

Tax Incidence Analysis

Prepared by the Tax Research Division, Minnesota Department of Revenue

October 29, 2019

2019 Special Session Tax Bill, As Enacted Omnibus Tax Bill (2019 1st SS, Chapter 6)

As enacted, the tax bill included the following tax law changes:

- **Income Tax -- Personal**
 - Start tax calculations with Federal Adjusted Gross Income rather than Federal Taxable Income. Establish a state standard deduction to match the federal standard deduction, repeal personal exemptions, maintain dependent exemptions, and limit itemized deductions to generally match federal law. Reduce the standard deduction based on income in manner similar to the limitation on itemized deductions.
 - Reduce the second income tax rate to 6.8% and reduce the fourth bracket threshold.
 - Expand the working family credit, primarily for taxpayers with no children and taxpayers with three or more children.
 - Increase the maximum Social Security subtraction and decrease the phase-out threshold.
- **Sales Tax:**
 - Create a number of exemptions for specific local government projects.
 - Create an exemption for sales by county agricultural societies at county fairs.
 - Create exemptions for other specific groups.
- **Property Taxes:**
 - Decrease the state property tax levy for commercial-industrial and seasonal recreational property.
 - Increase aids to schools, cities and counties.
 - Increase school building bond credit.
- **Taxes on Business (Corporate and Non-corporate):**
 - Conform to most federal tax changes in the definition of income, except for the international provisions of the Tax Cuts and Jobs Act (TCJA). Conform to Section 179 expensing and bonus depreciation with the 80% addback and 5-year recovery.
 - Create an 80% net operating loss (NOL) limitation, similar to the federal limit on NOLs.
 - Enact three Minnesota-specific provisions that expand the corporate tax base.
- **MinnesotaCare Taxes:** Repeal the sunset of the MinnesotaCare provider taxes, extending the tax at a rate of 1.8% after December 31, 2019.

These tax law changes modified the burden of state and local taxes compared to what it would be under prior law. The bill's impact can be estimated using the database and underlying models developed for the *Minnesota Tax Incidence Study*. **Because the latest study projects income and taxes to calendar year 2021, this analysis generally estimates the impact of law changes in that calendar year.**

The analysis is limited to **permanent** changes in tax law. **Law changes that are phased in over several years or have a delayed effective date are modeled as if fully effective in 2021.**

Impact of Proposals on Minnesota State & Local Tax Burdens on Minnesota Residents

The combined increase in tax collections in the bill is estimated to be \$692.4 million in 2021, of which **\$628.6 million** is borne by Minnesota residents. The largest component of the change is the extension of the MinnesotaCare provider taxes, which will increase tax collections by \$676.5 million, of which **\$619.7 million** is borne by Minnesota residents. Excluding the extension of the MinnesotaCare taxes, the bill increases the net tax burden on Minnesota residents by **\$8.9 million**.

- **Income Tax Changes (nonbusiness):** Proposed changes in income tax provisions would reduce tax revenue by \$192.0 million, decreasing the tax burden on Minnesota residents by **\$180.5 million**. The provisions include a mix of tax increases and tax decreases. The increased standard deduction, reduction in the 2nd income tax rate, and changes to the working family credit and social security subtraction will generally reduce taxes. The repeal of the dependent exemptions, reduction in the fourth bracket threshold, and changes to itemized deductions will generally increase taxes.
- **Income Tax Changes on Non-Corporate Businesses** (sole proprietors, S-corps, and partnerships): Conforming to most of the changes to the federal tax base will raise taxes on non-corporate business income by \$216.0 million, with **\$190.2 million** borne by Minnesota residents.
- **Corporate Tax Changes:** Corporate franchise tax revenue will increase by \$68.0 million. After full adjustment, some of the burden would be borne in higher prices, some in lower wages, and some in lower returns to business owners. Tax burdens for Minnesota residents would rise by an estimated **\$49.6 million** (about 73% of added revenue). The remainder would be borne by nonresidents or the federal government (in lower federal corporate tax revenue). These estimates apply to the long-term burden, after businesses have fully adjusted to the change in tax burdens.
- **Property Tax Changes:** State property taxes on business property and seasonal recreational property will decline by **\$50.0 million**. The net impact on Minnesota residents is estimated to be **-\$29.4 million**. Homeowner and renter property tax refunds will decrease, increasing resident tax burdens by **\$1.3 million**. Local property taxes will decrease by \$49.3 million. The net decrease on Minnesota residents is estimated to be \$41.3 million.
- **Sales and Excise Tax Changes:** State sales taxes will decline by \$1.4 million, decreasing the tax burden on Minnesota residents by **\$1.4 million**. However, local sales taxes will increase by \$23.4 million, of which \$20.5 million is borne by Minnesota residents. The net increase on Minnesota residents is estimated to be **-\$19.1 million**.
- **MinnesotaCare Tax Changes:** The extension of the provider taxes at a rate of 1.8% in calendar year 2021 is forecast to be \$676.5 million, of which **\$619.7 million** is borne by Minnesota residents.

Law Changes Not Included in this Analysis

- **Temporary changes** to the Angel Investment Credit, the sales tax on construction projects, and conformity to several small federal changes.
- **Timing changes** to the Historic Preservation Credit and Minnesota’s response to the temporary extension of bonus depreciation.
- **Small changes** or changes that affect few taxpayers, including the subtraction for medical cannabis production expenses and changes to the Section 529 plan credit.

Results by Population Decile: Change in Minnesota State and Local Tax Burdens

Table 1 shows the changes in dollars of tax burden by decile.

- The average increase in total taxes paid is 1.95%. Increases are highest in the second, third and fourth deciles, and the size of the increase declines with income. The first and tenth deciles have the smallest increase in total taxes, with an increase of 1.41% and 1.50%, respectively.
- Residents in the 10th decile will pay 31.6% of the proposed tax increases while those in the first decile will pay 1.6% of the proposed tax increases.

Table 1.
Dollars of Minnesota State and Local Tax Burden
Special Session 2019 Tax Bill

Estimated Calendar Year 2021 Impact

2021 Population Decile	Income Range	Percent of All Households	Percent of All Income	Minnesota State and Local Tax Burden				
				Current Law Tax Burden (\$1000s)	Proposed Tax Burden (\$1000s)	Change in Tax Burden (\$1000s)	Decile's Share of Total Change in Tax	Percent Increase in Burden Over Prior Law
1	14,528 & under	10%	0.9%	\$ 696,883	\$ 706,696	\$ 9,813	1.6%	1.41%
2	14,529 to 23,941	10%	2.0%	\$ 652,976	\$ 675,265	\$ 22,289	3.5%	3.41%
3	23,942 to 33,681	10%	3.0%	\$ 901,013	\$ 935,559	\$ 34,546	5.5%	3.83%
4	33,682 to 44,730	10%	4.0%	\$ 1,198,265	\$ 1,239,477	\$ 41,212	6.6%	3.44%
5	44,731 to 57,679	10%	5.2%	\$ 1,644,243	\$ 1,691,677	\$ 47,434	7.5%	2.88%
6	57,680 to 74,178	10%	6.7%	\$ 2,166,073	\$ 2,218,621	\$ 52,548	8.4%	2.43%
7	74,179 to 96,071	10%	8.7%	\$ 2,878,877	\$ 2,945,769	\$ 66,892	10.6%	2.32%
8	96,072 to 127,270	10%	11.4%	\$ 3,773,063	\$ 3,850,110	\$ 77,047	12.3%	2.04%
9	127,271 to 185,600	10%	15.6%	\$ 5,119,836	\$ 5,197,971	\$ 78,135	12.4%	1.53%
10	185,601 & over	10%	42.5%	\$ 13,229,741	\$ 13,428,381	\$ 198,640	31.6%	1.50%
ALL MINNESOTA HOUSEHOLDS		100%	100.0%	\$32,260,968	\$32,889,524	\$ 628,556	100.0%	1.95%

Detail for the 10th Decile

Lower Half	185,601 to 262,353	5%	11.2%	\$ 3,516,975	\$ 3,556,096	\$ 39,121	6.2%	1.11%
Next 4%	262,354 to 636,247	4%	15.3%	\$ 4,711,487	\$ 4,771,076	\$ 59,589	9.5%	1.26%
Top 1%	636,248 & over	1%	16.1%	\$ 5,001,278	\$ 5,101,208	\$ 99,930	15.9%	2.00%
Full Decile	185,601 & over	10%	42.5%	\$ 13,229,741	\$ 13,428,381	\$ 198,640	31.6%	1.50%

Table 2 shows the change in tax burden by decile as a percent of income.

- Minnesota residents' state and local tax burden would increase by an average of 0.23% of income. The increased tax burden is largest for the lowest deciles and declines at higher income ranges, except for the very highest incomes. The burden for the top decile would increase by 0.17%, but the top 1 percent of filers would see an increase by 0.23% of income, similar to the average increase.

Table 2.
Tax burden as Percent of Income
Impact of Tax Changes in Special Session 2019 Tax Bill
 Estimated Calendar Year 2021 Impact

2021 Population Decile	Income Range	Percent of All Households	Minnesota State and Local Tax Burden as Percent of Income		
			Current Law	Proposed Law	Change
1	14,528 & under	10%	27.61%	28.00%	0.39%
2	14,529 to 23,941	10%	11.93%	12.34%	0.41%
3	23,942 to 33,681	10%	11.01%	11.43%	0.42%
4	33,682 to 44,730	10%	10.75%	11.12%	0.37%
5	44,731 to 57,679	10%	11.34%	11.67%	0.33%
6	57,680 to 74,178	10%	11.61%	11.89%	0.28%
7	74,179 to 96,071	10%	11.94%	12.22%	0.28%
8	96,072 to 127,270	10%	11.95%	12.19%	0.24%
9	127,271 to 185,600	10%	11.82%	12.00%	0.18%
10	185,601 & over	10%	11.23%	11.40%	0.17%
ALL MINNESOTA HOUSEHOLDS		100%	11.63%	11.86%	0.23%

Detail for the 10th Decile

Lower Half	185,601 to 262,353	5%	11.37%	11.50%	0.13%
Next 4%	262,354 to 636,247	4%	11.13%	11.27%	0.14%
Top 1%	636,248 & over	1%	11.23%	11.45%	0.22%
Full Decile	185,601 & over	10%	11.23%	11.40%	0.17%

Table 3 shows the change in dollars of tax burden by tax type.

- **Personal income tax** reductions benefit all deciles but are weighted toward the higher incomes. The reductions are partially offset by income tax increases associated with pass-through businesses, which are concentrated at higher incomes. All but the top decile have a net decrease in income taxes.
- **The extension of the MinnesotaCare taxes** is the single largest change and disproportionately affects the lower deciles. The lowest five deciles earn 15.1% of all income but are estimated to pay 28.7% of the increase in the Minnesota Care taxes.

Table 3. Change in Minnesota State and Local Tax Burden by Tax Type
Special Session 2019 Tax Bill

Estimated Calendar Year 2021 Impact, by Tax Type
Dollars in \$1,000s

2021 Population Decile	Income Range	Percent of All Households	Percent of All Income	Change in Tax Burden						
				Income Tax (Personal)	Income Tax-- Flow-Through*	Corporate Tax	Property Tax Net of PTR	Sales and Excise Taxes	Minnesota Care Provider Taxes	Total
1	\$14,528 & under	10%	0.9%	\$ (8,872)	\$ 626	\$ 1,449	\$ (3,065)	\$ 645	\$ 19,030	\$ 9,813
2	14,529 to 23,941	10%	2.0%	\$ (6,716)	\$ 53	\$ 1,893	\$ (1,988)	\$ 772	\$ 28,276	\$ 22,289
3	23,942 to 33,681	10%	3.0%	\$ (3,402)	\$ 1,224	\$ 2,364	\$ (2,574)	\$ 940	\$ 35,995	\$ 34,546
4	33,682 to 44,730	10%	4.0%	\$ (4,890)	\$ 1,875	\$ 2,806	\$ (3,031)	\$ 1,089	\$ 43,362	\$ 41,212
5	44,731 to 57,679	10%	5.2%	\$ (7,745)	\$ 3,423	\$ 3,260	\$ (4,040)	\$ 1,261	\$ 51,275	\$ 47,434
6	57,680 to 74,178	10%	6.7%	\$ (9,122)	\$ 4,506	\$ 3,893	\$ (5,579)	\$ 1,499	\$ 57,351	\$ 52,548
7	74,179 to 96,071	10%	8.7%	\$ (13,549)	\$ 7,350	\$ 4,855	\$ (7,227)	\$ 1,867	\$ 73,597	\$ 66,892
8	96,072 to 127,270	10%	11.4%	\$ (21,657)	\$ 10,059	\$ 6,099	\$ (9,205)	\$ 2,327	\$ 89,424	\$ 77,047
9	127,271 to 185,600	10%	15.6%	\$ (40,171)	\$ 12,538	\$ 7,994	\$ (11,315)	\$ 3,001	\$ 106,087	\$ 78,135
10	185,601 & over	10%	42.5%	\$ (64,580)	\$ 148,512	\$ 14,982	\$ (21,305)	\$ 5,763	\$ 115,267	\$ 198,640
ALL MINNESOTA HOUSEHOLDS		100%	100.0%	\$ (180,702)	\$ 190,166	\$ 49,593	\$ (69,329)	\$ 19,163	\$ 619,665	\$ 628,556

Detail for the 10th Decile

Lower Half	\$185,601 to 262,353	5%	11.2%	\$ (32,333)	\$ 14,128	\$ 5,233	\$ (7,239)	\$ 1,926	\$ 57,405	\$ 39,121
Next 4%	262,354 to 636,247	4%	15.3%	\$ (26,319)	\$ 39,912	\$ 6,071	\$ (8,540)	\$ 2,246	\$ 46,219	\$ 59,589
Top 1%	636,248 & over	1%	16.1%	\$ (5,928)	\$ 94,472	\$ 3,677	\$ (5,526)	\$ 1,591	\$ 11,643	\$ 99,930
Full Decile	\$185,601 & over	10%	42.5%	\$ (64,580)	\$ 148,512	\$ 14,982	\$ (21,305)	\$ 5,763	\$ 115,267	\$ 198,640

*Includes the impact on business income from sole proprietorships, S corporations, partnerships, and farms.

Suits Indexes of Proposed Changes

Table 4 provides detail of the overall impact of the bill by tax type, in the same manner as shown on Table 3-1 in the *Tax Incidence Study for all current-law taxes*. (See page 44 of that report.)

Income and Estate Taxes

Changes to the individual income tax make the tax system more progressive with a combined Suits Index of +1.74. Total tax increases on Minnesota households are estimated to be \$59.2 million.

- The reductions in personal income taxes are progressive, although the benefit increases with income, except for the first two deciles. The Suits Index for these changes is +0.112.
- Individual income tax increases for flow-through entities are highly progressive, with most of the increase concentrated in the highest decile. The Suits Index for these changes is +0.485.
- The corporate franchise tax increases are moderately regressive with a Suits Index of -0.187.

State Sales and Excise Taxes

The changes to state sales and excise taxes make the tax system more regressive with a combined Suits Index of -0.331. Sales and excise tax increases on Minnesota households are estimated to be \$618.3 million. The largest component is the extension of the MinnesotaCare taxes, which increases taxes on Minnesota residents by \$619.7 million. That is offset by a slight decrease in the general sales tax.

State Property Taxes

The changes to state property taxes overall make the tax system more progressive with a combined Suits Index of +0.137. State property taxes on Minnesota households are estimated to decrease -\$29.4 million, largely driven by decreases in taxes on commercial and industrial property.

Local Taxes

Changes to local taxes make the tax system more progressive with a combined Suits Index of +0.218. Total local tax decreases on Minnesota households are estimated to be \$20.8 million. Local property taxes are estimated to decrease overall.

**Table 4. Impact of Special Session 2019 Tax Bill on State and Local Tax Collections and Tax Burdens
Calendar Year 2021**

All dollars in millions

All dollar values rounded to nearest tenth of a million dollars. All values that are truly zero are shown as blanks.

Tax Type	Change in Collections	As Imposed			After Shifting		Suits Index for Tax Change *
		MN Households	Non-Residents	Business	MN Households	Exported	
State Taxes							
Taxes on Income and Estates							
Individual income tax--Personal	-192.0	-180.5	-11.5		-180.5	-11.5	+0.112
Individual income tax--Flow-through	216.0	190.2	25.8		190.2	25.8	+0.485
Corporate franchise tax	68.0			68.0	49.6	18.4	-0.187
Estate tax							
Total Income and Estate Taxes	91.9	9.6	14.3	68.0	59.2	32.7	+1.740
Taxes on Consumption							
State sales taxes							
General sales tax	-1.4	-1.4	-0.0		-1.4	-0.0	+0.250
Sales tax on motor vehicles							
Motor fuels excise tax							
Alcoholic beverage excise taxes							
Cigarette and tobacco excise taxes							
Insurance premiums taxes							
Gambling taxes							
MinnesotaCare taxes	676.5	619.7	56.8		619.7	56.8	-0.331
Solid waste management taxes							
Total Consumption Taxes	675.1	618.3	56.8	-	618.3	56.8	-0.331
Taxes on Property							
Residential recreational property	-1.5	-1.2	-0.3		-1.2	-0.3	+0.137
Commercial	-31.4			-31.4	-17.4	-13.9	+0.139
Industrial	-10.6			-10.6	-5.8	-4.7	+0.065
Utility	-6.6			-6.6	-5.0	-1.6	+0.211
Motor vehicle registration tax							
Mortgage and deed taxes							
Total Property Taxes	-50.0	-1.2	-0.3	-48.5	-29.4	-20.6	+0.137
Property Tax Refunds							
Homeowners	1.3	1.3			1.3		-0.618
Renters							
Total Property Tax Refunds	1.3	1.3			1.3		-0.618
Total State Taxes	718.3	628.0	70.8	19.4	649.4	68.9	-0.151
Local Taxes							
Property Taxes							
General Property Tax	-49.3	-16.8	-0.2	-32.4	-41.3	-7.9	+0.206
Homeowners (before PTR)	-16.1	-16.1			-16.1		+0.169
Residential rec & 2nd homes	-0.9	-0.7	-0.2		-0.7	-0.2	-0.008
Commercial	-4.7			-4.7	-2.6	-2.1	+0.139
Industrial	-1.6			-1.6	-0.9	-0.7	+0.065
Farm (other than residence)	-20.5			-20.5	-16.8	-3.7	+0.280
Rental Housing	-4.7			-4.7	-3.7	-1.1	+0.152
Utility	-0.9			-0.9	-0.7	-0.2	+0.211
Mining Production Taxes (taconite)							
Wheelage Taxes							
Taxes on Consumption							
Local Sales Taxes including motor vehicle excise taxes	23.4	11.5	1.4	10.5	20.5	2.8	-0.194
Local Gross Earnings Taxes							
Total Local Taxes	-25.9	-5.3	1.2	-21.8	-20.8	-5.1	+0.218
Total State and Local Taxes	692.4	622.8	72.0	-2.4	628.6	63.8	-0.149

Parts may not sum to totals due to rounding.

* Suits indexes for a reduction in regressive taxes (such as the sales tax) are shown as positive because the tax cut makes the system less regressive.

Appendix I: Technical Notes

A. Assumptions about Changes in Local Property Taxes

- Local government levies will change in response to changes in state aids and credits. Standard assumptions are used by the Property Tax Division to estimate the magnitude of those changes.

B. Estimating the Incidence of Changes in Business Taxes (“Incremental Incidence”)

- As explained on pages 70-71 of the 2019 *Tax Incidence Study*, the incidence of a change in the level of business taxes (“incremental incidence”) will differ from the incidence of existing business taxes (“average incidence”). Average incidence divides an existing business tax into three parts – the national average tax on all capital, the sector differential, and the Minnesota differential. In contrast, a change in the level of a business tax is all treated as a change in the Minnesota differential.
- If the level of Minnesota business taxes changes, this will generally change the amount of *federal tax* paid by the business – either the federal corporate income tax or the federal individual income tax for flow-through businesses. For a corporation paying federal tax at the 21% rate, each additional \$1,000 in Minnesota tax will reduce the federal tax burden by \$210. So \$210 of the \$1,000 of Minnesota tax burden is borne by the federal government in foregone tax revenue. The burden of the remaining \$790 in tax may be shifted to consumers in higher prices or to workers in lower compensation – or it may reduce the after-tax income of the business owner. This analysis assumes federal tax rates of 21% for corporate tax and 18% for individual income tax.
- The extent to which the tax burden will be shifted to consumers or workers will depend on the nature of the market. Minnesota tax changes are most likely to result in price changes if the market is local and close competitors face the same change in tax. Businesses selling in national or international markets are much less likely to shift the added cost to consumers by raising prices (or reduce their price in response to a tax cut). *As in the incidence study, the incidence results assume the market has had time to fully adjust to any tax changes.*
- The incidence of the **business tax** changes in the bill (as modeled here) is as follows:
 - Corporate tax increases: 46% shifted to Minnesota consumers, 27% shifted to Minnesota workers, less than 1% borne by Minnesota owners, and 27% borne by nonresidents and the federal government.
 - Business property tax changes: 27% of the burden to Minnesota consumers and renters, 12% to Minnesota workers, 6% to Minnesota owners (non-farm), 20% to Minnesota farm owners, and 35% to nonresidents and the federal government.
 - Individual income tax increases on flow-through income: The burden is assumed to fall on the recipient of the income, as modeled using the House Income Tax Simulation (HITS) Model.