

Federal Taxable Income, the starting point for calculating Minnesota income tax

What is federal taxable income (FTI)?

Federal taxable income is the tax base used to calculate federal income tax liability. It is also the starting point for calculating Minnesota taxable income, the tax base used to calculate Minnesota income tax liability. Federal taxable income equals federal adjusted gross income (FAGI) after deductions and exemptions.

$$\boxed{\begin{array}{l} \text{Federal} \\ \text{adjusted} \\ \text{gross income} \\ \text{(FAGI)} \end{array}} - \boxed{\begin{array}{l} \text{Standard} \\ \text{or} \\ \text{Itemized} \\ \text{deductions} \end{array}} - \boxed{\begin{array}{l} \text{Personal} \\ \text{and} \\ \text{Dependent} \\ \text{exemptions} \end{array}} = \boxed{\begin{array}{l} \text{Federal} \\ \text{taxable} \\ \text{income} \\ \text{(FTI)} \end{array}}$$

What kinds of income are included in FAGI?

FAGI includes most kinds of income: wages, salaries, and tips; taxable interest; dividends; alimony received by the taxpayer; business income or loss; capital gains or losses; other gains or losses; taxable IRA distributions; taxable pension and annuity distributions (the taxable portion is typically determined by whether or not the contributions to the pension or annuity were included in FAGI when they were made); income from rental real estate, royalties, partnerships, S corporations, and trusts; farm income or loss; unemployment compensation; and taxable Social Security benefits (the amount taxable depends on the individual's income level; at most, 85 percent of benefits are included in FAGI). FAGI does not include child support received by the taxpayer.

What kinds of income are excluded from FAGI?

FAGI excludes: deductible IRA, SEP, and SIMPLE contributions; nontaxable employee fringe benefits; student loan interest payments; Health Savings Account contributions and investment income; moving expenses; one-half of self-employment tax; health insurance premiums (for self-employed taxpayers only); penalty on early withdrawal of savings; alimony paid by the taxpayer; and, through tax year 2011, \$250 of teacher classroom expenses and \$4,000 of tuition expenses for higher education. FAGI does not exclude child support paid by the taxpayer.

What deductions are allowed from FTI?

Taxpayers may claim either the standard deduction or itemized deductions. In tax year 2009, the most recent year for which data is available, 60 percent of Minnesotans claimed the standard deduction and 40 percent itemized.

How much is the standard deduction?

In tax year 2012, the standard deduction is as follows:

- \$11,900 for married couples filing joint returns
- \$5,950 for married couples filing separate returns
- \$8,700 for head of household filers
- \$5,950 for single filers

What itemized deductions are allowed?

In tax year 2012, itemized deductions are allowed for the following:

- Payments of state and local property taxes and either income or sales taxes
- Mortgage interest
- Charitable contributions
- Medical expenses in excess of 7.5 percent of income
- Casualty and theft losses in excess of 10 percent of income
- Job expenses and miscellaneous expenses (most only allowed in excess of 2 percent of income)

What personal and dependent exemptions are allowed?

Taxpayers may claim one personal exemption each and one dependent exemption for each dependent claimed. For tax year 2012, the personal and dependent exemptions are \$3,800 each. A family of four qualifies for four exemptions, totaling \$15,200.

Are there limits on deductions and exemptions?

The federal Revenue Reconciliation Act of 1990 (RRA 1990) limited itemized deductions for taxpayers with incomes over a threshold. This limit takes away some of the benefit of the deduction for higher income taxpayers. Taxpayers subject to the limit have their deductions reduced by 3 percent of their AGI over the applicable thresholds. But they are always guaranteed 20 percent of the deductions, no matter how high their AGIs are.

RRA 1990 also provided for personal and dependent exemptions to be phased out for taxpayers with incomes over a threshold. Affected taxpayers lose 2 percent of their total exemption amount for each \$2,500 of income over the threshold.

The federal Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 gradually phased out the limitation on itemized deductions and the phaseout of exemptions over five years, from 2006 to 2010, so that in tax year 2010, the limitation and the phaseout were not in effect. The federal Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended the elimination of the deduction limitation and the exemption phaseout to tax years 2011 and 2012. In tax year 2013 the limitation of itemized deductions and the phaseout of exemptions will be reinstated.

The table shows the income thresholds for the itemized deduction limitation and the personal exemption phaseout in effect in tax year 2009. The income thresholds are adjusted annually for inflation, and the inflation adjustment will resume in 2013 if the limitation and phaseout are reinstated.

Tax year 2009	Itemized deduction limit begins at	Exemption phaseout begins at
Married joint filers	\$166,800	\$250,200
Married separate filers	\$83,400	\$125,100
Single filers	\$166,800	\$166,800
Head of household filers	\$166,800	\$208,500

For more information: Contact legislative analyst Nina Manzi at 651-296-5204 or Joel Michael at 651-296-5057. Also see the House Research publication [Income Tax Terms: Deductions and Credits, August 2011](#).

The Research Department of the Minnesota House of Representatives is a nonpartisan office providing legislative, legal, and information services to the entire House.