VARIOUS TAXES
Tax Incentives for Economic Development Outside the Metro Area

February 25, 2002

	Yes	No
Separate Official Fiscal Note Requested		X
Fiscal Impact		
DOR Administrative Costs/Savings	X	

Department of Revenue
Analysis of S.F. 3127 (Samuelson)

	Revenue Gain or (Loss)			
	F.Y. 2002	F.Y. 2003	F.Y. 2004	F.Y. 2005
		(000's)		
General Fund				
State property tax levy impact *	$	$	$0	$0
Homeowner PTR impact of abatement			(Unknown)	(Unknown)
Income Tax	($0)	(Unknown)	(Unknown)	(Unknown)
Corporation Franchise Tax	($0)	(Unknown)	(Unknown)	(Unknown)
Sales tax	$0	(Unknown)	(Unknown)	(Unknown)

* A procedural amendment is needed to avoid a revenue reduction. See Revenue Detail below.

Property tax provision: effective for taxes payable 2003 and thereafter.
Sales tax provision: sales made after June 30, 2002
Income tax: various provisions effective either for taxable years beginning after December 31, 2001 or after December 31, 2002.

EXPLANATION OF THE BILL

Property tax provision

Current Law: There are no property tax exemptions that are based solely on a company's location outside of the seven county metropolitan area.

Proposed Law: Section 11 of the bill allows a statutory or home rule city in the nonmetropolitan area of Minnesota to exempt new improvements to a qualified business from the state general levy for a period not to exceed 20 years. If the qualifying business is relocating from another city in the nonmetropolitan area, the city granting the exemption must obtain approval for the relocation from the governing body of the city of origin of the business.

Section 23 of the bill allows political subdivisions to grant abatements to qualified businesses under this proposal for up to 20 years.

Income tax provision:

Current Law: No state income tax credits are available to provide tax incentives for companies located outside of the seven county metropolitan area. Current law also lacks any deduction for financial institutions or changes to the apportionment formula associated with companies located outside of the seven county metropolitan area.

Proposed Law: This bill enacts four tax credits (see table below) for companies located outside of the seven county metropolitan area, it provides a new deduction for financial institutions and it makes changes to the apportionment formula.

List of Tax Credits in S.F. 3127

Name of Credit	Type of Credit
Economic Development Credit	Granted by DTED
RAIN Investment Credit	25 % investment tax credit
Equity Investment Tax Credit	25% equity investment tax credit
Investment Tax Credit	7.5% investment tax credit

The economic development credits are granted by the Department of Trade and Economic Development. The ceiling on the dollar value of these credits is the incremental income tax attributable to the applicant's project. These credits are refundable.

Contributors to a regional angel investment network fund, RAIN fund, could get a tax credit of up to $250,000. Up to ten RAIN funds could be established. Each fund makes equity investments in emerging companies located in communities in Minnesota outside the metropolitan area. The credits have a fifteen-year carry over.

Taxpayer who make investments in equities in companies located in communities in Minnesota outside the metropolitan area could get a tax credit of up to $50,000. This credit is non-refundable and has a five-year carryover.

Taxpayers who make purchases of equipment in companies located in communities in Minnesota outside the metropolitan area, and they make them between July 1, 2002 and December 31, 2005 could receive a tax credit. The credit is based on a formula that measures how much of the equipment's value exceeds a statewide average cost.

The calculation of the apportionment formula is altered under the bill to exclude Minnesota property and payroll associated with companies that are located outside of the metropolitan area. Financial institutions could alter the calculation of their apportionment formula provided that they make loans to companies located outside of the metropolitan area. In addition, financial institutions can exclude the interest income earned on loans made to companies located outside of the metropolitan area.

Sales tax provision:

Current Law: There are no sales tax exemptions that are based solely on a company's location outside of the seven county metropolitan area.

Proposed Law: Companies located outside of the seven county metropolitan area could receive a sales tax exemption for otherwise taxable goods and services used in a business. Construction materials associated with improvements by the same companies could also be exempt.

REVENUE ANALYSIS DETAIL

Property Tax:

- The statewide tax rate for the state general levy is set each year to raise the total levy specified in law. As written, the proposal raises the possibility of a loss of state general property tax levy if cities fail to notify county assessors or the Department of Revenue of exemptions granted during the assessment year. Assuming that the proposal is amended to ensure that notification by cities is timely, the proposed exemption will increase the state general levy tax rate to offset the exemptions. The higher state tax rate will shift tax burden onto other commercial/industrial and seasonal recreational property subject to the state levy, without reducing the specified statewide levy.
- The proposed abatements by political subdivisions could cause an increase in property tax levies on other property to avoid a revenue loss. Because information is not available about potential development of qualified businesses, the potential shift of property tax burden to other property including homeowners, and the possible increase in homeowner property tax refunds, cannot be estimated.

Income Tax & Sales Tax:

- The bill offers significant tax incentives to encourage companies to locate or expand outside of the metropolitan area. The use of the complicated and interlocking tax incentives in this bill is not known at this time. Due to the lack of data about the incentive effect of this bill, the revenue impact of the income and sales tax provisions is unknown.

ADMINISTRATIVE/OPERATIONAL IMPACT

There will be significant administrative or operational costs to DOR in administration of this bill. This is an extremely complicated tax credit. A number of new forms will need to be developed. In addition, additional staff time will be required to interpret the tax structure and to defend it from legal challenges.

Source: Minnesota Department of Revenue
Tax Research Division
http://www.taxes.state.mn.us/polic.html#analyses

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