

October 22, 2020

	Yes	No
DOR Administrative Costs/Savings	X	

Department of Revenue
Analysis of 5th Special Session Laws 2020, Chapter 3, Article 7

	Fund Impact			
	<u>F.Y. 2020</u>	<u>F.Y. 2021</u>	<u>F.Y. 2022</u>	<u>F.Y. 2023</u>
	(000's)			
Like-Kind Exchanges				
Individual Income Tax	\$0	(\$900)	\$200	\$200
Corporate Franchise Tax	<u>\$0</u>	<u>(\$1,100)</u>	<u>\$300</u>	<u>\$300</u>
Like-Kind Exchanges Total	\$0	(\$2,000)	\$500	\$500
Section 179 Expensing				
Individual Income Tax	\$0	(\$63,800)	(\$47,300)	(\$39,100)
Corporate Franchise Tax	<u>\$0</u>	<u>(\$24,200)</u>	<u>(\$17,900)</u>	<u>(\$14,800)</u>
Section 179 Total	\$0	(\$88,000)	(\$65,200)	(\$53,900)
General Fund Total				
Individual Income Tax	\$0	(\$64,700)	(\$47,100)	(\$38,900)
Corporate Franchise Tax	<u>\$0</u>	<u>(\$25,300)</u>	<u>(\$17,600)</u>	<u>(\$14,500)</u>
Total	\$0	(\$90,000)	(\$64,700)	(\$53,400)

The treatment of like-kind exchanges is effective retroactively for tax years 2018 and 2019 only. Full conformity to Section 179 is effective beginning with tax year 2020.

EXPLANATION OF THE BILL

Like Kind Exchanges and Section 179 Expensing (Article 7, Sections 1-3)

Like-Kind Exchanges. Federal law allows certain business or investment property to be exchanged for property of a like kind without recognizing any gain or loss at the time of the exchange. The Tax Cuts and Jobs Act (TCJA) disallowed the deferral of gains for most like-kind exchanges except for real property, beginning with tax year 2018. Minnesota conformed to this change in 2019.

Effective retroactively for tax years 2018 and 2019 only, the bill allows a taxpayer with a gain from a like-kind exchange that was disallowed under the TCJA to deduct the full value of the replacement property in the year the property was placed in service, to the extent that it is included in Section 179 property. Other Section 179 property would still be subject to the 80% addback and subtractions over five years.

Section 179 Expensing. Section 179 of the Internal Revenue Code allows a taxpayer to treat the cost of qualified business property as an expense in the year the property is placed in service. The current limit on Section 179 expensing is \$1.0 million. That amount is reduced by one dollar for every dollar of property placed in service over \$2.5 million, so a taxpayer who places \$3.5 million or more of property in service during the tax year is ineligible. Those thresholds are indexed for inflation beginning in tax year 2019.

EXPLANATION OF THE BILL (Cont.)

Under prior Minnesota law, a taxpayer was required to add back 80% of the difference between the amount deducted federally and the amount that was allowed under pre-2003 federal law (up to \$25,000, reduced by one dollar for each dollar that total expenses exceed \$200,000). The amount of the addback may be subtracted in equal parts over the next five years.

The bill fully conforms to the federal limits on Section 179 expensing beginning with tax year 2020, eliminating the need for the addbacks and associated subtractions. Subtractions will continue to be claimed for additions made before tax year 2020.

REVENUE ANALYSIS DETAIL

- The estimates are based on estimates for the federal legislation prepared by the staff of the Joint Committee on Taxation, dated December 18, 2017.
- The estimate was adjusted to reflect projected capital expenditures from the April 2020 forecast from IHS Markit.
- The estimate was divided between the individual income tax and corporate franchise tax based on the percentage of eligible property owned by entities subject to each tax.
- The estimate was apportioned to Minnesota and adjusted for differences in federal and state tax rates and federal and state fiscal years.
- The proposal would reverse the impact of conformity to the TCJA for taxpayers who have disallowed deferral of like-kind exchanges and instead claimed Section 179 expensing for that property.
- Based on information from 2018 individual income tax returns, about 65% of disallowed like-kind exchanges were reported on returns that also had Section 179 expensing. Those taxpayers could subtract the full value of the replacement property in the year it was placed in service, eliminating the need for the additions and subtractions.
- Beginning in 2020, all Section 179 property would be eligible for a full deduction in the year the property is placed in service.
- All of the tax year 2020 impact is allocated to FY 2021. Other tax years were allocated 30% / 70% to fiscal years.

Minnesota Department of Revenue
Tax Research Division
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