



**INDIVIDUAL INCOME TAX
Social Security Subtraction
Net Investment Income Tax**

March 17, 2021

| | | |
|----------------------------------|------------|-----------|
| | Yes | No |
| DOR Administrative Costs/Savings | X | |

Revised to Correct Investment Tax Calculation

Department of Revenue
Analysis of S.F. 558 (Eken)

| | Fund Impact | | | |
|------------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
| | <u>F.Y. 2022</u> | <u>F.Y. 2023</u> | <u>F.Y. 2024</u> | <u>F.Y. 2025</u> |
| | | (000's) | | |
| Social Security Subtraction | \$0 | (\$504,700) | (\$538,800) | (\$573,100) |
| Tax on Net Investment Income | <u>\$0</u> | <u>\$588,600</u> | <u>\$635,400</u> | <u>\$670,900</u> |
| General Fund | \$0 | \$83,900 | \$96,600 | \$97,800 |

Effective beginning with tax year 2022.

EXPLANATION OF THE BILL

Current Law: A taxpayer may subtract a portion of social security income when calculating Minnesota taxable income. For 2021, the maximum subtraction is \$5,290 for married joint filers, \$2,645 for married separate filers, and \$4,130 for single and head of household filers.

The subtraction is reduced by 20% of provisional income over the following thresholds for 2021: \$80,270 for married joint filers, \$40,135 for married separate filers, and \$62,710 for single and head of household filers. Provisional income is income used to calculate the federally taxable portion of social security benefits. The thresholds and maximum subtractions are adjusted annually for inflation.

Proposed Law: The entire amount of social security benefits received by a taxpayer during the tax year is allowed as a subtraction.

The proposal also creates a tax on all net investment income of individuals, estates, and trusts over \$250,000. Net investment income includes interest, dividends, annuities, royalties, and other gains not derived from a trade or business.

For nonresidents and part-year residents, the tax is assumed to be apportioned to Minnesota in the same way as the current income tax.

By December 1, 2022, and each year after, the Commissioners of the Department of Revenue and the Department of Management and Budget must estimate the reduction in revenue from the proposed social security subtraction for the current tax year.

By January 15th of the following year, the Commissioners must determine and publish the tax rate on net investment income for the previous tax year to sufficiently offset the projected revenue loss. The tax rate is rounded to the nearest one-tenth of one percent.

REVENUE ANALYSIS DETAIL

Social Security Subtraction

- The House Income Tax Simulation Model (HITS 7.0) was used to estimate the revenue impact. These simulations assume the same economic conditions used by Minnesota Management and Budget for the forecast published in February 2021. The model uses a stratified random sample of tax year 2018 individual income tax returns compiled by the Minnesota Department of Revenue.
- Tax year impacts were allocated to the following fiscal year.
- About 392,900 returns would be affected in tax year 2022. The average reduction in tax would be \$1,196.

Tax on Net Investment Income

- The estimate is based on a sample of tax year 2018 individual income tax returns compiled by the Minnesota Department of Revenue.
- In 2018, there was about \$19.6 billion in net investments attributed to Minnesota.
- The rate to cover the cost of the full social security subtraction in tax year 2022 is estimated to be 3.0%.
- The tax rate would change year to year to generate enough revenue to cover the social security subtraction.
- Since investment income is volatile the rate could change substantially from year to year, and the actual collections could differ from the annual estimates.
- About 35,300 returns would be affected in tax year 2022. The average increase in tax would be approximately \$16,660.

Minnesota Department of Revenue
Tax Research Division
[https://www.revenue.state.mn.us/
revenue-analyses](https://www.revenue.state.mn.us/revenue-analyses)