Minnesota Budget Bites

Fiscal and tax information in bite-sized pieces

June 2000

The 2000 Legislative Session: What Happened?

Much of the 2000 session was dominated by a disagreement about the basic budget numbers and what they meant for decision-makers. The Department of Finance's financial forecast stated there was a $549 million "structural balance" for fiscal year 2003, meaning that ongoing new spending or tax cuts could not exceed this amount. House Republicans argued that the forecast underestimated the amount of resources available.

In the end, the House, Senate, and Governor split $525 million of ongoing resources three ways, with each allotted $175 million to spend as they wanted. The House spent their share on tax cuts, primarily income tax rate reductions. The Governor used his third to reduce vehicle registration fees, and the Senate used their allocation for investments, mainly in K-12 education. The shrinking of the tax reductions - from a House omnibus bill that cut taxes by over $850 million a year - to its final version brought about a tax bill that is fiscally responsible and benefits all Minnesota taxpayers to some degree.

Income Tax Rate Cuts

Minnesota income tax rates in all three brackets have been lowered, for a total tax reduction of over $150 million per year. From their current levels of 5.5%, 7.25%, and 8%, the rates have been dropped to 5.35%, 7.05%, and 7.85%.

Minnesota Working Family Credit

The Minnesota Working Family Credit (WFC) is the state's counterpart to the federal Earned Income Tax Credit (EITC), a refundable credit for low-income households based on their earned income and family size. The 2000 tax bill increases the WFC by about $12 million per year, approximately $10 million of which is funded by the TANF Reserve (federal welfare dollars). This is an increase in the WFC of 13.8%. The average Working Family Credit is now $483, or 33% of the federal EITC.

Because the legislature increased the Working Family Credit as a counterpart to income tax cuts, it makes sense to analyze the effects of these two tax changes together. To demonstrate the effect of these tax cuts on total tax burden and therefore on a household's budget, column 3 of Table 1 (above right) outlines this tax reduction as a percentage of income. The chart shows that, in dollar amounts, the tax savings increase as income increases. However, the total tax reduction is roughly the same percentage of income for all income groups, although slightly higher in the bottom incomes, for whom the WFC has a significant impact on overall tax obligations, and on the top of the income scale, for whom the income tax makes up the largest part of the total tax burden.

Table 1: Tax Savings by Income Level: Income Tax Rate Reductions and Working Family Credit Increase

Federal Adjusted Gross Income	Average Tax Cut	Average Tax Cut as a Percentage of Income
Less than $9,999	$7	0.18%
$10,000 - $19,999	$24	0.16%
$20,000 - $29,999	$28	0.11%
$30,000 - $49,999	$42	0.11%
$50,000 - $74,999	$73	0.12%
$75,000 - $99,999	$111	0.13%
$100,000 - $149,999	$161	0.14%
$150,000 - $199,999	$231	0.15%
$200,000 - $499,999	$367	0.15%
$500,000 or more	$1,301	0.15%
All Filers	**$66**	**0.13%**

Data Source: House Research and MN Department of Revenue

2000 Sales Tax Rebate

Once again, the legislature is providing a sales tax rebate to return funds that the state has on hand. The rebate will return $635.6 million to Minnesota taxpayers, ranging from $168 to $2,400 for married and head-of-household filers and $95 to $1,200 for single filers.

The basic eligibility criteria for the 2000 Sales Tax Rebate is similar to the 1999 rebate. The taxpayer must meet one of the following criteria:

1. Filed for a property tax rebate on a 1998 Minnesota income tax return,
2. Filed a 1998 income tax return and had at least $1 of tax liability before refundable credits and was not claimed as a dependent on another taxpayer's return,
3. Had homeowner property taxes reduced to $0

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in 1998 due to tornado relief, or

4. Was a non-resident but paid at least $10 in Minnesota sales tax on non-business purchases.

In addition, taxpayers who do not meet the above criteria qualify for the following rebate amounts:

1. Dependents age 18 or older with wage income will receive 35% of the rebate amount for non-dependents of the same income.
2. Individuals who receive social security or railroad retirement benefits will receive a rebate of $95.
3. Persons who were not dependents and filed a 1998 income tax return in order to claim a refundable credit or to get a return of withholding or estimated tax payments will receive the minimum rebate amount for their filing status.

Minnesota residents will receive their rebates automatically in the mail in August; non-residents need to file an application. Taxpayers must file their 1998 income tax returns by November 30, 2000, to be eligible. An additional $8.5 million will be mailed to persons who were eligible for the 1999 rebate but whose income tax returns were not filed by last year's rebate deadline but were filed by June 15, 2000. Therefore, **persons who have not filed a 1998 Minnesota income tax return still have time to file a return to qualify for the 2000 rebate.** (For filing assistance, contact AccountAbility Minnesota at (612) 288-9476.)

In addition to the sales tax rebate, $18 million in agricultural disaster relief will be distributed to farmers in distressed areas.

The combined effects of the income tax rate cuts, WFC changes, and the sales tax rebate are indicated below in Table 2.

Auto Tabs Reduction

The motor vehicle registration tax (commonly called "tabs") is made up of two portions: a $10 flat fee and an additional tax amount. The additional tax is 1.25% of the base value of the vehicle, but the amount of base value subject to the additional tax is reduced as the vehicle ages. For the first two years of the vehicle's life, the additional tax is levied on 100% of the vehicle's base value; for years 3 and 4, the tax is based on 90% of the value; and declines in a similar fashion until the 10th year, when the tax is based on 10% of the vehicle's value. At the 11th and following years, the additional tax is set at $25, making the total minimum tabs fee $35.

This year's tax bill made changes to the maximum tabs

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Table 2: Tax Savings by Income Level and Family Type: Income Tax Rate Reductions, Working Family Credit Increase, and Sales Tax Rebate

Family type and federal adjusted gross income	Dollar amount reduction from income tax/ WFC changes	Percentage income tax reduction from income tax/ WFC changes	Estimated Sales Tax Rebate
$10,000 income			
· Married couple, 2 dependents	$117	13.6%	$168
· Head of household, 1 dependent	$73	14.1%	$168
· Single filer, no dependents	$7	4.8%	$116
$25,000 income			
· Married couple, 2 dependents	$61	27.5%	$231
· Head of household, 1 dependent	$33	5.5%	$253
· Single filer, no dependents	$27	2.7%	$210
$50,000 income			
· Married couple, 2 dependents	$42	3%	$312
· Head of household, 1 dependent	$56	2.7%	$338
· Single filer, no dependents	$64	2.7%	$259
$100,000 income			
· Married couple, 2 dependents	$120	2.8%	$476
· Head of household, 1 dependent	$134	2.8%	$523
· Single filer, no dependents	$133	2.5%	435
$500,000 income			
· Married couple, 2 dependents	$647	2.1%	$1,522
· Head of household, 1 dependent	$634	2.0%	$1,522
· Single filer, no dependents	$622	2.0%	$1,128

Data Source: House Research. Assumptions: Taxpayers have the same income in 1998 and 2000; married spouses have equal shares of income; taxpayers making under $50,000 claim the standard deduction and families making $50,000 or more claim itemized deductions of 22% of gross income; and taxpayers receive the Working Family Credit when eligible.

amount. The tax will be calculated as usual and the amount due in the first year of the vehicle's life will be the same. In the second year, the total amount of tax is capped at $189 and in the 3rd and following years, it is capped at $99. The minimum remains at $35. It is difficult to get a good estimate of who benefits from this change. The majority of vehicles are already registered for less than $99. The owners of these vehicles will receive no tax reduction. In addition, the motor vehicle registration tax is a regressive tax, taking a larger share of income from lower-income families. Reducing the tax on expensive vehicles may increase the regressivity of the tax.

Tabs are a dedicated revenue source to the highway user trust fund; therefore reducing tab fees means a loss in funding. The 2000 tax bill transfers general fund money for the lost tab revenue directly to the highway user fund in 2001 and 2002; in following years, it dedicates 32% of the motor vehicle excise tax (collected when a vehicle is purchased) to the highway fund. There are concerns that this transfer will be insufficient and leave a funding hole in the future.

Property Tax

Despite a lot of attention to the issue, there were no changes in property tax rates this session. The agricultural education credit was increased by $22 million starting in the 02-03 biennium, which should lighten the property tax obligation on farms. It is likely that significant changes to the property tax system will be part of the administration's "Big Plan" effort to reform the state's tax system in the 2001 session.

Capital Investments/Bonding

The Capital Investment bill (HF 4078) passed by the 2000 legislature spent $640.3 million for various projects, primarily construction or improvements of buildings and other physical structures. This was considerably more than the $443 million proposed by the Governor in his 2000 Capital Budget, but about midway between the House's $532 million bonding bill and the Senate's $762 million proposal. The capital investment bill is commonly called the "bonding bill," as most of the projects are funded through bonding (or state borrowing), although $98 million of this year's total comes from the state's general fund.

The Governor chose to use his line-item veto authority to remove several projects from the bill. However, the legislature was successful in passing veto overrides to retain funding for cultural development grants in Pelican Rapids and St. James, the Lanesboro Center for the Arts, the Guthrie Theatre, and an organ donor vehicle. They did not override his vetoes of funding for the Center for Agricultural Innovation in Olivia, St. Croix Valley Heritage Center, a Cold Weather Testing Center in International Falls, or retaining walls for a housing development in Landfall. These vetoes brought the final new spending total to $636.82 million.

The capital investment bill cancels nearly $30 million in funding for projects approved in past years but not yet spent. The Governor had proposed $37.2 million in cancellations in his Capital Budget; the legislature chose not to cancel some projects targeted by the Governor, but approved additional cancellations. Cancellations brought the final cost of the bill down to $606.907 million.

It is difficult to comprehensively compare all capital investment items considered by the legislature, as not all of these items are included in the capital investment bill, especially if they are funded through methods other than bonding. For example, the House omnibus capital investment bill contained transportation proposals; the Senate addressed transportation investments in their omnibus transportation bill. Table 3 below describes only HF 4078 and the technical corrections bill.

Table 3: Capital Investments by General Funding Area

Administration	$81.45 million
Agriculture	~~$21.7 million~~ $21.2 million after veto
Amateur Sports Commission	$1.11 million
Arts	$4.5 million
CAAP Board	$0
Commerce/Public Service	$0
Corrections	$18.035 million
Dept. of Children, Families & Learning	$80.741 million
Dept. of Health	$7.135 million
Dept. of Human Services	$12.471 million
Dept. of Natural Resources	~~$73.177 million~~ $73.027 after veto
Dept. of Trade & Econ. Development	~~$51.382 million~~ $48.582 after vetoes
Historical Society	$5.75 million
Housing	$2 million
Iron Range Resources & Rehab. Board	$0
Military Affairs	$3.625 million
Minnesota State Academies	$3.066 million
Minnesota State Colleges & Universities (MNSCU)	$131.021 million
Minnesota Zoological Gardens	$1 million
Office of Environmental Assistance	$2.2 million
Perpich Arts Center	$877,000
Public Safety	$2.844 million
Transportation	$0
University of Minnesota	$100.213 million
Veterans Affairs	$25,000
Veterans Home Board	$11.7 million
Water & Soil Resources Board	$23.8 million
Cancellations	-$29.913 million
Finance (Bond Sale Expenses)	$448,000
Total New Spending	**$636.82 million**
Net Total spending (after cancellations)	**$606.907 million**

Data Source: House Fiscal Analysis

Poverty Despite Work in Minnesota

Across the country and in Minnesota, parents work hard to support their families. Thousands of families are faced with low wages and limited job opportunities, combined with a lack critical work supports, including child care, health care, and affordable housing.

Nationally, the following trends are occurring:

- From the late 1970's to 1997, poverty among working families with children increased 45%, bringing the poverty rate of this group to 11.5%.
- The share of children living in poverty has increased 32% between 1970 and 1997. At the same time, the poverty rate among adults grew 21% and poverty among the elderly declined 57%.
- The gap between the rich and the poor is at its highest point since World War II.
- Employment trends predict that future job growth will be concentrated in low-paying industries.

In Minnesota, the conditions are as follows:

- Most poor families include employed parents.
- The child poverty rate remains unacceptably high at 14%. Minnesota follows the national trend that children have the highest poverty rate of any age group.
- The majority of working poor parents are employed in services or retail, the two lowest paying sectors of our economy.

Our new report, *Poverty Despite Work in Minnesota*, takes a closer look at the characteristics of working poor families and economic trends contributing to poverty. It concludes with policy strategies that enable families to become more self-sufficient: addressing the affordable housing crisis, improved access to health care, providing child care assistance to more working families, raising the state's minimum wage, pursuing tax fairness for low-income families, and reforming Unemployment Insurance.

Please use the order form enclosed in this newsletter to request a copy of *Poverty Despite Work* or any of our previously released publications.

Thank you for your interest and support during what has been a busy, exciting, and fun year! Please take a moment to fill out the short feedback survey enclosed in this newsletter and let us know how we are doing.

Nan Sonia

The Minnesota Budget Project provides independent research, analysis, and outreach on budget and tax policy issues, emphasizing their effect on low- and moderate-income persons and the organizations that serve them.

The Minnesota Budget Project is an initiative of Minnesota Council of Nonprofits. This publication was made possible through a grant from the Ford Foundation.

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