HOUSE RESEARCH Bill Summary

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Overview

Reimposes levy limits for taxes payable in 2007 only for counties and for cities with a population of 2,500 or more.

Conforms Minnesota's income tax to the increased federal standard deduction for married filers, and to federal law changes enacted since April 15, 2005.

Excludes military pension income from Minnesota's income tax, phased in from 25% in 2006 to 100% in 2009

Provides a one-time income tax credit of up to $50,000 for expenditures made to modernize dairy cattle operations in Minnesota. The credit equals 10 percent of expenditures made in tax years 2006 through 2011.

Provides a refundable income tax credit for expenses related to becoming a U.S. citizen. The maximum credit is $300 and the credit is limited to taxpayers with incomes under $30,000.

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Accelerates the phase-in of single factor sales apportionment under the corporate franchise tax by three years from tax year 2014 under present law to 2011 under the bill.

Provides a sales tax exemption of up to $10,000 annually for construction materials and supplies to improve and expand class 1c and 4c resorts.

1 **Levy year; definition.** Provides a definition of "levy year" or "taxes levied in" as the year in which the taxes voted by the local governmental unit are to be certified to the county auditor. Effective the day following final enactment.

2 **Special levies.** Changes the special levies that are allowed for taxes payable in 2007. Special levies are those amounts that may be levied outside of, or in addition to, the unit's levy limitation. Strikes special levies for:

- payments to the state armory commission for armory bonds,
- matching funds under certain federal or state grant programs,
- abatements for economic development purposes under Minn. Stat. § 469.1815,
- increases in employer contribution payments for public employee retirement benefits since 2001,
- operations of a lake improvement district,
- repaying transportation related state or federal loans for mandated projects,
- certain transitional amounts related to the completed state takeover of court administration costs (obsolete),
- certain payments to police and firefighter relief associations,
- storm sewer improvement district costs, and
- funding the prevention of cruelty to animals.

Special levies are retained to pay:

- debt service,
- property taxes levied against referendum market value,
- the unreimbursed costs of natural disasters,
- errors in the prior year's levy certification, and

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- the operation and maintenance of qualified county jails.

Current amounts levied for the purposes listed in the repealed special levies are included in the levy limit base subject to the limit.

Effective the day following final enactment.

3 **Levy limit base.** Defines the levy limit base for taxes payable in 2007 as the sum of the local unit's total property tax levy for taxes payable in 2006 plus the taconite aid amounts the local unit was certified to receive in 2006 under Minn. Stat. §§ 298.28, 298.282 and the LGA and county program aid amounts under Minn. Stat. §§ 477A.011 to 477A.03, less the amounts that would have qualified for the remaining special levies under the new laws. Effective the day following final enactment.

4 **Adjusted levy limit base.** Defines the adjusted levy limit base as the governmental unit's levy limit base plus a percentage increase for annual inflation computed from the most recent implicit price deflator for government expenditures and investment, and a percentage increase for the growth, if any, in the number of households within the local governmental unit.

Effective the day following final enactment.

5 **Property tax levy limit.** Defines the levy limit for taxes payable in 2007 for the applicable local units of government. Under the statute, counties and cities with a population of 2,500 or more would be subject to levy limits. Except for allowable adjustments for annexations and change in local government service responsibilities, the levy limit is equal to the adjusted levy limit base minus the amounts the local unit will receive in state aid in 2007 under Minn. Stat. §§ 298.28, 298.282, and 477A.011 to 477A.014, and minus the estimated amount of wind energy production tax revenues the local unit will receive in 2007.

Effective the day following final enactment.

6 **Special levies; natural disasters.** Updates a cross-reference to the new clause number for the special levy allowed in the case of costs for natural disasters.

Effective the day following final enactment.

7 **Update of tax administration provisions.** Adopts federal tax administrative provisions made between April 15, 2005, and December 31, 2006, that Minnesota references for state tax administration purposes under chapter 289A. None of the three federal acts enacted since April 15, 2005, changed federal provisions that Minnesota provisions refer to in chapter 289A.

Effective the day following final enactment.

8 **Update to federal definition of taxable income.** Adopts all of the federal changes to taxable income effective at the same time the federal changes were effective. The three new federal laws and important changes were:

- **The Energy Tax Incentives Act of 2005** , Public Law 109-58, enacted August 8, 2005, generally provides for the acceleration of the deduction of capital expenditures for companies providing energy and energy services to U. S. consumers and was

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generally effective for expenses incurred under contracts entered into after April 11, 2005.

- **The Katrina Emergency Tax Relief Act of 2005** , Public Law 109-73, enacted September 23, 2005, provides additional tax incentives for individuals and corporations to make charitable contributions after August 25, 2005, and before January 1, 2006, and additional tax relief to victims of the hurricane. Generally effective between August 25, 2005, and January 1, 2007.

- **The Gulf Opportunity Zone Act of 2005** , Public Law 109-135, enacted December 21, 2005, provides similar tax provisions available under the Hurricane Katrina bill to Hurricane Rita and Wilma victims and charitable givers. Also allows additional section 179 expensing or 50 percent bonus depreciation on business property placed in service in the areas damaged by Hurricane Katrina (between August 28, 2005, and December 31, 2007, for equipment and December 31, 2008, for structures).

9 **Additions to federal taxable income.** Strikes the addition to Minnesota taxable income for the difference between the current federal standard deduction for married filers and the standard deduction for married filers in effect before enactment of WFTRA, effective in tax year 2006. This has the effect of conforming Minnesota's standard deduction for married filers to the federal standard deduction for tax years 2006 to 2008, years in which Minnesota would otherwise allow a lower standard deduction for married filers than is allowed at the federal level.

Also strikes the adjustment to the calculation of the addition to Minnesota taxable income for state income and sales taxes deducted at the federal level that was enacted in 2005 because Minnesota did not conform to the increased standard deduction.

10 **Subtractions from taxable income; military pensions.** Allows an income tax subtraction for military retirement pay. Phases in the subtraction over a four-year period, using the lesser of the following percentages and amounts for each year:

2006	25%	$7,500
2007	50%	$15,000
2008	75%	$22,500
2009 and following years	100%	no maximum

11 **Update to other references to the Internal Revenue Code in chapter 290.** Adopts federal changes to federal adjusted gross income used for computing individual alternative minimum tax and household income which is used to compute the dependent care and K-12 education credit; changes to the federal earned income tax credit; and changes to the federal definition of "qualified research expenses." The main changes to federal adjusted gross income are described in section 0.

For the federal earned income credit that Minnesota uses as a basis for the Working Family Credit, individuals who lived in the Hurricane Katrina, Rita, or Wilma disaster areas are allowed to elect to use their 2004 earned income rather than 2005 earned income in

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calculating their 2005 credit.

The federal definition of "qualified research expenses," which Minnesota uses to compute the Minnesota C corporation Research and Development Credit, was changed, effective for amounts paid or incurred after August 8, 2005, to allow 100 percent of amounts paid to small businesses, universities and federal labs for qualified energy research as a qualifying research expense (old law allowed only 65 percent of amount paid).

12 **Change in ratio nonresidents use to compute Minnesota tax.** Removes the new military pension subtraction proposed in section 0from both the numerator and denominator of the ratio used to calculate a part year or nonresident individual's Minnesota income tax. Also clarifies that Minnesota nonrefundable credits are either prorated by the nonresident ratio or allowed in full in the case of credits generated solely by Minnesota activity.

13 **Dairy investment credit.** Allows a dairy investment credit against individual income and corporate franchise taxes. The credit equals 10 percent of the first $500,000 of qualifying expenditures for improvement of buildings or facilities or acquisition of equipment used for dairy cattle in Minnesota. Qualifying expenditures include: barns; fences; watering facilities; feed storage and handling equipment; scales; milking, robotic, and milk storage equipment; and manure management facilities including digesters and energy production equipment.

The credit is nonrefundable and may only be used to offset liability. Unused credit amounts may be carried forward for up to 15 tax years.

A taxpayer may claim the credit for expenditures made between December 31, 2005, and January 1, 2012. The maximum credit is $50,000; this maximum applies to entities such as partnerships and S corporations as well as to individual taxpayers.

14 **Marriage penalty credit.** Strikes the adjustment to the calculation of the marriage penalty credit enacted in 2005 because Minnesota did not conform to the increase standard deduction. Effective beginning in tax year 2006.

15 **Citizenship credit.** Provides a refundable income tax credit for non-citizens of the United States equal to 100 percent of qualified citizenship expenses. The maximum credit is $300 per year and no credit is allowed for individuals or married couples with household income greater than $30,000. Defines "qualified citizenship expenses" as fees paid after the individual starts the citizenship process by filing the federal Application to Register Permanent Residence to the time the individual becomes a citizen of the United States for

- enrollment of the taxpayer, spouse, or any dependent of the taxpayer over age 18 in an English language class offered by a school district or a licensed school and

- fees paid to the federal government for submission of the federal N-400 naturalization application and required fingerprinting

Effective for tax years beginning after December 31, 2005.

16 **Alternative minimum tax.** Allows a subtraction of military pension income from alternative minimum taxable income, to complement its subtraction from federal taxable income as provided in section 0.

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17 **Single factor sales apportionment; regular corporations.** Accelerates phase-in of single factor sales apportionment of income from an 8-year phase-in to a 5-year phase-in, still beginning with tax year 2007 for regular corporations, but reaching 100 percent sales apportionment in tax year 2011 rather than 2014. The current law and proposed phase-schedules are as follows:

Tax year	Sales Percentage, current law	Sales percentage, proposed
Present law	75%	75%
2007	78%	80%
2008	81%	85%
2009	84%	90%
2010	87%	85%
2011	90%	100%
2012	93%	100%
2013	96%	100%
2014	100%	100%

18 **Update of references to Internal Revenue Code in the property tax refund chapter.** Adopts the federal changes that affect household income, which uses the definition of federal adjusted gross income as a starting point.

19 **Federal update; estate tax.** Changes the date through which Minnesota incorporates the federal estate tax from April 15, 2005, to December 31, 2005. Since there has not been a federal change in the estate tax since the last update, this change does not have any substantive effect.

20 **Sales tax exemption; resort construction materials.** Adds a sales and use tax exemption for construction materials and supplies used in physically expanding or making capital improvements to class 1c and 4c resorts, including any portion of the resort classified as class 3 commercial property. The exemption would be administered as a tax refund and is limited to $10,000 of tax per resort per calendar year. The tax must first be paid, after which the owner may file a refund claim with the Department of Revenue. Effective for sales and purchases made after June 30, 2006.

21 **Tax collected.** Clarifies that sales tax must be collected on purchase of resort construction materials. These purchases will be eligible for a sales tax refund under section 0.

22 **Sales tax refund.** Include purchase of resort construction materials in the list of items for which sales tax refund claims may be filed. Requires that the owner of the resort apply for the refund.

23 **Application.** Requires a contractor, subcontractor, or builder who purchases construction materials that are exempt under section 0, to provide the resort owner with the information necessary to apply for the sales tax refund.

24 **Hurricane Katrina relief.** Adopts the Internal Revenue Service's position that employee leave donations to charities providing Hurricane Katrina relief do not generate adjusted gross income to the employee donating the leave. Effective for the 2005 and 2006 tax years.