-pay. The general fund revenues resulting from this tax will reduce the state structural budget deficit and support essential general fund programs.

The Governor's proposal will create a new state property tax levied against the incremental value above $1,000,000 of single-unit residential properties, including residential and agricultural homesteads, non-homesteaded residential and seasonal recreational properties. An estimated 9,400 properties will pay an average of $6,000 more in property taxes annually. A property valued at $1,100,000 would pay an estimated $1,050 in additional tax while a $3,000,000 home would pay an additional $21,000 in tax.

The median income of the affected homesteaders is estimated to be over $440,000. It is estimated that 85 percent of affected non-agricultural homesteaders have annual incomes in excess of $100,000.

To ensure that seasonal recreational property value over $1,000,000 is not subject to both this new statewide levy and the current law statewide levy on seasonal recreational property, the value of seasonal recreational property over $1,000,000 will be exempted from the existing state property tax. The state levy on seasonal recreational property will be reduced by a proportionate amount to the reduction in the tax base so that additional levy is not shifted onto other seasonal recreational property owners.

	FY 2012	FY 2013	FY 2014	FY 2015
New State Residential Property Tax	28,475	57,361	58,335	59,576
Reduction in existing State Property Tax on Seasonal Recreational Property	(530)	(1,068)	(1,086)	(1,109)

Income Tax Interactions	0	(3,893)	(4,106)	(3,669)
Net Change	27,945	52,400	53,143	54,798

The Governor's proposal increases property taxes on residential property over $1,000,000 in value. These taxes will increase itemized deductions, reducing income tax receipts an estimated $3.9 million in FY2013. The new tax also increases the eligible amount of property tax refunds for affected homesteads. The property tax refund impact is estimated to be negligible because most affected homesteaders who are income-eligible are projected to already receive the maximum allowable refund.

Key Goals and Measures

The Department of Revenue's Tax Incidence Study demonstrates that the property tax is a regressive tax. That is, people with higher incomes pay a smaller share of their income in property taxes than people with lower incomes. The Governor's proposal, by increasing taxes on the highest-valued residential properties, will make Minnesota's property tax system less regressive.

Statutory Change: Amends Minn. Stat. § 275.025; 290A.04, subd. 2h; and establishes a new section 275.026

Program: Special Taxes
Change Item: Increase Cigarette and Tobacco License Fees

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$40	$5	$40	$5
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(40)	$(5)	$(40)	$(5)

Recommendation
The Governor recommends adjusting the license fees for tobacco products distributors to $300 every two years, which would be equal to cigarette distributors, and increasing the license fee for cigarette and tobacco subjobbers to $150 every two years.

Rationale

Under current law, the license fee for a two-year distributor license is $300 for cigarette distributors, and $75 for tobacco products distributors. The proposal would make the tobacco license fees equal to those for cigarettes. In addition, the low fee for the tobacco distributor license frustrates compliance efforts as individuals are increasingly likely to buy the license and use it to purchase untaxed products from an out-of-state distributor and then sell the untaxed tobacco products in state.

A subjobber is someone who purchases taxed products from a wholesaler not for retail sales but for wholesale distribution to retailers. The taxes have already been paid by the distributor and do not need to be paid by the subjobber but the subjobber needs to be licensed. Subjobber license fees are $24 for a cigarette subjobber and $20 for a tobacco subjobber. The proposal would increase the license fee to $150 for a two-year period.

License fees were last raised in the 1989. At that time, the cigarette distributor fee was raised from $150 to $300; the tobacco products distributor fee was increased from $37.50 to $75; the cigarette subjobber fee was increased from $12 to $24; and the tobacco products subjobber fee was increased from $10 to $20.

The effective implementation date would be for license applications received after June 30, 2011.

Key Goals and Measures
The fee increases will make the tobacco distributor and the subjobber licenses more equivalent to the cigarette distributor license fee. While these fee revenues are deposited into the general fund, the higher fee levels will be more commensurate with the staff costs incurred to research applicants, issue licenses, and monitor the regulated activities. The fee changes are also anticipated to discourage the illegal sale of untaxed cigarette and tobacco products.

Statutory Change: Minn. Stat. § 297F.03, subds. 5 & 6

Program: Special Taxes
Change Item: Repeal Credit for Cigarette and Tobacco Bad Debts

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$20	$85	$85	$85
Health Impact Fund				
Expenditures	0	0	0	0
Revenues	20	75	75	75
Net Fiscal Impact	$(40)	$(160)	$(160)	$(160)

Recommendation

The Governor recommends repeal of the Minnesota statute that allows a tax credit against the excise tax on cigarette and tobacco products for unpaid debts owed to distributors by retailers and considered bad debt under Section 166(a) of the Internal Revenue Code. The proposal is estimated to increase general fund resources by $200,000 in FY 2012-13, including health impact fee revenues that are transferred to the general fund.

Rationale

The credit for bad debt shifts a cost of business onto the tax system that would be more appropriately born by cigarette distributors the same as bad debts incurred by all other businesses. Under current law, if a cigarette and tobacco distributor grants credit to a retailer of cigarette and tobacco products, and the retailer fails to pay the distributor, the distributor may deduct that loss as an expense under the federal tax code if the bad debt meets the definition of Section 166(a) of the IRC. State law then allows a credit for those bad debts against the cigarette and tobacco taxes collected from distributor. The proposed change would eliminate this benefit and place distributors of cigarette and tobacco products on par with other businesses. Like other businesses, distributors would continue to benefit from the relevant federal income tax treatment for bad debts.

The bad debt claims averaged $127,000 for CY2003 to CY2005, prior to the Health Impact Fee. Since FY2006, in addition to the cigarette and tobacco taxes, offsets are now provided for the health impact fees and additional cigarette stamp related charges, including sales tax on cigarettes. While the total taxes and fees show some annual variability, such as with occasional business failures, it is estimated that repeal of the bad debt credit will increase monies retained by $160,000 on an ongoing basis.

The effective implementation date would be for bad debts arising on or after July 1, 2011.

Key Goals and Measures

The proposal would simplify tax administration and allow the recognition of bad debts as business expense to be aligned with the income tax system rather than the excise tax on cigarette and tobacco products.

Statutory Change: Minn. Stat. § 297F.14, subd. 4

Program: Special Taxes
Change Item: Surplus Lines - Equalize Rates

Preliminary Budget Option

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$90	$200	$200	$200
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(90)	$(200)	$(200)	$(200)

Recommendation

The Governor recommends increasing the tax rate for nonadmitted insurance purchased directly by an insured from 2 percent to 3 percent of the premium paid to be consistent with the 3 percent rate applied under current law when such insurance is purchased through a surplus lines agent. The change will increase general fund revenues by $290,000 in FY 2012-13.

Rationale

Surplus lines insurance may be purchased through the use of a surplus lines agent or it may be purchased directly by the insured. Surplus lines include unusual or higher risk insurance that is not offered for sale by Minnesota licensed insurers. Under current law, the purchase of surplus lines insurance purchased through a surplus lines agent is subject to a 3% gross premium tax while an identical nonadmitted insurance policy purchased directly from an insurer is subject to a 2% gross premiums tax. Currently, the state collects $400,000 of tax on independently procured insurance so an increase in the rate will gain an additional $200,000 of annual revenue.

The change will be effective for premiums collected after July 21, 2011.

Key Goals and Measures

This recommended change furthers the Governor's objectives for a fairer tax system by ensuring that purchasers of nonadmitted insurance are taxed the same regardless of from whom the insurances is purchased.

Statutory Change: Minn. Stat. § 297I, subds. 9 and 10

Program: Special Taxes

Change Item: Nonadmitted Insurance Reform

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues	$400	$900	$400	$900
Other Fund				
Expenditures	0	0	0	0
Revenues	0	0	0	0
Net Fiscal Impact	$(400)	$(900)	$(400)	$(900)

Recommendation

The Governor recommends conforming to the federal provisions of the Nonadmitted and Reinsurance Reform Act of 2010 (NRRA). These conforming changes would increase revenues by $1.3 million in FY 2012-13.

Rationale

Prior to recent federal law changes the insurance premiums paid by companies or others for nonadmitted insurance were spread across all states based on risk for the purposes of determined insurance premiums tax owed Minnesota. The NRRA changed that approach and provides for a tax on gross premiums paid by an insured person based on where insured person is domiciled, regardless of where the risk is located. The federal law is crafted to supersede state law and the proposed change amends Minnesota statutes to make them consistent with the federal provisions by providing that insurance premiums tax be paid in this state if the insured person is domiciled in Minnesota rather than being allocated according to the location of risk.

Under the NRRA the states will either:

1) establish uniform and consistent allocation and payment rules for surplus lines premium taxes under a compact or other agreement, or
2) The tax laws of the home state of the insured will apply to the entire transaction.

Minnesota will provide for the authority to tax 100% of the gross premium of a surplus lines policy for which Minnesota is the home state. Minnesota will consider a compact or other sharing agreement for multi-state policies in the future but it’s imperative that we can begin taxing the entire premiums until such time in order to protect our revenue.

Key Goals and Measures

This recommended change promotes tax simplicity and transparency by aligning state and federal law in this area.

Statutory Change: Minn. Stat. § 297I.01, 297I.05, 297I09, 297I10, 297I30.

Program: Special Taxes
Change Item: Eliminate Bottle Tax; Simplify Tax on Wine & Spirits

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	0	0	0	0
Revenues—repeal bottle tax	$(840)	$(940)	$(970)	$(1,000)
Revenues—adjust excise tax	830	930	950	970
Revenues—gross receipts tax	8	9	9	9
Revenues—sales tax	21	23	24	24
Other Fund				
Expenditures	0	0	0	0
Revenues—Legacy Funds	1	1	1	1
Net Fiscal Impact	$(20)	$(23)	$(14)	$(4)

Recommendation

The Governor recommends simplifying the tax system by eliminating the bottle tax and making a revenue neutral adjustment to the excise tax for wine and distilled spirits.

Rationale

In 1986 Minnesota adopted a bottle tax equal to $0.01 per container to help offset the costs of administering a liquor stamping requirement. The stamping requirement as a means of regulating liquor has been repealed but the bottle tax remains; eliminating the bottle tax would allow for more efficient administration of liquor taxes. To offset the revenue loss from the elimination of the bottle tax, the excise tax on wine and distilled spirits would be increased by $0.01 per liter. The change would not affect excise taxes for beer. While no changes are made in the gross receipts or sales tax, there are minor interaction effects with those taxes.

The effective implementation date would be for sales made after June 30, 2011.

Key Goals and Measures

The change will make state government more efficient by simplifying the taxation of wine and distilled spirits with by eliminating the bottle tax. The recommendation achieves tax simplification in a revenue neutral manner.

Statutory Change: Minn. Stat. § 297G.03, subd. 1; and 297G.03, subd. 4

EXPLORE MINNESOTA TOURISM

Change Item: 1% Car Rental Tax Increase Dedicated for Marketing

Item included in Explore MN Tourism Budget Area. Shown Here for Informational Purposes.

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Revenues	$2,600	$3,000	$3,100	$3,300
Transfer Out	2,600	3,000	3,100	3,300
Special Revenue Fund				
Transfer In	2,600	3,000	3,100	3,300
Expenditures	2,600	3,000	3,100	3,300
Net Fiscal Impact	$0	$0	$0	$0

Recommendation

The Governor recommends a 1 percent increase in the tax on car rentals to be dedicated to Minnesota tourism marketing and promotion. A 1 percent tax increase is estimated to generate $2.6 million or more per year to support statewide tourism marketing. The majority of Minnesota car rental revenues are captured at MSP airport, and beyond the MSP airport, most additional collections are within the metro area. The impact would be that most of the new tourism marketing revenue would come primarily from out of state visitors.

Rationale

Currently, Minnesota's tourism office budget ranks 28th nationally. Minnesota is ranked 22nd in traveler spending, 18th in travel generated employment, 14th in travel generated payroll and 9th in travel-generated tax receipts. Regional competitors including Wisconsin, South Dakota, Illinois, Michigan and Montana outspend Minnesota. To be competitive in generating out-of-state visitors, there is a need for increased funding for marketing and promotion. This strategy provides a direct link between travel-generated spending and funding for travel marketing. Funding generated will go directly into marketing and promotion programs and activities. The current advertising budget for Explore Minnesota is about $3 million. An additional $3 million annually would allow a significant increase in these efforts to reach both in-state and out-of-state markets.

Tourism contributes greatly to the Minnesota economy. The leisure and hospitality industry has $11 billion in annual sales and employs more than 243,000 people (nearly 11% of total private sector employment). Almost $700 million in sales taxes is collected on those sales, accounting for 17 percent of Minnesota's sales tax revenues.

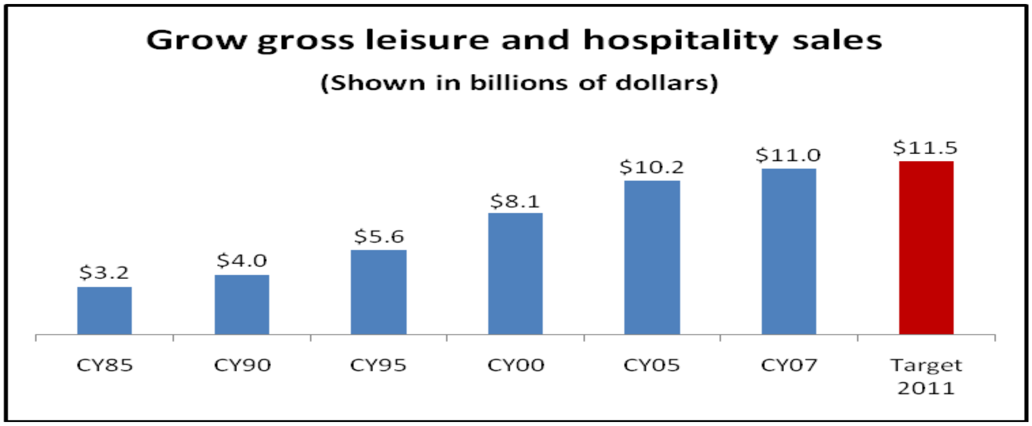
The proposed effective date would be July 1, 2011. Adjustments would need to be made with the Department of Revenue due to programming, notification to rental companies, a change to printed materials and changes in accounting to track and report the tax. Operationally, many states and cities across the country impose relatively high taxes and fees on car rentals. Beyond this, additional taxes and fees are imposed at major airports across the country. In Minnesota, the majority of car rental revenues are captured at the MSP airport.

Key Goals and Measures

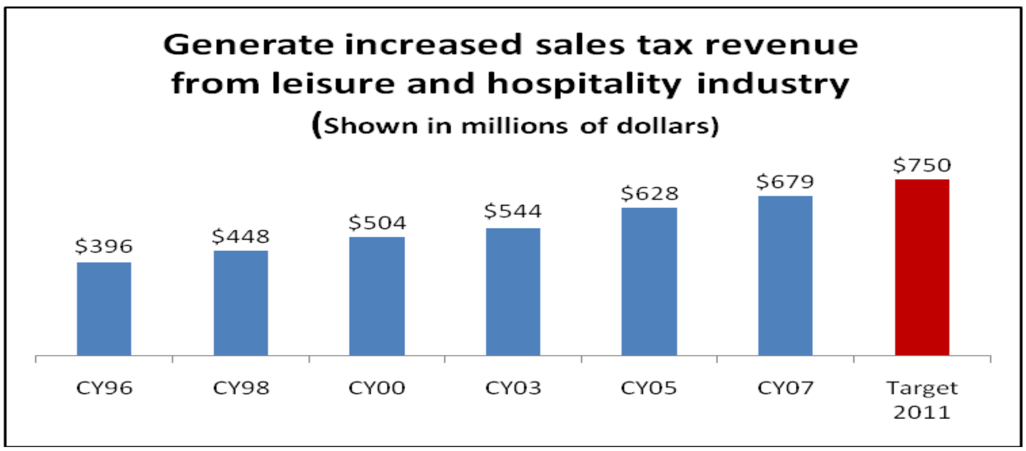
The agency's primary goals and measures are:

1. Increase the number of resident and nonresident travelers in the state.
   Estimated # of travelers: 39 million

2. Grow gross receipts/sales in Minnesota.
   Leisure & hospitality gross sales: 2008 - $11.2 billion

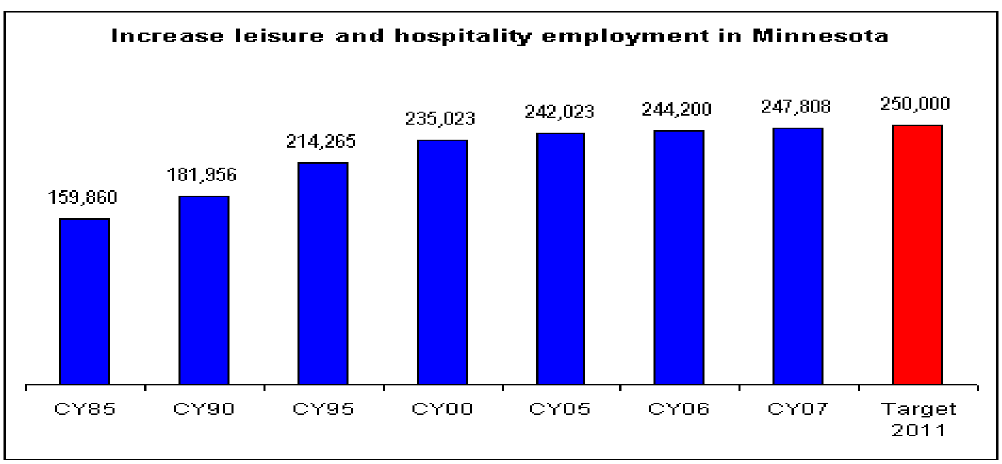


3. Generate increased state and local sales tax revenue.
   Sales tax revenues from leisure & hospitality: 2008 - $695 million



4. Increase leisure and hospitality employment in Minnesota.
   Number of leisure & hospitality jobs: 2008 - 245,788

   Wages: 2008 - $4 billion



Statutory Change: M.S. 297A.64 Rental motor vehicle tax

HEALTH DEPT

Program: POLICY QUALITY & COMPLIANCE

Change Item: Eliminate the Direct Grants from MERC

Item included in Health Dept. Budget Area. Shown Here for Informational Purposes.

Fiscal Impact ($000s)	FY 2012	FY 2013	FY 2014	FY 2015
General Fund				
Expenditures	$0	$0	$0	$0
Revenues	0	4,613	4,613	4,613
Other Fund				
Expenditures	0	(4,613)	(4,613)	(4,613)
Revenues	0	(4,613)	(4,613)	(4,613)
Net Fiscal Impact	$0	$(4,613)	$(4,613)	$(4,613)

Recommendation

The Governor recommends eliminating the direct grants from the Medical Education and Research Costs (MERC) program, for an annual state savings of $4.613 million beginning in FY 2013. Since the late 1990s, MERC funding has helped hospitals cover the costs associated with being an education and research institution. MERC dollars are distributed two different ways—through the general distribution and as direct grants. This proposal eliminating the direct grants does not affect the amount awarded through the general distribution formula. (See the Department of Human Service's Governor's Recommendations for other MERC related change items.)

Rationale

MERC direct grants of $5.350 million are distributed according to statute as follows:

- $1.475 million - University of Minnesota /Fairview
- $1.8 million - University of Minnesota / Academic Health Center
- $2.075 million - University of Minnesota / Dental School.

The grant to University of Minnesota/Fairview receives a fifty percent federal match, therefore the state total of the grants is $4.613 million and the federal share is $737,500. The state share of the grants is from dedicated cigarette tax revenue.

The direct grants were enacted as part of the 2007 legislation that changed the general distribution formula for MERC from a formula weighted 67% education/33% Medical Assistance volume to a formula based 100% on Medical Assistance volume. In addition to the creation of these three direct grants, a grant to Mayo was also implemented to transition from the old formula to the new formula. The Mayo grant was sunset during the FY 2010-11 biennium.

This proposal would eliminate the direct grants and redirect the cigarette tax revenue to the general fund.

Statutory Change: 62J.692, subdivision 4, section 297F.10, subdivision 1,

Change Item: Extension of the Petrofund Sunset

Item included in Commerce Dept Budget Area. Shown Here for Informational Purposes.

Fiscal Impact ($000s)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Petroleum Tank Fund				
Expenditures	$0	$18,188	$18,188	$18,188
Revenues	0	26,333	26,333	26,333
Net Fiscal Impact	$0	($8,145)	($8,145)	($8,145)

Recommendation

The Governor recommends amending the repealer date (i.e. 'sunset date') in M.S. 115C.13 from June 30, 2012 to June 30, 2017. This legislation would result in a five-year extension of the Petroleum Tank Release Cleanup Fund (Petrofund) program at the Department of Commerce, as well as provide funding for other programs at the Minnesota Pollution Control Agency and the Department of Employment and Economic Development (separate *Change Item* documents are provided by both of those agencies in their budgets).

Rationale

Federal financial responsibility regulations require that petroleum storage tank owners have at least $1 million of coverage to address contamination from leaking tanks and to pay third-party liability claims. The 'sunset' of the Petrofund, which has served as the tank owners' financial assurance mechanism since 1987, would negatively impact their ability to comply with federal law and would likely result in financial hardships for those tank owners who could not obtain alternative coverage and were obligated to incur the costs related to investigating and cleaning up petroleum contamination on their own. Extension of the 'sunset date' would have no impact on the Department's current operations, since no increases in staffing or annual Petrofund reimbursement program budgets are anticipated. The effective implementation date would be the first day of the extension: July 1, 2012. The new sunset on the PetroFund will be June 30, 2017.

All current and proposed expenditures are fully covered by the Petrofund fee; thus, there is no effect on the General Fund. The Petrofund program's revenue is generated by a fee on gasoline and other petroleum products. Of the $18.2 million is spending each year, $1.052 million each year is for the Petroleum Tank Release Cleanup Board while $11 million is provided in claims.

Key Goals and Measures

The key goal of the Petrofund program is to provide timely financial assistance to those who are cleaning up contaminated soil and groundwater from leaking petroleum storage tanks, with the ultimate goal of helping to protect the public health and welfare and the environment. These objectives go hand-in-hand with the Minnesota Milestones statewide goal regarding water use, which states, in part, "A clean and abundant water supply is essential to economic and human health."

The principal measure for whether or not the Petrofund is providing financial assistance in a timely manner is the 'application backlog'. Minnesota Statute §115C.09 provides that initial applications be reviewed within 60 days of receipt and supplemental applications within 120 days of receipt. The status of the 'application backlog' is assessed weekly by the Petrofund Director and reported to the five-member Petrofund Board at their bi-monthly meetings. The Petrofund staff is currently reviewing applications within the 60-day and 120-day deadlines. The Petrofund has consistently processed reimbursement applications in a timely manner (as illustrated in the following table), and it is anticipated that these high compliance rates will continue into the foreseeable future.

Year	Applications Received	Applications Reviewed Within 60 and 120 Days	Compliance Rate
FY08	807	807	100%
FY09	735	735	100%
FY10	721	681*	94%*

*Short-term lack of compliance due to the departure of one of the three analysts that process applications for reimbursement.

Statutory Change: Change the sunset date contained in M.S. 115C.13 to June 30, 2017

Purpose
To provide general property tax relief payments directly to qualifying homeowners and renters.

Funding Source
State General Fund

Program Description
There are 3 types of general property tax relief programs provided by the State directly to homeowners and renters through the issuance of refund payments.

1) **Homeowner's Property Tax Refund Program (PTR**) is a state-paid refund providing property tax relief directly to homeowners whose property taxes are high relative to their incomes. The refund varies depending on the income and the property tax of the homeowner. The maximum refund is $2,350 and homeowners whose income exceeds $98,289 are not eligible (income threshold for refunds claims filed in 2010). The program uses household income which is a broad measure that includes most type of income.
2) **Targeting Property Tax Refund Program** is a state-paid refund providing property tax relief to homeowners who have large property tax increases from one year to the next. A homeowner qualifies if the property tax increase on their home has increased more than 12% over the previous year's tax and the increase is over $100. There is no maximum income limit for eligibility for this refund. The refund equals 60% of the increase over the greater of (1) 12% of the previous year's tax or (2) $100. The maximum refund is $1,000.
3) **Renter's Property Tax Refund Program** is a state-paid refund providing tax relief directly to renters whose rent and "implicit" property taxes are high relative to their incomes. For ease of administration the portion of the rent assumed to be attributed to property taxes paid on the apartment is assumed to equal 19% of rent paid. Renters whose income exceeds $53,539 are not eligible for refunds (income threshold for refund claims filed in 2010). The program uses a broad measure of household income that includes most type of income. The maximum refund is $1,520. The refund will vary depending on the amount of rent and the amount of income.

Population Served

Filed 2008 payable in 2009	Number of returns	Total Refund Amount	Average per return
Homeowner's PTR	360,800	$269.3 million	$746
Targeting Homeowner	42,000	$6.088 million	$146
Renter's PTR	304,500	$180 million	$591 .

Current Law

Property Tax Refunds:	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Homeowners	$ 252,191	$ 295,400	$ 304,700	$ 318,000	$ 334,000
Renters	$ 171,799	$ 186,000	$ 145,200*	$ 199,900	$ 203,100
Targeting	$ 7,581	$ 6,088	$ 2,400	$ 3,960	$ 6,050
Total	$ 431,571	$ 487,488	$ 452,300	$ 521,860	$ 537,100

*FY 2011 estimates for renters refund reflect the 2009 unallotment action that was ratified by the 2010 legislature. This reduced rate of rent attributable to property taxes from 19% to 15%.

Legal Citation: M.S. 290A.23; 2010 First Special Session, Chap. 1, Art. 13

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Purpose
To provide aid payments to enrolled owners of forested land as an incentive to practice long-term sustainable forest management.

Funding Source
State General Fund

Program Description
The Sustainable Forest Incentive Act (SFIA) was created in 2001 and allows annual payments to be made to enrolled owners of forested land as an incentive to practice long-term sustainable forest management. The participants must be enrolled for a minimum of 8 years and a covenant is recorded. The payment is calculated using 3 formulas based on the average property tax for timberland. The formula that provides the largest payment per acre will be used and the minimum incentive amount is $7.00 per acre. To be enrolled in the program, a participant must meet all of the following requirements:

- Participants must own 20 or more contiguous acres of land in Minnesota, of which at least 50% is forested. Participants may be private individuals, corporations or partnerships, and can be either residents or nonresidents of Minnesota.
- There can be no delinquent property taxes owed on the land prior to enrolling and participants must stay current with their taxes while enrolled in the program.
- The land must have an active forest management plan in place that was prepared by an approved plan writer that is approved by the Department of Natural Resources. All management activities prescribed in the plan must meet the recommended timber harvesting and forest management guidelines created by the Minnesota Forest Resources Council. The land cannot be used for residential or agricultural purposes.
- Participants with more than 1,920 acres enrolled must allow year-round non-motorized access to fish and wildlife resources.

There were 1,675 claimants enrolled in FY 2011.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011*	Estimated F.Y. 2012	Estimated F.Y. 2013
SFIA payment	$ 6,098	$ 6,983	$ 5,728	$ 15,079	$ 16,304
Total	$ 6,098	$ 6,983	$ 5,728	$ 15,079	$ 16,304

*Payments in FY 2011 were capped at $100,000 per participant under the unallotment action that was ratified by the 2010 legislature. This cap impacted 5 of the 1,675 participants.

Legal Citation: M.S. 290C.08; 2010 First Special Session, Chap. 1, Art. 13

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Purpose
To provide general support aid and property tax relief to municipal governments.

Funding Source
State General Fund

Program Description
Minnesota has a long history of supplementing local government revenues with state general fund aid payments. Local government aid (LGA) provides general purpose financial support to some cities. In 2011, 760 of the 854 cities were certified to receive LGA. The purposes described for LGA are to help communities with limited property tax wealth provide basic local services; to offset the cost of state mandates; and to limit the overall property tax burden.

LGA is set as a fixed dollar amount in statute that is distributed among the cities on a formula basis using several factors to determine the size of the payment to an individual city. Cities with greater property tax wealth do not receive LGA. In general, the formula attempts to target aid to those cities with the lowest tax capacity and highest need. The formula has changed many times since it was enacted in 1971. For cities with population of 2,500 or more need is determined by factors such as population decline, age of housing stock, household size and number of vehicular accidents. For cities with population less than 2,500, need is determined by population decline, age of housing stock, percent of commercial/industrial property and a population adjustment factor. There are 21 additional aid amounts for individual cities based on unique local circumstances. Beyond the basic formulas, there are three special adjustments that impact more than one city:

- Greater MN regional center base aid of $60 times the population greater than 5,000 population up to $2,500,000 (27 cities);
- Jobs base aid of $25.20 per job for cities over 5,000 in population up to $4,750,000 (82 cities). This adjustment is reduced for cities that also receive regional center aid;
- $8.50 per capita for cities under 5,000 population in recognition of the fact that these cities do not qualify for state Municipal Street Aid (672 cities).

LGA is paid in to the cities in two payments, one in July and one in December.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Local Government Aid (LGA)	$ 430,638	$ 481,529	$ 426,438	$ 527,101	$ 527,101
Total	$ 430,638	$ 481,529	$ 426,438	$ 527,101	$ 527,101

Legal Citation: M.S. 477A.03; 2010 First Special Session Chapter 1, Article 13; 2010 Regular Session Chapter 215

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Purpose
To provide general purpose aid to counties and for general property tax relief.

Funding Source
State General Fund

Program Description
County program aid (CPA) is paid from the state general fund as general purpose aid for the counties and to provide property tax relief. In 2003, several county aids were restructured into a single program called county program aid (CPA). The programs eliminated in the restructuring were attached machinery aid, homestead and agricultural credit aid, manufactured home and agricultural credit aid, county criminal justice aid and family preservation aid.

CPA payments are determined using a formula that consists of three components (1) a county need aid component that recognizes revenue need based on a measure of population over 65, a measure of crimes, and number of households receiving food stamps; (2) a county tax-base equalization aid component that factors measures of population and net tax capacity; and (3) a county transition aid component that provides transitional adjustments aid for following seven counties: Cook, Aitkin, Chippewa, Traverse, Kanabec, Kittson, and Wilkin. Other individualized aid amounts are occasionally targeted to specific counties. CPA payments are made twice a year, one in July and one in December.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
County Program Aid	$ 160,696	$ 194,883	$ 164,935	$ 197,460	$ 197,454
Total	$ 160,696	$ 194,883	$ 164,935	$ 197,460	$ 197,454

Legal Citation: M.S. 477A; 2010 Regular Session Chap. 215, Article 13; 2010 First Special Session, Chap. 1, Art. 13

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Purpose
To provide general property tax relief for owners of qualifying residential homestead properties.

Funding Source
State General Fund

Program Description
As part of the 2001 property tax reform measures, a new homestead credit was enacted for agricultural and residential homesteads. This was done to lessen the fiscal impact of the classification rate changes for homesteads.

Residential and agricultural homesteads receive a benefit from the state-funded market value credit that is shown on their property tax statement as a subtraction from their property taxes. The residential homestead market value credit amount is equal to 0.4 percent of market value up to a maximum credit of $304, which occurs on a home valued at $76,000. The credit begins to decrease by 0.09% of each dollar over $76,000, but may never be less than $0. Homes valued above $414,000 do not receive the credit.

Local governments receive a state reimbursement for the reduction in property taxes due to residential and agricultural homestead market value credit. The reimbursement is paid out twice a year to local governments, once in October and once in December. During some budget shortfall periods, the state has not fully compensated local governments for the credit. However, the taxpayer still received the credit which showed as a reduction on their property tax statement.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Residential Hmstd Market Value Cr	$ 256,202	$ 238,340	$ 150,952	$ 264,921	$ 255,406
Prior Year Credits	$ 912	$ 1,035	$ 694	$ 719	$ 686
Total	$ 257,114	$ 239,375	$ 151,646	$ 265,630	$ 256,092

Legal Citation: M.S. 273.1384**;** 2010 Minn. Laws Regular Session, Chap. 215, Art. 13; 2010 First Special Session, Chap. 1, Art. 13

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Program: Agricultural Homestead Market Value Credit — Narrative

Purpose
To provide general property tax relief for owners of qualifying agricultural homestead properties.

Funding Source
State General Fund

Program Description
As part of the 2001 property tax reform measures, a new homestead credit was enacted for agricultural and residential homesteads. This was done to lessen the fiscal impact of the classification rate changes for homesteads. The agricultural credit is designed to reduce the tax on agricultural homestead land beyond the house, garage and immediately surrounding one acre of land (non-HGA). The home, garage, and immediately surrounding one acre of land would receive the residential homestead market value credit the same as it applies to other homestead properties

The agricultural homestead market value credit is a state funded credit that is shown on the property tax statement as a subtraction from their property taxes. Property in the 2a agricultural homestead classification is eligible for an agricultural credit. For agricultural homestead property with a taxable market value on the non-HGA property of $115,000 or less, the credit is equal to 0.3 percent of the taxable market value of the property. The maximum credit is limited to $345 and this amount is reached at $115,000. This credit decreases as the market value increases to $345,000. At $345,000 of agricultural land value or more, the credit is equal to $230.

Local governments receive a state reimbursement for the reduction in property taxes due to the agricultural homestead market value credit. The reimbursement is paid out twice a year to local governments, once in October and once in December. During some budget shortfall periods, the state has not fully compensated local governments for the credit. However, the taxpayer still received the credit which showed as a reduction on their property tax statement.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Agricultural Hmstd Market Value Credit	$ 25,049	$ 23,790	$ 23,446	$ 24,419	$ 23,322
Total	$ 25,049	$ 23,790	$ 23,446	$ 24,419	$ 23,322

Legal Citation: M.S. 273.1384, subd. 2; 2010 Minn. Laws Regular Session Chap. 215, Art. 13; 2010 First Special Session, Chap. 1, Art. 13

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Purpose
To provide property tax relief related to 1988 property tax law changes.

Funding Source
State General Fund

Program Description
Disparity Reduction Aid (DRA) was created by the 1988 Legislature to provide relief for high tax rate areas as part of the conversion from mill rates and assessed values to net tax capacities. It was first payable to taxing jurisdictions in 1989. While initially paid to all qualifying local jurisdictions, the city amounts were cancelled (and shifted to LGA) beginning with aids paid in 1994. In addition, the amounts originally computed for special taxing districts were rolled into county DRA beginning with aids paid in 1995. DRA applies only to local net tax capacity rates; it has no effect on the state tax rate or any referendum market value rates.

After the initial tax rate is determined, DRA is applied to further reduce the rate to the properties within the unique taxing area. DRA amounts generally remain unchanged from year to year unless the total tax rate in a unique taxing area drops below 90 percent. In 2010 the state paid $18 million in DRA to local governments. About 15 percent of the state's unique taxing areas receive DRA.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Disparity Reduction Aid	$ 18,094	$ 16,729	$ 17,783	$ 19,593	$ 18,007
Total	$ 18,094	$ 16,729	$ 17,783	$ 19,593	$ 18,007

Legal Citation: M.S. 273.1398

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Purpose
To provide reimbursement to local governments for loss of property tax revenue for properties damaged by a disaster.

Funding Source
State General Fund

Program Description
Qualifying property owners within a designated disaster area may receive an abatement of current year property taxes. An abatement of current year taxes may be granted by the county board if 50% of the homestead dwelling or other building was destroyed.

The state reimburses the local jurisdictions for abatements and credits for property located in a declared disaster or emergency area. The disaster credit reduces the property tax of the homestead in the following payable year after damage suffered within a declared disaster or emergency area. The property is reassessed after the damage, and the difference between the original and reassessed value is multiplied by the ratio of the number of full months remaining in the year divided by 12 months. This product is then multiplied by the prevailing local tax rate to obtain the credit amount. The credit program first became effective in 1984.

Cities in a disaster area where 5 percent or more of the tax base is destroyed due to the disaster are eligible to receive tax base replacement aid for the first year the reduced tax base is in effect.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Disaster Credit	$ 763	$ 217	$ 101	$ 542	$ 14
Local Option Abatement Reimburse	$ 249	$ 0	$ 250	$ 0	$ 0
Local Option Disaster Credit	$ 0	$ 133	$ 4	$ 34	$ 1
Tax Base Replacement Aid	$ 0	$ 131	$ 0	$ 0	$ 50
Total	$ 1,012	$ 481	$ 355	$ 576	$ 65

Legal Citation: M.S. 273.1231 through 273.1235

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Purpose

To provide a property tax credit for farmers with cattle herds that have faced eradication or other controls in a zone designated to control and eliminate the spread of bovine tuberculosis.

Funding Source

State General Fund

Program Description

The bovine tuberculosis credit was designed to reduce the property tax for those farm parcels located within an area identified as the Bovine Tuberculosis Modified Accredited Zone. The credit equals the greater of $5 per acre for the first 160 acres, or $5 per acre times five acres times the highest number of animals tested as part of a whole herd test during 2006-2008. (In the first year the credit equaled the tax on class 2a or 2b agricultural land.) The credit expires when the state is declared bovine TB free.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Bovine TB Credit	$ -	$ 324	$ 426	$ 448	$ 431
Total	$ -	$ 324	$ 426	$ 448	$ 431

Legal Citation: M.S. 273.113

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Purpose
To encourage economic development and job retention in certain border cities.

Funding Source
State General Fund

Program Description
Starting for taxes payable in 1989, the Disparity Reduction Credit reduces property taxes for commercial/industrial, public utility and apartment properties located in five designated border cities of Breckenridge, Dilworth, East Grand Forks, Moorhead, and Ortonville. This property tax credit does not apply to the debt service levy or school district taxes, other than the state equalized levies. The credit is an amount sufficient to reduce the property taxes to 2.3% of the qualified properties market value. The state reimburses those border cities for the reduction in property taxes.

The border city reimbursement is available to the same five designated border cities to reimburse them for tax exemptions granted within a border city zone.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Disparity Reduction Credit	$ 5,316	$ 5,482	$ 5,132	$ 5,969	$ 5,800
Border City Reimbursement	$ 13	$ 13	$ 13	$ 13	$ 13
Total	$ 5,329	$ 5,495	$ 5,145	$ 5,982	$ 5,813

Legal Citation: M.S. 273.1398; 469.1735

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Program: Wetlands Reimbursement Credit — Narrative

Purpose
To provide payment to counties for revenue loss associated with exemptions due to the creation of Wetland Preservation Areas.

Funding Source
State General Fund

Program Description
This provides a payment to counties for lost property tax revenues resulting from the exemption of land in a wetland preservation area. This provision was adopted in 1991 but was utilized for the first time in for taxes payable in 2004. It currently applies to a very limited number of parcels. Only 3 counties currently receive a reimbursement.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Wetlands Reimbursement Credit	$ 8	$ 6	$ 6	$ 6	$ 6
Total	$ 8	$ 6	$ 6	$ 6	$ 6

Legal Citation: M.S. 275.295

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Purpose
To provide additional revenue for funding various distributions of the taconite production tax.

Funding Source
State General Fund

Program Description
The taconite state aid was enacted in 2001 in response to the shutting down of many mining operations. The aid payment is a set in statute at 22 cents per taxable ton of iron ore concentrates. The taconite state aid appropriation is added to the total taconite production tax collected under M.S. 298.27 as if the dollars were taconite production taxes paid by a mining company. The annual state aid payment is equal to 22 cents per taxable ton of iron ore produced. The taconite state aid and taconite production taxes are distributed based on a formula in M.S. 298.28 and distributed as if the aid were production tax revenues. The distributions are sent to local jurisdictions and other entities within the Taconite Tax Relief area. In 2009, those distributions totaled $98,144,786 million which is the combined total collected from both the taconite production tax and the taconite state aid. The distributions were as follows:

- $12,240,195 taconite cities and townships
- $18,859,169 taconite school districts
- $14,216,385 taconite counties
- $9,656,986 property tax relief and misc.
- $30,742,360 Iron Range Resource Board
- $12,429,692 Other (includes Taconite Economic Development Fund, Range Assoc. of Municipalities and Schools and Hockey Hall of Fame)

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Taconite State Aid	$ 8,527	$ 7,757	$ 6,750	$ 6,590	$ 7,545
Total	$ 8,527	$ 7,757	$ 6,750	$ 6,590	$ 7,545

Legal Citation: M.S. 298.285

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Purpose

State aid reimbursement to 4 counties for additional homestead property tax credits for homeowners in a limited geographic area surrounding the taconite tax relief area.

Funding Source

State General Fund

Program Description

The supplemental taconite homestead credit was created in 1980. The property tax credit is given to homeowners in five school districts located in 4 counties. The state reimbursement for the credit is paid to the counties of Aitkin, Crow Wing, Itasca and St. Louis.

The supplemental taconite homestead credit is similar to the taconite homestead credit that was created in 1970. The taconite homestead credit is for homeowners in the taconite tax relief area. The supplemental taconite homestead credit provides the same credit but to an area just surrounding the taconite tax relief area. Both the supplemental and the taconite homestead credit are equal to either 57% or 66% of the property tax depending on various factors such as the value of iron ore in the assessment district, proximity to mines, etc. The maximum amount of the homeowner credit is $289.80 for those receiving the 57% credit and $315.10 for those receiving the 66% credit. Homeowners in the limited geographic area receiving the supplemental and taconite homestead credit also receive the statewide homestead and agricultural market value credits.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Supplemental Taconite Homestead Credit	$ 5,211	$ 5,178	$ 5,215	$ 5,269	$ 5,321
Total	$ 5,211	$ 5,178	$ 5,215	$ 5,269	$ 5,321

Legal Citation: M.S. 273.1391

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Purpose

To provide property tax relief to school districts that no longer receive the defunct taconite occupation tax reduction.

Funding Source

State General Fund

Program Description

Taconite Aid Reimbursement is provided to school district #317 in Itasca County in order to reimburse the district for the "occupation tax" reduction received under M.S. §273.135 Subd. 2(c) before the law was changed in 1978. The affected school districts receive a reimbursement equal to the amount the district received in 1980. This payment has remained constant at $561,050 over the years.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Taconite Aid Reimbursement	$ 561	$ 561	$ 561	$ 561	$ 561
Total	$ 561	$ 561	$ 561	$ 561	$ 561

Legal Citation: M.S. 477A.15

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Purpose
To compensate cities and towns for reductions in their tax base due to the implementation of a new rule pertaining to the assessment of utility property.

Funding Source
State General Fund

Program Description
The utility transition aid was created in 2008 to provide a payment to local governments experiencing a loss of property base market valuation due to a Minnesota Department of Revenue rule change on public utility properties. The rule change was necessary to ensure that the valuation rules for utility properties were adequately assessing properties at their market values per the statutory requirement. The result of the rule change was a reduction in market value for many utility properties. A transition aid was enacted for those local jurisdictions that lost a large percent of their tax base due to the valuation changes. A city or town is eligible for aid if the difference between their net tax capacity under the old rules for assessment year 2007 versus under the under the new rule exceeds 4%. The aid was first paid in calendar year 2009 to 43 cities and townships. The aid will continue for each qualifying municipality until the current valuation of public utility property exceeds its 2007 valuation under the old utility assessment rules.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Utility Valuation Transition Aid	$ -	$ 2,102	$ 3,024	$ 1,508	$ 980
Total	$ -	$ 2,102	$ 3,024	$ 1,508	$ 980

Legal Citation: M.S. 477A.16

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Purpose
To provide state aid to counties containing an Indian reservation where the tribe operates a casino and has a tax agreement with the state.

Funding Source
State General Fund

Program Description
This aid provides state tax relief to counties containing an Indian reservation where the tribe operates a casino and has an agreement with the state to collect taxes. If the total payment exceeds $1.1 million, reductions will be made first to counties that do not have a per capita income less than 80% of the same state level or have 30% or more of total market value of real property that is tax exempt. The aid is equal to 10% of the state share of the taxes collected from the Indian reservation under a tax agreement, up to a maximum of $1.1 million per year. The Counties receiving the aid are Carlton, Cass, Cook, Goodhue, Itasca, Mahnomen, Mille Lacs, Pine, Redwood, St. Louis, Scott, and Yellow Medicine.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Indian Casino Aid	$ 669	$ 754	$ 754	$ 754	$ 754
Total	$ 669	$ 754	$ 754	$ 754	$ 754

Legal Citation: M.S. 270C.19

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Purpose
To provide aid to help pay for the services of the lawyers and staff needed for public legal defense.

Funding Source
State General Fund

Program Description
After a set amount is made available for County Program Aid, a reduction of $500,000 is made available to the State of Minnesota Board of Public Defense to help cover the costs of attorney and staff services needed to provide criminal and juvenile public legal defense services to indigent clients. These funds may be used at the board's discretion. However, at the end of the fiscal year any funds not used are to be applied to the next fiscal year's County Program Aid.

A reduction of $214,000 is made available to Minnesota Management and Budget and the Department of Education for their work in preparing Local Impact Notes.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Public Defender Costs	$ 495	$ 493	$ 500	$ 500	$ 500
Local Impact Notes	$ 214	$ 214	$ 214	$ 214	$ 214
Total	$ 709	$ 707	$ 714	$ 714	$ 714

Legal Citation: M.S. 477A.03

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Purpose
To provide payment for property tax revenue loss due to the placement of the Shooting Star Casino land into trust status.

Funding Source
State General Fund

Program Description
The additional payment to Mahnomen County was started in 2006 and made permanent in 2008. The state payment was enacted to offset the loss of property tax revenue due to the placement of the White Earth Tribal Band's Shooting Star Casino into trust status. The Shooting Star casino was one of the largest taxpayers in the county making up 15% of the counties total property tax revenue. A federal judge ruled that the White Earth Band's casino was not subject to county property taxes because the land was purchased through the federal White Earth Land Settlement Act and was automatically placed into trust. The tribe stopped paying taxes in 2006 and the federal court ruling occurred in 2009. The payment to Mahnomen County is to be split between the local tax jurisdictions with $450,000 to the county, $80,000 to the city of Mahnomen and $70,000 to Mahnomen School District #432.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Mahnomen Property Tax Reimburse	$ 600	$ 600	$ 600	$ 600	$ 600
Total	$ 600	$ 600	$ 600	$ 600	$ 600

Legal Citation: 2008 Minn. Laws Chapter 154, Article 1

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Purpose
To provide senior citizens whose property taxes are high relative to their income an option to defer a portion of their property taxes in order to help them remain in their homes. The counties are reimbursed by the state for the deferral of property taxes of program participants.

Funding Source
State General Fund

Program Description
This program allows senior homeowners whose property taxes are high relative to their incomes to be able to defer a portion of their property taxes until a later time. The tax deferred is a loan that must be paid back when the property is sold, transferred, upon death or if property no longer qualified as a homestead. The tax deferral constitutes a lien on the property. The deferral amount is the property taxes that are greater than 3% of the participant's household income. The eligibility requirements for the program include the following: the homeowner must be 65 years or older (if married the other spouse must be older than 62); total household income must be $60,000 or less; and the home must have been owned and occupied as a homestead for at least 15 years.

The state general fund cost is the amount of the reimbursement for the property deferrals. For property taxes payable in 2010 there were 271 homes in the program.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Senior Deferral Reimbursement	$ 504	$ 608	$ 838	$ 1,048	$ 1,310
Total	$ 504	$ 608	$ 838	$ 1,048	$ 1,310

Legal Citation: M.S. 290B.09

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Purpose
To provide payment to counties and cities for participation in the local performance measurement programs established by the Council on Local Results and Innovation.

Funding Source
State General Fund

Program Description
This payment was established in the 2010 omnibus tax bill as part of a package to improve property tax reform, accountability, value and efficiencies. The 2010 legislation created the Council on Local Results and Innovation which is made up of 11 members. The council is directed to develop by February 15, 2011, ten standard performance measures for the counties and ten for the cities aimed at measuring efficiency and effectiveness of counties and cities in providing services. The council will also establish minimum standards for a comprehensive performance measurement system for counties and cities. Counties and cities that choose to participate in the reporting of standard measurements are eligible for reimbursement by the state of 14 cents per capita, up to a maximum of $25,000. The state auditor would certify participation in the program to the Commissioner of Revenue. The first payments could be made to participating counties and cities in FY 2012.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Performance Measurement Reimb.	$ -	$ -	$ -	$ 940	$ 880
Total	$ -	$ -	$ -	$ 940	$ 880

Legal Citation: M.S. 6.91; 2010 Minn. Laws Regular Session Chapter 389, Article 2

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Purpose
To provide state aid support to the retirement pensions of local peace officers and firefighters.

Funding Source
State General Fund

Program Description
Police State Aid: The initial revenue source for this aid is derived mainly from the auto insurance premium tax, but the available aid is limited to the employers' actual pension obligations each year. Because the revenue usually exceeds the employers' obligations, an "excess police state-aid holding account" is used to allocate the excess revenue to an ambulance account or to additional amortization aid.

Fire State Aid: The initial revenue source for this aid is derived mainly from the fire insurance premium tax ("fire, lightning, sprinkler leakage and extended coverage premiums"). An additional amount of fire aid is also allocated from the annual appropriation for amortization aid.

Insurance Surcharge Aid: This is a state aid to firefighters' relief associations in cities of the first class. The funding is a two percent surcharge on insurance premiums on fire, lightning, and sprinkler leakage in first class cities.

Amortization State Aid: An annual appropriation was provided in 1997 to fund this aid to police or salaried firefighters' pension associations that have an unfunded actuarial accrued liability. Certain reductions to the aid to the Minneapolis association are made annually, depending in part on investment returns.

Firefighters Relief: This payment provides additional funding to support a minimum fire state aid amount for volunteer firefighter relief association pension benefits.

Supplemental Police/Fire Amortization State Aid: This payment provides additional state aid to amortize the unfunded liability of local police and salaried firefighter relief associations, the Teacher's Retirement Association and the St. Paul Teacher's Retirement Association. Like the amortization aid, the supplemental aid terminates when a relief association becomes fully funded.

Current Law

Police and Fire State Aids	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Police State Aid	$ 60,827	$ 57,471	$ 59,957	$ 59,344	$ 61,829
Fire State Aid	$ 23,727	$ 20,522	$ 22,533	$ 23,211	$ 23,866
Insurance Surcharge	$ 2,250	$ 2,499	$ 2,499	$ 2,499	$ 2,499
Amortization State Aid	$ 2,092	$ 3,626	$ 4,963	$ 4,963	$ 4,963
Firefighter Relief Association	$ 609	$ 609	$ 722	$ 722	$ 722
Supplemental Amortization State Aid	$ 572	$ 829	$ 1,000	$ 1,000	$ 1,000
Total	$ 90,077	$ 85,601	$ 88,674	$ 91,739	$ 94,879

Legal Citations: M.S. 69.031; M.S. 2971.10; M.S. 424A.10; M.S. 423A.02

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Purpose
To provide a state aid to cities, counties, towns and other non-school jurisdictions to offset an employer contribution rate increase for the Public Employees Retirement Association (PERA).

Funding Source
State General Fund

Program Description
PERA is a fixed general aid payment to non-school local governments. PERA aid is paid to any county, city, town or special taxing district with an account or accounts in the Public Employees Retirement Association (PERA). It is intended to offset the cost of the increase to the PERA employer contribution rates that were effective beginning in fiscal year 1998. The aid is equal to 0.7% of the jurisdiction's fiscal year 1997 PERA payroll. The amounts will remain the same from year to year, but could potentially decrease in the future if the current PERA payroll drops significantly below the fiscal year 1997 level. The aid payments are scheduled to terminate on June 30, 2020.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
PERA Aid	$ 14,520	$ 14,390	$ 14,384	$ 14,384	$ 14,384
Total	$ 14,520	$ 14,390	$ 14,384	$ 14,384	$ 14,384

Legal Citation: M.S. 273.1385

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Purpose
To provide compensation for the property taxes lost to local government when the Department of Natural Resources (DNR) acquires natural resource land for the state.

Funding Source
State General Fund

Program Description
The payment in lieu of taxes (PILT) was created in 1979 to compensate local governments for state acquired natural resource lands. State-owned land is exempt from property taxes. The reasons given for PILT are to compensate local governments for loss of property taxes and to help pay for the cost of basic services provided for the state owned land. The amount of the payment has changed over the years. The current payment is based on a per-acre rate, the appraised value of the land, or a share of receipts generated from the land. The payment method depends on the land's category of PILT eligibility. The various types of land that are natural resource land for the purpose of calculating PILT are: 1) non-hunting lands that were privately owned prior to DNR's acquisition; 2) hunting grounds that were privately owned prior to DNR's acquisition; 3) consolidated conservation lands that are designated as a state park, state recreation area, scientific and natural area, or wildlife management area; and 4) some tax-forfeited land administered by the county. The 2009 payment rate for most acquired land was either $5.114 per acre or three-quarters of 1% of the appraised value of the land, whichever was greater. The 2009 payment rate for tax-forfeited land was $1.278 per acre.

The PILT payments are given to eligible counties, townships and school districts. The statute sets out the distribution of the payment to the counties with a portion to be deposited in county general revenue fund to provide tax levy reduction and a portion for resource development. The appropriation is made initially to the Department of Natural Resources and then transferred to the Commissioner of Revenue. PILT payments are made once a year in the first local government aid payment which is made in July. The payment amount includes an annual inflation adjustment.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
DNR PILT	$ 21,026	$ 21,824	$ 21,777	$ 26,490	$ 26,801
Total	$ 21,026	$ 21,824	$ 21,777	$ 26,490	$ 26,801

Legal Citation: M.S. 477A.11 through 477A.145

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Purpose
For equity purposes, interest is paid on some tax refunds if they are not paid to the taxpayer within a certain period of time.

Funding Source
State General Fund

Program Description
Interest is due and paid to the taxpayer on certain tax refunds if they are not paid within a set statutory time frame. The interest rate paid on refunds is the same rate that the taxpayer would owe on underpayments. The interest rate for 2010 and 2011 is 3%. The interest rate is announced prior to the start of each calendar year and is calculated based on the prime rate charged by banks.

The goal of the Department of Revenue is to pay refunds in a timely fashion and minimize any interest accrual. However, delays in paying refunds and interest accrual can occur for various reasons such as tax disputes that are resolved via court cases, audits and administrative appeals.

For individual income tax and corporate franchise tax, interest on refunds is computed starting 90 days after the due date or the date the return is filed (whichever is later). For both sales and use tax and withholding taxes, interest generally accrues from the date of payment. However, for sales tax refunds of tax paid on capital equipment, certain building materials, and purchaser refunds, interest is computed starting 90 days after the refund claim is filed.

Interest payments can fluctuate greatly from year to year typically as a result of court cases. The unusually low payments of tax refund interest forecast for fiscal year 2011 are partly due to a delay in refund payments that will shift $236.4 million in refunds (and associated interest) from fiscal year 2011 to fiscal year 2012. This delay was the result of both administrative changes announced at the same time as 2009 unallotments and a 2010 Legislative law change.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Tax Refund Interest	$ 8,185	$ 20,037	$ 9,700	$ 21,500	$ 12,000
Total	$ 8,185	$ 20,037	$ 9,700	$ 21,500	$ 12,000

Legal Citation: M.S. 289A.56; 2010 Minn. Laws, First Special Session, Chapter 1, Article 12, Sec. 6.

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Purpose

To encourage more participation in the political process and to make candidates less dependent on large dollar contributions the state reimburses donors who contribute to political candidates and political party units.

Funding Source

State General Fund

Program Description

The PCR program was enacted in 1990. Under the current PCR program, political contributions made by Minnesotans to qualifying political candidates and political party units are eligible for a state refund of up to a total of $50 per person (of $100 per couple) in any calendar year. The refund program is available to political party units and legislative and state-wide candidates who agree to limit their spending by signing a Public Subsidy Agreement. Political candidates and parties are provided with special forms to document their contributions. This documentation is sent to the Department of Revenue, and a refund check is sent to the original donor. In essence, the contributor is donating state general fund money to a political candidate or party. The program is supported through an open appropriation from the general fund.

The program was suspended for political contributions made in fiscal years 2010 and 2011 by 2009 Governor's unallotment actions that were ratified by the 2010 legislature. Expenditures shown for fiscal year 2010 are refunds for contributions made prior to July 1, 2009.

Current Law

	Actual F.Y. 2009	Actual F.Y. 2010	Estimated F.Y. 2011	Estimated F.Y. 2012	Estimated F.Y. 2013
Political Contribution Refund	$ 5,715	$ 1,720	$ 0	$ 5,400	$ 6,400
Total	$ 5,715	$ 1,720	$ 0	$ 5,400	$ 6,400

Legal Citation: M.S. 290.06; 2010 Minn. Laws, First Special Session, Chapter 1, Article 13, Sec. 4.

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