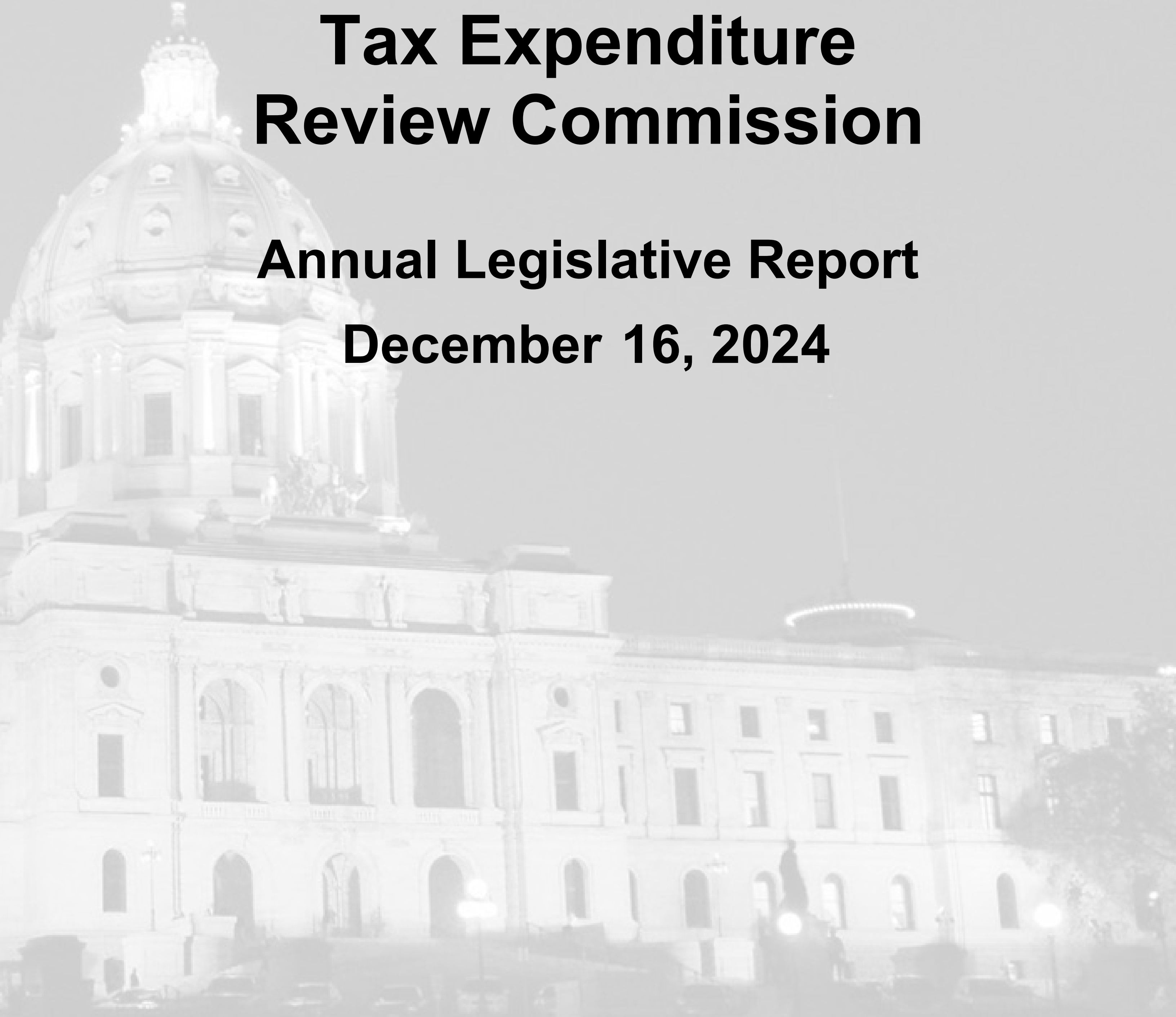
Tax Expenditure Review Commission

Annual Legislative Report

December 16, 2024



Prepared by the Legislative Budget Office on behalf of the Tax Expenditure Review Commission.

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December 16, 2024

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To the Honorable Chairs,

This report is submitted on behalf of the Tax Expenditure Review Commission pursuant to [Minnesota Statutes 2024, section 3.8855, subdivision 7.]

The Tax Expenditure Review Commission was created to review Minnesota's tax expenditures and evaluate their effectiveness and fiscal impact. The Tax Expenditure Review Commission must submit an annual report by December 16th to the legislative committees with jurisdiction over tax policy to detail the results of the Commission’s reviews of tax expenditures in the previous calendar year.

In 2024, the Commission continued on its course of conducting initial reviews of tax expenditures to identify their policy objectives and potential metrics for evaluation. The Commission reviewed 45 tax expenditures in 2024, approving an objective statement and directing the Legislative Budget Office to begin an evaluation of these policies.

More detail of the Commission’s work in 2024 is provided within this report.

Sincerely,

Senator Ann H. Rest, Chair

Representative Esther Agbaje, Vice Chair

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Executive Summary

This report is submitted on behalf of the Tax Expenditure Review Commission (Commission) pursuant to [Minnesota Statutes 2024, section 3.8855, subdivision 7.]

The Commission met on January 25, 2024, marking the first of six meetings convened in 2024. The Commission was presented with 45 initial reviews of tax expenditures throughout the calendar year. Each initial review included a description of the tax expenditure, additional background information, a proposed objective statement, and potential metrics to evaluate each tax expenditure.

On some occasions the Commission provided modifications to the proposed objective statements and requested that technical clarifications be made to certain reviews. The Commission adopted an objective statement for all 45 tax expenditures presented and directed the Legislative Budget Office (LBO) to begin evaluating these tax expenditures.

One activity of note is the adoption of TERC Resolution 1 on July 10, 2024. The Commission voted favorably to require the Commissioner of Revenue to call to order the first meeting of each calendar year. While the enacting statute of the Commission was clear on who should call the inaugural meeting, the language was silent on who should call the first meeting after new members are assigned to the Commission by January 31 of each odd-numbered year. The adopted resolution was designed to address this issue.

This report provides additional detail to the activities of the Commission in 2024.

Introduction

The Tax Expenditure Review Commission was established under Laws of Minnesota 2021, 1st Special Session, chapter 14, article 11, section 4, to review Minnesota's tax expenditures and evaluate their effectiveness and fiscal impact. Details on the establishment of the Commission, its membership, duties, review requirements, staff support, and reporting requirements are codified under Minnesota Statutes 2024, section 3.8855.

This report provides an overview of the Commission and its activities in calendar year 2024. The overview covers the Commission's membership; the Commission's duties and responsibilities; and a summary of the six meetings convened in 2024. A more detailed account of each meeting and the initial reviews presented at each respective meeting are provided in appendices B-F.

Under Laws of Minnesota 2023, chapter 64, article 15, section 1, the Commission is allowed to conduct evaluations of tax expenditures concurrently with the completion of initial reviews. Previously, the Commission's statute required all initial reviews to be completed before evaluations could begin. Under the law change, the Commission has directed the LBO to conduct evaluations of each tax expenditure after an initial review has been presented and an objective has been formally adopted by the Commission. Accordingly, the LBO continues to conduct initial reviews on the remaining tax expenditures while performing evaluations on the tax expenditures approved for evaluation, on behalf of the Commission. The LBO is drafting evaluations that are in process as of this report date and have not yet been completed for the Commission's consideration. The LBO intends to begin presenting tax expenditure evaluations to the Commission beginning in calendar year 2025.

To supplement the report, a general overview of tax expenditures is included which provides a brief history of tax expenditures and a summary of Minnesota tax expenditures. Any reporting on estimated fiscal impacts in this supplemental section is based on the 2024 Tax Expenditure Budget published by the Department of Revenue (DOR) on November 1, 2024.

Up until this point, the Commission has only been presented with material based on the 2022 Tax Expenditure Budget, published on February 1, 2022. The initial reviews included in appendices B-F were produced using the 2022 Tax Expenditure Budget. The Commission can expect initial reviews and estimates of fiscal impact to reflect the 2024 Tax Expenditure Budget for the next two years.

A note of gratitude is extended to Commission members for their participation on the Commission. A special thank you goes out to legislative staff and the DOR for their engagement and feedback that informed the work throughout the calendar year.

Tax Expenditure Review Commission

The structure, duties, and work of the Commission during the 2024 calendar year are outlined below.

Commission Members

Minnesota Statutes 2024, section 3.8855, subdivision 3 governs the nine-member commission, plus two ex-officio, nonvoting members. Membership, as defined by statute, must include:

- Two members of the Senate appointed by the Senate Majority Leader;
- Two members of the Senate appointed by the Senate Minority Leader;
- Two members of the House of Representatives appointed by the Speaker of the House;
- Two members of the House of Representatives appointed by the Minority Leader;
- The Commissioner of Revenue or a designee.
- If the chair of the house or senate committee with primary jurisdiction over taxes is not an appointed member, the chair is an ex officio, nonvoting member of the Commission.

The 2024 Tax Expenditure Review Commission members are:

House of Representatives

- Rep. Esther Agbaje, Vice Chair
- Rep. Greg Davids
- Rep. Steve Elkins
- Rep. Jim Joy

Department of Revenue

- Commissioner Paul Marquart

Senators

- Sen. Steve Drazkowski
- Sen. Matt D. Klein
- Sen. Ann H. Rest, Chair
- Sen. Bill Weber

Ex-Officio Members

- Rep. Aisha Gomez

Duties and Responsibilities

The duties of the Commission are defined in Minnesota Statutes 2024, section 3.8855, subdivision 4:

- For not more than three years after the Commission is established, the Commission must complete an initial review of the state's tax expenditures. The initial review must identify the purpose of each of the state's tax expenditures if none was identified in the enacting legislation in accordance with Minnesota Statutes 2024, section 3.192. The Commission may also identify metrics for evaluating the effectiveness of an expenditure.

- The Commission must review and evaluate Minnesota's tax expenditures on a regular, rotating basis.

  a) The Commission must establish a review schedule that ensures each tax expenditure will be reviewed by the Commission at least once every ten years.
  b) The Commission may review expenditures affecting similar constituencies or policy areas in the same year, but the Commission must review a subset of the tax expenditures within each tax type each year.
  c) To the extent possible, the Commission must review a similar number of tax expenditures within each tax type each year.
  d) The Commission may decide not to review a tax expenditure that is adopted by reference to Federal law.

- Before December 1 of the year a tax expenditure is included in a Commission report, the Commission must hold a public hearing on the expenditure, including but not limited to a presentation of the review components listed in Minnesota Statutes 2024, section 3.8855, subdivision 5.

Additionally, under subdivision 6, the DOR Tax Research Division must provide the Commission with the summary data required to complete certain statutorily required review components.

Subdivision 7 states that LBO staff must provide professional and technical assistance to the Commission as the Commission deems necessary, including assistance with the annual report.

2024 Commission Meetings

This section provides a brief discussion of Commission activities during 2024. Detailed summaries of the five meetings convened between January and September can be found in appendices B-F. An appendix for the December meeting is not provided. Meeting agendas, minutes, and meeting materials can be found on the Tax Expenditure Review Commission website.

Also included in this section is the list of 45 tax expenditures initial reviews, representing ten different tax types, that were approved by the Commission to move forward for evaluation. The list is in the order the initial reviews were presented to the Commission.

January 25, 2024

The LBO presented the evaluation process the office intends to follow to evaluate the effectiveness and efficiency of tax expenditures. Additionally, four initial reviews were presented to the Commission. No formal motions or actions were taken by the Commission.

March 15, 2024

Five tax expenditure initial reviews were presented to the Commission. The Commission moved to adopt the four initial reviews presented at the January 25 Commission meeting and the five initial reviews presented at the March 15 Commission meeting. The Commission directed the LBO to evaluate the nine tax expenditures. The Commission requested the initial review of the Home Mortgage Interest Deduction, the Subtraction on Interest on Contributions to a First-Time Homebuyer Account, and the Angel Investment Credit for the next Commission meeting.

July 10, 2024

The Initial reviews of the three tax expenditures requested at the March 15 meeting were presented by the LBO and adopted by the Commission with a modification to the objective of the Home Mortgage Interest Deduction. The Commission directed the LBO to evaluate the three tax expenditures. The Commission adopted resolution TERC-1 to require the Commissioner of Revenue to call to order the first meeting every year.

August 16, 2024

The LBO presented three initial reviews to the Commission and presented for a second time nine initial reviews that were originally presented in 2022, but never acted upon. The Commission adopted all 12 initial reviews and directed the LBO to evaluate the tax expenditures. The Commission requested that technical clarifications be added to three initial reviews detailed in Appendix E.

September 18, 2024

Five tax expenditure initial reviews were presented to the Commission. The Commission adopted the initial reviews and directed the LBO to evaluate the five tax expenditures.

December 4, 2024

The DOR provided and overview of the November 1, 2024, Tax Expenditure Budget, and the LBO provided a high-level overview of the draft annual legislative report. The Commission also discussed potential changes to the TERC statute, Commission member appointments and planning for the first Commission meeting in 2025. An appendix with additional detail for this meeting is not included.

Table 1. Tax Expenditure Objectives Approved by the TERC in 2024

Count	Initial Review Title	Tax Type	2022 TEB Number
1	Marriage Credit	Individual Income Tax	1.84
2	Employer Transit Pass Credit	Individual Income Tax	1.87
3	Employer Transit Pass Credit	Corporate Franchise Tax	2.28
4	Solar Energy Systems	General Sales and Use Tax	4.27
5	Credit for Small Brewers	Alcoholic Beverage Tax	7.07
6	Open Space Property	Property Tax	13.06
7	Data Center Equipment	General Sales and Use Tax	4.72
8	Wind Energy Conversion Systems	General Sales and Use Tax	4.26
9	Microdistillery Credit	Alcoholic Beverage Tax	7.08
10	Small Winery Credit	Alcoholic Beverage Tax	7.09
11	Home Mortgage Interest Deduction	Individual Income Tax	1.66
12	Interest on Contributions to First-Time Homebuyer Account	Individual Income Tax	1.81
13	Angel Investment Credit	Individual Income Tax	1.94
14	Residential Heating Fuels	General Sales and Use Tax	4.14
15	Residential Water Services	General Sales and Use Tax	4.15
16	Sewer Services	General Sales and Use Tax	4.16
17	Property Partitioned Between Co-Owners	Deed Transfer Tax	10.01
18	Distributions by Personal Representatives	Deed Transfer Tax	10.02
19	Cemetery Lots	Deed Transfer Tax	10.03
20	Exchange of Permanent School Fund Lands	Deed Transfer Tax	10.04
21	Mortgage or Lien Foreclosure Sales	Deed Transfer Tax	10.05
22	Decree of Marriage Dissolution	Deed Transfer Tax	10.06

23	Bingo at Certain Organizations	Lawful Gambling Tax	11.01
24	Bingo at Fairs and Civic Celebrations	Lawful Gambling Tax	11.02
25	Infrequent Bingo Occasions	Lawful Gambling Tax	11.03
26	Smaller Raffles	Lawful Gambling Tax	11.04
27	Lawful Gambling Under Certain Conditions	Lawful Gambling Tax	11.05
28	Credit for Certain Raffles	Lawful Gambling Tax	11.06
29	Working Family Credit	Individual Income Tax	1.90
30	Beginning Farmer Management Credit	Individual Income Tax	1.103
31	Beginning Farmer Incentive Credit	Individual Income Tax	1.104
32	Research and Development Credit	Individual Income Tax	1.86
33	Research and Development Credit	Corporate Franchise Tax	2.27
34	Housing Contribution Credit	Individual Income Tax	1.97
35	Housing Contribution Credit	Corporate Franchise Tax	2.32
36	Housing Contribution Credit	Insurance Premiums Tax	12.09
37	Telecommunications Equipment	General Sales and Use Tax	4.21
38	Farm Machinery Exemption	General Sales and Use Tax	4.39
39	Building Materials for Residences of Disabled Veterans	General Sales and Use Tax	4.54
40	Construction Materials for Certain City Projects	General Sales and Use Tax	4.73
41	Power Line Credit	Property Tax	13.10
42	Agricultural Loans	Mortgage Registry Tax	9.01
43	Government Housing Programs	Mortgage Registry Tax	9.02
44	Bookmobiles Exemption	Motor Vehicle Sales Tax	5.10
45	Ready-Mixed Concrete Trucks	Motor Vehicle Sales Tax	5.12

Tax Expenditure Overview

The Concept of a Tax Expenditure

Minnesota Statutes 2024, section 270C.11, subdivision 6 defines *tax expenditure* to mean:

"… a tax provision which provides a gross income definition, deduction, exemption, credit, or rate for certain persons, types of income, transactions, or property that results in reduced tax revenue, but excludes provisions used to mitigate tax pyramiding."

Tax expenditures are alternative policy means by which governments deliver financial support to specific activities, entities, or groups of people. Many view tax expenditures as a form of forgone revenue.

Accurately estimating the total forgone revenue from all tax expenditures is not as simple as taking the sum of tax expenditure estimates based on the number of tax expenditures claimed. Tax expenditure estimates are likely to differ from the amount of revenue receipts that would otherwise be recovered with the repeal of a particular provision. The availability of multiple tax filing options makes it challenging to anticipate filing behavior decisions of taxpayers in the case of a single tax provision's repeal. In some cases, there are tax impact interactions that could result in over-or-understating the impact of combining tax expenditure impacts.

Nevertheless, the practice of aggregating different tax expenditures is used in the following section to estimate cumulative fiscal impacts to the state of Minnesota by tax type. The 2024 Tax Expenditure Budget published by the DOR was referenced for estimates of forgone revenue.

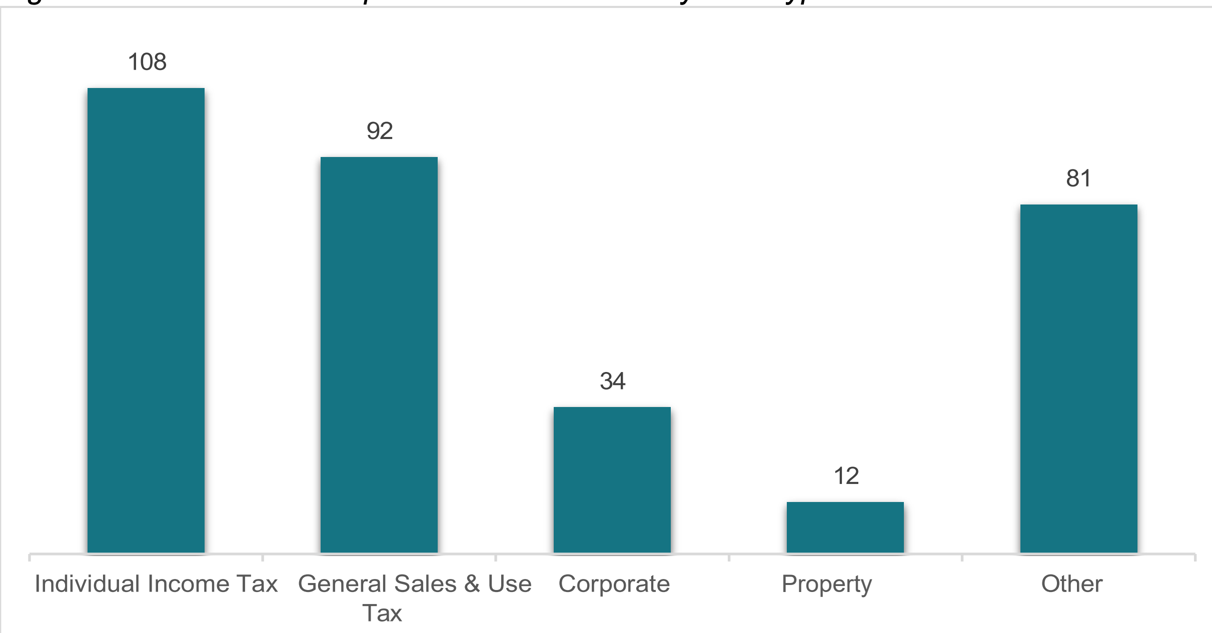
Minnesota Tax Expenditures

Though adding tax expenditures together raises many issues, a simple addition of tax expenditures allows us to visualize the magnitude of tax expenditures. An analysis of tax expenditure estimates included in the 2024 Tax Expenditure Budget, suggests that the state of Minnesota forgoes approximately $48.8 billion in state and local tax revenue through the implementation of tax expenditures in the FY2024-25 biennium. This sum is equal to 71 percent of the current biennium tax revenue estimate based on 2024 end-of-session tax revenue estimates.[1] These numbers do not include those tax relief policies listed as line items in the state's direct spending appropriations. Additionally, the Tax Expenditure Budget only includes provisions that the DOR anticipates will be claimed through fiscal year 2027.

[1] See Consolidated Fund Statement – End of 2024 Legislative Session (2024). https://mn.gov/mmb-stat/documents/budget/operating-budget/enacted/2024/eos24-cfs.pdf

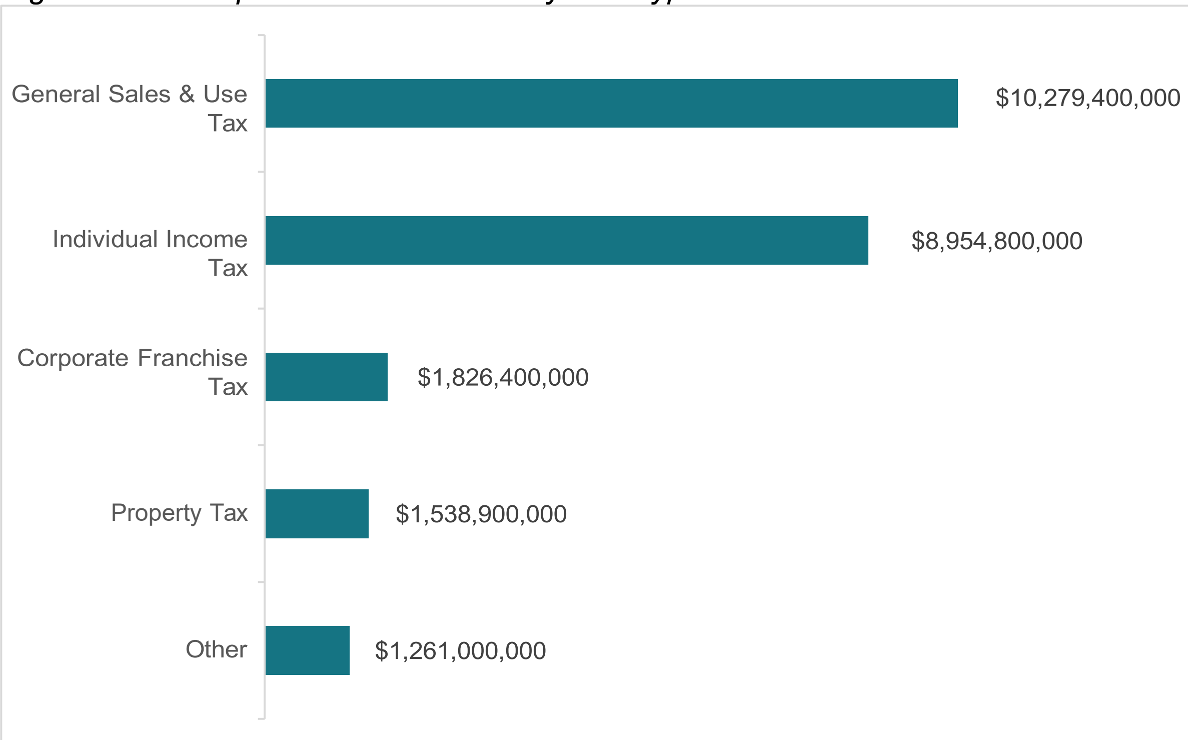
The DOR identifies 327 tax expenditures in the 2024 Tax Expenditure Budget, categorizing them into 16 different tax types. A chapter is dedicated to each tax type in the Tax Expenditure Budget. Please reference that document for more details on each tax type. As a tax type, Individual Income Tax has the highest number of tax expenditures with 108 provisions, followed by General Sale & Use Tax with 92, and Corporate Franchise Tax with 34. Figure 1 illustrates the distribution of tax expenditure provisions across tax types. Twelve tax type categories are combined into the "Other" category.

Figure 1. Count of Tax Expenditure Provisions by Tax Type



At $10.28 billion, General Sale & Use Tax incurs the most revenue forgone in terms of dollar amount. Individual Income Tax is second at $8.95 billion. The Minnesota Department of Revenue estimates that individual income tax expenditures will increase in forgone revenue by 8.4 percent from FY2024 to FY2025. Forgone revenue from General Sales and Use tax expenditures are estimated to increase by 2.5 percent from FY2024 to FY2025. Property tax expenditures are projected to increase by 3.1 percent during this period. Corporate Franchise Tax expenditures are projected to decrease in forgone revenue by 1.5 percent from FY2024 to FY 2025. If aggregated, all 327 tax expenditures across all tax types are projected to increase in forgone revenue by 4.5 percent from FY2024 to FY2025. See a distribution of fiscal year 2024 forgone revenue estimates by tax type in Figure 2. Tax expenditure estimates are for illustrative purposes only, and actual revenue impacts are likely smaller due to tax impact interactions.

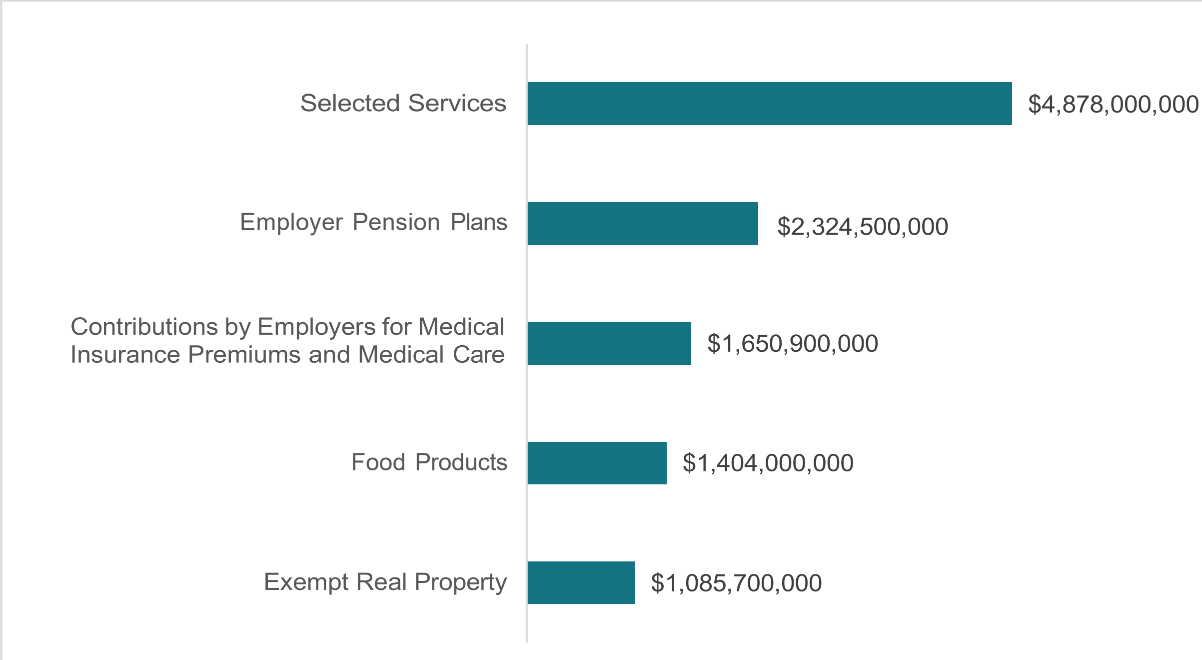
Figure 2. Tax Expenditure Estimates by Tax Type in Fiscal Year 2024



Minnesota tax expenditures are composed of many provisions with comparatively small fiscal impacts and a few provisions with large estimated fiscal impacts. To help illustrate this further, 92 percent, or 301 of the 327 tax expenditures included in the 2024 Tax Expenditure Budget, are each estimated below $150 million in forgone revenue for FY 2024.

The “Selected Services” tax expenditure is estimated to incur the highest revenue forgone estimated at $4.88 billion in fiscal year 2024. “Selected Services” is part of the General Sales and Use tax type and includes a variety of business and consumer purchases such as legal services, management consulting, personal care, and repair and maintenance, among others. Services exempt from General Sales and Use Tax are defined in Minnesota Statutes, section 297A.61, subdivision 3. The second and third largest tax expenditure estimates for fiscal year 2024 fall under the Individual Income tax type: “Employer Pension Plans,” estimated at $2.32 billion and “Contributions by Employers for Medical Insurance Premiums and Medical Care,” estimated at $1.65 billion in forgone revenue. Both are Federal conformity tax expenditures enacted in 1933. “Food Products” is another General Sales and Use Tax expenditure, and the fourth largest tax expenditure, estimated at $1.4 billion for fiscal year 2024. “Exempt Real Property” (not otherwise exempt from property tax in Federal law or the Minnesota Constitution) is the fifth largest estimated tax expenditure for fiscal year 2024, at just over $1 billion in foregone revenue. A visual comparison of these top five tax expenditure estimates is provided in Figure 3.

Figure 3. Top Five Tax Expenditure Estimates by Dollar Amount in Fiscal Year 2024



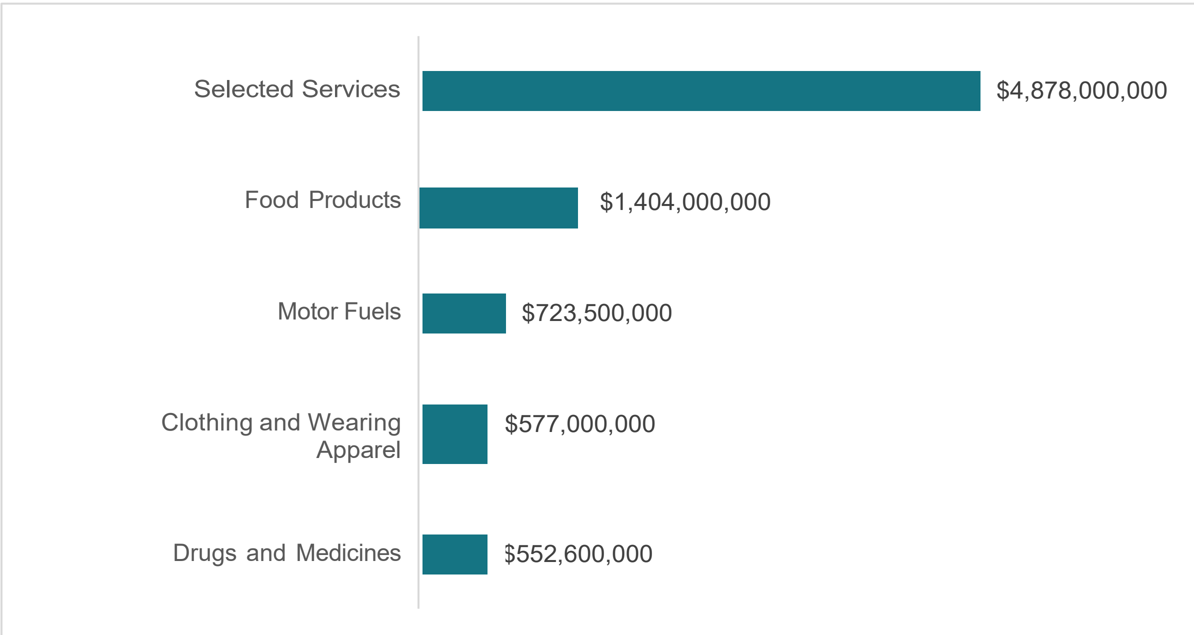
General Sales and Use Tax Expenditure

Minnesota is one of 45 states that levies a sales and use tax. Minnesota has collected a sales tax under Minnesota Statutes 2024, section 290A and section 295.75 since 1967.

The tax base consists of the gross receipts from the sale of tangible personal property or services to the final user. Sales and Use tax is generally considered a consumption tax.

Purchasers or users of taxable goods and services are subject to the tax. Holders of sales and use tax permits collect and remit the tax. Holders of direct pay permits remit the tax directly. The state's five largest general sales and use tax expenditure estimates are illustrated in Figure 4.

Figure 4. Top Five General Sales and Use Tax Expenditure by Dollar Amount in Fiscal Year 2024



Minnesota has a relatively high sales and use tax compared to other states, with the state tax rate at 6.875 percent, and an average combined state and local sales tax rate of 8.04 percent. The 2024 Minnesota Tax Incidence Study indicates that the state's general sales and use taxes are considered to be regressive.[2] The study reports that the sales and use tax burden as a percentage of income falls steadily from 7.33 percent of total income for the poorest ten percent of Minnesota households to 1.24 percent of income for the richest ten percent of Minnesota households.

General sales and use tax expenditures incur the largest forgone revenue or tax benefits to consumers, at an estimated $10.28 billion. Many of the tax exemptions for items such as "Selected Services", "Food Products", "Clothing", and "Drugs and Medicines", among others, were enacted along with sales and use tax in 1967. Since then, they have acted as a counterbalance to reduce the regressivity of the sales tax and work to achieve a saving-consumption neutrality in terms of the reference tax system.

Sales and use tax and tax expenditures affect the relative prices of goods and services. The tax burden or benefit can be transmitted out of Minnesota through tax exporting. The 2024 Minnesota Tax Incidence study shows that 19 percent of the sale tax burden was shifted to nonresident taxpayers in 2021.

[2] Minnesota Department of Revenue Tax Research Division. 2024 Minnesota Tax Incidence Study. Revised Marched 15, 2024. Available at https://www.revenue.state.mn.us/tax-incidence-studies

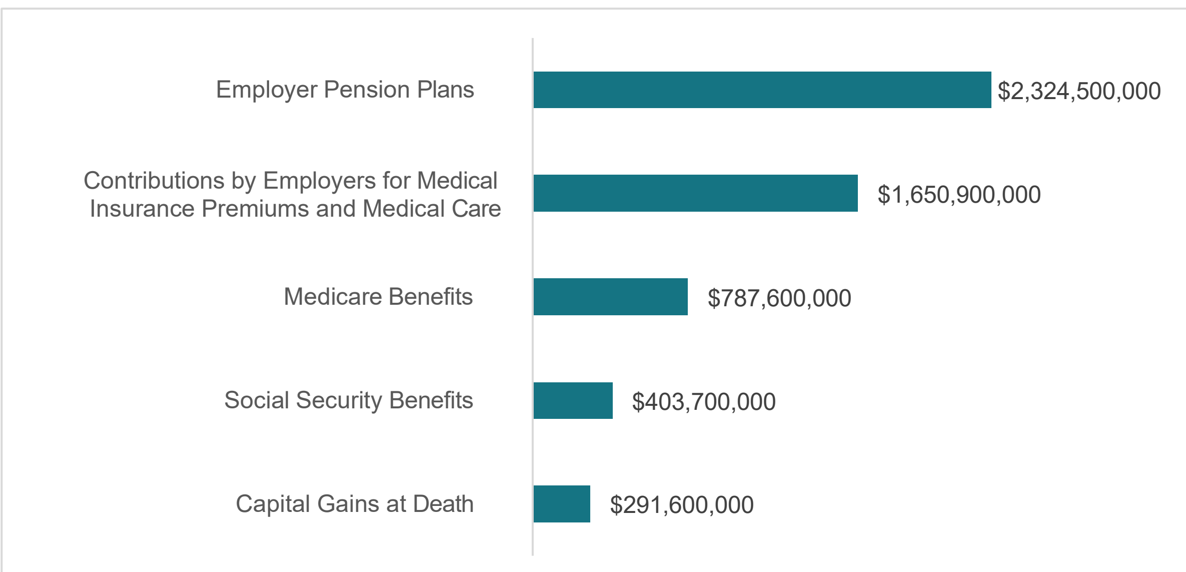
Individual Income Tax Expenditure

Minnesota introduced its individual income tax in 1933, and the tax structure remained largely unchanged until 1984. In 2019, Minnesota shifted to using Federal Adjusted Gross Income (FAGI) as the starting point for calculating state income taxes. From there, state-specific additions and subtractions are applied, followed by a progressive tax rate structure based on income thresholds.

The tax base consists of the FAGI modified by state additions, exemptions, and subtractions. This tax falls on individual taxpayers and a trust or estate with income that meets or exceeds the filing requirements.

Minnesota is a “static date” conformity state, meaning that it must regularly adopt changes to keep up with the changes in the Federal tax code. Many individual income tax expenditures are adopted as Federal conformity provisions. There are 60 individual income tax expenditures that conform to Federal deduction or Federal exclusion policies. The fiscal estimates of the top five Federal conformity individual income tax expenditure provisions are illustrated in Figure 5.

Figure 5. Top Five Federal Conformity Individual Income Tax Expenditure Estimates by Dollar Amount in Fiscal Year 2024



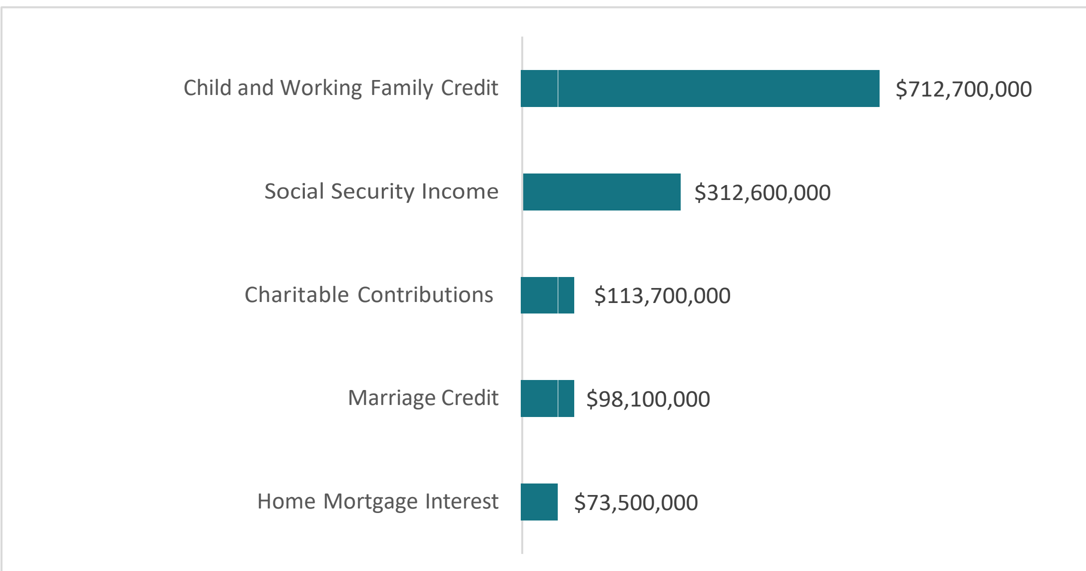
Forty-eight individual income tax expenditures are state-discretionary policies, originated and enacted by the state legislature. These are not Federal conformity provisions. Of these,12 tax expenditures are nonrefundable credits and nine are refundable credits. Not all individual income tax expenditures are credits. Figure 6 provides a count of individual income tax expenditures by provision type, including those that are Federal conformity provision types.

Figure 6. Count of Individual Income Tax Expenditures by Provision Type

Provision Type	Count of Individual Income Tax Expenditures
Credit	24
Deduction	7
Federal Exclusion	40
Federal Deduction	20
Preferred Computation	1
Subtraction	16

Figure 7 provides the revenue loss estimate of the top five individual income tax expenditures that are discretionary policies of the state of Minnesota.

Figure 7. Top Five State Discretionary Individual Income Tax Expenditures by Dollar Amount in Fiscal Year 2024



Corporate Franchise Tax Expenditure

The corporate franchise tax was enacted in 1933 along with individual income tax. A tax rate of 9.8 percent has been in effect on Minnesota taxable corporate income since 1990. As of January 2024, this is the highest statutory corporate tax rate in the country.[3] The State of Minnesota adopted an 8-year phase-in of 100 percent sales apportionment in 2005. This means that a corporation's Minnesota tax liability is calculated solely on its share of sales in Minnesota, without regard to its property or payroll factors. For more detail on the mechanics of sales apportionment, see item 2.4.01 in the 2024 Tax Expenditure Budget.

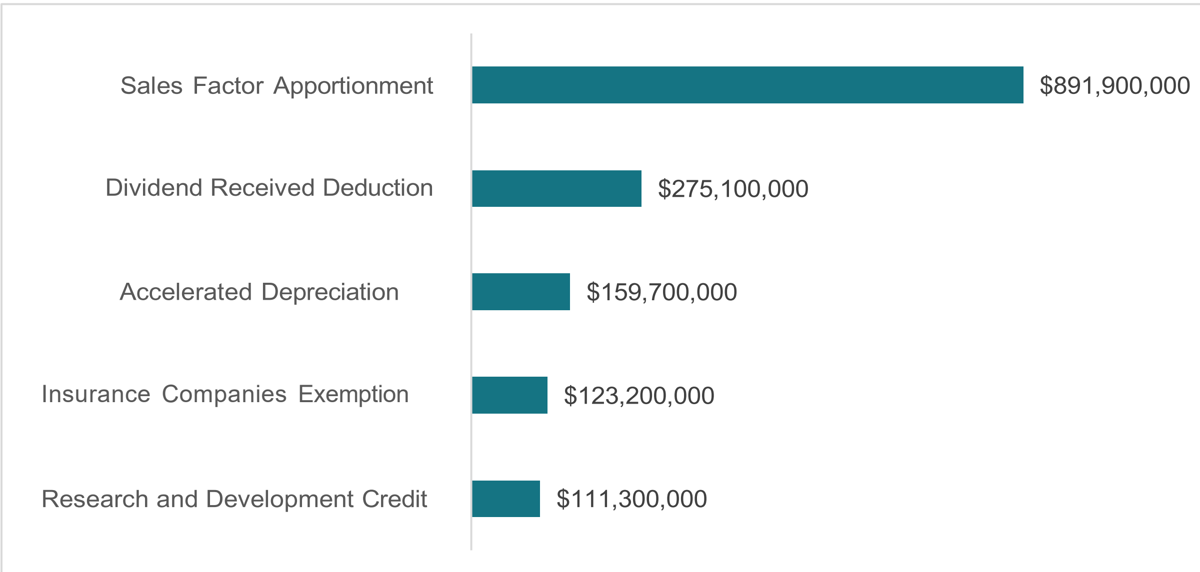
Under Laws of Minnesota 2019, 1st Special Session chapter 6, article 1, the state partially conformed to the Federal Tax Cuts and Jobs Act with respect to base-broadening provisions relating to the business interest deductions, net operating loss limits, and employer deduction limits.

Domestic and international corporations and financial institutions that have a physical or economic presence in the state of Minnesota, bear this tax liability on income that excludes expenses considered to be reasonable and necessary to generate that income.

[3] Loughead, Katherine. State Corporate Income Tax Rates and Brackets, 2024. Tax Foundation. Available at https://taxfoundation.org/data/all/state/state-corporate-income-tax-rates-brackets-2024/

The 2024 Tax Expenditure Budget reports 34 corporate franchise tax expenditures, of which 19 are Federal conformity items. The sum of corporate franchise tax expenditures estimates in fiscal year 2024 is over $1.8 billion. The top five largest corporate franchise tax expenditures by estimated fiscal impact are illustrated in Figure 8.

Figure 8. Top Five Corporate Franchise Tax Expenditures by Dollar Amount in Fiscal Year 2024



Evaluation

As an integral part of the tax system, tax expenditures affect the distribution of income and influence how people and businesses work, save, and invest. Due diligence in evaluation becomes essential to ensure that tax expenditures constitute sound public policy and meet the objectives for which they were created.

The enacting legislation of the Tax Expenditure Review Commission, Minnesota Statutes 2024, section 3.8855, provides the Commission with nine components that must be reviewed under a full analysis. The review components will be prioritized to inform the evaluation design for each tax expenditure. These components are:

(1) provide an estimate of the annual revenue lost as a result of the expenditure;

(2) identify the purpose of the tax expenditure if none was identified in the enacting legislation in accordance with section 3.192;

(3) estimate the measurable impacts and efficiency of the tax expenditure in accomplishing the purpose of the expenditure;

(4) compare the effectiveness of the tax expenditure and a direct expenditure with the same purpose;

(5) identify potential modifications to the tax expenditure to increase its efficiency or effectiveness;

(6) estimate the amount by which the tax rate for the relevant tax could be reduced if the revenue lost due to the tax expenditure were applied to a rate reduction;

(7) if the tax expenditure is a significant tax expenditure, estimate the incidence of the tax expenditure and the effect of the expenditure on the incidence of the state's tax system;

(8) consider the cumulative fiscal impacts of other state and federal taxes providing benefits to taxpayers for similar activities; and

(9) recommend whether the expenditure be continued, repealed, or modified.

In addition to the statutorily required components, there are many resources available to the Commission to guide its approach to tax expenditure evaluation. At the Federal level, the Joint Committee on Taxation and the Congressional Budget Office dedicate considerable resources to analyzing tax expenditures. The Department of Treasury produces research on certain policies; the Internal Revenue Service publishes educational material on available tax expenditures; and the Government Accountability Office published an evaluation framework to assess tax expenditures.

Additionally, many states have established a formal tax expenditure evaluation policy, with more than half of the states having completed evaluations on selected tax expenditures. The state of Minnesota has previously conducted several in-depth analyses on select tax expenditures, such as the Small Business Investment Tax Credit (Angel Tax Credit),[4] the Research Tax Credit,[5] and the Minnesota Historic Rehabilitation Tax Credit.[6] The Office of the Legislative Auditor has been providing valuable insight into the LBO evaluation process. These resources and evaluations provide strong guidance to the Commission as it begins evaluations of all Minnesota's tax expenditures.

In general, an evaluation may consist of a qualitative analysis, such as participant surveys; a quantitative analysis of descriptive statistics; or a more complex econometric analysis in an attempt to find causal relationships between a tax expenditure and achieving its stated objective. The choice among evaluation techniques is subject to the specific question at hand and the availability of information and data.

The LBO has been directed by the Commission to begin evaluating certain tax expenditures. The LBO intends to begin presenting tax expenditure evaluations to the Commission beginning in calendar year 2025.

The LBO is coordinating with executive branch agencies to identify and access relevant data collected and maintained by the state that can be used to assess the impact of these tax expenditures. Partnering agencies include the DOR, the Public Utilities Commission, the Department of Commerce, the Department of Transportation, and the Department of Public Safety.

The LBO looks forward to completing these evaluations and presenting its findings to the Commission. The Commission can choose to consider the findings of these evaluations to inform their recommendations to the legislature to repeal, continue, or modify each tax expenditure.

[4] See 2014 report by Economic Development Research Group, Inc and Karl F. Seidman Consulting Services provided to the Minnesota Department of Revenue. Available at https://www.revenue.state.mn.us/sites/default/files/2014- 02/evaluation_of_the_mn_angel_tax_credit_program.pdf

[5] See 2017 report by the Office of the Legislative Auditor Program Evaluation Division on the Minnesota Research Tax Credit. Available at https://www.auditor.leg.state.mn.us/ped/pedrep/researchcredit.pdf

[6] See 2024 report prepared by the University of Minnesota Extension on behalf of the State Historic Preservation Office at the Minnesota Department of Administration. Available at https://conservancy.umn.edu/items/1d621f65-2fb2-428c-b2a7-951f0c39432f

Appendix A. Glossary

This glossary provides definitions for terms that have been previously defined in Minnesota Statutes, Minnesota DOR published reports, Federal agency reports, or industry reference materials. See references and links to source materials.

Business Tax Credit - A credit against the corporate franchise tax claimed by a C corporation; or a credit against the individual or fiduciary income tax claimed by a pass-through entity that is allocated to its partners, members, or shareholders. Minnesota Statutes 2024, section 270C.11, subdivision 6(1) i, ii.

Deductions - Also called Subtractions for Minnesota tax purposes, are income tax provisions that reduce the amount of individual or business income that is taxable. For examples of Minnesota deductions and subtractions, see Department of Revenue Subtractions and Deductions webpage https://www.revenue.state.mn.us/subtractions-and-deductions.

Effective Tax Rate – A taxpayer's tax liability as a percentage of their taxable income after credits, subtractions and deductions are factored for.

Exclusions - Property tax provisions that lower tax liability by subtracting the amount of the exclusion from the property's estimated market value to arrive at a lower taxable market value. For examples of Minnesota exclusions, see the DOR's Property Tax Program webpage at https://www.revenue.state.mn.us/property-tax- programs.

Normal Tax Base – Also referred to as a reference tax base. "A reference tax system reflects a particular conceptual basis for taxation as well as other features necessary to implement and administer the tax code."
https://www.cbo.gov/publication/57695

Progressive Tax - A tax for which the effective tax rate rises as income rises.
https://www.revenue.state.mn.us/sites/default/files/2024-03/2024-tax-incidence-study-final-online-revision_0.pdf

Regressive Tax - A tax for which the effective tax rate falls as income rises. See 2024 MN Tax Incidence Study.

Significant Tax Expenditure – According to Minnesota Statute, is a tax expenditure, but excluding any tax expenditure that:

(i) is incorporated into state law by reference to a Federal definition of income;
(ii) results in a revenue reduction of less than $10,000,000 per biennium; or
(iii) is a business tax credit;
Minnesota Statutes 2024, section 270C.11, subdivision 6(3) i, ii, iii.

Subtractions - "Allowable deductions to an individuals adjusted gross income. Claiming subtractions reduces your income taxable to Minnesota." For examples of Minnesota deductions and subtractions, see DOR Subtractions and Deductions webpage https://www.revenue.state.mn.us/subtractions-and-deductions.

Tax Credits – A tax provision that directly reduces the amount of tax liability that would otherwise be owed. A *refundable* credit may reduce a tax liability to zero and allow the taxpayer to receive a refund if the credit amount is greater than the tax amount. A *nonrefundable* credit may only reduce a tax liability to zero despite the full value of the credit. For examples of Minnesota tax credits, see the Minnesota DOR's 2024 Tax Expenditure Report available at https://www.revenue.state.mn.us/sites/default/files/2024-11/2024-tax-expenditure-budget-published-version-cover.pdf

Tax Expenditure - A tax provision which provides a gross income definition, deduction, exemption, credit, or rate for certain persons, types of income, transactions, or property that results in reduced tax revenue, but excludes provisions used to mitigate tax pyramiding.
Minnesota Statutes 2024, section 270C.11, subdivision 6(4).

Tax Incidence - "The ultimate burden of the tax after the person or business firm legally obligated to pay the tax alters its behavior in response (if it does alter its behavior). In some cases, namely taxes imposed directly on households, both the impact and the incidence are the same. In other cases, such as taxes on businesses, some or all of the incidence may be shifted from the business to others." For this definition and other tax incidence related terms see the glossary included in the Minnesota DOR’s 2024 Tax Incidence Study available at https://www.revenue.state.mn.us/sites/default/files/2024-03/2024-tax-incidence-study- final-online-revision_0.pdf

Tax Pyramiding - Imposing sales taxes under chapter 297A on intermediate business-to-business transactions rather than sales to final consumers.
Minnesota Statutes 2024, section 270C.11, subdivision 6(6).

Appendix B. TERC Meeting January 25, 2024

Commission Member Attendance

Present	Excused
Sen. Ann H. Rest, Chair	Rep. Greg Davids
Rep. Esther Agbaje, Vice Chair	Rep. Aisha Gomez (ex-officio)
Sen. Steve Drazkowski	Sen. Bill Weber
Rep. Steve Elkins	
Rep. Jim Joy	
Sen. Matt Klein	
Commissioner Paul Marquart	

Meeting Summary

Chair Rest called the hybrid meeting of the Tax Expenditure Review Commission to order, and a quorum was present. The meeting minutes from November 30, 2023, were approved as presented. The Legislative Budget Office (LBO) described the proposed process for evaluating tax expenditures and presented four tax expenditure initial reviews. The four initial reviews included in this appendix are:

- **Marriage Credit** (Minnesota Statutes 2024, section. 290.0675)
- **Employer Transit Pass Credit** (Minnesota Statutes 2024, section 290.06, subdivision 28)
- **Solar Energy System Exemption** (Minnesota Statutes 2024, section 297A.67, subdivision 29)
- **Credit for Small Brewers** (Minnesota Statutes 2024, section 297G.04, subdivision 2)

Seven tax expenditure initial reviews were on the agenda to be presented at this meeting. Chair Rest deferred the remaining tax expenditures on the agenda to the next meeting and asked that there be three additional tax expenditures presented at the next meeting. Chair Rest encouraged members to contact the LBO Director if they have a particular tax expenditure to suggest for the next meeting.

Commission Motions and Actions

No formal motions or official actions were made by the Commission at this meeting. Chair Rest proposed that the Commission take action at the next meeting on the four tax expenditures presented at this meeting.

Commission Revisions to Presented Reviews

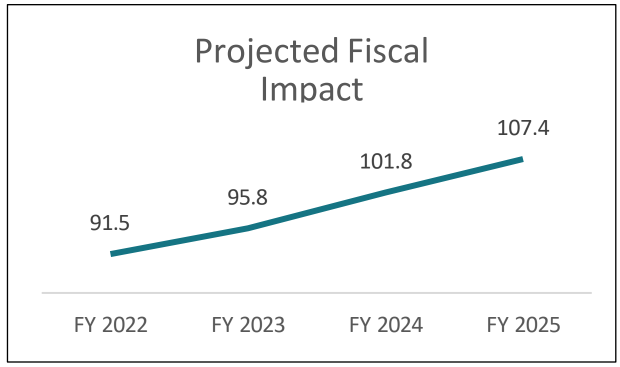
The Commission did not make changes or propose additional considerations to the presented objective of the tax expenditures or potential metrics identified by the LBO.

Marriage Credit

Tax Expenditure Initial Review - TEB 1.84

Tax Expenditure Facts

Year Enacted	1999
Statute	Minnesota Statutes, Section 290.0675
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	$101,800,000 – Fiscal Year 2024
Latest Claims Estimate	433,010 – Tax Year 2021
Expiration Date	None



Tax Expenditure Description

A nonrefundable credit is allowed against the individual income tax for a married couple filing a joint return if both spouses have earned income or taxable pension or taxable social security income and their income situation results in a "marriage penalty" due to the size of the state income tax brackets. The credit compensates for the extent to which the income tax is higher due to the tax brackets for a joint return compared to the two spouses filing as single persons.

The credit is based on two variables: the joint taxable income of the couple and the earned income (including taxable pension and social security income) of the lesser-earning spouse. Beginning in tax year 2022, the credit does not apply unless joint taxable income is at least $44,000 and the earned income of the lesser-earning spouse is at least $28,000.[1]

This credit was enacted in 1999 and was last modified in 2013.

Additional Background Information

Beneficiaries of the tax credit are qualified married joint filers who would otherwise fall into lower income tax brackets had they filed their taxes individually. To determine the credit amount, the qualified taxpayers must complete form 2023 Schedule M1MA, Marriage Credit, in addition to form M1, Individual Income Tax.

The Department of Revenue administers this tax expenditure. The Marriage Credit reduces the amount of income tax revenue that would otherwise be generated. State income tax collections are deposited in the state General Fund, except as provided in the Minnesota Constitution or Minnesota Statutes, section 290.62.

[1] The description of the tax expenditure differs from the 2022 Tax Expenditure Budget published by Department of Revenue to reflect the inflation-adjustment in 2022.

Proposed Tax Expenditure Objective for Consideration

The objective of the marriage credit is to reduce marriage penalties resulting from Minnesota income tax rate brackets for qualified two-earner married couples who file a joint return.

Sources

The proposed objective can be found under the bill summary of H.F. 1998 from the 81st Legislative session (1999 - 2000).[i]

Marriage penalties and bonuses can arise under a progressive rate structure when a couple files their return jointly. Minnesota Marriage Credit was enacted in 1999 to offset the marriage penalties on qualified two-earner married couples without increasing the marriage bonuses.[ii]

Potential Metrics and Performance Measures

A measure of the marriage penalty under Minnesota's income tax structure can be modeled after the methodology proposed in the working paper, "Defining and Measuring Marriage Penalties and Bonuses," published by U.S. Department of Treasury.[iii] The difference between the amount of marriage penalty and eligible marriage penalty credit can be indicative of the effectiveness of this policy. The distributive effect of the effective tax rate and a redistributive equity analysis using the Suits Index can be utilized to assess the equity among the different income groups.

Contact Information and Disclaimer

This tax expenditure review was prepared by the Legislative Budget Office for the Tax Expenditure Review Commission pursuant to Minnesota Statutes 2023, section 3.8855, subdivision 4.

Notice: Proposed tax expenditure objective statements are not binding authority and should not be used as a legal interpretation of any tax expenditure statute.

For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For more information, please visit the [Tax Expenditure Review Commission website](#).

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[i] Rest; Pugh; Dawkins; Winter; Marko. Bill Summary. H. F. 1998. Tax Reduction. Minnesota House Representative. https://www.house.mn.gov/hrd/bs/81/HF1998.pdf.

[ii] Manzi, N and J. Michaels. The Minnesota Income Tax Marriage Credit. Research Department. Minnesota House of Representatives. 2017. https://www.house.mn.gov/hrd/pubs/mrgcred.PDF.

[iii] Bull N, Holtzblatt. J, Nunns J., and R. Rebelein. "Defining and Measuring Marriage Penalties and Bonus." OTA Papers 82-Revised, U.S. Department of the Treasury. 1999. https://home.treasury.gov/system/files/131/WP-82.pdf.

Employer Transit Pass Credit

Tax Expenditure Initial Review - TEB 1.87

Tax Expenditure Facts

Year Enacted	2000
Statute	Minn. Stat. § 290.06, Subd. 28
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	Direct measure is not available
Latest Claims Estimate	Direct measure is not available
Expiration Date	None

Estimated fiscal impact is less than $50,000 per year through Fiscal Year 2025.

Tax Expenditure Description

A nonrefundable credit is allowed against the individual income tax equal to 30 percent of the expense incurred by the taxpayer to provide transit passes to the taxpayer's employees. The transit pass must be for use in Minnesota. If the employer purchases the transit passes from the transit system and resells them to the employees, the expenses used for the credit are the difference between the amount the employer paid for passes and the amount charged to employees.

Approximately 430 returns claimed this credit in tax year 2019.

Additional Background Information

A similar corporate franchise tax credit was enacted in 2000 to offset some of the employer's expense of providing transit passes to their employees (TEB 2.28).

The Employer Transit Pass Credit reduces the amount of individual income tax revenue that would otherwise be generated. Income tax revenue is deposited in the state General Fund. The credit is administered by the Department of Revenue.

Proposed Tax Expenditure Objective for Consideration

The objective of the Employer Transit Pass Credit is to incentivize Minnesota employers to subsidize transit passes for their employees to encourage the use of public transit.

Sources

The proposed objective is based on audio hearings for standalone companion bills pertaining to the Employer Transit Pass Credit for H.F. 723 and S.F. 813 from the 1999 session.[i]

Potential Metrics and Performance Measures

Possible evaluations and measures of this tax credit could include a historical look at utilization trends of the tax credit as well as an analysis of public transportation routes designed to address user demand from employers utilizing the tax credit. Beyond that, survey data from businesses using the tax credit could provide insight into its usefulness and in evaluating its impact in expanding the available labor force or measure possible impacts on employee retention as a result of providing this transportation option for employees.

Other Considerations

Several policy objectives were discussed in testimony or were identified through other sources beyond that stated in the tax expenditure objective. During testimony, it was mentioned that by incentivizing employers to provide transit passes to employees, it could help alleviate traffic congestion, reduce the wear-and-tear on highways and roadways, and address parking scarcity issues in densely populated urban areas. Additionally, it was mentioned that such a tax credit would help connect employers to a broader talent pool of employees, particularly those who desire more economical transportation and parking options.

At the Federal level, Executive Order 13150 mandated that all Federal agencies in the National Capital Region implement a transportation subsidy program by October 1, 2000. The Internal Revenue Service's Public Transportation Subsidy Program was established to encourage employees to use public transportation when commuting to and from work to improve air quality, reduce traffic congestion, and conserve energy by reducing the number of single occupancy vehicles on the road.[ii]

The Commission may want to consider these policy objectives in addition to, or in place of, the proposed tax expenditure objective stated above.

Contact Information and Disclaimer

This tax expenditure review was prepared by the Legislative Budget Office for the Tax and Expenditure Review Commission pursuant to Minnesota Statutes 2023, section 3.8855, subdivision 4.

Notice: Proposed tax expenditure objective statements are not binding authority and should not be used as a legal interpretation of any tax expenditure statute.

For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For information on the Tax Expenditure Review Commission, please visit https://www.lbo.mn.gov/TERC/index.html.

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[i] Minn. H., Hearing on H.F. 723 before the H. Comm. on Taxes, 81st Minn. Leg., Reg. Sess. (Mar. 23, 1999), available at https://www.lrl.mn.gov/media/file?mtgid=811061; Minn. Sen., Hearing on S.F. 813 before the Sen. Comm. on Taxes, 81st Minn. Leg., Reg. Sess. (Mar. 29, 1999), available at: https://www.lrl.mn.gov/media/file?mtgid=811202.

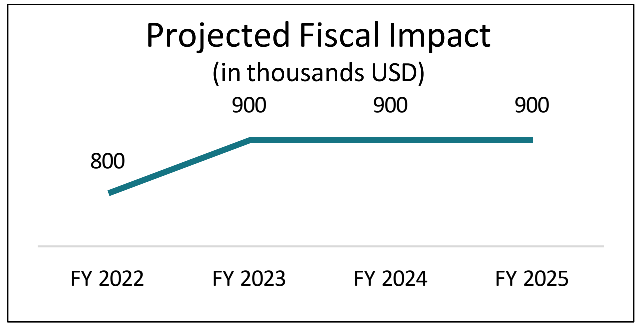
[ii] Treasury Inspector General for Tax Administration. (2008). Review of the Internal Revenue Service's Public Transportation Subsidy Program. Washington D.C.: Department of the Treasury. Available at https://www.treasury.gov/tigta/auditreports/2018reports/201810033fr.pdf.

Employer Transit Pass Credit

Tax Expenditure Initial Review - TEB 2.28

Tax Expenditure Facts

Year Enacted	2000
Statute	Minn. Stat. § 290.06, Subd. 28
Tax Type	Corporate Franchise Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	$900,000 – Fiscal Year 2024
Latest Claims Estimate	Direct measure of this estimates is not available
Expiration Date	None



Tax Expenditure Description

A nonrefundable credit is allowed against the corporate franchise tax equal to 30 percent of the expense incurred by the taxpayer to provide transit passes to the taxpayer's employees. The transit pass must be for use in Minnesota. If the employer purchases the transit passes from the transit system and resells them to the employees, the expenses used for the credit are the difference between the amount the employer paid for passes and the amount charged to employees.

Proposed Tax Expenditure Objective for Consideration

The objective of the Employer Transit Pass Credit is to incentivize Minnesota employers to subsidize transit passes for their employees to encourage the use of public transit.

Sources

The tax expenditure objective is based upon audio hearings for standalone companion bills pertaining to the Employer Transit Pass Credit for HF723[i] and SF813[ii] from the 1999 session.

Other Considerations Regarding the Proposed Tax Expenditure for Consideration

Several policy objectives were discussed in testimony or were identified through other sources beyond that stated in the tax expenditure objective. During testimony, it was mentioned that by incentivizing employers to provide transit passes to employees, that could help alleviate traffic congestion, reduce the need for or reduce the wear-and-tear on highways and roadways, and address parking scarcity issues in densely populated urban areas.

Additionally, it was mentioned that such a tax credit would help connect employers to a broader talent pool of employees, particularly those who desire more economical transportation and parking options.

At the Federal level, Executive Order 13150, mandated that all Federal agencies in the National Capital Region implement a transportation subsidy program by October 1, 2000. The Internal Revenue Service's (IRS) Public Transportation Subsidy Program (PTSP) was established to encourage employees to use public transportation when commuting to and from work to improve air quality, reduce traffic congestion, and conserve energy by reducing the number of single occupancy vehicles on the road.[iii]

The Commission may want to consider these policy objectives in addition to or in place of the proposed tax expenditure objective stated above.

Potential Metrics and Performance Measures

Possible evaluations and measures of this tax credit could include a historical look at utilization trends of the tax credit as well as an analysis of public transportation routes designed to address user demand from employers utilizing the tax credit. Beyond that, survey data from businesses using the tax credit could provide insight into its usefulness and in evaluating its impact in expanding the available labor force or measure possible impacts on employee retention as a result of providing this transportation option for employees.

Contact Information and Disclaimer

This tax expenditure review was prepared by the Legislative Budget Office for the Tax and Expenditure Review Commission pursuant to Minnesota Statute 3.8855.

Notice: Proposed tax expenditure objective statements are not binding authority and should not be used as a legal interpretation of any tax expenditure statute.

For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For information on the Tax Expenditure Review Commission, please visit https://www.lbo.mn.gov/TERC/index.html.

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[i] Minn. H., Hearing on H.F. 723 before the H. Comm. on Taxes, 81st Minn. Leg., Reg. Sess. (Mar. 23, 1999), available at https://www.lrl.mn.gov/media/file?mtgid=811061

[ii] Minn. Sen., Hearing on S.F. 813 before the Sen. Comm. on Taxes, 81st Minn. Leg., Reg. Sess. (Mar. 29, 1999), available at: https://www.lrl.mn.gov/media/file?mtgid=811202

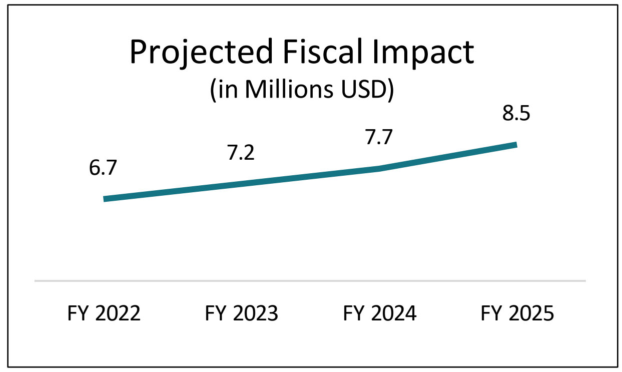
[iii] Treasury Inspector General for Tax Administration. (2008). Review of the Internal Revenue Service's Public Transportation Subsidy Program. Washington D.C.: Department of the Treasury. Available at https://www.treasury.gov/tigta/auditreports/2018reports/201810033fr.pdf

Solar Energy Systems

Tax Expenditure Initial Review - TEB 4.27

Tax Expenditure Facts

Year Enacted	2005
Statute	Minn. Stat. § 297A.67, Subd. 29
Tax Type	General Sales and Use Tax
Provision Type	Exemption - Particular Goods and Services
Latest Fiscal Impact Estimate	$7,700,000 – Fiscal Year 2024
Latest Claims Estimate	Direct measure of this estimate not available
Expiration Date	None



Tax Expenditure Description

Solar energy systems are exempt from the sales and use tax. A solar energy system is a set of devices whose primary purpose is to collect solar energy and convert and store it for useful purposes including heating and cooling buildings or other energy-using processes, or to produce generated power by means of collecting, transferring, or converting solar-generated energy.

Additional Background Information

Individual components of a solar energy system are covered under this expenditure. A solar energy system generally includes solar thermal electric and solar photovoltaic technologies. A similar sales tax exemption for photovoltaic devices was enacted in 2001 and expired in 2005.[i]

Beneficiaries of the exemption on solar energy systems include all taxpayers who purchase a solar energy system, or components to solar energy system. This exemption reduces the amount of sales and use tax revenue that would otherwise be generated. General sales and use tax collections are deposited in the state General Fund except as provided in the Minnesota Constitution or Statutes 297A.94. This exemption is administered by the Department of Revenue.

Proposed Tax Expenditure Objective for Consideration

The objective of the solar energy systems general sales and use tax exemption is to incentivize and promote the implementation and utilization of solar energy systems in the state of Minnesota to achieve a greater percentage of renewable energy contributions to the state's electricity fuel generation mix.

Sources

An explicit tax expenditure objective was not identified in the legislative record.

The goals and benchmarks under Minnesota Statute 216B.1691 for renewable energy standards were considered to develop an objective for this tax expenditure. Per MS 216B.1691, subd. 2f, by 2020 at least 1.5 percent of retail electric sales to retail customers must be generated by solar energy. The statute establishes a goal that by 2030, 10 percent of retail electric sales must be generated by solar energy. The use of tax incentives is one of several state efforts to promote renewable energies. Other efforts focus on increasing supply, supporting demand, funding the development of supporting infrastructure, and funding research. Minnesota's legislative efforts in these areas are further summarized by the Minnesota House Research Department's 2005 Short Subjects brief, Minnesota Statutes Promoting Renewable Sources of Electricity.[ii]

Nineteen separate states and U.S. territories have implemented a sales tax exemption to promote the use of solar energy across residential use, commercial use, and utility providers.[iii] This includes the states bordering Minnesota. At the Federal level, a nonrefundable tax credit is available for homeowners that install certain energy efficient technologies.

Potential Metrics and Performance Measures

An analysis of the program's participation by submission of exemption certificates may identify trends in uptake of the tax incentive.[iv]

A review of the state's solar capacity over time categorized by sector contribution (residential, commercial, community, and utility) may identify increases in implementation of solar energy systems. An analysis of the geographical distribution of solar energy systems throughout the state may indicate variance in the utilization of solar energy systems by region.

A review of solar energy projects permitted by the Minnesota Department of Commerce may provide further insights into trends in solar energy implementation and utilization.

A comprehensive report to analyze the state's solar potential was prepared for the Department of Commerce and The Minnesota Solar Pathways Project in 2018.[v] This report may be referenced to consider alternatives to assess the state's solar potential and the relationship to the solar energy systems tax exemption.

Contact Information and Disclaimer

This tax expenditure review was prepared by the Legislative Budget Office for the Tax Expenditure Review Commission pursuant to Minnesota Statute 3.8855.

Notice: Proposed tax expenditure objective statements are not binding authority and should not be used as a legal interpretation of any tax expenditure statute.

For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For more information, please visit the Tax Expenditure Review Commission website.

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[i] Laws of Minnesota 2001, chapter 5, article 12, section 44.

[ii] Elef, B. (2005, December). Minnesota Statutes Renewable Sources of Electricity. St. Paul: Research Department of the Minnesota House of Representatives, https://www.house.leg.state.mn.us/hrd/pubs/ss/ssrnegst.pdf.

[iii] Programs. (2022, September). Retrieved from Database of State Incentives for Renewables and Efficiency (DSIRE): https://programs.dsireusa.org/system/program.

[iv] Minnesota Department of Revenue. (2019, July). Form ST3, Certificate of Exemption.

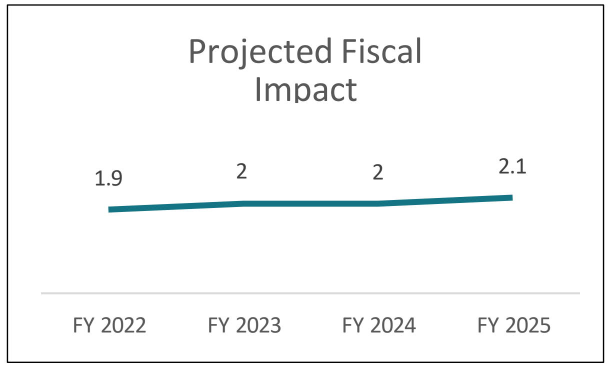
[v] Putnam, M; Perez, M. (2018). Solar Potential Analysis Report. Napa: Clean Power Research.

Credit for Small Brewers

Tax Expenditure Initial Review - TEB 7.07

Tax Expenditure Facts

Year Enacted	1985
Statute	Minn. Stat. § 297G.04, subd. 2
Tax Type	Alcoholic Beverages Taxes
Provision Type	Credit
Latest Fiscal Impact Estimate	$2,000,000 – Fiscal Year 2024
Latest Claims Estimate	Latest figure of claims filed is not available
Expiration Date	None



Tax Expenditure Description

A credit is allowed to a brewer who manufactures less than 250,000 barrels of beer in the calendar year preceding the year for which the credit is claimed. The credit is $4.60 per barrel on 25,000 barrels sold in a fiscal year, with a maximum credit of the lesser of the brewer's tax liability or $115,000.

Additional Background Information

Beneficiaries of this tax exemption include in-state and out-of-state brewers who produced less than 250,000 barrels of fermented malt beverages in the previous calendar year and sell beer in Minnesota. The exemption is administered by the Department of Revenue and the Department of Public Safety. The Credit for Small Brewers reduces the amount of excise tax revenue that would otherwise be generated. State alcohol excise tax collections are deposited in the state General Fund except as provided in the Minnesota Constitution or Statutes 297G.10.

Proposed Tax Expenditure Objective for Consideration

The objective of the credit for small brewers is to promote development and survivorship among small brewers.

Sources

An explicit tax expenditure objective was not identified in the legislative record.

Other states, including New York, Washington, and Wisconsin, provide a similar tax incentive to small brewers as defined by each respective state. The New York Alcohol Beverage Production Credit was enacted in 2012 to offset the excise taxes paid by in-state producers.[i] The Washington Legislative Auditor inferred the objective of the state's microbrewery exemption was to provide tax relief to in-state breweries as the industry develops.[ii] Most similar in policy design to Minnesota's tax expenditure is Wisconsin's Tax Credit to Eligible Producers. The enacting language of this tax credit stated that the legislation was enacted "to encourage and preserve a competitive market in the brewing industry."[iii]

At the Federal level, a rate reduction was passed in 2017 under the Tax Cuts and Jobs Act, cutting the excise tax rate in half on the first 60,000 barrels produced by a domestic brewer who produces no more than 2,000,000 barrels in total per calendar year.[iv] The rate reduction was made permanent under the Taxpayer Certainty and Disaster Tax Act of 2020, which was written into the 2021 Consolidated Appropriations Act.[v]

A similar credit is provided by Minnesota to microdistilleries. The legislative record on that policy was considered in drafting this proposed objective.

Other Considerations Regarding Proposed Tax Expenditure Objective

As of March 29, 2023, there were 190 microbreweries, 12 small breweries, and 70 brew pubs licensed by the Minnesota Department of Public Safety. A brewery license designation is determined by production limits. Microbreweries are limited to 2,000 barrels of production annually. Small breweries and brew pubs are limited to 3,500 barrels of production annually. A Minnesota brewery producing over 3,500 barrels annually is considered a large brewer for the purpose of licensure. All license designations are eligible for the credit for small brewers.[vi]

Potential Metrics and Performance Measures

The following are evaluation considerations with respect to administrative and enforcement actions.

Performance measurement: Statistical analysis of claims to assess counts, regional distribution, and trends in claims over time.

Performance attribution: Calculate the effective tax rate and differential as a result of the tax credit. Financial analysis of participating brewers to assess free cash flow trends.

Performance appraisal: Conduct an operating ratio analysis to understand the impact of the tax credit on a producer's budgetary solvency. Assess whether budgetary solvency has improved over time as a result of the tax credit.

Contact Information and Disclaimer

This tax expenditure review was prepared by the Legislative Budget Office for the Tax Expenditure Review Commission pursuant to Minnesota Statutes 2023, section 3.8855, subdivision 4.

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For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For more information, please visit the [Tax Expenditure Review Commission website].

[i] Mark A. Nickerson; Linda Hall. "New York Pours Tax Incentives in the Craft Brewing Industry," *The CPA Journal*, October 2017, 28. https://www.cpajournal.com/2018/11/22/icymi-new-york-pours-tax-incentives-into-the-craft-brewing-industry/

[ii] Washington Joint Legislative Audit and Review Committee. 20-07 Final Report: 2020 Tax Preference Performance Reviews Microbrewers. December 2020. Accessed on 01/31/2023. https://leg.wa.gov/jlarc/taxReports/2020/microbrewers/f_final/default.html

[iii] Laws of Wisconsin 1973, Chapter 256.

[iv] Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat 2170.

[v] "Tax Reform – Craft Beverage Modernization Act (CBMA) Notice," Alcohol and Tobacco Tax and Trade Bureau, accessed on March 16, 2023, https://www.ttb.gov/alcohol/craft-beverage-modernization-and-tax-reform-cbmtra.

[vi] Licensure counts were provided by the Minnesota Department of Public Safety Alcohol and Gambling Enforcement Division on March 29, 2023.

Appendix C. TERC Meeting March 15, 2024

Commission Member Attendance

Present

Sen. Ann H. Rest, Chair

Rep. Esther Agbaje, Vice Chair

Rep. Greg Davids

Rep. Steve Elkins

Rep. Jim Joy

Sen. Matt Klein

Paul Marquart, Commissioner

Excused

Sen. Steve Drazkowski

Rep. Aisha Gomez (ex-officio)

Sen. Bill Weber

Meeting Summary

Chair Rest called the hybrid meeting of the Tax Expenditure Review Commission (TERC) to order, and a quorum was present. The meeting minutes from January 25, 2024, were approved as presented. The Legislative Budget Office (LBO) presented five tax expenditure initial reviews for the Commission's consideration. The five initial reviews included in this appendix are:

- **Open Space Property** (Minnesota Statutes 2024, section. 273.112)
- **Data Center Equipment** (Minnesota Statutes 2024, section 297A.68, subdivision 42)
- **Wind Energy Conversion Systems Exemption** (Minnesota Statutes 2024, 297A.68, subdivision 12)
- **Microdistillery Credit** (Minnesota Statutes 2024, 297G.03, subdivision 5)
- **Small Winery Credit** (Minnesota Statutes 2024, 297G.03, subdivision 6)

Two of these initial reviews, Open Space Property and Data Center Equipment, were left over from the January 25, 2024, meeting agenda. All five reviews from this meeting's agenda were presented at this meeting.

Vice Chair Agbaje suggested three initial reviews for the LBO to bring to the next meeting: Angel Investment Credit, First-Time Homebuyer Account, and Home Mortgage Interest.

Commission Motions and Actions

Vice Chair Agbaje moved to adopt the five initial reviews presented at this meeting as well as the four initial reviews presented at the January 25, 2024, meeting, and for the LBO to proceed with evaluations of these nine initial reviews. The motion prevailed.

Commission Revisions to Presented Reviews

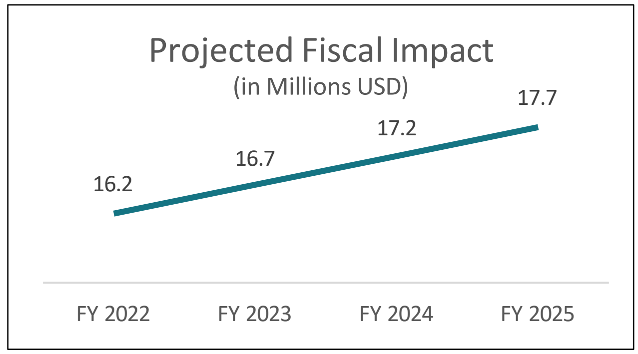
The Commission did not make changes or propose additional considerations to the presented objective of the tax expenditures or potential metrics identified by the LBO.

Open Space Property

Tax Expenditure Initial Review - TEB 13.06

Tax Expenditure Facts

Year Enacted	1969
Statute	Minn. Stat. § 273.112
Tax Type	Property Tax
Provision Type	Preferential Computation
Shift in Tax Burden	$17,200,000 – Fiscal Year 2024
Latest Claims Estimate	~240 parcels – Tax Year 2021
Expiration Date	None



Tax Expenditure Description

Private recreational, social, open space, and park land is given preferential valuation and tax deferral as long as it meets certain criteria.[i] For property tax purposes, the property is valued at its current use rather than at a higher value that would reflect its potential use. Qualifying property includes golf courses, ski areas, and archery and firearms ranges. When the open space property no longer qualifies for preferential valuation, taxes are due equal to the amount by which the preferential valuation reduced the tax for the previous seven years.

The Minnesota Open Space Property Tax Law was enacted in 1969. Several changes have been made since enactment, and this provision was last modified in 2005.

Approximately 240 parcels received preferential valuation under this provision in 2021.

Additional Background Information

Deferral programs value and tax property based on its current use, not the amount the property would likely sell for on the open market. For example, property in the open space program used as a golf course but highly desirable for residential development is valued based solely on its use as a golf course, not based on the substantially higher value it would command if sold to a land developer for its highest-and-best (residential in this example) use.[ii] Thus, property in the open space program has a lower taxable value and subsequent tax liability than would otherwise prevail under normal assessment and valuation practices.[iii] Taxable values and class rates determine how property tax burdens are distributed amongst properties in a particular taxing jurisdiction.[iv]

The open space program is administered by local assessors and county auditors. The assessor calculates two values for open space properties, an estimated market value (EMV) based on highest-and-best use, and a taxable market value (TMV) based on current use. The auditor calculates tax liability on both amounts, and the difference between tax liability based on EMV and tax liability based on TMV is deferred so long as the property meets open space requirements. When the property is no longer eligible for open space deferral the owner must pay back the amount of property tax deferred for the current year and six preceding years.[v]

Program beneficiaries include owners of qualifying private recreational, social, open space, or park land. Property in the open space program contributes a smaller amount to the tax base, requiring a higher local tax rate to produce the same levy amount. This dynamic effectively shifts a portion of the property tax burden from qualifying to non-qualifying properties in the unique taxing area. Tax shifting can occur when one or both elements of property tax capacity – taxable market value and classification rate – change due to market trends, legislative actions, reassessments, property improvements, use changes, or provisions such as open space.

Proposed Tax Expenditure Objective for Consideration

The open space property tax law is intended to encourage the preservation and development of private outdoor, recreational, open space and park land which would otherwise not occur or have to be provided by governmental authority.

Sources

The proposed objective is based on the policy statement included in Minnesota Statutes 273.112:

> "*The present general system of ad valorem property taxation in the state of Minnesota does not provide an equitable basis for the taxation of certain private outdoor recreational, open space and park land property and has resulted in excessive taxes on some of these lands. Therefore, it is hereby declared that the public policy of this state would be best served by equalizing tax burdens upon private outdoor, recreational, open space and park land within this state through appropriate taxing measures to encourage private development of these lands which would otherwise not occur or have to be provided by governmental authority*."[vi]

Potential Metrics and Performance Measures

Publicly available parcel level data can be used to measure:

- The longevity of properties in the open space program
- Deferment value over time
- Open space property use and geographical distribution
- The amount of open space property over time

How many open space properties are used for golf, skiing, archery, or other qualifying uses but for the preferential valuation and deferment? A full evaluation may survey or partner with owners of open space property to estimate the effect of open space provisions on the supply of private outdoor recreational lands.

Contact Information and Disclaimer

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For more information, please visit the Tax Expenditure Review Commission website.

[i] Minnesota Statutes 2023, section 273.112, subdivision 3 lists specific ownership, use, and non-discrimination requirements.

[ii] "Highest-and-best use" – the use that provides the highest return to the land – is a common appraisal concept used to estimate the market value of a property. Highest-and-best use depends on several factors including but not limited to zoning, use of surrounding properties, market pressures, location, local building codes, and accessibility. The use must be physically possible, legally permissible, financially feasible, and maximally productive. For a brief discussion of highest-and-best use, see Minnesota Department of Revenue, *Minnesota Property Tax Administrator's Manual* (July 2023), 66, https://www.revenue.state.mn.us/sites/default/files/2023-09/combined-module.pdf.

[iii] Minnesota Department of Revenue, *Auditor Treasurer Manual* (August 2021), 51-52, 76-77, https://www.revenue.state.mn.us/sites/default/files/2021-08/Auditor-Treasurer%20Manual%20-%20August%202021.pdf. A useful comparison of special valuation and deferral programs can be found on page 59.

[iv] For a brief overview of property taxes in Minnesota, see Jared Swanson, et. al., *Overview of Property Taxes: A Presentation to the Property and Local Tax Division* (Minnesota House Research and Fiscal Analysis Departments, January 2023), https://www.house.mn.gov/hrd/issinfo/2023PTHandout.pdf. Minnesota House Research also provides a useful summary of property tax terms available at https://www.house.mn.gov/hrd/pubs/ss/ssptterm.pdf.

[v] *Minnesota Property Tax Administrator's Manual*,142.

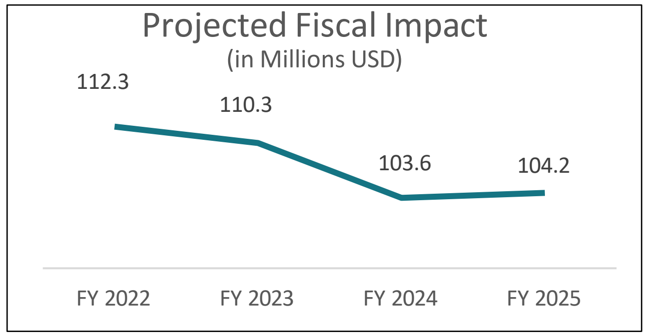
[vi] Minnesota Statutes 2023, section 273.112, subdivision 2, https://www.revisor.mn.gov/statutes/cite/273.112#stat.273.112.2.

Data Center Equipment

Tax Expenditure Initial Review - TEB 4.72

Tax Expenditure Facts

Year Enacted	2011
Statute	Minn. Stat. § 297A.68, subd. 42
Tax Type	General Sales and Use Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	$103.6 million – Fiscal Year 2024
Latest Claims Estimate	41 Qualified Data Centers as of January 2024
Expiration Date	July 1, 2042



Tax Expenditure Description

Enterprise information technology equipment and computer software for use in a qualified data center are exempt from the sales and use tax. Electricity used or consumed in the operation of a qualified data center is also exempt.

To qualify, a data center must:

- Be comprised of one or more buildings consisting of at least 25,000 square feet.
- Must have a total cost of construction or refurbishment, investment in enterprise information technology equipment, and computer software of at least $30 million within a 48-month period. For a refurbished data center, the investment must be at least $50 million within a 48-month period.
- The facility that houses the enterprise technology equipment must have uninterruptible power supplies, generator backup power, or both sophisticated fire suppression and prevention systems, and enhanced security, as specified.

The exemption applies to purchases made within twenty years of the first qualifying purchase. The exemption is administered as a refund.

This exemption was enacted in 2011, effective for sales and purchases made from July 1, 2012, through June 30, 2042. The requirements were modified in 2013.

Additional Background Information

A data center can generally be understood as a “facility that houses information technology infrastructure for building, running, and delivering applications and services, and for storing and managing the data associated with those applications and services.”[i]

Data center construction or refurbishment projects must be certified by the Minnesota Department of Employment and Economic Development (DEED) to qualify for the exemptions.[ii] Sales tax is paid on qualifying equipment and software at the time of purchase then refunded by the Department of Revenue (DOR) by completing form ST11, Sales and Use Tax Refund Request.[iii] Electricity used or consumed in the operation of a qualified facility is exempt upon submittal of a blanket exemption certificate (Form ST3) to the local utility provider. A qualified data center may include one or more businesses operating enterprise information technology equipment as co-owners or tenants of the building or buildings that constitute the facility.[iv]

Beneficiaries of data center sales tax exemptions include owners and tenants of qualifying data center facilities. There are currently 15 qualified data centers certified as new construction projects and 26 qualified data centers certified as refurbishment projects.[v] Thirty-five qualified data centers are located in the seven-county metropolitan area, and six qualified data centers are located in greater Minnesota.

Qualified data center exemptions reduce the amount of sales and use tax revenue that would otherwise be generated. State general sales and use tax collections are deposited in the state General Fund, except as provided by the Minnesota Constitution or Statutes 297A.94.

Proposed Tax Expenditure Objective for Consideration

The objective of qualified data center sales and use tax exemptions is to create jobs in the construction and data center industries.

Sources

The proposed objective is based the statement of purpose specified in Minnesota Statutes 297A.68, subdivision 42(g).

Potential Metrics and Performance Measures

A full review may use data collected by DEED during the certification process, sales tax refund data collected by DOR, or a survey of qualifying data centers to estimate:

- The number and value of exemptions claimed by type (equipment, software, or utility exemptions)
- The number of new or refurbished construction projects undertaken but for the exemptions
- The number of new jobs created but for the exemptions
- Direct, indirect, and induced economic impacts
- Cost to administer the program
- The longevity of qualified data centers

Other Considerations

Currently 32 states offer tax incentives to attract or expand data centers. Sales tax exemptions are the most common incentive type, but qualifications, thresholds, and exempt items or services vary by state.[vi]

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For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For more information, please visit the [Tax Expenditure Review Commission website](#).

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[i] "What is a data center?" IBM website, accessed January 22, 2024, https://www.ibm.com/topics/data-centers.

[ii] "Data Center Sales Tax Incentives," Minnesota Department of Employment and Economic Development website, accessed January 22, 2024, https://mn.gov/deed/business/financing-business/tax-credits/data-center-credit/. The DEED program guide and application can be found at https://mn.gov/deed/assets/data-center-application-master_tcm1045-309365.pdf.

[iii] Page 3 of Instructions for Form ST11, Sales and Use Tax Refund Request, includes a description and example of documentation the purchaser must submit with their refund application. https://www.revenue.state.mn.us/sites/default/files/2021-03/st11_0.pdf.

[iv] "Qualified Data Centers," Minnesota Department of Revenue Website, last updated November 13, 2020, https://www.revenue.state.mn.us/qualified-data-centers; Minnesota Department of Revenue, "Revenue Notice #16-07: Sales and Use Tax Exemptions – Qualified Data Centers (October 10, 2016), https://www.revenue.state.mn.us/revenue-notice/16-07-sales-and-use-tax-exemptions-qualified-data-centers-revocation-revenue-notice.

[v] A list of data center projects can be found at https://mn.gov/deed/assets/data-center-project-list_tcm1045-531119.pdf.

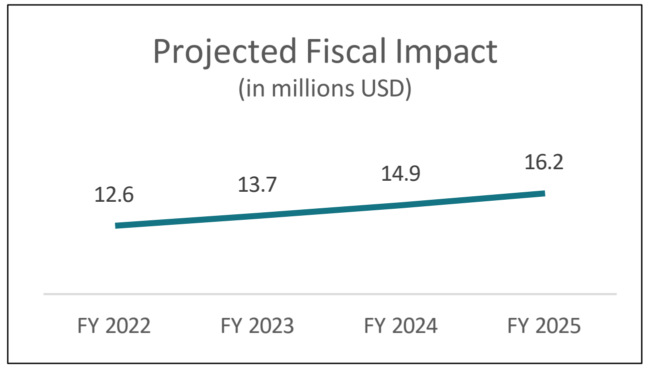
[vi] Scott Wright, Alla Raykin, and Laurin E. McDonald, "Tricks and Traps of Data Center State Tax Incentives," *Tax Notes State* 111 (January 2024):17-38, https://www.taxnotes.com/special-reports/tax-technology/tricks-and-traps-data-center-state-tax-incentives/2023/12/28/7hmb7. The article includes a table listing data center incentives by state with legal references.

Wind Energy Conversion Systems

Tax Expenditure Initial Review - TEB 4.26

Tax Expenditure Facts

Year Enacted	1992
Statute	Minn. Stat. § 297A.68, subd. 12
Tax Type	General Sales and Use Tax
Provision Type	Exemption - Particular Goods and Services
Latest Fiscal Impact Estimate	$14,900,000 – Fiscal Year 2024
Latest Claims Estimate	Direct measure of this estimate is not currently available
Expiration Date	None



Tax Expenditure Description

Wind energy conversion systems and the materials used to manufacture, install, construct, repair, or replace them are exempt from the sales and use tax if the systems are used as an electric power source. Wind energy conversion systems include any device which converts wind energy to a form of usable energy, such as a wind charger, windmill, or wind turbine. The estimates do not include purchases that would also qualify as capital equipment (Item 4.19).

This exemption was first enacted in 1992, and expired June 30, 1996. In 1997, it was re-enacted for one year. The exemption was made permanent in 1998.

Additional Background Information

Beneficiaries of the tax exemption include wind energy producers and all taxpayers that purchase a wind energy conversion system. To claim the exemption, buyers must complete an exemption certificate and supply it to the equipment seller.[i] This exemption is administered by the Department of Revenue. This exemption reduces the amount of sales and use tax revenue that would otherwise be generated. General sales and use tax collections are deposited in the state General Fund except as provided in the Minnesota Constitution or Statutes 297A.94.

Proposed Tax Expenditure Objective for Consideration

The objective of the wind energy conversion general sales and use tax exemption is to incentivize and promote the implementation and utilization of wind energy systems in Minnesota. The exemption is meant to achieve a greater percentage of renewable energy contributions to the state's electricity fuel generation mix.

Sources

An explicit tax expenditure objective was not identified in the legislative record.

The proposed objective is informed by legislative discussion to a property tax exemption for wind energy production introduced under HF1185 and SF1112 during the 1991 Regular Session. In the April 10, 1991, House Energy Committee, the bill's author noted the goal of the legislation was to change some of the ways energy is used and to make renewable energy a more attractive industry for producers.[ii] The property tax exemption on wind energy systems is separate from the sales and use tax exemption of this review.

Per the House Taxes Committee meeting held on May 15, 1991, a similar exemption existed in the 1980s relating to wind energy generating systems where the market value of equipment was exempt from the valuation of property.[iii] The law referenced was enacted in 1978 and expired in 1984.[iv] With a renewed interest in exploring renewable sources of energy, HF1185 renewed the exemption to include new wind generators.

The state's renewable energy standards as stated in Minnesota Statutes, section 216B.1691 were also considered in developing the proposed objective. More information on Minnesota's efforts to promote renewable energy sources is described in the Minnesota House Research Department's 2005 Short Subjects brief, Minnesota Statutes Promoting Renewable Sources of Electricity.[v]

Potential Metrics and Performance Measures

An analysis of the program's participation by submission of exemption certificates may identify trends in uptake of the tax incentive.

A review of the state's wind capacity over time may identify increases in implementation of wind energy systems.

An analysis of the geographical distribution of wind energy systems throughout the state can indicate variance in the utilization of wind energy systems by region.

A review of wind energy projects permitted by the Minnesota Public Utilities Commission may provide further insights into trends in wind energy implementation and utilization despite the fact that those projects are likely to qualify under the capital equipment exemption (4.19).

A technical report that analyzed Minnesota's economic potential for distributed wind was prepared by the National Renewable Energy Laboratory in 2018.[vi] This report may be referenced to consider alternatives to assess Minnesota's wind potential based on production and consumption levels.

Contact Information and Disclaimer

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For questions regarding this review, please contact the Legislative Budget Office at 651-297-7146 or lbo@lbo.mn.gov.

For more information, please visit the Tax Expenditure Review Commission website.

[i] Minnesota Department of Revenue. (2019, July). Form ST3, Certificate of Exemption.

[ii] Minn. H., Hearing on H.F. 1185 before the H. Comm. on Energy, 77th Minn. Leg., Reg. Sess. (April 10, 1991), available at: https://www.lrl.mn.gov/media/file?mtgid=771367.

[iii] Minn. H., Hearing on H.F. 1185 before the H. Comm. on Taxes, 77th Minn. Leg., Reg. Sess. (May 15, 1991), available at: https://www.lrl.mn.gov/media/file?mtgid=771801.

[iv] Laws of Minnesota 1978, chapter 786, sections 10 and 11.

[v] Elef, B. (2005, December). Minnesota Statutes Renewable Sources of Electricity. St. Paul: Research Department of the Minnesota House of Representatives, https://www.house.leg.state.mn.us/hrd/pubs/ss/ssrnegst.pdf.

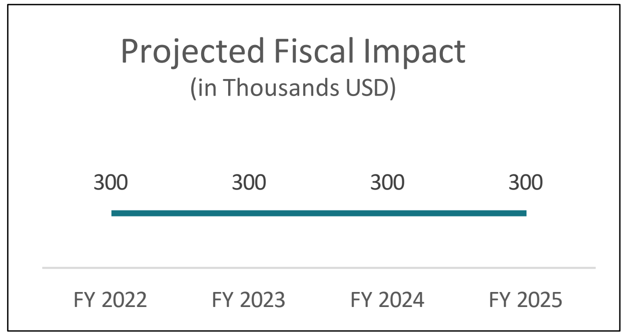
[vi] McCabe, Kevin, Sigrin, Benjamin O., Lantz, Eric J., and Mooney, Meghan E. 2018. "Assessment of the Economic Potential of Distributed Wind in Colorado, Minnesota, and New York." https://doi.org/10.2172/1419628.

Microdistillery Credit

Tax Expenditure Initial Review - TEB 7.08

Tax Expenditure Facts

Year Enacted	2014
Statute	Minn. Stat. § 297G.03, subd. 5
Tax Type	Alcoholic Beverages Taxes
Provision Type	Credits
Latest Fiscal Impact Estimate	$300,000 – Fiscal Year 2024
Latest Claims Estimate	Latest figure of claims filed is not available
Expiration Date	None



Tax Expenditure Description

A microdistillery, operating in the state, producing less than 40,000 proof gallons of premium distilled spirits, is allowed a credit of $1.33 per liter on 100,000 liters sold to consumers at retail per fiscal year. The total credit allowed may not exceed the lesser of the tax liability or $133,000.

The exemption was enacted in 2014.

In fiscal year 2020, 35 microdistilleries claimed this credit.

Additional Background Information

Beneficiaries of the tax exemption include in-state microdistilleries that meet specific production requirements. This exemption is administered by the Department of Revenue and the Department of Public Safety. The Microdistillery Credit reduces the amount of excise tax revenue that would otherwise be generated. State alcohol excise tax collections are deposited in the state General Fund except as provided in the Minnesota Constitution or Statutes 297G.10.

Proposed Tax Expenditure Objective for Consideration

The objective of the microdistillery credit is to promote development and survivorship of small producers in the craft distillery market.

Sources

The language for the tax credit was introduced under HF1826 during the 2013 Regular Session. Discussion to the tax credit, in a 2014 House Tax Committee hearing, compares the tax credit's function to that of the small brewer's credit, "to provide space through the tax code for small brewers to develop."[i]

A purpose statement for this policy was included in the third engrossment of the 2014 omnibus supplemental tax bill (H.F. 3167-3E). Most recently, similar language was included in the second engrossment of H.F. 991 in the 2021 Regular Session, proposing to retroactively introduce a purpose statement. The objective statement proposed in this review expands on the language found in these previously introduced bills.

Surrounding states do not have a similar tax credit.

Potential Metrics and Performance Measures

The following are evaluation considerations with respect to administrative and enforcement actions.

Performance measurement: Statistical analysis of claims to assess counts, regional distribution, and trends in claims over time.

Performance attribution: Calculate the effective tax rate and differential as a result of the tax credit. Perform a financial analysis of participating distillers to assess free cash flow trends.

Performance appraisal: Conduct an operating ratio analysis to understand the impact of the tax credit on a producer's budgetary solvency. Assess whether budgetary solvency has improved over time as a result of the tax credit.

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For more information, please visit the Tax Expenditure Review Commission website.

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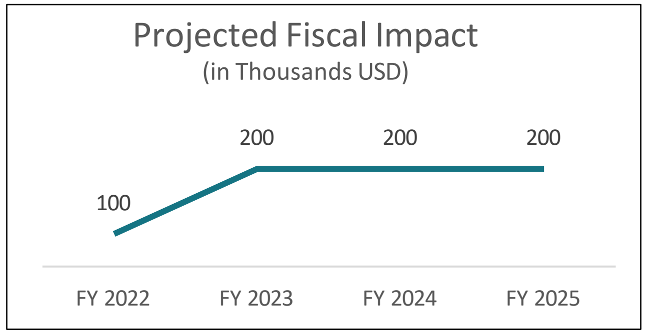
[i] Minn. H., Hearing on H.F. 1826 before the H. Comm. on Taxes, 88th Minn. Leg., Reg. Sess. (March 13, 2014), available at https://www.lrl.mn.gov/audio/house/2014/taxes031314.mp3.

Small Winery Credit

Tax Expenditure Initial Review - TEB 7.09

Tax Expenditure Facts

Year Enacted	2017
Statute	Minn. Stat. § 297G.03, subd. 6
Tax Type	Alcoholic Beverage Taxes
Provision Type	Credit
Latest Fiscal Impact Estimate	$200,000 – Fiscal Year 2024
Latest Claims Estimate	Latest figure of claims filed is not available
Expiration Date	None



Tax Expenditure Description

A credit is allowed to a winery that manufactures less than 75,000 gallons of wine and cider in the calendar year immediately preceding the fiscal year for which the credit is claimed. The credit for the fiscal year is the lesser of the tax liability or $136,275. In 2020, 71 wineries claimed this credit.

Additional Background Information

Under Minnesota Statutes 2023, section 297G.03, subdivision 1, an excise tax is imposed on distilled spirits and wine manufactured, imported, sold, or possessed in Minnesota. Beneficiaries of the tax credit include small wineries, defined as producers who manufactured less than 75,000 gallons of cider and wine in the preceding calendar year.

The Commissioner of Revenue is required to submit an annual report to the chairs and ranking minority members of the House and Senate tax committees that includes the number of credit claimants and amount of revenue foregone during the previous fiscal year.[i]

The Small Winery Credit reduces the amount of alcoholic beverage tax revenue that would otherwise be generated. Alcoholic beverage tax receipts are deposited in the state General Fund. This credit is administered by the Department of Revenue.

Proposed Tax Expenditure Objective for Consideration

The objective of the small winery tax credit is to promote development and survivorship of small wineries.

Sources

An explicit tax expenditure objective was not identified in the legislative record.

The policy was introduced in S.F. 866 during the 2017 Regular Legislative Session. Discussion of S.F. 866 in the Senate Taxes Committee on March 8, 2017, describes the bill's policy as extending to small wineries the same tax benefits allowed to small brewers and small distilleries.[ii]

Potential Metrics and Performance Measures

The following are evaluation considerations with respect to administrative and enforcement actions.

Performance measurement: Statistical analysis of claims to assess counts, regional distribution, and trends in claims over time.

Performance attribution: Calculate the effective tax rate and differential as a result of the tax credit. Financial analysis of participating distillers to assess free cash flow trends.

Performance appraisal: Conduct an operating ratio analysis to understand the impact of the tax credit on a producer's budgetary solvency. Assess whether budgetary solvency has improved over time as a result of the tax credit.

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] "Report regarding the small winery tax credit," Minnesota Legislative Reference Library Website, accessed December 5, 2023, https://www.lrl.mn.gov/mndocs/mandates_detail?orderid=11643.

[ii] Minn. Sen., Hearing on S.F. 866 before the Sen. Comm. on Taxes, 90th Minn. Leg. Sess. (March. 8, 2017), available at: https://www.lrl.mn.gov/media/file?mtgid=900329.

Appendix D. TERC Meeting July 10, 2024

Commission Member Attendance

Present	Excused
Sen. Ann H. Rest, Chair	Rep. Steve Elkins
Rep. Esther Agbaje, Vice Chair	Commissioner Paul Marquart
Rep. Greg Davids	Sen. Matt Klein
Sen. Steve Drazkowski	
Rep. Aisha Gomez (ex-officio)	
Rep. Jim Joy	
Sen. Bill Weber	

Meeting Summary

Chair Rest called the hybrid meeting of the Tax Expenditure Review Commission to order, and a quorum was present. The meeting minutes from March 15, 2024, were approved as presented. The Legislative Budget Office (LBO) presented three tax expenditure initial reviews. The three initial reviews included in this appendix are:

- **Home Mortgage Interest** (Minnesota Statutes 2024, section 290.0122, subdivision 2, 5, and 290.0132, subdivision 19(b))
- **Interest on Contributions to First-Time Homebuyer Account** (Minnesota Statutes 2024, section 290.0132, subdivision 25, and 462D.01-06)
- **Angel Investment Credit** (Minnesota Statutes 2024, section 290.0692 and 116J.8737)

Commission Motions and Actions

Vice-Chair Agbaje moved to adopt the proposed tax expenditure objectives, as amended, and proceed with tax expenditure evaluations for the three tax expenditures presented. The motion prevailed.

Vice Chair Agbaje moved TERC-1, a resolution requiring the Commissioner of Revenue to convene the first Tax Expenditure Review Commission meeting each year. The motion prevailed.

Commission Revisions to Presented Reviews

The Commission amended the objective statement of the Home Mortgage Interest Deduction. The objective stated below reflects the change approved by the Commission.

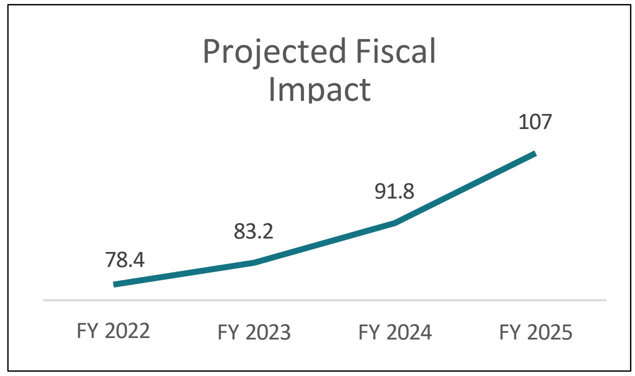
- **Home Mortgage Interest** (Minnesota Statutes 2024, section 290.0122, subdivision 2, 5, and 290.0132, subdivision 19(b))
    - "The objective of the Minnesota Home Mortgage Interest Deduction is to recognize expenses incurred in generating personal income or wealth and encourage homeownership at all levels of income."

Home Mortgage Interest

Tax Expenditure Initial Review - TEB 1.66

Tax Expenditure Facts

Year Enacted	1933
Statute	Minn. Stat. § 290.0122, Subd. 2, 5 and 290.0132, Subd.19(b)
Tax Type	Individual Income Tax
Provision Type	Minnesota Personal Deduction
Latest Fiscal Impact Estimate	$91,800,000 – Fiscal Year 2024
Latest Claims Estimate	138,100 – Tax Year 2021
Expiration Date	None



Tax Expenditure Description

A taxpayer may take an itemized deduction for interest paid on debt secured by a principal or second residence. Mortgage interest is deductible on up to $750,000 of debt used to buy, build, or improve a principal or second residence. If the debt is used for any other purpose, the limitation is $100,000 of debt. If more than one home is involved, the limitations apply to the total amount. This deduction is one of several deductions subject to the limitation of itemized deductions for higher-income taxpayers.

Home mortgage interest was deductible without limitation until restrictions were enacted in 1987. In 2018, the Federal limitation was temporarily decreased from $1 million to $750,000 in debt. In 2019, Minnesota established its own itemized deduction for home mortgage interest, with a limit of $750,000.

Additional Background Information

The existing Minnesota mortgage interest deduction (MID) limit of $750,000 was adopted under HF5 of the first special session of 2019, aligning with the Federal MID limit established by The Tax Cuts and Jobs Act (TCJA) of 2017.

A Federal interest expense deduction has existed since the inception of the income tax in 1913. The initial deduction covered any business and personal interest expenses.[i] Over the last century, household use of debt has become more commonplace, and in response, the deduction has been limited to personal mortgage interest with restrictions on deductible amounts and eligible homes.[ii] MID only applies for a secured mortgage debt. Interest on home equity is deductible at the Federal level only if the borrowed funds are to buy, build, or significantly improve the home that the equity is secured against.[iii] However, home equity interest is explicitly excluded from qualified residence interest that can be deducted under Minnesota Statutes, section 290.0122, subdivision 5(1).

The MID is an itemized deduction. This means that to benefit from it, taxpayers must forgo the standard deduction. The standard deduction was nearly doubled under the TCJA of 2017. This has led to fewer taxpayers itemizing their deductions and thus fewer taxpayers benefiting from the MID.[iv]

Beneficiaries of this tax expenditure are homeowners with mortgage interest payments who file an itemized deduction. This exemption is administered by the Department of Revenue. The MID reduces the amount of income tax revenue that would otherwise be generated. State income tax collections are deposited in the state General Fund except as directed by Minnesota Statutes, section 290.62.

Proposed Tax Expenditure Objective for Consideration

The objective of the Minnesota Home Mortgage Interest Deduction is to recognize expenses incurred in generating personal income or wealth and to encourage homeownership at all levels of income.

Sources

An explicit tax expenditure objective was not identified in the Minnesota legislative record.

The proposed objective is informed by a 2013 report published by The Minnesota House of Representatives Research Department, *A Review of Selected Tax Expenditures*.[v] The House Research report summarizes modern arguments for the policy's rationale and suggest the rationale for the policy was "more likely to allow recognition of expenses related to generating income." This objective is proposed in the context that an interest deduction against the income tax was allowed on all interest, without distinction between personal, business, household, and living expenses, dating back to the introduction of the Federal income tax in 1913.[vi] Restrictions to the mortgage interest deduction were introduced at the Federal level in 1986 and consequently adopted by Minnesota.[vii]

Additionally, the Congressional Research Service (CRS) proposes that tax deductions serve four key purposes in the tax code: to account for substantial personal expenses; encourage activities like homeownership and charitable giving; alleviate burdens from state and local taxes; and adjust for income-earning expenses.[viii] These arguments were also taken into consideration in developing a proposed objective.

Other Considerations Regarding Proposed Tax Expenditure Objective

A popular argument for the MID is that it was designed to encourage homeownership and home maintenance. The CRS argues that there is no evidence in the legislative record that this was the purpose of the MID.[ix] Additionally, research suggest that there is little evidence that MID increases the rate of home ownership and can may actually have unintended economic impacts to the housing market.[x]

Potential Metrics and Performance Measures

A calculation of the average effective tax rate of taxpayers claiming a MID can help assess the impact of the deduction on tax rates.

An assessment of the rate of claims before and after the TCJA of 2017 can be useful in understanding how take-up of the MID has been impacted by the expansion of the standard deduction.

The Commission may want to understand how the MID interacts with horizontal equity, the equal treatment for taxpayers in similar financial situations. This can encompass a comparison of effective tax rates of homeowners who take the MID with those who do not but have a similar income level. Granted, there are many variables that factor into homeownership status besides a tax filer's reported income level and there are limitations in identifying the homeownership status of taxpayers that do not claim the deduction.

Similarly, the Commission may want to understand how the MID impacts vertical equity to evaluate whether the MID contributes to making the income tax system progressive and whether it has impacted the equitable distribution of tax burdens. This can involve an analysis of the distribution of MID benefits across different income levels to assess the income tax liability distribution and compare that to average effective tax rates.

Ultimately, the Commission may want to understand trends in homeownership rates overtime and if there is a correlation with MID claims.

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] Joint Committee on Taxation. *Present Law and Background Relating to Tax Incentives for Residential Real Estate*. July 18, 2022. Available at https://www.jct.gov/publications/2022/jcx-16-22/

[ii] Congressional Research Service. *Tax Expenditures Compendium of Background Material on Individual Provisions, Committee on the Budget United States Senate*. December 2022. Available at https://www.congress.gov/117/cprt/SPRT49569/CPRT-117SPRT49569.pdf

[iii] Internal Revenue Service. *Publication 936 (2023), Home Mortgage Interest Deduction*. Last updated January 10, 2024. Available at https://www.irs.gov/publications/p936

[iv] Hembre, Erik and Dantas, Raissa, *Tax Incentives and Housing Decisions: Effects of the Tax Cut and Jobs Act.* October 8, 2021. Page 5. Available at https://ssrn.com/abstract=3779520

[v] Minnesota House of Representatives House Research Department. *A Review of Selected Tax Expenditures*. November 2013. Pages 31-34. Available at https://www.house.mn.gov/hrd/pubs/taxexpend.pdf

[vi] Keightley, Mark. The Mortgage Interest and Property Tax Deductions: Analysis and Options. Congressional Research Service. Published January 18,2011. Updated March 18, 2014. Page 4. Available at https://crsreports.congress.gov/product/pdf/R/R41596

[vii] Supra note V.

[viii] Lowry, Sean. *Tax Deductions for Individuals: A Summary*. Congressional Research Service. March 17, 2017. Available at https://crsreports.congress.gov/product/pdf/R/R42872

[ix] Congressional Research Service. Background Material on Individual Provisions. Page 385.

[x] Sommer, Kamila, and Paul Sullivan. 2018. "Implications of US Tax Policy for House Prices, Rents, and Homeownership." *American Economic Review*, 108 (2): 241–74.

Interest on Contributions to a First-Time Homebuyer Account

Tax Expenditure Initial Review – TEB 1.81

Tax Expenditure Facts

Year Enacted	2017
Statute	Minn. Stat. § 290.0132 subd. 25; 462D.01-.06
Tax Type	Individual Income Tax
Provision Type	Minnesota Subtraction
Latest Fiscal Impact Estimate	Less than $50,000 – Fiscal Year 2024
Latest Claims Estimate	Fewer than 60 returns – Tax Year 2020
Expiration Date	None

Estimated fiscal impact is less than $50,000 per year through Fiscal Year 2025

Tax Expenditure Description

A subtraction from Federal adjusted gross income is allowed for interest on contributions to a first-time homebuyer account. The beneficiary of the account must be a Minnesota resident. The account may be used to pay eligible costs related to the purchase of a home, including down payments, eligible closing costs, and the cost of constructing or financing construction of a single-family residence.

A maximum of $14,000 for individuals and $28,000 for married joint filers may be contributed to the account each year. The total lifetime contribution limit is $50,000 for individuals and $100,000 for married joint filers. The maximum amount allowed in an account is $150,000.

Additional Background Information

Information regarding accounts opened with financial institutions are reported to the Commissioner of Revenue in the form and manner required by the Commissioner. Financial institutions include banks and credit unions. The holder of the account must designate a first-time home buyer as the qualified beneficiary. The account holder may be the qualified beneficiary, though does not need to be.[i]

This subtraction is administered by the Department of Revenue, and it reduces the amount of income tax revenue that would otherwise be generated. State income tax collections are deposited in the state General Fund, as directed by Minnesota Statutes, section 290.62.

Proposed Tax Expenditure Objective for Consideration

The objective of the interest on contributions to a first-time homebuyer account subtraction is to support and encourage first-time home buyers to save for the purchase of a home.

Sources

The proposed objective for this subtraction was discussed by the bill author during a hearing in the House State Government Finance Committee on March 7, 2017.[ii]

Potential Metrics and Performance Measures

An analysis of the program's participation based on the submission of the Schedule M1HOME form to the Department of Revenue may identify trends in utilization of the tax incentive.

The Schedule M1HOME form is required to file for the subtraction and records contributions and withdrawals to designated First-Time Homebuyer Savings accounts.[iii] An analysis of these transactions may show the usage and efficacy of this program, and whether it incentivizes this type of saving.

A review of home purchases in Minnesota before and since the program's inception may depict a change in the number of first-time homebuyer purchases in the state. A comparison with direct spending programs may provide indications to program efficiency.

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For more information, please visit the [Tax Expenditure Review Commission website].

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[i] Laws of Minnesota 2022, chapter 462D, section 462D.02-03.

[ii] Minn. H., Hearing on H.F. 1234 before the H. Comm. on State Government Finance. 90th Minn., Leg., Reg. Sess. (March 7, 2017.) https://www.house.mn.gov/Committees/minutes/90021/56940.

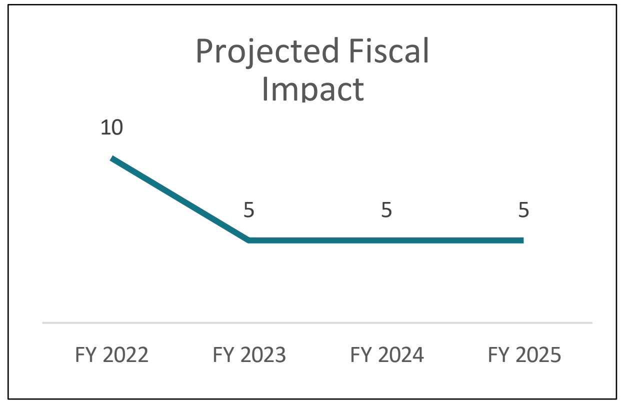
[iii] Minnesota Department of Revenue. (2022, December). Schedule M1HOME, First-Time Homebuyer Savings Account. www.revenue.state.mn.us/sites/default/files/2022-12/m1home_22.pdf.

Angel Investment Credit

Tax Expenditure Initial Review - TEB 1.94

Tax Expenditure Facts

Year Enacted	2010
Statute	Minn. Stat. § 290.0692 and 116J.8737
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Actuals	$4,378,987 – Tax Year 2023[i]
Latest Claims Actuals	231 investments in Tax Year 2023[ii]
Expiration Date	January 1, 2025



Tax Expenditure Description

A refundable credit is allowed to investors for investments in a small business, provided that the investor or investment fund, the investment, and the small business each meet specified requirements. The credit is equal to 25 percent of the qualifying investment. The maximum credit for a tax year is $250,000 for a married couple filing a joint return and $125,000 for other filers.

A qualified investor is an individual who invests at least $10,000 in a calendar year. A qualified investment fund is a pass-through entity that invests at least $30,000 in a calendar year. A small business must have its headquarters and at least 51 percent of its employees and payroll in Minnesota. It must have fewer than 25 employees and be engaged in innovation in high technology or in developing a new proprietary technology. Other requirements are specified.

The total amount of the credit was limited to $11 million for tax year 2010, to $12 million per year for tax years 2011 through 2013, and to $15 million for 2014 through 2016. Credit certificates are approved and issued by the Department of Employment and Economic Development. Any portion of a tax year's credits that is not allocated can be carried forward to a subsequent tax year.

This credit was enacted in 2010, for tax years 2010 through 2014. These provisions were modified in 2013. In 2014, the credit was increased and extended to tax year 2016. In 2019, the credit was extended to tax years 2019 and 2021, with a limit of $10 million each year. In 2021, the credit was extended to tax year 2022 with a limit of $5 million. In 2023, the credit was extended to tax year 2024 with a limit of $5 million. The 2023 change is noted in the Projected Fiscal Impact chart above.[1]

Additional Background Information

The Department of Employment and Economic Development's (DEED) 2024 annual report to the Legislature states 266 credit certificates were issued for the 2023 tax year, of which 231 made a qualifying investment. In

[1] The description provided in the 2022 Tax Expenditure Budget was edited to include the extension of the credit in 2023.

total, $4,378,987 qualifying investments were made in the same year. The credits from a tax year that are not allocated can be carried forward to a subsequent year. Businesses that received investments reported hiring 133 new employees, and an additional 637 jobs classified as indirect hires (770 total jobs). Indirect hires are listed as contract workers, agency staffers, consultants, and others indirectly employed.[iii]

Beneficiaries of this tax credit include small business investors who meet specified requirements. DEED administers the exemption and issues credit certificates. This tax expenditure reduces the amount of individual income tax revenue that would otherwise be collected. Income tax revenue is deposited in the state General Fund except as directed by Minnesota Statutes, section 290.62.

To be eligible for the tax credit, a business receiving the investment must:

(1) apply and receive certification for the calendar year in which the investment was made prior to the date on which the qualified investment was made;

(2) not issue securities that are traded on a public exchange;

(3) not issue securities that are traded on a public exchange within 180 days after the date on which the qualified investment was made; and

(4) not have a liquidation event within 180 days after the date on which the qualified investment was made.[iv]

Proposed Tax Expenditure Objective for Consideration

The objective of the angel investment credit is to encourage investment in innovative small businesses in Minnesota.

Sources

The proposed objective for the angel investment credit is adapted from Minnesota Statutes section 116J.8737, subdivision 2, which defines qualified small businesses, and the second engrossment of omnibus tax bill H.F. 991, introduced during the 2021 regular legislative session.[v] The statement of purpose listed in H.F. 991-2E was not included in subsequent engrossments, but the corresponding language extending the credit sunset date was included in later engrossments and in H.F. 9, the omnibus tax bill enacted during the 2021 first special session.

Potential Metrics and Performance Measures

Performance measures listed in H.F. 991-2E included "the increase in the number of businesses that receive these investments, the number of people employed by these businesses in the state, the productivity of these businesses, or the sales of these businesses."[vi]

DEED is required to annually produce a report to the legislature detailing the metrics of the program.[vii] Such metrics include the number of credits issued, credit recipients, location of businesses receiving investments, the total amount of investment received by each business, among other required metrics. This report can be used to monitor the change in these metrics between years to determine the impact of the program.

A report was prepared in 2014 for the Minnesota Legislature evaluating the angel tax credit program from 2010 to 2012. While this study does not include data from before the enactment of the program, it does show a marked increase in investment through the first years of the angel investment credit program.[viii]

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[i] Minnesota Department of Employment and Economic Development, *Minnesota Angel Tax Credit Program: 2023 Annual Report.* March 8, 2024. Pages 7-8. https://mn.gov/deed/assets/2023-atc-annual-report_tcm1045-614285.pdf

[ii] Ibid.

[iii] Ibid.

[iv] Minnesota Statutes 2023, section 116J.8737, subdivision 2(e).

[v] Minnesota House Omnibus Tax Bill, HF991-2E, 92nd session (2021), https://www.revisor.mn.gov/bills/text.php?number=HF991&version=2&session=ls92&session_year=2021&session_number=0. The purpose statement begins at line 210.23.

[vi] Ibid.

[vii] Minnesota Statutes 2023, section 116J.8737, subdivision 9.

[viii] Economic Development Research Group, *Evaluation of the Minnesota Angel Tax Credit Program: 2010-2012*. January 31, 2014. https://www.revenue.state.mn.us/sites/default/files/2014-02/evaluation_of_the_mn_angel_tax_credit_program.pdf.

Appendix E. TERC Meeting August 16, 2024

Commission Member Attendance

Present

Sen. Ann H. Rest, Chair

Rep. Esther Agbaje, Vice Chair

Rep. Steve Elkins

Rep. Jim Joy

Sen. Matt Klein

Sen. Bill Weber

Rep. Aisha Gomez (ex-officio)

Rep. Greg Davids

Excused

Sen. Steve Drazkowski

Commissioner Paul Marquart

Meeting Summary

Chair Rest called the hybrid meeting of the Tax Expenditure Review Commission to order, and a quorum was present. The meeting minutes from July 10, 2024, were approved as presented. The Legislative Budget Office (LBO) described the proposed process for evaluating tax expenditures and presented three tax expenditure initial reviews. The three initial reviews included in this appendix are:

- **Deed Transfer Tax Exemptions** (Minnesota Statutes 2024, section 287.22)
- **Heating Fuel and Utility Service Exemptions** (Minnesota Statutes 2024, section 297A.67, subdivision 15 and 16)
- **Lawful Gambling Tax Expenditures** (Minnesota Statutes 2024, section 349.166 and 297E.02)

Following the presentation of the above initial reviews, nine tax expenditure objectives previously presented for consideration in 2022 were presented again to receive approval in order to evaluate those tax expenditures. The nine initial reviews are also provided in this appendix, and include:

- **Working Family Credit** (Minnesota Statutes 2024, section 290.0671)

- **Beginning Farmer Management Credit** (Minnesota Statutes 2024, section 290.06, subdivision 3.37 and section 41B.0391)
- **Beginning Farmer Incentive Credit** (Minnesota Statutes 2024, section 290.06, subdivision 3.37 and section 41B.0391)
- **Research and Development Credit** (Minnesota Statutes 2024, section 290.068)
- **Housing Contribution Credit** (Minnesota Statutes 2024, section 290.0683, section 462A.40, and section 2971.20)
- **Telecommunications Equipment** (Minnesota Statutes 2024, section 297A.68, subdivision 35a)
- **Farm Machinery Exemption** (Minnesota Statutes 2024, section 297A.69, subdivision 4(1) and section 297A.61, subdivision 12)
- **Building Materials for Residences of Disabled Veterans** (Minnesota Statutes 2024, section 297A.71, subdivision 11)
- **Construction Materials for Certain City Projects** (Minnesota Statutes 2024, section 297A.71, subdivision 44 and section 297A.9905)

Commission Motions and Actions

After the presentation of the three new initial reviews for consideration, Representative Agbaje moved to adopt the proposed tax expenditure objective statements for the three tax expenditures presented for the first time to the Commission on August 16, 2024, and directed the Legislative Budget Office to proceed with tax expenditure evaluations in accordance with Minnesota Statutes 2024, section 3.8855.The motion also provided the Legislative Budget Office the ability to make any technical corrections to the reviews necessary. The motion prevailed.

After the presentation of the nine objective statements for consideration Representative Agbaje moved to adopt the proposed tax expenditure objective statements for those tax expenditures presented to the Commission for consideration on August 16, 2024, as originally presented in 2022 by the Legislative Budget Office, for the purpose of evaluating those tax expenditures. The motion also directed the Legislative Budget Office to proceed with tax expenditure evaluations in accordance with Minnesota Statutes 2024, section 3.8855 and to make technical corrections as proposed the Commission. The motion prevailed.

Commission Revisions to Presented Reviews

The Commission made the following changes and proposed the following additional considerations to the presented objective of the tax expenditures or potential metrics identified by the LBO.

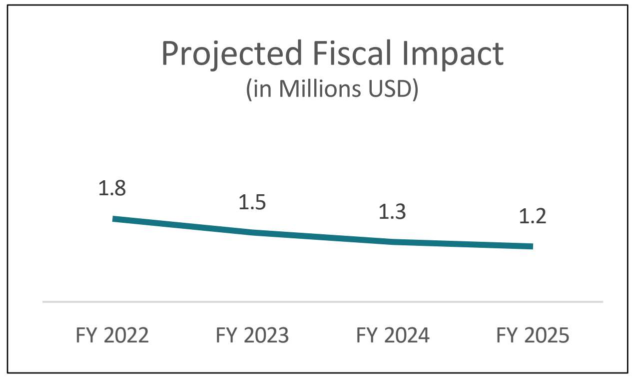
- **Deed Transfer Tax Exemptions** (Minnesota Statutes 2024, section 287.22)
    - Technical footnote clarification on the definition of a tax expenditure
    - Technical language correction replacing “proposed tax expenditure objectives for consideration” to “proposed tax expenditure objectives”
- **Beginning Farmer Incentive Credit** (Minnesota Statutes 2024, section 290.06, subdivision 3.37 and section 41B.0391)
    - Clarification that the projected fiscal impact was for the 2025 credit sunset and was projected before the credit extension
- **Research and Development Credit** (Minnesota Statutes 2024, section 290.068)
    - Language clarification elaborating that the corporate tax credit refers to corporations
    - Technical correction changing the projected fiscal impact from 56,000 to the correct value of 56 million

Deed Transfer Tax Exemptions

Tax Expenditure Initial Review – TEB 10.01 to 10.06

Tax Expenditure Facts

Years Enacted	1961-1997
Statute	Minn. Stat. § 287.22
Tax Type	Deed Transfer
Provision Type	Exemptions
Fiscal Impact Estimate	$1,300,000 (All Exemptions) – Fiscal Year 2024
Claims Estimate	Direct measure of this estimate is not currently available
Expiration Date	None



Note: The graph shows the combined fiscal impact of exemptions listed in Table 1.

Tax Expenditure Description

The State of Minnesota imposes a tax when real estate is granted, assigned, transferred, or otherwise conveyed by deed or instrument.[i] The following types of property transfers or sales are exempted from the deed transfer tax pursuant to M.S. 287.22. Note that several exemptions listed in statute do not meet the criteria of a tax expenditure and are therefore excluded from the tax expenditure budget and this review.[ii]

Table 1: Deed Transfer Tax Exemptions

TEB	Tax Expenditure Description	Year Enacted	Fiscal Impact FY24
10.03	A deed transferring one or more cemetery lots is exempt.	1961	$100,000
10.02	A deed of distribution by a personal representative is exempt. This type of transaction commonly occurs during the probate process to settle a decedent's estate.	1975	< $50,000
10.01	A deed to or from a co-owner partitioning undivided interest in the same piece of property is exempt. For example, tenants in common agree that each tenant will be assigned particular tracts of land within a jointly owned property.	1984	< $50,000
10.04	A deed or other instrument issued pursuant to a Permanent School Fund land exchange is exempt. Subject to the Minnesota Constitution, M.S. 92.122, and related statutes, school trust land may be exchanged in order to improve management, reduce costs, compensate for diminished revenues, or improve future revenue potential.	1991	< $50,000

10.05	A sheriff's certificate of sale or a certificate of redemption given to the mortgagor in a mortgage or lien foreclosure sale is exempt.	1993	$900,000
10.06	Real estate conveyed pursuant to a decree of marriage dissolution is exempt.	1997	$300,000

Additional Background Information

The current deed transfer tax rate is 0.33 percent of consideration (the price paid for the real property, including the fair market value of any land exchanged) when the consideration exceeds $3,000. When consideration is equal to or less than $3,000, no consideration is given, or the transfer is made pursuant to a consolidation or merger, a minimum flat tax of $1.65 applies. For reference, the difference between an instrument taxed at the minimum rate and one that is marginally above the minimum threshold ($3,001) is $8.25.

The deed transfer tax was originally enacted in 1961 at a rate of $1.10 for consideration of $1,000 or less plus 55¢ for each $500 in excess of $1,000. In 1987, the rate was changed to $1.65 for consideration of $500 or less plus $1.65 for each additional $500. In 2001, the tax was restated as 0.33 percent of consideration (the equivalent of $1.65 per $500) when the consideration exceeded $500. If consideration was $500 or less, a minimum tax of $1.65 applied. In 2019, the minimum tax threshold was changed from $500 to $3,000.

Chapter 287 was recodified in 1999 making technical changes, eliminating outdated language, adding definitions, clarifying language, and arranging provisions in a more logical order. Of note for this review, the term "consideration" was defined, the definition of "real property" as applied to the deed tax was clarified, and the determination of tax liability was clarified.[iii]

The tax is paid by the seller to the county treasurer when the deed is recorded.[iv] For example, a residential property purchased for $250,000 would incur a deed tax liability of $825 ($250,000 * .0033). Each county remits 97 percent of revenues to the state for deposit in the general fund. The county retains the remaining three percent to cover administrative expenses.

Beneficiaries of deed transfer tax exemptions include persons or entities that convey real estate by a deed or instrument listed in Table 1.

Proposed Tax Expenditure Objectives:

Five of the six deed tax exemptions identified in the Tax Expenditure Budget and shown in Table 2 are clarifications that help define the tax base. Put another way, these exemptions help answer who or what is subject to the deed tax. The exemption for exchanges of Permanent School Fund (PSF) lands is intended to help ensure maximum financial return consistent with PSF goals and fiduciary responsibilities specified in statute and in the Minnesota Constitution.

Table 2: Deed Tax Exemption Objectives

Exemption	Public Policy Objectives
Cemetery Lots	▪ Define the tax base for the application of the deed transfer tax.
Distributions by Personal Representatives	▪ Define the tax base for the application of the deed transfer tax.
Property Partitioned between Co-Owners	▪ Define the tax base for the application of the deed transfer tax.

Exchange of Permanent School Fund Lands	▪ Help ensure the Permanent School Fund secures maximum financial return consistent with fund goals stated in M.S. 127A.31 and fiduciary responsibilities imposed by Article 11, Section 8 of the Minnesota Constitution.
Mortgage and Lien Foreclosure Sales	▪ Define the tax base for the application of the deed transfer tax.
Decree of Marriage Dissolution	▪ Define the tax base for the application of the deed transfer tax. ▪ Lessen the financial burden on individuals undergoing divorce proceedings.

Sources

The recorded legislative history associated with deed tax exemptions is limited and does not directly identify intended public policy objective(s). The objectives identified in this report are based on a review of statute language and archived legislative committee discussions.

Minnesota statutes 287.21 imposes the deed tax on "each deed or instrument by which any ***real property*** in this state is granted, assigned, transferred, or otherwise conveyed. The tax applies against the ***net consideration***" (emphasis author).

- Minnesota statutes 287.20, subdivision 7 defines real property as "any fee simple estate, and any estate for life, as defined in chapter 500."
- Minnesota statutes 287.20, subdivision 2 defines consideration as "the total monetary value given in return for a conveyance of real property including all lump-sum payments, all prior or future installment payments that are required under the agreement between the parties, and the fair market value of any property taken, or to be taken, in exchange" less the amount of any liens or encumbrances that remain on the property at the time of sale that are not removed as a result of the sale.
- Minnesota statutes 287.20, subdivision 7 defines partition as "the division by conveyance of real property that is held jointly or in common by two or more persons into individually owned interests. If one of the co-owners gives consideration for all or a part of the individually owned interest conveyed to them, that portion of the conveyance is not a part of the partition."

The construction of statute language and archived legislative committee discussions suggest that deed taxes are intended to be applicable to voluntary conveyances of real estate with full ownership rights between unaffiliated parties (the grantor and grantee do not share an existing interest in the property). If this assumption is correct, then the deed tax exemptions identified in the Tax Expenditure Budget, with the exception of Permanent School Fund land exchanges, may function to define the tax base.[v]

A cemetery lot does not meet the definition of real property because lot ownership rights are limited – it can be used for burial purposes only – compared to a fee simple estate, which represents the maximum ownership interest that is allowed under law. The Minnesota Supreme Court has described cemetery lot ownership interest as "a kind of perpetual easement" or "a special kind of perpetual license or privilege."[vi]

Real estate partitioned between co-owners or distributed pursuant to a decree of marriage dissolution does not involve the transfer of real estate from one party to another, but the division of an existing interest shared by both parties. An additional or alternative objective of the exemption for real estate conveyed pursuant to a decree of marriage dissolution may be to lessen the financial burden on individuals undergoing divorce proceedings.

Conveyance of real estate by deed of distribution from a personal representative, a certificate of sale from a mortgage or lien foreclosure sale, or a certificate of redemption from a mortgage or lien foreclosure sale is not considered a voluntary transfer for the purposes of the deed tax. These instruments would not be used but for events (death of the property owner or loan default) the property owner, mortgagor, or mortgagee would presumably avoid if another alternative were possible.

The deed tax exemption for Permanent School Fund (PSF) land exchanges helps ensure the fund secures maximum financial return consistent with PSF goals and fiduciary responsibilities specified in statute and the Minnesota Constitution. The effective transfer of financial resources from the PSF to the General Fund that would occur but for this exemption may be considered an unintended consequence of the Minnesota deed tax that is remedied by the exemption.

Potential Metrics and Performance Measures

Conveyances of real estate that fall within one of the five exemption categories discussed above are not subjected to the deed tax, therefore the exemptions are achieving their objective of defining the tax base.

The deed tax exemption for Permanent School Fund land exchanges reduces a cost associated with land management that would exist but for the exemption, thus furthering PSF goals and fiduciary responsibilities specified in statute and the Minnesota Constitution.

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] Descriptions of deed tax exemptions in this review may differ slightly from the Tax Expenditure Budget for explanatory purposes.

[ii] There are several exemptions in statute that do not meet the definition of a tax expenditure and are not included within the tax expenditure budget. For example, some are obsolete such as Minnesota Statutes 2023, section 287.22 subdivision 15 which exempts a transfer on death deed under section 507.071, and any affidavit or other document to the extent it references a transfer on a death deed. Other excluded exemptions are clarifications such as subdivision 4 which is an expenditure clarifying plats are not conveyances of real property.

[iii] Laws of Minnesota 1999, chapter 31.

[iv] Minnesota Statutes 2022, section 287.24.

[v] For a brief discussion on the Decree of Marriage Dissolution exemption, see Minn. Sen., Hearing on S.F. 493 before the Sen. Comm. On Taxes, 80th Minn. Leg., Reg. Sess. (April 8, 1997), available at https://www.lrl.mn.gov/media/file?mtgid=801295 (audio media, file 2/2). For a brief discussion on mortgage or lien foreclosure sale exemptions, see Minn. Sen., Hearing on S.F. 585 before the Sen. Property Tax Division, 78th Minn. Leg., Reg. Sess. (March 10, 1993), available at https://www.lrl.mn.gov/media/file?mtgid=780787 (audio media).

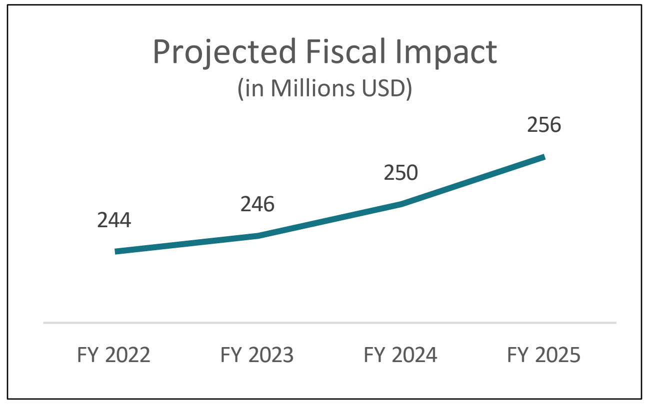
[vi] Erickson v. Sunset Memorial Park Ass’n, 259 Minn. 532, 108 N.W.2d 434 (Minn. Supreme Court 1961).

Heating Fuel and Utility Service Exemptions

Tax Expenditure Initial Review – TEB 4.14 - 4.16

Tax Expenditure Facts

Years Enacted	Various – See Table 1
Statute	Minn. Stat. § 297A.67, subd. 15 and 16
Tax Type	General Sales and Use Tax
Provision Type	Exemption – Particular Goods and Services
Fiscal Impact Estimate	$250 Million (All Exemptions) – Fiscal Year 2024
Claims Estimate	Direct measure of this estimate is not currently available.
Expiration Date	None



Note: The graph shows the combined fiscal impact of exemptions listed in Table 1.

Tax Expenditure Description

Residential heating fuels, residential water services, and all sewer services are exempt from the sales and use tax. The following descriptions were taken from the Department of Revenue Tax Research Division 2022 Tax Expenditure Budget report.

Table 1: Heating Fuel and Utility Service Exemptions

TEB	Tax Expenditure Description	Year Enacted	Fiscal Impact FY24
4.14	An exemption from the sales and use tax applies to all fuel oil, coal, wood, steam, hot water, propane gas, and liquefied petroleum gas sold to residential customers for residential use. Purchases of natural gas by residential customers who use natural gas for their primary source of residential heat are exempt for the six billing months of November through April. Likewise, the purchase of electricity is exempt for six months for customers using electricity as the primary source of residential heat.	1978	$135,000,000
4.15	The furnishing of water for residential use is exempt from the Minnesota sales and use tax.	1979	$27,000,000
4.16	The furnishing of sewer services is exempt from the Minnesota sales and use tax. Sewer service has never been subject to the sales and use tax.	*	$88,200,000

Beneficiaries of these exemptions include residential water and sewer utility customers, commercial sewer customers, and purchasers of heating fuel for residential use.

These exemptions reduce sales tax revenue by an estimated 250 million dollars annually. Sales tax revenue is deposited in the state General Fund except as provided by Minnesota Statutes 297A.94. The Department of Revenue administers sales tax registrations, remittances, and exemptions.

Proposed Tax Expenditure Objective for Consideration

The objective of the heating fuel and utility service exemptions is to lessen the effective tax burden of lower-income households and reduce the regressivity of the sales and use tax.

Sources

The legislative record does not explicitly state a public policy objective for these exemptions. The proposed objective is based on Minnesota tax reform debates and the generally acknowledged rationale for exempting goods or services that could be reasonably considered basic necessities.

The Minnesota legislature debated enactment of a sales and use tax from the early 1930s until passage in 1967. Critics argued the tax was regressive and would place a disproportionate burden on low-income households.[i] Governor Floyd B. Olson vetoed an early attempt to enact sales tax legislation in 1935, stating that "a sales tax falls the heaviest upon those least able to pay…it must be admitted that 80 percent of the various sales taxes will be collected on the necessities of life."[ii] A three percent sales and use tax was eventually enacted in the 1967 Property Tax Reform and Relief Act that included exemptions for food, prescribed drugs, and clothing, among other items.[iii]

States have historically exempted basic necessities – goods or services considered necessary to attain a generally accepted standard of living – to lessen the effective tax burden on lower-income households and reduce the regressivity of the sales tax.[iv] For the purposes of this review, it is assumed that heating fuel and utility services could be reasonably considered basic necessities.

Potential Metrics and Performance Measures

The sales and use tax is generally described as regressive because the effective tax rate (tax paid as a percentage of income) falls as income rises.[v] For example, the Department of Revenue estimates that the combined effective general sales and use tax rate for the 2nd income decile of Minnesota households is 4.47 percent, while the effective rate for the highest income decile is 1.35 percent.[vi] A full review may assess the degree to which this exemption lowers regressivity using income data from the Minnesota Department of Revenue and consumer expenditure data from the U.S. Bureau of Labor Statistics. A full review may also compare the effectiveness of the tax expenditure with policy alternatives such as credits, rebates, or direct payments.

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] David Maeda, "Tax was a hard sell," *Session Weekly* 17, no. 6 (March 10, 2000): 22, https://www.lrl.mn.gov/docs/pre2003/other/P615/2000/v17n6.pdf; David Maeda, "Putting the tax before the sale," *Session Weekly* 17, no. 12 (April 21, 2000): 4, https://www.lrl.mn.gov/docs/pre2003/other/P615/2000/v17n12.pdf.

[ii] Minn. House Journal, 49th Leg., Reg. Sess. 2067-2071(1935), https://www.leg.mn.gov/archive/vetoes/1935veto_HF1564.pdf.

[iii] Laws of Minnesota 1967, 1st Spec. Sess. chapter 32, article 13, section 25, https://www.revisor.mn.gov/laws/1967/1/Session+Law/Chapter/32/pdf/.

[iv] Frederick W. Derrick and Charles E. Scott, "Sales Tax Exemptions and Credits: Time to Reevaluate," *Atlantic Economic Journal* 23, no. 4 (1995): 276. For a table of states that offer food and drug exemptions, see "State Sales Taxes – Food and Drug Exemptions," Federation of Tax Administrators, updated January 1, 2023, https://taxadmin.memberclicks.net/assets/docs/Research/Rates/sales.pdf.

[v] Stephanie Hunter McMahon, *Principles of Tax Policy* (St. Paul: West Academic, 2018), 215-216.

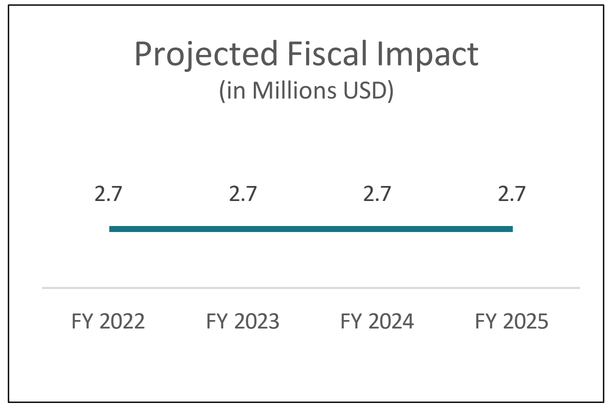
[vi] Minnesota Department of Revenue, Tax Research Division, *2021 Minnesota Tax Incidence Study: An Analysis of Minnesota's Household and Business Taxes* (October 20, 2022), 11-12, 29,32-33, https://www.revenue.state.mn.us/sites/default/files/2023-08/2021-tax-incidence-study-post-pub-revisions-v2.pdf.

Lawful Gambling Tax Expenditures

Tax Expenditure Initial Review – TEB 11.01 to 11.06

Tax Expenditure Facts

Years Enacted	1984-2000
Statutes	Minn. Stat. § 349.166 and 297E.02
Tax Type	Lawful Gambling Taxes
Provision Types	Exemptions; Credit
Fiscal Impact Estimate	$2,700,000 (All Expenditures) – Fiscal Year 2024
Claims Estimates	See Table 1 Below
Expiration Date	None



Note: The graph shows the combined fiscal impact of the tax expenditures discussed in this review.

Tax Expenditure Description

Minnesota Statutes 2023, section 349.166 allows organizations to conduct some lawful gambling activities under certain conditions without a license.[i] Organizations that are exempt or excluded from licensing requirements are also exempt from lawful gambling taxes.

Table 1: Lawful Gambling Tax Exemptions

TEB	Tax Expenditure Description	Year Enacted	Annual Claims	Fiscal Impact FY24
11.02	The lawful gambling tax is not imposed on bingo conducted by an organization in connection with a county fair, the state fair, or a civic celebration. To qualify, the bingo cannot be conducted for more than twelve consecutive days and no more than four applications can be applied for and approved in a calendar year.	1984	NA	< $50,000
11.03	An exemption from the lawful gambling tax is allowed for bingo conducted by an organization which conducts bingo on four or fewer days in a calendar year. This exemption does not apply if the organization holds a lawful gambling license.	1984	NA	< $50,000
11.04	If the value of all raffle prizes awarded by an organization in a calendar year does not exceed $1,500, then the raffles of that organization are exempt from the lawful gambling tax. The exemption also applies if the organization qualifies under Section 501(c)(3) of the Internal Revenue Code and	1984	1,400	$200,000

	the value of all raffle prizes awarded at one event in a calendar year does not exceed $5,000.			
11.01	An exemption from the lawful gambling tax is allowed for bingo conducted within a nursing home or a senior citizen housing project or by a senior citizen organization if certain conditions are met. The prizes for a single bingo game cannot exceed $10, and total prizes awarded at a single bingo occasion cannot exceed $200.	1985	NA	< $50,000
11.05	All types of lawful gambling except linked bingo games are exempt from the lawful gambling taxes if certain conditions are met. To qualify, an organization must conduct lawful gambling on no more than five days in a calendar year and cannot award more than $50,000 in prizes for lawful gambling in a calendar year.	1986	2,300	$2,500,000
11.06	An organization may claim a credit against the lawful gambling tax equal to the tax resulting from a raffle if the net proceeds have been used exclusively to relieve the effects of poverty, homelessness, or physical or mental disability for an individual or family.	2000	17	< $50,000

Additional Background Information

In fiscal year 2023, lawful gambling tax revenue totaled $193 million. Taxable gross receipts totaled $4.572 billion while exempt gross receipts totaled $55.6 million. Thus, approximately 1.2 percent of lawful gambling sales were exempt from lawful gambling taxes in fiscal year 2023.[ii]

Lawful gambling net receipts (gross receipts less prizes paid) are subject to one of two tax structures depending on the game type. A flat tax of 8.5 percent is imposed on net receipts from paper bingo, paddlewheel, and raffles. A variable rate tax (referred to in statute as the combined net receipts tax), is imposed on paper and electronic pulltabs, tipboards and electronic bingo that increases as an organization's annual net receipts exceed certain thresholds.[iii] Tax proceeds are deposited in the state General Fund. Lawful gambling taxes are administered by the Department of Revenue.

The lawful gambling tax was enacted in 1984 and covered, raffles, paddlewheels, pulltabs, and tipboards. A separate tax on pulltabs was enacted in 1986, and that tax was extended to tipboards in 1988. In 1989, an additional tax was imposed on the combined receipts of an organization from pulltabs and tipboards. The tax rates for both taxes were reduced in 1998, 1999, and 2000. In 2012, the combined net receipts tax was restructured and extended to newly authorized electronic games. In 2023, the combined net receipts tax was reduced.[iv]

Except for smaller raffles and bingo at senior citizen organizations and nursing homes, an organization that conducts exempt lawful gambling activities must obtain a permit from the Gambling Control Board prior to the event. Permits are classified as either exempt or excluded activities. Exempt and excluded permits cannot be issued to a licensed organization.

Beneficiaries of lawful gambling tax expenditures include organizations that conduct activities under the conditions specified in Minnesota Statutes 2023, section 349.166, and are summarized in Table 1.

Proposed Tax Expenditure Objective for Consideration

The exemptions identified in the Tax Expenditure Budget and shown in Table 2 are intended to simplify compliance with, and enforcement of, lawful gambling and to reduce administrative burden. The credit against the lawful gambling tax for certain raffles is intended to direct a higher amount of net raffle proceeds used exclusively to relieve the effects of poverty, homelessness, or disability than would occur but for the credit.

Table 2: Lawful Gambling Tax Expenditure Objectives

Exemption	Tax Expenditure Objectives for Consideration
Bingo at Certain Organizations	Simplify compliance with and enforcement of lawful gambling and reduce administrative burden.
Bingo at Fairs and Civic Celebrations	Simplify compliance with and enforcement of lawful gambling and reduce administrative burden.
Infrequent Bingo Occasions	Simplify compliance with and enforcement of lawful gambling and reduce administrative burden.
Smaller Raffles	Simplify compliance with and enforcement of lawful gambling and reduce administrative burden.
Lawful Gambling Under Certain Conditions	Simplify compliance with and enforcement of lawful gambling and reduce administrative burden.
Credit	**Tax Expenditure Objective for Consideration**
Credit for Certain Raffles	Direct a higher amount of net raffle proceeds used exclusively to relieve the effects of poverty, homelessness, or disability than would occur but for the credit.

Sources

An explicit tax expenditure objective was not identified in the legislative record for the exemptions listed in Table 2. The objective identified in this report is based on a review of statute language and conversations with the Gambling Control Board. In FY23, there were 1,144 licensed gambling organizations, while 3,347 exempt permits and 587 excluded bingo permits were issued to 2,562 nonprofit organizations.[v] Significant additional resources would be needed to fully license and enforce exempt activities, and it is likely that costs would outweigh additional revenues. In addition, certain organizations may choose to forgo exempt gambling activities if subjected to licensing requirements and the lawful gambling tax.

The credit against the lawful gambling tax for certain raffles was introduced in House File (HF) 97 during the 1999 legislative session. The bill was heard in the House Governmental Operations and Veterans Affairs Policy committee on February 15, 1999, and included a discussion of intended purpose. The bill was amended and re-referred to the Taxes committee but did not receive a further hearing. On March 23, 2000, the language of HF 97 was offered as an amendment to HF 4127, the House omnibus tax bill, during a Ways and Means hearing. HF 97 and the bill author are mentioned in connection with the amendment.[vi]

Potential Metrics and Performance Measures

Further conversations with the Gambling Control Board and the Department of Revenue may help determine to what extent lawful gambling exemptions simplify compliance with and enforcement of lawful gambling and reduce administrative burden, and if any updates should be considered.

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[i] State of Minnesota Gambling Control Board, *Annual Report: Fiscal Year 2023* (November 10, 2023), 2, 13, https://mn.gov/gcb/publications/reports/.

[ii] Ibid, 7, 12.

[iii] For a summary of Minnesota lawful gambling taxes and example calculations, see Alexandra Haigler, *Gambling Taxes*, (Minnesota House Research Department, February 2020), https://www.house.mn.gov/hrd/pubs/gambtax.pdf. Note that Minnesota Statutes, section 297E.02, subdivision 6(b) exempts sports-themed tipboards from both the flat tax and combined net receipts tax.

[iv] For a more detailed history of lawful gambling in Minnesota, see John Williams, *Gambling in Minnesota: A Short History* (Minnesota House Research Department, March 2005), https://www.lrl.mn.gov/docs/2005/other/050336.pdf.

[v] Gambling Control Board, *Annual Report*, 1.

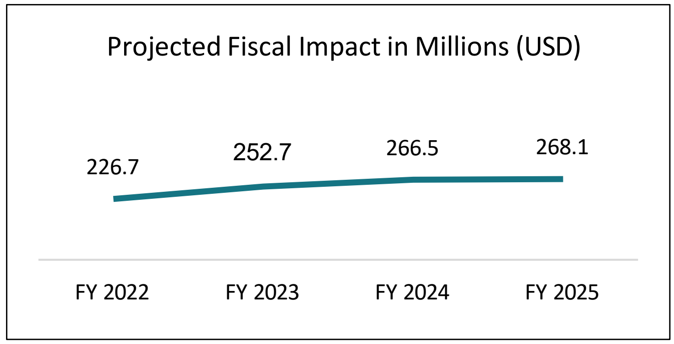
[vi] Minn. House, Hearing on H.F. 97 before the House Comm. on Governmental Operations and Veterans Affairs Policy, 81st Minn. Leg., Reg. Sess. (February 15, 1999), available at: https://www.lrl.mn.gov/media/file?mtgid=810423; Minn. House, Hearing on H.F. 4127 before the House Comm. on Ways and Means, 81st Minn. Leg., Reg. Sess. (March 23, 2000), available at https://www.lrl.mn.gov/media/file?mtgid=812518.

Working Family Credit

Tax Expenditure Initial Review - TEB 1.90

Tax Expenditure Facts

Year Enacted	1991
Statute	Minn. Stat § 290.0671
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	$227,191,168 - Tax Year 2020
Latest Claims Estimate	371,570 - Tax Year 2020
Expiration Date	None



Tax Expenditure Description

The Minnesota working family credit is a refundable credit against the individual income tax allowed to taxpayers who are eligible for the Federal earned income credit. To qualify, the taxpayer (or spouse) must have income from wages or self-employment. A taxpayer is not eligible if investment income exceeds a specified amount ($11,000 for tax year 2023). Although the Minnesota working family credit generally uses the same eligibility requirements and definitions as the Federal earned income credit, except for income limits and the required use of a social security number, the calculation of the state credit is separate.[*]

Additional Background Information

This tax credit is administered by the Department of Revenue. Beneficiaries of this tax expenditure are individuals residing in Minnesota. A part-year resident can apply for a partial credit according to rates specified in law.[1] The state fund impacted by this tax expenditure is the state General Fund.

Proposed Tax Expenditure Objective for Consideration

The objective of the working family credit is to encourage work and help families raise their income above the poverty guideline levels**.**

Sources

The proposed tax expenditure objective is adopted from A Review of Selected Tax Expenditures by the Minnesota House Research Department in 2013.[2]

Other Considerations Regarding the Proposed Tax Expenditure Objective

Minnesota House Research cited the same proposed tax expenditure objective in its 2016 report, the Federal Earned Income Tax Credit and the Minnesota Working Family Credit, and in its 2022 report, the Working Family Credit and Federal Earned Income Credit.[3],[4]

[*] The description from the 2022 Tax Expenditure Budget published by DOR has been updated by the LBO to account for law changes since the original publication of this document.

Descriptions to the intent of this tax credit in committee by legislative members align with the proposed tax expenditure objective.[5]

The proposed objective is also reconciled on the Federal level. The report published by House Committee on Budget of US Congress, The Earned Income Tax Credit Boosts Work, Reduces Poverty, and Provides Other Benefits for Working Americans, shared the similar objective.[6] Numerous academic studies and evaluations by other States also collaborated with the proposed sentiment.

Potential Metrics and Performance Measures

The Commission can consider an incidence analysis to understand the distribution of beneficiaries throughout the state, studying the variance across income, demographic characteristics (family size, family type), and geography.

Another potential metric is to examine how the poverty level and labor participation rate evolved over time in relation to the participation rate of working family credit recipients.

Economic modelling can be applied to study the short term and long term economic and fiscal impacts of the working family credit.

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[1] Minnesota Statutes 2021, section 290.06 subdivision 2c(e)

[2] Dalton, P, Manzi, N and J, Michael. (2013). *A Review of Selected Tax Expenditures*. St. Paul: Research Department of the Minnesota House of Representatives

[3] Manzi, N and J, Michael. (2016). *The Federal Earned Income Tax Credit and the Minnesota Working Family Credit*. St. Paul: Minnesota House of Representatives Research Department

[4] Williams, Sean. (2022). *The Working Family Credit and Federal Earned Income Credit*. St. Paul: Minnesota House of Representatives Research Department

[5] Minn. House. Hearing on H.F. 516 before the House Tax Committee on Taxes, 90th Minn. Leg., Reg. Sess. (Feb. 19, 2017), available at: https://www.house.leg.state.mn.us/hjvid/90/889769 (video)

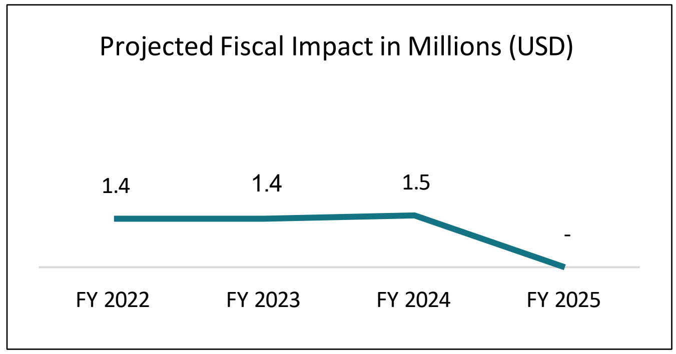
[6] Yarmuth, J (2018). *The Earned Income Tax Credit Boosts Work, Reduces Poverty, and Provides Other Benefits for Working Americans*. Washington DC: Committee on the Budget of U.S. House of Representatives

Beginning Farmer Management Credit

Tax Expenditure Initial Review - TEB 1.103

Tax Expenditure Facts

Year Enacted	2017
Statute	Minn. Stat. § 290.06, Subd.38
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	$472,457 - Tax Year 2020
Latest Claims Estimate	382 - Tax Year 2020
Expiration Date	2030



Tax Expenditure Description

A beginning farmer may claim a nonrefundable credit for participating in a financial management program approved and certified by the Minnesota Rural Finance Authority. The credit is equal to the cost of participating in the program, up to $1,500 per year. The credit may be taken for up to three years while the farmer is in the program. Any unused credit may be carried forward for up to three years. The credit was enacted in 2017 and will expire after 2030. Approximately 370 returns claimed this credit in tax year 2020.

Additional Background Information

This tax expenditure is administered by Rural Finance Authority. Beneficiaries of this tax expenditure are the beginning farmers residing in Minnesota. The state fund impacted by this expenditure is the State General Fund.

Proposed Tax Expenditure Objective for Consideration

The objective of the beginning farmer management credit is to incentivize beginning farmers to participate in a financial management program approved by the Rural Finance Authority to improve the farming operation success rate in the state of Minnesota.

Sources

The proposed tax expenditure objective was informed by the relationship of the beginning farmer management credit to the beginning farmer incentive credit. Further, a review of academic literature suggests that improved business planning[7] and financial management programs[8] result in higher profitability and financial efficiency for beginning farmers. The logic implied by these studies informs the drafting of the proposed tax expenditure objective, assuming this aligns with the intention of the legislature.

A possible metric for Minnesota's Beginning Farmer Management Credit includes an incidence analysis to understand the distribution of beneficiaries throughout the state, studying the variance across demographics of beginning farmers, experience levels, and locations.

An effectiveness study can be conducted to examine whether participation in financial management programs selected by the Rural Finance Authority led to the successful operations of beginning farmers.

An analysis of registration enrollment for financial management programs approved by the Rural Finance Authority can be performed to gauge whether this incentive has increased participation in the education programs.

Nebraska requires financial management education programs for beginning farmers applying for a beginning farmer tax credit. An evaluation of that program by the state's Legislative Auditor reports on the number of claims submitted and the total dollar value of approved claims[9]. As participation in the financial management program is required to qualify for the larger Beginning Farmer Tax Credit, it is difficult to assess whether enrollment rates in the education program are impacted by the financial management program credit.

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[7] Mishra, A., Wilson, C., & Williams, R (2009). Factors affecting financial performance of new and beginning farmers. Agricultural Finance Review, Vol. 69 pages 160-179

[8] Katchova, A.L. and R. Dinterman. (2018). Evaluating Financial Stress and Performance of Beginning Farmers during the Agricultural Downturn. Agricultural Finance Review, Vol.78

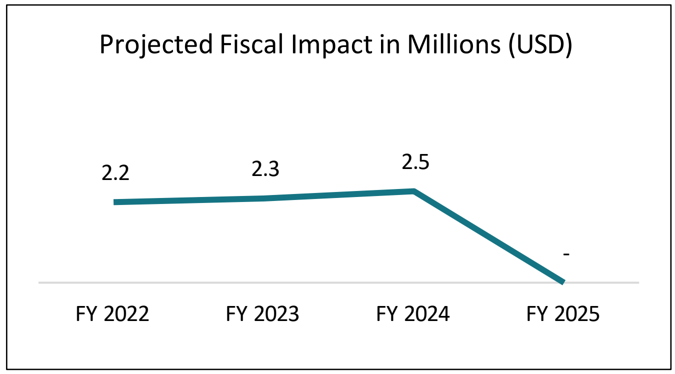
[9] Office of the Legislative Auditor (2018) The Beginning Farmer Tax Credit Act: Performance on Selected Metrics. Lincoln. Performance Audit Committee – Nebraska Legislature.

Beginning Farmer Incentive Credit

Proposed Tax Expenditure Objective Review - TEB 1.104

Tax Expenditure Facts

Year Enacted	2017
Statute	Minn. Stat § 290.06, Subd. 37 and 41B.0391
Tax Type	Individual Income Tax
Provision Type	Credit
Latest Fiscal Impact Estimate	$2,454,443 – Tax Year 2020 *Projections pre-sunset extension.
Latest Claims Estimate	620 – Tax Year 2020
Expiration Date	2030



Tax Expenditure Description

A nonrefundable credit is available to taxpayers who sell or rent agricultural assets to a beginning farmer. The credit equals one of the following:

- 8 percent of the sale price or market value of the asset, up to $50,000.
- 10 percent of the gross rental income in each of the first three years of a rental agreement, up to $7,000 per year; or
- 15 percent of the cash equivalent of the gross rental income in each of the first three years of a rent-share agreement, up to $10,000 per year.

Any unused credit may be carried forward for up to 15 years. The total value of credits is capped at $6.5 million for 2023 and $4 million in later years. The credit was enacted in 2017 and will expire after 2030.

Additional Background Information

This tax expenditure is administered by Rural Finance Authority. Beneficiaries of this tax expenditure are asset owners residing in Minnesota, including individual farmers, "pass through" entities, and partnerships. A nonresident or part-year resident can apply for a portion of the credit, using the percentage calculated in section 290.06, subdivision 2c, paragraph (e). The state fund impacted by this tax expenditure is the State General Fund.

Proposed Tax Expenditure Objective for Consideration

The objective of the beginning farmer incentive credit is to lower the barrier of entry for a beginning farmer and make them more financially competitive.

Sources

The objective is described in testimony of HF608 by the bill's author, Representative Nels Pierson, before the twenty-sixth meeting of the House Tax Committee during 2017-2018 session.

Other Considerations Regarding Proposed Tax Expenditure Objective

Nebraska enacted a Beginning Farmer Tax Credit Act[10] in 1999, preceding Minnesota's program. The intent of Nebraska's legislation is described in the enacting language and coincides with the proposed tax expenditure objective proposed in this review. In addition, evaluation studies published by the Iowa Department of Revenue in 2015[11] and 2020[12] provided a comparable rationale for the objectives of a beginning farmer tax credit.

Potential Metrics and Performance Measures

Evaluations of similar tax credits include an incidence analysis to understand the distribution of beneficiaries throughout the state, studying the demographics across different asset owners, asset types, and locations. The 2020 Iowa Department of Revenue evaluation of a similar tax expenditure compared outcomes of participants in the beginning farmer program to outcomes for beginning farmers who did not participate in the tax credit program. The Iowa study evaluated outcomes across three measures:

- Farm income
- Ratio of farm expenses to net income'
- Continued engagement in farming

Evaluations of the credit could also center around survey data of program participants to determine the level of which the landowner was influenced to sell or rent their land to a beginning farmer based on the financial incentive received from the tax credit.

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[10] (1999) State of Nebraska Legislative Bill 630

[11] Girardi, A. (2015). *Beginning Farmer Tax Credit Program Tax Credit Program Evaluation Study*. State of Iowa: Tax Research and Program Analysis Section Iowa Department of Revenue.

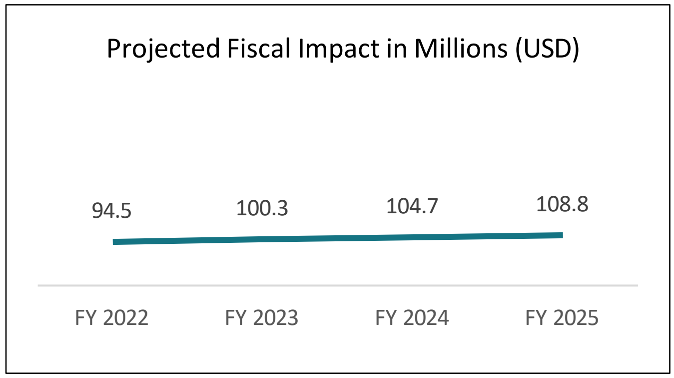
[12] Montgomery, E. (2020). *Beginning Farmer Tax Credit Program Tax Credits Program Evaluation Study*. State of Iowa: Tax Research and Program Analysis Section Iowa Department of Revenue.

Research and Development Credit

Tax Expenditure Initial Review - TEB 1.86 and 2.27

Tax Expenditure Facts

Year Enacted	1981
Statute	Minn. Stat. Section 290.068
Tax Type	Corporate Franchise Tax Credit, Individual Income Tax Credit
Provision Type	Credit
Latest Fiscal Impact Estimate	$56,359,000 -Tax Year 2019
Latest Claims Estimate	Direct measure of this estimate not available
Expiration Date	None



Tax Expenditure Description

Minnesota allows businesses conducting research and development within Minnesota to claim a nonrefundable credits against their corporate franchise taxes or individual income taxes (for pass-through tax entities, such as LLCs and S corporations). Expenditures include wages, costs of supplies, computer costs, 65 percent of contract costs paid to others for doing research, and certain contributions to nonprofit organizations engaged in research and development within Minnesota.

The tax credit is based on the excess of current-year research expenditures over a calculated base amount, but in most cases 50 percent of current-year research expenditures are eligible for the credit. The credit is 10 percent of the first $2 million of eligible expenditures and 4 percent of the excess over $2 million. Any credit that exceeds liability can be carried forward up to fifteen years.

Additional Background Information

This tax expenditure is structured in line with the Federal R&D credit in Section 41 of the Internal Revenue Code[13].

This tax expenditure is administered by the Department of Revenue. Beneficiaries of this tax expenditures are Individual taxpayers and Corporate "C-Corps" taxpayers. The state fund impacted by this tax expenditure is the State General Fund.

Proposed Tax Expenditure Objective for Consideration

The objective of Research and Development Credit is to create or retain jobs, increase research activity, and attract or retain business in Minnesota.

Sources

The Office of Legislative Auditor proposed the above statement as individual purposes in its 2017 Minnesota Research Tax Credit Evaluation Report[14]. The report was part of an evaluation of economic development incentive programs required by Minnesota session law[15].

Other Considerations Regarding the Proposed Tax Expenditure Objective

The proposed objective is in line with the policy intents offered by Congressional Research Services of US Congress in their 2022 report, Federal Research Tax Credit: Current Law and Policy Issues[16].

The Minnesota House Research Department states that the R&D credit serves an "economic development" purpose in its 2017 publishing, Short Subjects: Minnesota Research and Development Tax Credit[17].

The Federal R&D credit was enacted in 1981 and Minnesota was the first state to follow suit. The background of economic conditions during the early 1980's linked the rationale of the R&D credit to the economic theory of the Cobb-Douglas production Model[18]. One implication of the model is that innovation is the engine for growth[19]. Numerous academic studies reviewed by the LBO imply the same sentiment. Therefore, another potential purpose for the tax credit is to support innovation across industries in Minnesota.

Potential Metrics and Performance Measures

A possible metric for this tax expenditure includes an incidence analysis to understand the distribution of beneficiaries throughout the state, studying the variance across organizations of varying sizes, and industry.

Another potential metric is a Benefit-to-Cost Ratio, a comparison of the total R&D spending attributable to the credit's total revenue loss.

An effectiveness study can be conducted to examine whether a business entity is more likely to conduct R&D in Minnesota after taking the R&D credit into consideration.

Economic modelling can be applied to study the short term and long term economic and fiscal impacts of the tax credit.

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[13] 26 U.S.C. § 41

[14] Office of the Legislative Auditor. (2017). *Minnesota Research Tax Credit*. St. Paul: State of Minnesota

[15] Laws of Minnesota 2015, chapter 77, article 2, section 1, subdivision 2.

[16] Guenther, G. (2022). *Federal Research Tax Credit: Current Law and Policy Issues.* Washington D.C.: Congressional Research Service.

[17] Michael, J. (2017). *Short Subjects: Minnesota Research and Development Tax Credit*. St. Paul: Research Department of the Minnesota House of Representatives

[18] Aghion, Durlauf, Aghion, Philippe, Durlauf, Steven N, & ScienceDirect. (2005). *Handbook of economic growth. Volume 1B* (1st ed., Handbooks in economics bk. 22). Amsterdam: Elsevier.

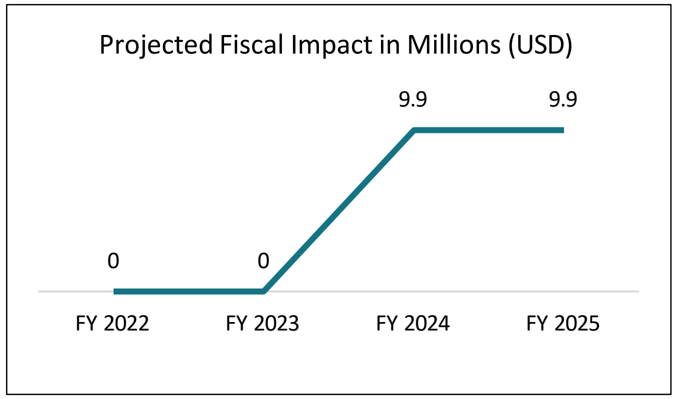
[19] Verba, M. (2019). *Growth and Innovation in the presence of Knowledge and R&D accumulation Dynamics*. Economics of Innovation and New Technology

Housing Contribution Credit

Tax Expenditure Initial Review - TEB 1.97, 2.32, and 12.09

Tax Expenditure Facts

Year Enacted	2021
Statute	Minn. Stat. § 290.0683; 462A.40; 297I.20
Tax Type	Individual Income, Corporate Franchise, Insurance Premiums
Provision Type	Nonrefundable Credit
Latest Fiscal Impact Estimate	Data not available
Latest Claims Estimate	Data not available
Expiration Date	December 31, 2028



Tax Expenditure Description

A nonrefundable credit is allowed for contributions to a designated account in the Housing Development Fund administered by the Minnesota Housing Finance Agency (MHFA). The account is to be used for grants and loans for low and moderate-income housing developments.

The credit is equal to 85 percent of contributions of at least $1,000 but not more than $2 million. Any unused credit may be carried over for up to 10 years. Total credits are limited to $9.9 million in each year. The credit was enacted in 2021 and is effective for tax years 2023 through 2028.

Note: The estimates shown on the graph are the total projected credits to be claimed against the corporate franchise tax, the individual income tax, and the insurance premiums tax.

Additional Background Information

An individual or business that contributes to the Minnesota Housing Tax Credit Contribution Account can reduce their income, franchise, or insurance premium tax liability by up to 85 percent of the contribution amount. The taxpayer may indicate that a contribution is intended for a specific qualified project.[20]

This expenditure reduces the amount of income tax that is collected. Income tax revenue is deposited in the state General Fund as provided by Minn. Stat. 290.62.

MS 462A.40, subd. 5 requires the MHFA to submit a report by January 15 of each year on the tax credits and financing provided in the previous fiscal year.

Proposed Tax Expenditure Objective for Consideration

The objective of the Minnesota Housing Tax Credit (Minn. Stat. 290.0683) is to increase the development and availability of affordable housing to persons and families of low and moderate incomes in Minnesota.

Sources

This statement was taken from companion bills SF 1866 and HF1971, as introduced (2021). Bill sections one through three are functionally identical to the language that was ultimately enacted in Laws 2021 and codified in statute. Section four of SF 1866 / HF1971 includes the statement shown above and indicates that the statement is intended to fulfill the requirements of MS 3.192 (Requirements for New or Renewed Tax Expenditures). Although there are some technical differences between SF 1866 / HF1971 and statute such as contribution thresholds, the credit is structured the same.

In addition, bill authors emphasized at Tax Committee hearings for SF 1866 and HF 1971 that the proposed legislation was intended to address a shortage of affordable housing in Minnesota.[21]

Other Considerations Regarding Proposed Tax Expenditure Objective

- Bills introduced in 2019 (HF1156/SF404) and 2018 (HF4072/SF3301) contain language similar to SF 1866 and current statute, including objectives that are identical to the statement shown above.
- Bill author testimony for SF 1866 and HF 1971 indicates that bill language was modeled after the North Dakota Housing Incentive Fund Tax Credit. This incentive was created in 2011 to help address an affordable housing shortage in western North Dakota.
- This credit was enacted in Laws 2021, First Special Session. A statement of intent was not included in Laws 2021 or the corresponding omnibus bill.[22]
- Other states that offer housing tax credits generally do so in order to encourage the development of affordable housing. For example, the stated purpose of the recently passed Kansas Housing Investor Tax Credit Act is to "bring housing investment dollars to communities lacking adequate housing".[23]

Potential Metrics and Performance Measures

MS 462A.40, subd. 5 requires the MHFA to provide a report by January 15 of each year that includes "a breakdown of the tax credits, grants, and loans by region of the state. The report shall also include information on planned financing in the current fiscal year." Staff anticipate using MHFA report data along with other state/Federal data to compare the historical rate of affordable housing development in Minnesota with the rate of development after the tax credit has been effective for three or more years, particularly the development of housing units that meet the criteria specified in MS 462A.40, subd. 2. A performance review could also compare geographical housing needs with the locations of tax credit supported development, depending on the availability of demographic and survey data – is the credit improving the allocation of affordable housing?

Contact Information and Disclaimer

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[20] MS 462A.40, Subd. 2-3 define what funds deposited in the Minnesota Housing Tax Credit Contribution Account can be

used for. https://www.revisor.mn.gov/statutes/cite/462A.40#stat.462A.40.2.

[21] Senate Tax Committee hearing, March 23, 2021. SF 1866 is discussed at 21:50 of the audio, available at www.senate.mn or the following direct link. House Tax Committee hearing, March 25, 2021. HF 1971 is discussed at 1:15 of the audio, available at www.house.leg.state.mn.us or the following direct link.

[22] See Minnesota Laws 2021, First Special Session chapter 14, article 1, sections 13, 15, and 16.

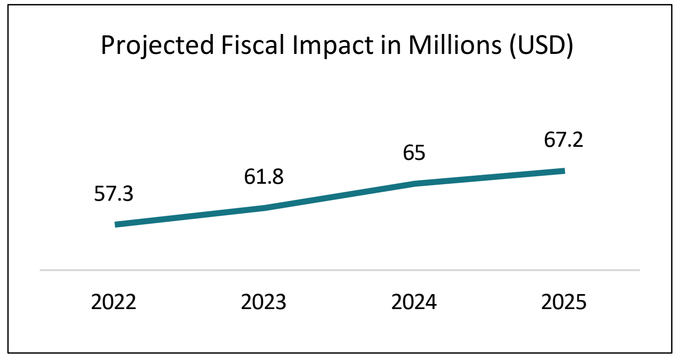
[23] Summary of Kansas HB 2237, available online at http://www.kslegislature.org/li/b2021_22/measures/documents/summary_hb_2237_2022.

Telecommunications Equipment

Tax Expenditure Initial Review - TEB 4.21

Tax Expenditure Facts

Year Enacted	2001
Statute	MS Section 297A.68, Subd. 35a
Tax Type	General Sales and Use Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	Data not available
Latest Claims Estimate	Data not available
Expiration Date	None



Tax Expenditure Description

An exemption from the sales and use tax is allowed for telecommunications, cable television, and direct satellite equipment purchased or leased for use directly by a telecommunications, cable television, or direct satellite service provider in providing telecommunications services that are ultimately sold at retail. The exemption applies regardless of whether purchases are made by the owner, a contractor, or a subcontractor.

The exemption includes machinery, equipment, and fixtures used in receiving, initiating, amplifying, processing, transmitting, retransmitting, recording, switching, or monitoring telecommunications services. It also includes repair and replacement parts and accessories for qualifying equipment. The exemption does not include wire, cable, or poles.

This exemption was enacted in 2001. In 2013, the exemption was repealed, effective July 1, 2013. In 2014, the exemption was reinstated, effective April 1, 2014. The exemption was expanded to include fiber and conduit in 2017.

Additional Background Information

This tax expenditure provides a specific economic benefit to telecommunications and pay television service providers.

An internet service provider does not provide telecommunications or pay television service as defined in MS 297A.61, Subd. 24-25 and therefore cannot purchase equipment exempt from the sales tax. When machinery and equipment is purchased that can be used in providing internet service as well as telecommunications and pay television services, the exemption applies only if the taxpayer can document that the machinery and equipment will be used principally in the providing of telecommunications or pay television services.[24]

The Minnesota Department of Revenue administers the sales and use tax. A purchaser must provide a completed certificate of exemption to the seller in order to claim the exemption.

This tax expenditure reduces the amount of sales tax that is collected. Sales tax revenue is deposited in the state General Fund except as provided by MS 297A.94.

Proposed Tax Expenditure Objectives for Consideration

The tax expenditure objective of the Telecommunications Equipment Exemption (MS 297A.68, subd. 35a) is to reduce potential tax pyramiding and promote transparency in the tax system by exempting telecommunications equipment that is used to provide taxable telecommunications services.

The tax expenditure objective of the 2017 amendment to the Telecommunications Equipment Exemption (MS297A.68, subd. 35a) that expanded the definition of "telecommunications or pay television machinery and equipment" to include fiber and conduit is to increase the deployment and accessibility of broadband internet service in Minnesota.

Sources

The tax expenditure objective statement for the general exemption is based on testimony from House and Senate Tax Committee hearings for companion bills HF2023 and SF1819, which were ultimately included in the 2001 tax omnibus bill HF 1.[25]

The proposed tax expenditure objective statement for the 2017 amendment is based on author testimony from House and Senate Tax Committee hearings for companion bills SF 955 and HF1250, which were ultimately included in the 2017 omnibus tax bill HF 1.[26]

Other Considerations Regarding the Proposed Tax Expenditure Objective

The legislature created a working group in 1997 to study the taxation of telecommunications services. The final report published in 1999 provided eight recommendations, including a sales tax exemption for telecommunication equipment used in providing taxable telecommunication services. The report contended that an exemption would (a) reduce potential tax pyramiding, (b) better align the Minnesota sales tax with the economic definition of a consumption tax, and (c) "send a welcoming message to telecommunication firms looking to locate in this state".[27]

Potential Metrics and Performance Measures

Staff anticipate that a qualitative assessment will be needed to determine if the tax expenditure is meeting its objective. This type of analysis may include an overview of consumption tax policy principles, the differences between a sales tax and gross receipts tax, the effects of potential tax pyramiding (such as changes in market behavior, embedded taxes, and cross-border effects), and the extent to which this expenditure helps align statutory sales tax rates with effective sales tax rates, if measurable.

An administrative and technical review may also be necessary based on the stated objective of the 2017 amendment referenced above. If the intent of the amendment was to expand broadband internet access, then the expenditure may need to be clarified to ensure that the exemption of fiber and conduit applies to internet service providers as well as telecommunications and pay television providers. Note that companion bills SF 3480 and HF 4422 introduced during the 2022 session proposed to specifically exempt fiber and conduit purchases made by a broadband or internet service provider, but the bill was not enacted.

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[24] See Revenue Notice #2-14 available at the Minnesota Department of Revenue website, https://www.revenue.state.mn.us/revenue-notice/02-14-sales-and-use-tax-exemption-purchases-telecommunications-equipment-internet.

[25] House Sales and Income Tax Division hearing (March 29, 2001). Audio recording available at https://www.lrl.mn.gov/media/file?mtgid=821004; Senate Income and Sales Tax Budget Division hearing (April 4, 2001). Audio recording available at https://www.lrl.mn.gov/media/file?mtgid=821052.

[26] Senate Tax Committee Hearing (February 23, 2017). SF 955 is discussed at 1:40 of the audio recording, available online at https://mnsenate.granicus.com/player/clip/1339?view_id=2&redirect=true&h=07b2ceec9c0962b8b3bf8b10604fc812; House Tax Committee Hearing (February 23, 2017). HF 1250 is discussed at 43:23 of the audio recording, available online at https://www.house.leg.state.mn.us/Committees/minutes/90023/56877.

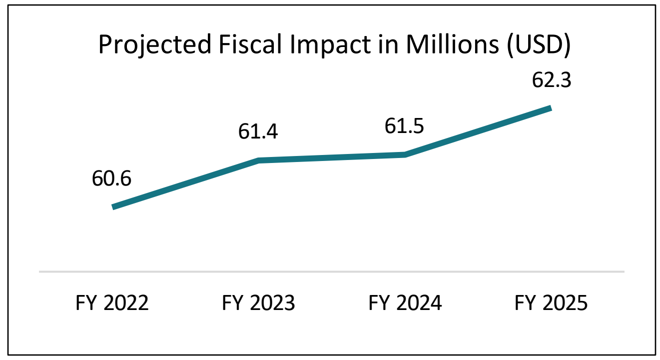
[27] Report of the Working Group on Taxation of Telecommunication Services (February 18, 1999). Available at the Minnesota Reference Library, https://www.lrl.mn.gov/.

Farm Machinery Exemption

Tax Expenditure Initial Review - TEB 4.39

Tax Expenditure Facts

Year Enacted	1981
Statute	Minn. Stat. § 297A.69, Subd. 4(1), and 297A.61, Subd. 12
Tax Type	General Sales and Use Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	Data not available
Latest Claims Estimate	Data not available
Expiration Date	None



Tax Expenditure Description

All farm machinery is exempt from the Minnesota sales and use tax. Qualifying farm machinery includes machinery, equipment, implements, and accessories used directly and principally in the production for sale of agricultural products, including livestock. Irrigation systems also qualify for exemption.

A reduced rate for farm machinery was first enacted in 1981 at 4 percent when the general rate was 5 percent. In 1985, the rate was reduced to 2 percent, and in 1991 it was increased to 2.5 percent when the general rate was increased by 0.5 percent. Used farm machinery was exempted in 1994 as a temporary provision, and the exemption was made permanent in 1997. In 1998, the rate on new equipment was phased out over two years, with the full exemption effective on July 1, 2000. The definition of farm machinery eligible for exemption has been expanded several times and was last modified in 2006.

Additional Background Information

This tax expenditure provides a specific economic benefit to agricultural producers who purchase qualifying farm machinery.

The Minnesota Department of Revenue administers the sales and use tax. A purchaser must provide a completed certificate of exemption to the seller in order to claim the exemption.

This tax expenditure reduces the amount of sales tax that is collected. Sales tax revenue is deposited in the state General Fund except as provided by MS 297A.94.

Proposed Tax Expenditure Objective for Consideration

The objective of the farm machinery exemption is to reduce potential tax pyramiding and promote transparency in the tax system by exempting machinery and equipment used directly in the agricultural production of tangible personal property ultimately intended to be sold at retail.[28]

Sources

The tax expenditure objective for consideration is informed by a review of statute language including MS 297A.69 and 297A.61. Statute, originating bills, committee hearings, and available legislative documentation do not directly state a purpose for the farm machinery exemption. Staff did not find an adopted objective statement in review of similar exemptions in other states.

Other Considerations Regarding Proposed Tax Expenditure Objective

Farm machinery, replacement parts, fertilizer, and other agricultural items are commonly exempted from sales tax in other states; a recent Colorado review identified 38 states that have total or partial exemptions for farm equipment.[29] The definition of agricultural "machinery" or "equipment" varies from state-to-state, but generally the item must be used directly and principally in producing tangible personal property intended for retail sale in order to qualify, similar to the Minnesota exemption. Items that are not directly used in the production process are generally taxable, suggesting that most states offer these types of exemptions primarily to reduce tax pyramiding and increase transparency.

The Commission may also want to consider if a primary or secondary objective of this expenditure is to provide a specific economic benefit to agricultural producers, for instance to support farming operations generally or to help small farmers replace worn-out equipment.

Potential Metrics and Performance Measures

Staff anticipate that a qualitative assessment will be needed to determine if the tax expenditure is meeting its objective. This type of analysis may include an overview of consumption tax policy principles, the differences between a sales tax and gross receipts tax, the effects of tax pyramiding (such as changes in market behavior, embedded taxes, and cross-border effects), and the extent to which this expenditure helps align statutory sales tax rates with effective sales tax rates, if measurable.

Stakeholder surveys and Department of Revenue data may help inform a cost-benefit analysis. For example, survey responses to a Colorado review of farm equipment exemptions indicated that agricultural producers found the exemption "impactful for purchases of more expensive equipment, such as tractors and combines," which was balanced against forgone state and local sales tax revenue.[30]

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[28] Tax pyramiding refers to the imposition of a sales tax at one or more stages of production and distribution before the final (retail) sale to consumers.

[29] Office of the State Auditor. (2022). Farm Equipment and Parts Exemption Evaluation Summary. Denver: State of Colorado. https://leg.colorado.gov/sites/default/files/te5_farm_equipment_parts_exemption.pdf

[30] Ibid.

Building Materials for Residences of Disabled Veterans

Tax Expenditure Initial Review - TEB 4.54

Tax Expenditure Facts

Year Enacted	1971
Statute	Minn. Stat. § 297A.71, Subd. 11
Tax Type	General Sales and Use Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	Direct measure of this estimate not available
Latest Claims Estimate	Direct measure of this estimate not available
Expiration Date	None

Estimated fiscal impact is less than $50,000 per year through fiscal year 2025.

Tax Expenditure Description

Building materials used to construct or remodel the residence of a disabled veteran are exempt from the sales and use tax. The exemption applies if the project is financed in whole or in part by the U.S. Government in accordance with United States Code, Title 38, Sections 2101 to 2105.

Additional Background Information

United States Code, Title 38, Sections 2101 to 2105 are administered as Specially Adapted Housing (SAH) grants and Special Home Adaptation (SHA) grants by the United States Department of Veteran's Affairs. The Minnesota Department of Revenue administers the sales tax exemption on a refund basis.31

Veterans with qualifying service-connected disabilities who are awarded SAH/SHA grant money to construct or modify their permanent home are eligible for the state sales tax exemption.[32] SAH and SHA grants are not subject to Federal or state income taxes.[33]

This tax expenditure reduces sales tax revenues. Sales tax revenue is deposited in the state General Fund except as provided by MS 297A.94.

Proposed Tax Expenditure Objective for Consideration

The objective of the building materials exemption for residences of disabled veterans (Minn. Stat. 297A.71, subd. 11) is to provide specific sales and use tax relief to disabled veterans who have been awarded a Federal grant for the construction or remodeling of their homes, ensuring that disabled veterans receive the full financial benefit of the Federal program.

Sources

This statement was adapted from Washington State statute[34]. Washington offers a similar tax expenditure that includes legislative findings and a statement of intent section written into statute.

Other Considerations Regarding Proposed Tax Expenditure Objective

Enacting legislation Laws 1971 Regular Session does not include a statement of purpose. This expenditure has not been significantly modified since initial enactment.[35]

A statement of purpose was not found in applicable committee meeting minutes. Audio or other media from this time is not available.

The Veteran's Homestead Exclusion (TEB # 13.02), which also provides tax relief for disabled veterans, includes a purpose statement in statute. "The purpose of this provision of law providing a level of homestead property tax relief for veterans with a disability, their primary family caregivers, and their surviving spouses is to help ease the burdens of war for those among our state's citizens who bear those burdens most heavily." [36]

Potential Metrics and Performance Measures

Comparing the annual number or amount of refunds issued by the Minnesota Department of Revenue for qualified building material costs with the number or amount of adapted housing grants awarded by the United States Department of Veteran's Affairs to Minnesota veterans may help identify the extent to which the tax exemption is being utilized in conjunction with Federal grants.

A survey among eligible population may also indicate public awareness of the tax benefit and likelihood of utilization.

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[31] Minnesota Rules 8130.6600 outlines the refund procedure for this exemption. https://www.revisor.mn.gov/rules/pdf/8130.6600/2022-06-09%2009:08:07+00:00

[32] Detailed program requirements can be found online at https://www.va.gov/housing-assistance/disability-housing-grants/ and https://www.benefits.va.gov/HOMELOANS/documents/docs/sah_handbook_for_design.pdf.

[33] See Minnesota Tax Expenditure Budget (2022) item 1.18 for more information.

[34] See Revised Code of Washington title 82 chapter 08 section 0207

[35] Minnesota Laws 1971, Chapter 124. Available online at https://www.revisor.mn.gov/laws/1971/0/Session+Law/Chapter/124/pdf/.

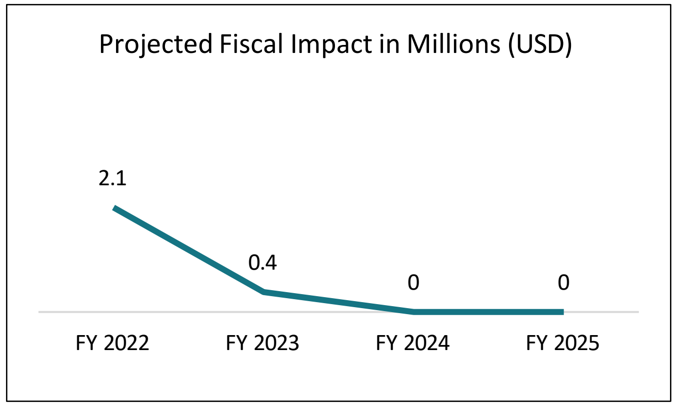
[36] Minnesota Statutes 2021, section 273.13 subdivision 34(l)

Construction Materials for Certain City Projects

Tax Expenditure Initial Review - TEB 4.73

Tax Expenditure Facts

Year Enacted	2012
Statute	Minn. Stat. § 297A.71, Subd. 44 and 297A.9905
Tax Type	General Sales and Use Tax
Provision Type	Exemption – Sales to Particular Purchasers
Latest Fiscal Impact Estimate	Direct measure of this estimate not available
Latest Claims Estimate	Direct measure of this estimate not available
Expiration Date	None



Tax Expenditure Description

Materials and supplies used or consumed in, and equipment incorporated into, the construction or improvement of a capital project of regional significance funded partially or wholly by a city of the first class are exempt. To qualify for this exemption, the project must be the construction, expansion, or renovation of a sports facility or convention or civic center and have a total construction cost of at least $40 million within a 24-month period. Funding must be drawn from the excess revenues generated by imposition of a local tax on retail sales.

Additional Background Information

Contractors engaged in eligible capital projects are direct beneficiaries of this exemption. Local municipalities are indirect beneficiaries of this exemption, assuming that qualifying sales tax exemptions are considered into lower construction bid entries for eligible projects. A reduction in sales and use tax receipts impacts the state's General Fund. The collection of sales and use tax is administered by the Department of Revenue.

Proposed Tax Expenditure Objective for Consideration

The objective of the sales tax exemption for construction materials for certain city projects is to provide an indirect means of assistance to local governments for capital projects funded wholly or partly by excess local tax revenues imposed under special law.

Sources

An explicit tax expenditure objective was not identified in the legislative record. However, an author's description to this exemption in 2017 describes the sales tax exemption as a means to help fund a city project[37]. Additionally, the state of Pennsylvania adopted a similar objective statement for a sales tax exemption on machinery and construction equipment used in a construction contract with a governmental unit including political subdivisions[38].

Other Considerations Regarding Proposed Tax Expenditure Objective

In 2017, MS § 297A.71 subd. 44 was amended to provide a sales tax exemption on construction materials, supplies, and equipment to the city of Plymouth to help fund capital improvements to the Plymouth Ice Center. During testimony before the House Tax Committee, the author of the original amendment, describes the amendment as a means of helping the city fund repairs in order to meet Federal requirements for refrigerant coolants and energy systems. This language was adopted into the 2017 omnibus tax bill, where the sales tax exemption was extended to the construction of a stadium located on land which is now Allianz field in St. Paul[39].

In 2012, this exemption was included in the legislation the included the construction of the U.S. Bank Stadium. Discussion in committee hearings on that specific bill references similar tax policy applying to the development of Target Field[40].

In 2021, the Office of the State Auditor of Colorado evaluated a similar sales tax exemption which applies more generally to contractors and subcontractors performing construction services for certain tax-exempt entities. A potential objective offered for consideration was "to avoid applying sales and use taxes to contractors' purchases of construction and building materials when completing projects for tax-exempt entities.[41]"

An analysis of this expenditure should also consider a broader policy objective of attracting and stimulating economic benefits towards the geographic region where such capital projects are pursued.

Potential Metrics and Performance Measures

The following are approaches taken by other state or district offices to evaluate the effectiveness or impact of a sales tax exemption on construction and building materials.

The Office of the State Auditor of Colorado identifies a challenge in evaluating a tax incentive if a quantifiable goal is not stated by the general assembly. Thus, the office relies on a survey of eligible contractors and subcontractors that would presumably file for the tax exemption to assess likelihood of participation and awareness by eligible beneficiaries.

Connecticut's Department of Economic and Community Development reports information limited to the total amount of sales tax revenue forgone for a variety of capital projects approved on the state's behalf[42].

Washington D.C. enacted a sales tax exemption on construction materials to increase the construction and availability of supermarkets within specific wards[43]. The district intended to achieve positive externalities of increased access to nutritious foods leading to positive health outcomes for residents of those wards. A report by the district's office of Revenue Analysis indicates the sum of claims associated with the exemptions and an analysis on the construction of supermarkets in targeted areas of the district. Similar metrics of direct outcomes are repeatable in Minnesota for construction projects. The report identifies challenges in measuring externalities intended by the program.

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[37] Minn. House, Hearing on HF 924 before the House Committee on Taxes, 90th Minn. Leg. Reg. Sess. (Mar. 3, 2017), available at: https://www.house.leg.state.mn.us/hjvid/90/889866 (video)

[38] Office of the Governor. (2022. Executive Budget. Harrisburg: Commonwealth of Pennsylvania.

[39] Laws of Minnesota 2017, 1st Special Session, Chapter 1, Article 3, Section 30.

[40] Minn. Sen., Hearing on S.F. 2391 before the Sen. Comm. on Taxes, 87th Minn. Leg., Reg. Sess. (Apr. 27, 2012), available at: https://www.lrl.mn.gov/media/file?mtgid=870932 (video)

[41] Office of the State Auditor. (2021). Construction and Building Materials Exemption Evaluation Summary. Denver: State of Colorado

[42] Department of Economic and Community Development. (2019). Annual Report. New Haven: State of Connecticut

[43] Office of Revenue Analysis. (2018). Review of Economic Development Tax Expenditures. Washington D.C. Government of District of Columbia.

Appendix F. TERC Meeting September 18, 2024

Commission Member Attendance

Present	Excused
Sen. Ann H. Rest, Chair	Sen. Bill Weber
Rep. Esther Agbaje, Vice Chair	Sen. Steve Drazkowski
Rep. Steve Elkins	
Rep. Jim Joy	
Rep. Greg Davids	
Sen. Matt Klein	
Rep. Aisha Gomez (ex-officio)	
Commissioner Paul Marquart	

Meeting Summary

Chair Rest called the hybrid meeting of the Tax Expenditure Review Commission to order, and a quorum was present. The meeting minutes from August 16, 2024, were approved as presented. The Legislative Budget Office presented five tax expenditure initial reviews. The five initial reviews included in this appendix are:

- **Power Line Credit** (Minnesota Statutes 2024, Sections 273.42 and 273.425)
- **Agricultural Loans** (Minnesota Statutes 2024, Section 287.04(9))
- **Government Housing Programs** (Minnesota Statutes 2024, Section 287.04(6))
- **Bookmobiles** (Minnesota Statutes 2024, Section 297B.03(8))
- **Ready-Mixed Concrete Trucks** (Minnesota Statutes 2024, Section 297B.03(9))

The five tax expenditure initial reviews were presented to the Commission and there were no objections on any of the proposed objectives. Chair Rest informed the Commission that the next meeting would be scheduled for the first week of December to review and discuss the TERC annual report. Chair Rest mentioned the December meeting may be fully remote due to Capitol Room G-15 undergoing technical upgrades.

Commission Motions and Actions

After the presentation of the five new initial reviews for consideration, Representative Agbaje moved to adopt the proposed objectives and directed the Legislative Budget Office to proceed with tax expenditure evaluations in accordance with Minnesota Statutes 2023, section 3.8855. The motion also provided the Legislative Budget Office the ability to make any technical corrections necessary. The motion prevailed.

Commission Revisions to Presented Reviews

The Commission made only one change to the five initial reviews presented by the LBO, requesting that a clarification be added to the Power Line Credit review as to which government entity assesses powerlines.

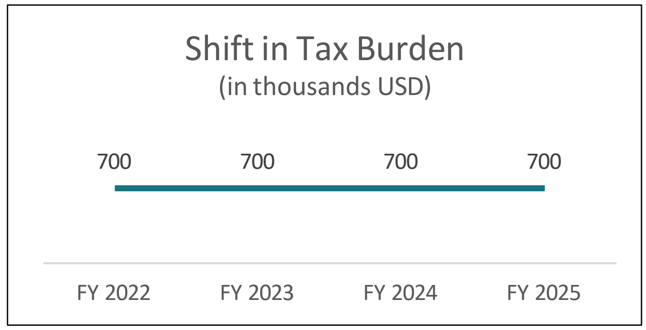
- **Power Line Credit** (Minnesota Statutes 2024, sections 273.42 and 273.425)
    - Technical footnote clarification stating that the Department of Revenue estimates and certifies the market value of power lines.

Power Line Credit

Tax Expenditure Initial Review – TEB 13.10

Tax Expenditure Facts

Year Enacted	1979
Statute	Minn. Stat. § 273.42 and 273.425
Tax Type	Property
Provision Type	Credit
Shift in Tax Burden	$656,358 – Taxes Payable 2024
Claims Estimate	4,100 parcels – 2021
Expiration Date	None



Tax Expenditure Description

The owner of land that is a homestead, agricultural land, residential rental property, or seasonal residential recreational property receives a property tax credit if the property is crossed by an electric transmission line of 200KV or more which was constructed after July 1, 1974. The credit is limited to 20 percent of the gross property tax for the parcel. If the parcel exceeds 40 acres, the maximum credit is 20 percent of a portion of the tax.[i]

Additional Background Information

The power line credit was one of several legislative responses to landowner and activist groups that opposed the routing and construction of a high-voltage transmission lines through western and central Minnesota during the 1970s.[ii] S.F. 896, enacted during the 1977 legislative session, required utilities to make annual payments to landowners on which high-voltage lines were sited, in addition to any negotiated one-time easement payments. The bill also established several policies and procedures regarding the designation of power line routes and eminent domain proceedings.[iii] In 1979, the annual power line payment was converted to a property tax credit.

To receive the credit, a property must be crossed by a transmission line of 200 kilovolts (kV) or greater that was constructed after July 1, 1974, and be classified as one of the property types specified in M.S. 273.42. Qualifying classes of property include:

- Agricultural and Nonagricultural Homesteads
- Nonhomestead Agricultural Land
- Rental Residential
- Commercial and Noncommercial Seasonal Residential Recreational

The credit is funded by 10 percent of property tax receipts on qualifying high-voltage transmission lines.[iv] In cities or townships, an electric transmission line qualifies if construction commenced after July 1, 1974, and it conducts voltage of 200 kV or greater. In unorganized townships, an electric transmission line qualifies if construction commenced after July 1, 1974, the line is longer than 1,500 feet, and it conducts voltage of 100 kV or greater. Qualifying transmission lines in cities and organized townships are taxed at the local rate where they are located; qualifying lines in unorganized townships are taxed at the countywide average rate.

Tax revenue set aside for the credit is apportioned to qualifying properties based on the length of transmission line that crosses the parcel relative to the total length of transmission line that runs through the city, organized township, or all unorganized townships in the county where the property is located.[v] An example calculation taken from the Minnesota Department of Revenue's *Auditor/Treasurer Manual* is shown below.[vi]

Table 1: Power Line Credit in an Organized Township

Row	Calculation	Values
1	Length of transmission line on the property	300 ft
2	Shared right-of-way percent	100%
3	Length of transmission line in the township	12,500 ft
4	Property's portion of the transmission line [Row 1 x Row 2 / Row 3]	2.40%
5	Township's total tax on the transmission line	$30,400
6	10% of tax on the transmission line [Line 5 x 10%]	$3,040
7	Power line credit [Line 4 x Line 6]	$73

The net tax capacity (NTC) of transmission lines within cities and lines of 69 kV and above in organized townships are subject to the state general property tax, including the NTC used to fund the power line credit.[vii]

The total value of the power line credit for taxes payable in 2024 was $656,358 according to Minnesota Department of Revenue property tax data.[viii] The individual value of the power line credit varies by location and over time depending on local or countywide average tax rates, property classification rates, and market values. For reference, the median credit amount for taxes payable in 2024 was $83.25 while the average credit amount was $159.47. The minimum credit amount was $10.04, and the maximum credit amount was $1,999.36.

Beneficiaries of the power line credit include owners of qualifying property crossed by a qualifying transmission line. The method by which the credit is funded effectively shifts property tax liability from owners of qualifying property to owners of other, non-qualifying property types. Revenues from transmission lines subject to the state general property tax are deposited in the state general fund.

Proposed Tax Expenditure Objective for Consideration

The objective of the power line credit is to compensate affected landowners for the negative impacts of having qualifying high-voltage transmission lines on their property.

Sources

Recorded legislative history does not directly identify a public policy objective for the power line credit. The objectives identified in this report were inferred from legislator interviews conducted as part of the Minnesota Powerline Oral History Project (referred to here as Powerline Project) and contemporary legislative publications.[ix] Powerline Project interviews were conducted before the credit was enacted in 1979, but after annual payments from utilities to affected landowners were established in 1977. It is assumed the intent of annual payment mandate was similar to the property tax credit that succeeded it. Interviewees discussed the development of the power line siting controversy from 1970 to 1977 and the legislative response including the introduction of annual payments that "hopefully will make living with the line a little easier."[x]

Potential Metrics and Performance Measures

A full tax expenditure review may examine:

- The change in credit value over time measured on a statewide per-mile average, sample parcel, or jurisdiction basis, and the relationship between credit value, parcel market value, and total property tax liability
- Complexity and cost of administration compared to credit amounts received and alternative incentive methods
- The value of the credit compared to the reduced income generating potential of affected properties, adjusted for land use
- Recent right-of-way acquisitions and the degree to which the power line credit helped facilitate agreement between the utility and the landowner

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For more information, please visit the [Tax Expenditure Review Commission website](#).

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[i] Minnesota Department of Revenue, Tax Research Division, *Tax Expenditure Budget: Fiscal Years 2022-2025* (February 1, 2022), 195. A short Department of Revenue FAQ on the power line credit can be found at https://www.revenue.state.mn.us/sites/default/files/2021-08/Power%20Line%20Credit%20FAQ_1.pdf. A 2015 presentation is also a helpful primer – https://www.revenue.state.mn.us/sites/default/files/2016-10/Power%2520Line%2520Credit.pdf. A property tax primer prepared by the House Research and Fiscal Analysis departments covering general concepts and terminology can be found at: https://www.house.mn.gov/hrd/issinfo/2023PTHandout.pdf.

[ii] For additional historical context, see the research guide created by the Minnesota Historical Society, available at https://libguides.mnhs.org/powerline/primary, including Paul Wellstone and Barry M Casper, *Powerline: The First Battle of America's Energy War* (Amherst: University of Massachusetts Press, 1981) and Edward P. Nelson, Charles L. Anderson, Willard Anderson, et al. *Minnesota Powerline Construction Oral History Project* (St. Paul, Minnesota: Minnesota Historical Society, 1981).

[iii] Laws of Minnesota 1977, Chapter 439, https://www.revisor.mn.gov/laws/1977/0/Session+Law/Chapter/439/pdf/, 1198.

[iv] In cities and organized townships, ten percent of the net tax capacity (NTC) of qualifying transmission lines is excluded (set aside) when determining taxable NTC and initial NTC-based tax rates. The initial rate is applied to both taxable NTC and the excluded ten percent of tax capacity to yield an amount in addition to the local levy amount that is used to pay power line credits. See M.S. 273.425. In unorganized townships, ten percent of county-wide tax receipts on qualifying transmission lines are allocated to a utility property tax credit fund that is used to pay power line credits. See M.S. 273.42, subd. 1. Only qualifying transmission lines constructed after July 1, 1974, are eligible for the credit, corresponding to the date which high-voltage transmission lines became subject to the Minnesota Power Plant Siting Act of 1973. The act included language that prohibits local units of government from using zoning, building, or other land use regulations to block the placement of large electric generating facilities or high-voltage transmission lines. See Laws of Minnesota 1973, Chapter 591, https://www.revisor.mn.gov/laws/1973/0/Session+Law/Chapter/591/pdf/. Transmission lines are considered Class 3 property for purposes of taxation. The Department of Revenue estimates and certifies the market value of utility operating property, including electric transmission lines. See https://www.revenue.state.mn.us/utility-and-pipeline-property-administration for assessment information.

[v] Minnesota Department of Revenue, *Auditor/Treasurer Manual* (August 2021), https://www.revenue.state.mn.us/auditor/treasurer-manual, 81, 114, 123, 127-129.

[vi] Ibid, 128.

[vii] Ibid, 117.

[viii] Jurisdiction-level property tax data can be accessed at https://www.revenue.state.mn.us/property-tax-history-data.

[ix] Charles Berg, interview by Edward P. Nelson, *Minnesota Powerline Construction Oral History Project*, https://www.lrl.mn.gov/docs/2012/other/120340.pdf, 36-37; David F. Fjoslien, interview by Edward P. Nelson, *Minnesota Powerline Construction Oral History Project*, https://www.lrl.mn.gov/docs/2012/other/120341.pdf, 38-39. Senate session review, 4; Minnesota Senate Information Office, *Session Review* (June 1977), https://www.lrl.mn.gov/docs/pre2003/other/770492.pdf, 4.

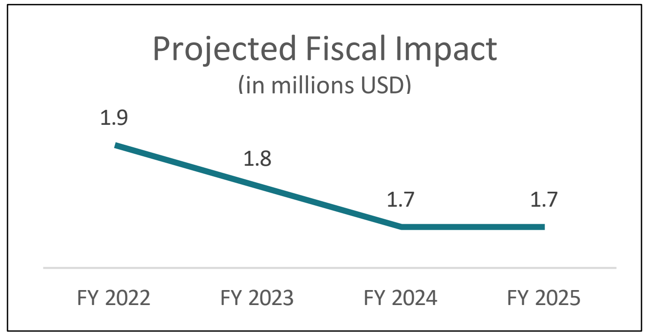
[x] Roger E. Strand, interview by Edward P. Nelson, *Minnesota Powerline Construction Oral History Project*, https://www.lrl.mn.gov/docs/2012/other/120379.pdf, 55-56.

Agricultural Loans

Tax Expenditure Initial Review – TEB 9.01

Tax Expenditure Facts

Year Enacted	2001
Statute	Minn. Stat. § 287.04(9)
Tax Type	Mortgage Registry Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	$1,700,000 – Fiscal Year 2024
Latest Claims Estimate	Direct measure of this estimate is not currently available
Expiration Date	None



Tax Expenditure Description

An exemption from the mortgage registry tax is allowed for an agricultural mortgage if the proceeds are used to acquire or improve real property that is classified as agricultural for property tax purposes. The fiscal impact estimate shown above excludes mortgages by Federal agencies because Federal law prohibits taxation by the state.

Additional Background Information

The mortgage registry tax (MRT) is imposed when a mortgage on Minnesota real property is recorded. The tax rate is 0.23 percent of the debt being secured by the mortgage. The mortgagor (borrower) is liable for the tax. The exemption does not apply to a house, residential garage, or surrounding one acre that is purchased with an agricultural property.[i]

Beneficiaries of the agricultural loan exemption include individuals who use the proceeds of a mortgage-secured loan that would not otherwise be tax exempt to acquire or improve qualifying real property.

Mortgage registry taxes are collected by county treasurers. On or before the 20th of each month, 97 percent of MRT revenue collected the preceding month is remitted for deposit in the state General Fund, while 3 percent is retained by the county to cover administrative expenses.

This exemption reduces the amount of mortgage registry tax revenue that would otherwise be collected. In fiscal year 2022, state revenues from the mortgage registry tax were approximately $203 million.[ii] Collections fluctuate from year-to-year based on the real estate market.

Mortgages given to Federal lenders such as the Farm Service Agency are exempt from state mortgage taxes pursuant to Federal law.[iii]

This exemption was enacted in 2001.[iv] Conforming and technical changes were enacted in 2009 and 2021.[v]

Proposed Tax Expenditure Objective for Consideration

The objective of the mortgage registry tax agricultural loan exemption is to increase the competitiveness of Minnesota banks offering agricultural loans with Federal lenders whose loans are not subject to the state mortgage registry tax.

Sources

The proposed objective is based on committee hearings for H. F. 52 and companion bill S. F. 290, introduced during the 2001 regular legislative session. Both bills were heard in committee but not included in the regular session tax omnibus bill, H. F. 2498.[vi] However, similar exemption language was included in tax omnibus bill H. F. 1, passed during the 2001 1st Special Session.[vii] Bill authors emphasized the need to "level the playing field" between local lenders and the Farm Service Agency (FSA), noting that Minnesota bank loans were subject to the mortgage registry tax, while FSA loans were not.[viii]

Potential Metrics and Performance Measures

A full review may compare the number and value of qualifying agricultural loans issued by Minnesota banks versus Federal lenders since the exemption was enacted.

Contact Information

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] Modification of Revenue Notice # 01-06: Mortgage Registry Tax – Exemption for Mortgages that Secure Qualifying Agricultural Loans, Minnesota Department of Revenue, Modified February 22, 2010, Accessed September 3, 2024, https://www.revenue.state.mn.us/sites/default/files/2011-11/RN_01-06.pdf; "Mortgage Registry Tax Agricultural Loan Exemption", Minnesota Department of Revenue, Accessed September 3, 2024, https://www.revenue.state.mn.us/mortgage-registry-tax-agricultural-loan-exemption.

[ii] "General Fund Analysis – Summary," Minnesota Management and Budget, accessed November 7, 2023, https://mn.gov/mmb/budget/current-budget/current/.

[iii] "Mortgage Registry, Tax Federal Government and Agencies," Minnesota Department of Revenue, last updated August 16, 2023, https://www.revenue.state.mn.us/mortgage-registry-tax-federal-government-and-agencies.

[iv] Laws of Minnesota 2001, 1st Spec. Session, chapter 5, article 7 section 25, https://www.revisor.mn.gov/laws/2001/1/Session+Law/Chapter/5/.

[v] Laws of Minnesota 2009, chapter 88, article 9, section 1, https://www.revisor.mn.gov/laws/2009/0/88/#laws.9.1.0; Laws of Minnesota 2021, 1st Spec. Session, chapter 14, article 13, section 10, https://www.revisor.mn.gov/laws/2021/1/14/#laws.13.10.0.

[vi] See House File 52, 82nd Minn. Leg., Reg. Sess. (introduced January 8, 2001), https://www.revisor.mn.gov/bills/bill.php?f=HF52&y=2001&ssn=0&b=house.

[vii] Laws of Minnesota 2001, 1st Spec. Sess. chapter 5, article 7, section 25, https://www.revisor.mn.gov/laws/2001/1/Session+Law/Chapter/5/.

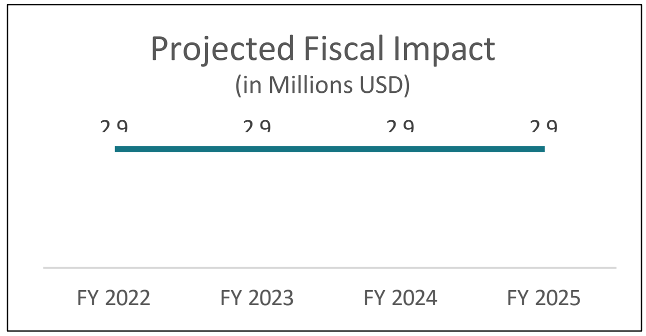
[viii] Minn. H., Hearing on H.F. 52 before the H. Div. on Property Taxes, 82nd Minn. Leg., Reg. Sess. (Jan. 22, 2001), https://www.lrl.mn.gov/media/file?mtgid=820225, file no. 1 at 01:10:11; Minn. Sen., Hearing on S.F. 290 before the Sen. Div. on Property Tax Budget, 82nd Minn. Leg., Reg. Sess. (Mar. 21, 2001), https://www.lrl.mn.gov/media/file?mtgid=820839, file no. 2 at 00:02:59.

Government Housing Programs

Tax Expenditure Initial Review - TEB 9.02

Tax Expenditure Facts

Year Enacted	2001
Statute	Minn. Stat. § 287.04 sub. 6
Tax Type	Mortgage Registry Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	$2,900,000 – Fiscal Year 2024
Latest Claims Estimate	Direct measure of this estimate is not currently available
Expiration Date	None



Tax Expenditure Description

An exemption from the mortgage registry tax is allowed for a mortgage loan made by a government agency under a low- and moderate-income housing program or other affordable housing program. The estimates exclude mortgages by Federal agencies because Federal law prohibits taxation by the state.

Additional Background Information

The mortgage registry tax (MRT) is imposed when a mortgage on Minnesota real property is recorded. The tax rate is 0.23 percent of the debt being secured by the mortgage. The mortgagor (borrower) is liable for the tax. In general, any mortgage loan given by the government for income-restricted housing will qualify for this exemption.[i]

Beneficiaries of the MRT exemption for government housing programs include all government agencies that make mortgage loans under low- and moderate-income housing programs or other affordable housing programs. This exemption reduces the amount of mortgage registry tax revenue that would otherwise be generated.

Mortgage registry taxes are collected by county treasurers. On or before the 20th of each month, 97 percent of MRT revenue collected the preceding month is remitted for deposit in the state General Fund, while 3 percent is retained by the county to cover administrative expenses.

An amendment to the exemption was made in 2021 to correct the formatting of the exemption as well as to allow an exemption for mortgage loans made under low- or moderate-income housing program if the assignee of the mortgage is a governmental agency. [ii]

Proposed Tax Expenditure Objective for Consideration
The objective of the government housing programs mortgage registry tax exemption is to incentivize and promote affordable housing in the State of Minnesota.

Sources

An explicit tax expenditure objective was not identified in the legislative record. The language surrounding the goals of the exemption was discussed in a presentation from the Mayors' Regional Housing Taskforce to the Senate Jobs, Housing, and Community Development Committee on January 12, 2001. In the presentation discussion, the task force encourages cities to "waive fees for affordable housing developments whenever possible" and discusses the need to shift away from Federal reliance on affordable housing.[iii]

Potential Metrics and Performance Measures

A review of the state's government agency funded affordable housing programs may identify trends in low- or moderate-income housing programs that qualify for this exemption across the state.

An analysis of the program's participation by submission of exemption certificates may identify trends in uptake of the tax incentive.[iv]

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For more information, please visit the Tax Expenditure Review Commission website.

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[i] Minnesota Department of Revenue. (2012, March). Modification of Revenue Notice # 01-05: Mortgage Registry Tax – Exemption for Mortgages that Secure Loans Made Under Qualifying Government Affordable Housing Programs. https://www.revenue.state.mn.us/sites/default/files/2011-11/RN_01-05.pdf.

[ii] Laws of Minnesota 2021, 1st Special Session, chapter 14, article 13, section 10.

[iii] Mayors' Regional Housing Task Force Presentation to the Senate Jobs, Housing, and Community Development Commission. January 12th, 2001.

[iv] Minnesota Department of Revenue. (2019, July). Form ST3, Certificate of Exemption.

Bookmobiles

Tax Expenditure Initial Review - TEB 5.10

Tax Expenditure Facts

Year Enacted	1994
Statute	Minn. Stat. § 297B.03(8)
Tax Type	Motor Vehicle Sales Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	Less than $50,000 per year
Latest Claims Estimate	Direct measure of this estimate is not currently available
Expiration Date	None

Estimated fiscal impact is less than $50,000 per year through fiscal year 2025.

Tax Expenditure Description

The purchase of a motor vehicle by or for a public library for use as a bookmobile or a library delivery vehicle is exempt from the motor vehicle sales tax.

Additional Background Information

According to the 2017 Minnesota Public Library Report, Minnesota has eight bookmobiles. Additionally, library service is available in all 87 counties. There are 141 public libraries and 12 regional public library systems in Minnesota. Twenty-seven libraries have multiple branches. Combined, there are 355 library locations throughout the state.[i]

Beneficiaries of the current tax exemption are local units of government that utilize bookmobiles to provide library services to individuals who may have limited accessibility to a library building. This exemption is administered by the Department of Revenue and reduces the amount of motor vehicle sales tax revenue that would otherwise be generated. State motor vehicle sales tax collections are deposited in the state Highway User Tax Distribution Fund and the Transit Assistance Fund.

Proposed Tax Expenditure Objective for Consideration

The objective to exempt bookmobiles from the motor vehicle sales tax is to reduce costs paid by local government entities for providing access to library services to individuals who have limited accessibility to a library building.

Sources

An explicit tax expenditure objective was identified in the legislative record. During the 1994 legislative session S.F. 2176 was introduced, the bill exempted bookmobiles from the motor vehicle excise tax. The bill was heard in the Senate Taxes and Tax Laws Subcommittee on Income and Sales Tax on March 22, 1994. The testimony mentioned there were 22 bookmobiles in Minnesota operated by large cities, counties, or regional public libraries. In rural communities, bookmobiles are used to bring library services to people who do not live near a library building. In urban communities, bookmobiles primarily serve people who lack mobility to get to a library building such as retirement homes and day care centers. Furthermore, the cost of purchasing and maintaining a bookmobile is a large expense for some local government entities, with bookmobiles costing approximately $100,000, not including additional costs for installing wheelchair lifts. Bookmobiles generally last around ten years before needing to be replaced. Prior to enactment of this exemption, bookmobiles were subject to a 6.5 percent motor vehicle sales tax rate, although public libraries are not taxed, which was deemed to be an equity issue.[ii] In 2023, the Minnesota Legislature increased the motor vehicle sales tax rate from 6.5 percent to 6.875 percent effective beginning in tax year 2024. This change will increase the estimated cost of this tax exemption in future years.

The Library Services Act of 1956 greatly expanded bookmobile services, especially in rural communities. Since the early 1990's, however, there has been a decline in bookmobile services attributed to the rise of digital technology, which allows people to access information via the internet.[iii]

Potential Metrics and Performance Measures

An analysis of the program's participation by submission of exemption certificates may identify historical trends in the use of the tax incentive.[iv]

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[i] "Minnesota Public Library Structure, 2017" Minnesota Department of Education. June 7, 2018. https://education.mn.gov/MDE/dse/Lib/sls/stat/

[ii] Minn. Sen., Hearing on S.F. 2176 before the Sen. Comm. on Taxes and Tax Laws Subcommittee on Income and Sales Taxes. 78th Minn. Leg., Reg. Sess. (Mar. 22, 1994), Part 1 of 2 available at: https://www.lrl.mn.gov/media/file?mtgid=782214.

[iii] Public Broadcasting Service. "A History of the Bookmobile." Premiered on July 19, 2011. Accessed on December 27, 2023. https://archive.pov.org/biblioburro/bookmobile/

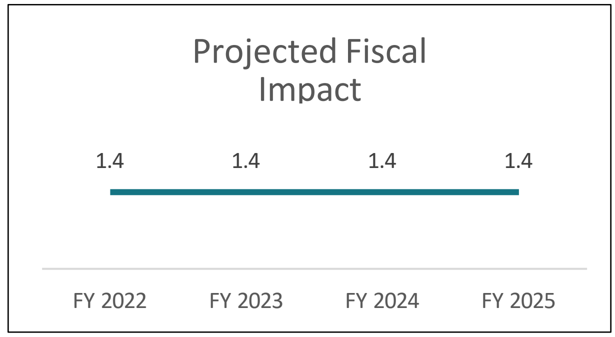
[iv] Minnesota Department of Revenue. (2019, July). Form ST3, Certificate of Exemption.

Ready-Mixed Concrete Trucks

Tax Expenditure Initial Review - TEB 5.12

Tax Expenditure Facts

Year Enacted	1998
Statute	Minn. Stat. § 297B.03(9)
Tax Type	Motor Vehicle Sales Tax
Provision Type	Exemption
Latest Fiscal Impact Estimate	$1,400,000 – Fiscal Year 2024
Latest Claims Estimate	Each year an estimated 150 vehicles qualify for this exemption.
Expiration Date	None



Tax Expenditure Description

The purchase of a ready-mixed concrete truck is exempt from the motor vehicle sales tax.

Additional Background Information

Members of the cement industry noted ready mix-concrete trucks are an integral part of the manufacturing process by facilitating the mixture of gravel, sand, concrete, and water which are the components of concrete, and therefore should be classified as capital equipment and be exempted from state sales tax.

According to audio testimony for standalone bill H.F.3575 from the 1998 session, classifying ready-mix concrete trucks as capital equipment allowed for more ease in administering the sales tax for concrete companies. Prior to enactment, concrete companies were exempt from paying sales tax on the delivery charge which was assessed based on many variables such as distance traveled and the time of day the concrete was delivered. Determining the exemption amount was administratively burdensome for concrete companies who were at times audited and fined for errors in applying the sales tax. The enacting legislation was intended to create more simplicity by allowing all sales of ready-mixed concrete to be subject to sales tax[i].

The Department of Revenue determined an estimated 150 vehicles each year qualify for this exemption. This exemption is administered by the Department of Revenue and reduces the amount of motor vehicle sales tax revenue that would otherwise be generated. State motor vehicle sales tax collections are deposited in the state Highway User Tax Distribution Fund and the Transit Assistance Fund.

Proposed Tax Expenditure Objective for Consideration

The objective of the ready-mixed concrete truck exemption is to treat ready-mixed concrete trucks as capital equipment exempt from the motor vehicle sales tax due to their integral part of the manufacturing process.

Sources

The proposed tax expenditure objective was derived from member discussion in committee, after hearing public testimony on the bill from industry representatives.[ii] Public testimony also mentioned other states, including Iowa[iii] and Wisconsin[iv] who passed legislation around the same time as Minnesota, are classifying ready-mixed concrete trucks to be part of the manufacturing process.

A standalone senate companion bill, S.F. 3208, was identified; however, no hearings were held during the 1998 session. In 2023, the Minnesota Legislature increased the motor vehicle sales tax rate from 6.5 percent to 6.875 percent effective beginning in tax year 2024. This change will increase the estimated cost of this tax exemption in future years.

Potential Metrics and Performance Measures

An analysis of exemption certificates submitted for the purchase of ready-mix concrete trucks may identify trends in uptake of the tax incentive.[v]

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For more information, please visit the [Tax Expenditure Review Commission website].

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[i] Minn. H, Hearing on H.F. 3575 before the H. Comm. on Taxes, 80th Minn. Leg., Reg. Sess. (Feb. 24, 1998) (audio file 1 of 2), available at https://www.lrl.mn.gov/media/file?mtgid=802429.

[ii] Ibid

[iii] Iowa Code Section 423.3(47).

[iv] Wisconsin Statutes, section 11.83(12).

[v] Minnesota Department of Revenue. (2019, July). Form ST3, Certificate of Exemption.

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