AN OVERVIEW OF GOVERNOR JESSE VENTURA'S FY 2002-03 BIENNIAL BUDGET RECOMMENDATIONS

This paper provides an overall description and detail of Governor Jesse Ventura's FY 2002-03 biennial budget recommendations. Part one is the summary section. Part two provides details organized according to the jurisdictions of the House of Representatives' fiscal committees and divisions.

The Overall Budget Picture

The Governor's Budget in Detail
- Family and Early Childhood Finance
- K-12 Education Finance
- Higher Education Finance
- Health and Human Services Finance
- Judiciary Finance
- Environment and Natural Resources Finance
- Agriculture and Rural Development Finance
- Jobs & Economic Development Finance
- State Government Finance
- Transportation Finance

Capital Investment

Tax Revenues, Local Aid and Credits

The Overall Budget Picture

The Governor is proposing a $43 billion budget for the 2002-03 biennium. Of this amount, $27.4 billion is the general fund budget. In addition, the Governor is proposing $291 in general fund revenue reductions. He would also transfer receipt of $162 million of motor vehicle sales tax revenues to the highway user tax distribution fund in FY 2002 reducing general fund revenues by that amount.

The Governor recommends that $911 million of the projected $924 million FY 2001 balance be used for another sales tax rebate. The additional $13 million would be used for other tax reductions, deficiency appropriations and other minor adjustments to appropriations.

The Governor's recommendations result in state general fund expenditures increasing by 11.0 percent in the FY 2002-03 biennium compared to the FY 2000-01 biennium. Also, in FY 2004-05 when the a number of the Governor's recommendations are in effect for both years of the biennium, general fund expenditures would increase another 13.1 percent.

Table 1 summarizes the general fund resources available and expenditure amounts for the current biennium (FY 2000-01) and the next biennium (FY 2002-03) and the planning estimates for FY 2004-05 assuming the Governor's recommendations for FY 2002-03 are enacted. The rows labeled "(Gov)" show changes from the base level.

Table 1

General Fund: Fiscal Years 2000-05

($ in millions)

	FY 00-01	FY 02-03	Percent Change	FY 04-05	Percent Change
Balance Forward	$1,921	$1,108		$1,207	
Revenues (Base)	$24,710	$28,211		$31,272	
Revenue Changes (Gov)	($916)	($787)		($145)	
Current Revenues	$23,795	$27,423	15.3%	$31,127	13.5%
Total Resources Available	**$25,715**	**$28,531**		**$32,334**	
Expenditures & Transfers (Base)	$24,599	$25,388		$26,310	
Expenditure Change (Gov)	$9	$1,936		$4,585	
Total Expenditures	**$24,607**	**$27,324**	**11.0%**	**$30,895**	**13.1%**
Balance Before Reserves	$1,108	$1,207		$1,440	
Reserves	$1,108	$1,161	4.7%	$1,241	
Budgetary Balance	**($0)**	**$47**		**$199**	

Base is from the November 2000 forecast.

Table 2 illustrates a fiscal year by fiscal year comparison of revenues and expenditures in the Governor's proposed budget. While FY 2002 general fund expenditures would drop 3.1 percent below the FY 2000 level, FY 2003 expenditures increase 14.7 percent over the FY 2002 level.

Table 2

General Fund by Fiscal Year: FY 2000-03
($ in millions)

	Nov. Forecast FY 00	Gov's Recs FY 01	% Change	Gov's Recs FY 02	% Change	Gov's Recs FY 03	% Change
Balance Forward	$1,921	$2,125		$1,108		$1,139	
Revenues (Base)	$11,681	$13,029		$13,764		$1,921	
Revenue Changes (Gov)		($916)		($1,009)			
Current Revenues	**$11,681**	**$12,114**	**3.7%**	**$12,755**	**5.3%**	**$14,668**	**15.0%**
Total Resources Available	**$13,602**	**$14,239**		**$13,864**		**$15,806**	
Expenditures & Transfers (Base)	$11,476	$13,123		$12,638		$12,750	
Expenditure Change (Gov)		$9		$87		$1,849	
Total Expenditures	**$11,476**	**$13,131**	**14.4%**	**$12,725**	**-3.1%**	**$14,599**	**14.7%**
Balance Before Reserves	$2,125	$1,108		$1,139		$1,207	
Reserves	$1,380	$1,108		$1,161		$1,161	
Budgetary Balance	**$746**	**($0)**		**($22)**		**$47**	

The Budget Situation

The November 2000 Forecast of General Fund Revenues and Expenditures showed that projected revenues would exceed expenditures by $2.086 billion for the FY 2002-03 biennium and by $924 million for the current biennium. The $924 million in the current biennium was designated for a tax rebate as required in Minnesota Statutes, Section 16A.1522.

The $2.086 billion for FY 2002-03 includes $334 million in tobacco settlement funds that were excluded from consideration when the 2000 Legislature was considering future resources available.

Expenditures for FY 2002-03 in the November forecast includes $737 million for planning estimate inflation. This amount was calculated by applying 2.0 percent inflation to almost all program expenditures. In preparing budget recommendations, the Governor included three percent per year increases for salaries and benefits and adjustments for changes in agency space rent and several other items. These "policy base changes" totaled $105 million. In the process of going from a "planning estimate" budget to one that included inflation in limited areas, the Governor had available another $632 million to allocate for other purposes.

Table 3 shows the differences between the Governor's budget recommendations and the projected expenditures in the November 2000 forecast. The Governor is recommending changes in the current biennium as well as those for the next biennium. The Governor's recommendations would allocate all available FY 2001 funds in FY 2001. However, the final amount available for the sales tax rebate would not be determined until after June 30, 2001.

Table 3

Governor's General Fund Recommendations: Change from November 2000 Forecast Base

Dollars in millions

FY 2001 Changes	
Sales Tax Rebate, Others	$912
Other Changes	$12
Net Changes - FY 2001	**$924**
FY 2002-03 Changes	
Individual Income Tax	$1,124
Corporate Franchise Tax	$40
Sales Tax	($544)
Motor Vehicle Taxes	$188
Statewide Property Tax	($470)
Other State Taxes	$13
Other Revenue Changes	($60)
Property Tax Aids and Credits	$1,388
Endowment - Tobacco Revenues	$334
K-12 Education	$105
Family & Early Childhood Education	$17
Higher Education	$99
Health & Human Services	$215
Environment & Agriculture	$16
Economic Development	$38
Judiciary/Criminal Justice	$91
Transportation	$47
State Government	$75
Debt Service	$22
Budget Reserve	$78
Other Changes	($40)
Ending Balance	$47
Planning Estimate Inflation	($737)
Net Changes - FY 2002-03	**2,086**

How the Governor Recommends Using the $2.1 Billion

Changes from the November 2000 Forecast for FY 2000-01

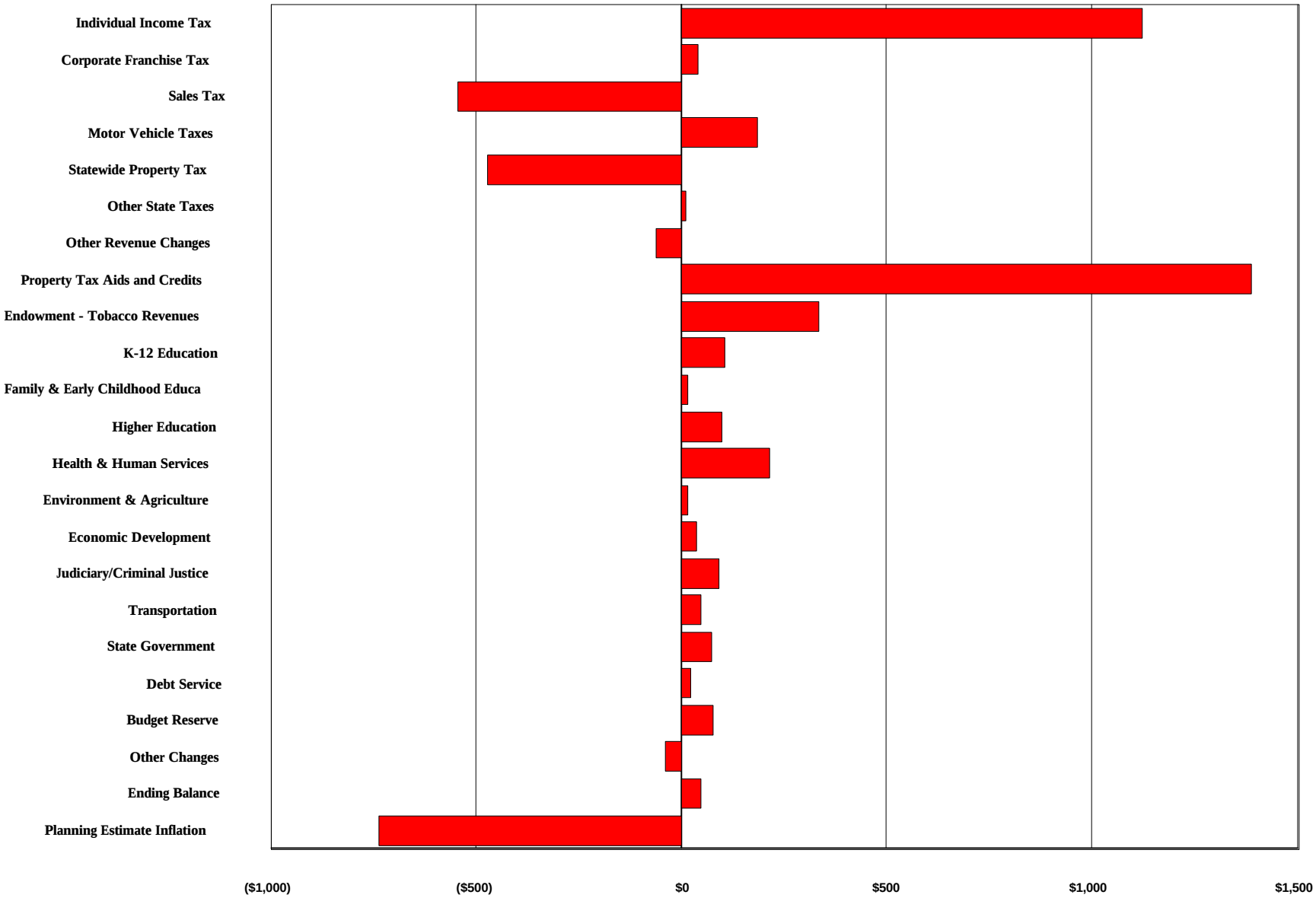

Table 4 show changes in the Governor's budget recommendations arranged by the jurisdictions of the House Fiscal Committees. This chart compares the Governor's recommendation for FY 2002-03 to the base for that year from the November 2000 forecast and to the FY 2000-01 appropriations also as estimated in the November forecast.

The November forecast base numbers for FY 2002-03 include what are referred to as "technical base adjustments". After adjusting for forecast changes for caseloads and enrollments, these numbers are that same numbers that legislative committees assumed were the "tails" during the 1999 and 2000 sessions.

Table 4

General Fund Expenditures by Committee
FY 2002-03 Governor's Recommendation Compared to FY 2000-01 & FY 2002-03 Base
Dollars in millions

	November Forecast FY 00-01	Base November Forecast FY 02-03	Gov's Rec FY 02-03	$ Change Governor FY 02-03 vs FY 00-01	% Change Governor FY 02-03 vs FY 00-01	$ Change Governor FY 02-03 vs FY 02-03 Base	% Change Governor FY 02-03 vs FY 02-03 Base
K-12 Education	$8,128	$8,386	$8,491	$363	4.5%	$105	1.3%
Family & Early Childhood Education	$434	$542	$560	$126	29.0%	$17	3.2%
Higher Education	$2,642	$2,668	$2,768	$126	4.8%	$99	3.7%
Property Tax Aids & Credits	$3,318	$3,467	$4,856	$1,538	46.3%	$1,388	40.0%
Health & Human Services	$5,433	$6,227	$6,441	$1,008	18.5%	$214	3.4%
Environment	$421	$402	$414	($6)	-1.5%	$12	3.0%
Agriculture	$135	$127	$130	($4)	-3.3%	$4	2.8%
Economic Development	$468	$366	$403	($64)	-13.8%	$38	10.3%
Judiciary \Criminal Justice	$1,174	$1,236	$1,326	$152	13.0%	$91	7.4%
State Government	$777	$716	$791	$14	1.9%	$75	10.5%
Transportation	$504	$161	$208	($296)	-58.7%	$47	29.1%
Debt Service	$567	$632	$654	$87	15.3%	$22	3.4%
Capital Projects	$176	$19	$19	($157)	-89.2%	$0	0.0%
Budget Reserve	$622	$622	$700	$78	12.5%	$78	12.5%

Price of Government

State law requires the Governor to make recommendations on the percent of Minnesota personal income represented by the amount of revenue raised by state and local governments. State and local government revenues include all revenues from all sources (including fees) except those that are transferred from the federal government. Under the Governor's recommendations, state and local government revenue is estimated to be 16.1percent of Minnesota personal income for FY 2002-03 and 15.6 percent for the FY 2004-05 biennium. These compare to an estimated 16.3 percent for the FY 2000-01 biennium. Table 5 on the next page shows the estimated state and local revenues compared to personal income in Minnesota.

Table 5

Price of Government
Governor's Targets for FY 2002-03 and FY 2004-05
Dollars in millions

	FY 98-99	FY 00-01	FY 02-03	FY 04-05
Minnesota Personal Income	$268,578	$303,063	$340,556	$382,314
Change		12.8%	12.4%	12.3%
State Government Revenues	$26,146	$29,885	$34,184	$38,338
% of Minnesota Personal Income	9.7%	9.9%	10.0%	10.0%
Local Government Revenues	$18,509	$19,441	$20,487	$21,483
% of Minnesota Personal Income	6.9%	6.4%	6.0%	5.6%
Total State and Local Government Revenues	$44,655	$49,326	$54,671	$59,821
Change		10.5%	10.8%	9.4%
% of Minnesota Personal Income	16.6%	16.3%	16.1%	15.6%

For more information on general budget issues, contact Bill Marx at 651-296-7176 or bill.marx@house.leg.state.mn.us

Family and Early Childhood Education Finance

The Governor's FY 2002-03 budget recommends a total of $559.6 million in general fund appropriations for programs administered by the Office of Community Services in the Department of Children, Families and Learning (CFL). This amount reflects an increase of $125.6 million, or 28.9 percent, above FY 2000-01 adjusted budget levels of $434.0 million. It also represents an increase of $17.4 million, or 3.2 percent, above current law spending ($542.2 million). The bulk of these additional funds can be traced to 1) the return of general fund appropriations for Basic Sliding Fee child care ($64.1 million), 2) a proposed consolidation of Minnesota's publicly subsidized child care programs (Basic Sliding Fee and Minnesota Family Investment Plan (MFIP) child care), and 3) to a lesser extent, scheduled increases in Adult Basic Education spending ($17.4 million).

Family & Early Childhood Education Finance
Governor's FY 02-03 General Fund Recommendations
(all dollars in thousands)

Department of Children, Families and Learning	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
Children & Family Support	269,281	372,715	390,094	45%	5%
Prevention	55,885	49,180	49,180	-12%	0%
Self-Sufficiency & Lifelong Learning	85,070	98,992	98,992	16%	0%
Libraries	23,677	21,346	21,346	-10%	0%
Total	**433,913**	**542,233**	**559,612**	**29%**	**3%**

Children & Family Support

The Governor recommends a $17.4 million increase in general fund spending to support the consolidation of two state-supported child care programs, Minnesota Family Investment Plan (MFIP) and Basic Sliding Fee. MFIP child care assistance subsidizes the child care costs of families receiving MFIP cash assistance. It may also be used to pay the child care costs of eligible families who have newly left the MFIP program. MFIP Child care was forecasted at $154.9 million for the 2002-03 biennium. The Basic Sliding Fee Child Care program, which is regaining full, direct appropriation funding ($54.1 million per year, November forecast) provides a child care subsidy to working families who are not receiving cash assistance through MFIP. The Governor's proposal to consolidate these programs seeks an appropriation of $280.4 million, which is a higher level of funding (3.2 percent above November forecast levels) than the sum of the two programs as they currently exist in law.

NOTE: In association with this consolidation, the Governor also seeks to 1) move the Higher Education Child Care Assistance Program (HESO) and the Dependent Care Tax Credit (DCTC) program to the Department of Children, Families and Learning, and 2) redefine the parameters of eligibility for MFIP Child Care assistance. ***If any or all of these changes occur, the fiscal impact would be in addition to the $17.4 million general fund increase discussed above.***

All other programs in this cluster of budget activities, including School Readiness, Early Childhood and

Family Education, Head Start, Way to Grow, and Health & Development Screening, are flat-funded at base budget levels provided for in current law.

Prevention

The Governor recommends the consolidation of three existing budget activities–Children's Trust Fund, Male Responsibility and Adolescent Parenting–into the Children's Trust Fund. This consolidation would require an expansion of the authority currently governing the use of Trust Fund moneys to include these additional responsibilities. Since the proposal seeks a simple shift of base-level funds from the Male Responsibility and Adolescent Parenting accounts to the Children's Trust Fund, the net fiscal impact of in this consolidation would be zero.

All other programs in this cluster of budget activities, including Family Collaboratives, Community Education Aid, Adults with Disabilities Aid, Hearing Impaired Adults, Violence Prevention Grants, Abused Children, Family Visitation Centers and After School Enrichment Grants are funded at base budget levels reflected in current law.

Self-Sufficiency & Lifelong Learning

The Governor recommends biennial funding of $66.9 million for Adult Basic Education, an increase of $17.4 million, or 35.3 percent, over FY 2000-01 spending levels of $49.4 million. This increase represents the changes in program law agreed to during FY 2000-01 biennial budget deliberations, and thus reflects only base budget funding.

All other programs in this cluster of budget activities, including Minnesota Economic Opportunity Grants, Transitional Housing, Emergency Services-Shelter, Adult Graduation Aid, GED tests, Food Shelf/Food Bank Programs, Family Assets for Independence, Lead Abatement are funded at base budget levels reflected in current law.

Libraries

All Library accounts, including Basic Support Grants, Multi-county, Multi-type Library Systems and Regional Library Telecommunications Aid are funded at base budget levels.

Implications of the Governor's Budget Recommendations:

The FY 2002-03 executive budget for Family and Early Childhood Education programs continues to reflect The Big Plan initiatives, placing a high priority on ways to make people self-sufficient. For most programs, current spending is maintained. The largest change in the FY 2002-03 budget proposal is the consolidation of all state-supported child care assistance programs, including two programs currently administered in agencies other than the Department of Children, Families and Learning. In addition, requested changes in income thresholds for MFIP Child Care eligibility (program entry to be changed from 75 percent median income to 50 percent median income, as contained in the budget request for the Department of Human Services) will impact both the number of families and the intensity of services provided for those families participating in the state's child care programs. Preliminary projections of this consolidation of programs and funds anticipate the use of federal TANF dollars to support the transition, with additional administrative costs for CFL to increase in each year beyond the 2002-03 biennium.

For additional information on Family & Early Childhood finance issues, contact Katherine Schill at 651-296-5384, or katherine.schill@house.leg.state.mn.us

K-12 Education Finance (revised 03/01)

For the FY 2002-03 biennium, the Governor recommends $8.5 billion in general fund state aid for K-12 education. This compares with the February forecast of current law 2002-03 K-12 education spending of $8.4 billion, an increase of $104.7 million, or 1.25 percent, from forecast to Governor's recommendation for the FY 2002-03 biennium. When compared to spending in FY 2001 of $4.23 billion, the FY 2002 recommended spending of $4.20 billion is a decrease of 0.9 percent. Compared with that recommended FY 2002 level, the recommended FY 2003 appropriation of $4.3 billion is an increase of 1.9 percent.

In addition to this general fund spending, the Governor recommends eliminating K-12 Trunk Highway Fund spending of $42,000 for the FY 2002-03 biennium, and adding new spending of $10 million for the FY 2002-03 biennium from the Disabled Workers Special Revenue Fund.

Education property taxes in the Governor's budget recommendations are unchanged from current law in FY 2002, and reduced significantly in FY 2003. Property taxes for FY 2002 (the pay 2001 property taxes already being levied) decreased by 18.7 million from FY 2001, or 1.0 percent, to $1.9 billion. School district property taxes for FY 2003 (payable 2002) in the Governor's budget are estimated to decrease by $861 million, or 44.3 percent from FY 2002, to $1.1 billion. A detailed explanation of the Governor's property tax changes can be found in the taxes section of this document.

The following summarizes the Governor's budget initiatives, with the costs expressed as a biennial total, from the general fund unless otherwise noted:

General Education

- Change pupil weighting to .5 for kindergarten pupils, 1 for pupils in grades 1-6, and 1.15 for pupils in grades 7-12. This change reduces the total number of pupils by approximately 11 percent, but all formula factors, including the basic formula amount, are adjusted so that the same revenue is paid out despite the change in pupil weights. The current pupil weights are .557 for kindergarten pupils, 1.115 for pupils in grades 1-3, 1.06 for pupils in grades 4-6 and 1.3 for pupils in grades 7-12.

- The Governor recommends that the basic formula amount increase in the FY 2003 by $60, approximately 1.4 percent. In FY 2002, the formula would remain at $3,964, and for FY 2003, it would be $4,461. There are two components to the $497 increase between FY 2002 and FY 2003: $60 represents the 1.4 percent increase, and $437 represents the change in pupil weights, as well as the roll-in of equity, supplemental, transition, and assurance of mastery revenues, and the elimination of a pension adjustment. The net cost of all these changes, including the formula increase, is $66.8 million.

- $14.1 million in savings from the elimination of Assurance of Mastery revenue. Currently, districts receive $22.50 per K-8 pupil unit.

- $21.2 million in savings from the elimination of Equity Revenue. Currently, districts which are receive the least Basic, Supplemental, Transition and Referendum revenue are eligible for Equity Revenue, on a sliding scale based on where they rank in those categories of revenue.

- $3.6 million in aid savings and $4.8 million in levy savings from the elimination of Supplemental Revenue. Some districts receive supplemental revenue, primarily as a grandfather for revenue from the late 1980s.

- $4.4 million in aid savings and $5.1 million in levy savings from the elimination of Transition Revenue. Transition revenue is intended to minimize the negative impact of formula changes on individual school district revenue. There are three components of transition revenue: transportation transition, compensatory transition and cooperation transition.

- $2.5 million in savings from the accelerated phase-out of Training & Experience (T&E) revenue. Currently, T&E revenue (based on the age and experience of a district's faculty) is being phased out through the exclusion of new teachers (since 1997) from a district's T&E revenue calculation. As a result, the phase-out will last until the last

teacher who was working in 1997 for a particular district leaves. The Governor's proposal would change the phase-out to a fixed term of three years.

- $524,000 in aid cost and $2.4 million of levy cost for a new three year hold harmless for districts who, by the Governor's proposed changes in General Education revenue would end up with less revenue than they had prior to the changes. The hold harmless would be eliminated after FY 2005.

- $53.4 million related to the elimination of the general education teacher retirement aid reduction. The aid reduction consists primarily of money that was recaptured from school districts when the districts' employer contribution to TRA was lowered. In addition, $60 per pupil unit is allocated to school districts that did not receive either an aid reduction or a reduction in their teacher retirement contribution costs. Of this cost, $47 million is to eliminate the general education teacher retirement aid reduction, and $6.4 million is for non-participating districts.

Education Excellence

- $10 million for Advanced Achievement and Accountability, to develop and provide initial assessment of students in individual schools, then categorize them based on the results of these assessments, and then allow the Department of Children, Families and Learning (DCFL) to provide continuous improvement for those schools.

- $15 million for the Performance Incentives Pool, to encourage districts to develop alternative compensation packages and career paths for teachers. A district or building which qualifies will receive $150 per pupil in additional revenue.

- $10 million from the Workforce Development Special Revenue Fund for Teachers for the 21st Century. The funding will be used to enhance recruitment of teachers in areas where there are shortages. The focus will be on loan forgiveness programs, tuition waivers, licensing changes, alternative licensing and mentoring and induction.

- $6.4 million for the Success for the Future Program, for American Indian students. The $6.4 million is partially offset by $3.7 million in savings achieved through the elimination of three current American Indian student programs: American Indian Language and Culture, American Indian Education and American Indian Post-Secondary Preparation Grants. The new program will focus on increasing retention and increasing coordination efforts in Indian Education programs.

- $1.5 million for the Internet System for Education and Employment Knowledge (ISEEK) and Jobs for America's Graduates. This spending is offset by a reduction of $2.3 million in the Education and Employment Transitions program.

Facilities and Technology

- $5.3 million to increase debt service equalization aid and create a second tier of equalization for districts with high debt. Current debt service aid is paid out using an equalizing factor of $4,000 on all qualified debt. The Governor's recommendation is to increase that to $5,000, which will increase aid to low value districts. In addition, districts with new debt after July, 2001, for which debt service exceeds 20 percent of their tax capacity, will receive aid based on an equalizing factor of $9,000.

Nutrition

- $285,000 to convert the "Fast Break for Learning" program from a grant program to a formula-based program with a per meal reimbursement rate of $1.04.

Lola and Rudy Perpich Minnesota Center for Arts Education

No new initiatives.

Minnesota State Academies for the Deaf and Blind

- $462,000 for improvements in program delivery and safety, including specialized & short-term services, hiring a safety director, residential and environmental safety needs, emergency communications (pagers) at the School for the Deaf and transportation needs.

Department of Children, Families and Learning

- $1 million in net general fund costs to create a Revolving Account for teacher licensure. Currently, teacher license fees are deposited in the general fund. These fees are projected to be $1.3 million for FY 2002 and later. The DCFL would use these funds to process teacher licenses. The net cost is $1 million, due to $2.6 million in loss to the general fund from the capturing of these fees into the revolving fund, and savings of $1.6 million due to converting part of the general fund budget costs to the revolving fund.

- $800,000 for additional DCFL staff for charter school financial management support, investigation of maltreatment of minors complaints, staffing at the Minnesota Library for the Blind and Physically Handicapped, and approving educational programs in care and treatment facilities.

- $520,000 to transfer the Children's Museum operating supplement from the Department of Administration to DCFL.

- $1.25 million transfer to move the funding of the Minnesota Foundation for Student Organizations from a stand alone appropriation to the DCFL budget.

Implications

The Governor's recommendations amount to a decrease of 1 percent in the first year of the biennium, and a 1.9 percent increase in the second year of the biennium, compared to the prior year. The increases are below the rate of inflation during the same period, creating the potential for financial difficulty at the district level. In addition, relative to the base funding already designated in current law, the Governor's recommendations amount to a 1.25 percent increase over the FY 2002-03 biennium (see the table below).

K-12 Education State Appropriations	Base Funding	Governor's Recommendation	Percent over Base
FY 2000	$3,878,912	$3,878,912	0.00%
FY 2001	$4,233,933	$4,233,933	0.00%
change from prior year	9.2%	9.2%	
FY 2002	$4,182,625	$4,195,717	0.31%
change from prior year	-1.2%	-0.9%	
FY 2003	$4,182,744	$4,274,352	2.14%
change from prior year	0.0%	1.9%	
FY 2004	$4,189,746	$4,279,340	2.09%
change from prior year	0.2%	0.1%	
FY 2005	$4,204,418	$4,291,814	2.04%
change from prior year	0.4%	0.3%	

The basic formula amount, which grew by 4.7 percent and 3.2 percent in FY 2000 and FY 2001, respectively, would not grow in FY 2002, and would only grow by 1.4 percent in FY 2003. This is the largest source of non-dedicated revenue for school districts. The Governor has asserted that this increase will allow for a 2 percent raise in instructional staff in the second year of the biennium.

While the elimination of some of the individual components of general education and the creation of new pupil weights has no impact on statewide revenue, there could be significant distributional impacts on individual districts. For example, a district with supplemental revenue greater than $4 per pupil (the amount rolled into the formula), would see a revenue reduction. On the pupil weighting side, a district with a population skewed toward secondary students at a rate greater than the average would lose revenue. No district will lose money in FY 2003, FY 2004 or FY 2005, due to the hold harmless revenue, after FY 2005, some individual districts could see significant revenue reductions. Further, since the hold harmless is calculated **after** the formula increase of $60 is factored in, for many districts the $60 will be used to hold them harmless, resulting in no net increase in revenue.

For additional information about K-12 education finance issues, contact Greg Crowe at 651-296-7165, or greg.crowe@house.leg.state.mn.us

Higher Education Finance

The Governor's general fund budget for higher education for the FY2002-03 biennium is $2.767 billion. This represents an increase of $125.9 million or 4.8 percent over FY 2000-01 current spending. Of this amount, $26 million is in base adjustments, mainly for enrollment, with the Governor recommending a $99 million or 3.7 percent increase over the FY 2002-03 adjusted base. On an annual basis the Governor recommends total new spending in FY2002 of $1.02 million or an increase of .1percent from FY 2001. In FY 2003, the Governor recommends total new spending of $41.2 million or an increase of 3 percent over FY 2002. Higher education represents 10.1 percent of the Governor's FY 2000-03 General Fund budget. The following summarizes the Governor's higher education initiatives:

Higher Education Finance FY 02-03
Governor's General Fund Recommendations
(all dollars in thousands)

	November Forecast FY 2000-01	Current Law FY 2002-03	Governor's Recs FY 2002-03	Percentage Change Gov. FY 2002-03 vs. November FY 2000-01	Percentage Change Gov. vs. Current Law FY 2002-03
HESO	321,335	321,272	331,151	3.05%	3.07%
MnSCU	1,130,491	1,141,567	1,182,212	4.58%	3.56%
Mayo Foundation	3,097	3,274	3,434	10.88%	4.89%
U of M	1,186,853	1,202,258	1,250,876	5.39%	4.04%
Total	**2,641,776**	**2,668,371**	**2,767,673**	**4.77%**	**3.72%**

Higher Education Services Office

- The Governor recommends a total increase of $9.77 million for FY 2002-03. He also recaptures $30.1 million from increases in the federal PELL grant and recycles it for various improvements in the State Grant program.

- $5.5 million to change to grant program to reflect actual tuition and fees paid by individual students on a per credit basis.

- $10.6 million to extend State Grant eligibility from 4 years of attendance to 4 years of aid through a baccalaureate degree.

- $14 million to reduce the assigned family responsibility on independent students in the State Grant program.

- $10 million to increase the Living and Miscellaneous Expense allowance by 2.5% annually.

- $4 million to expand TRIO type college access programs.

- $3.5 million to expand services through the MINITEX interlibrary loan system.

- $1.5 million for projected cost increases in the interstate tuition reciprocity program.

Minnesota State Colleges and Universities

- The Governor recommends increases of $13.4 million in FY 2002 and $27.25 million in FY 2003 for a total of $40.65 million or 3.6% over the biennium.

- The Governor also recommends an additional $7 million be appropriated to MnSCU from the Workforce Development Fund for regional centers of excellence.

Mayo Foundation

- The Governor recommends total funding of $3.434 million for FY 2002-03, an increase of $.337 million or 10.8%.

- For the medical school the Governor recommends $92 thousand to increase the capitation grant per student from the current level of $14,405 to $15,125 in FY 2002 and $15,881 in FY 2003.

- For the Family Practice Residency program the Governor recommends an inflationary increase of $19 thousand.

- For the St. Cloud residency program the Governor recommends an inflationary increase of $49 thousand.

University of Minnesota (U of M)

- The Governor recommends increases of $21.32 million in FY 2002 and $27.23 million in FY 2003 for a total of $48.62 million or 4.04% over the biennium. Of this amount $8 million in FY2002 is a one-time appropriation for the medical school leaving $13.39 million in FY 2002 and $40.62 overall for general inflation.

- The Governor recommends an additional $8 million in appropriations to the Department of Health from the Medical Education and Research endowment for purposes related to the medical school.

For more information on Higher Education Finance issues, contact Doug Berg, 651-296-5346 or at doug.berg@house.leg.state.mn.us

Health and Human Services Finance

The Governor proposes to spend $6.4 billion from the General Fund on Health and Human Services for the FY 2002-03 biennium, an increase of $1.0 billion (19 percent) from the previous biennium (see Table 1 below). In addition to the $6.4 billion above, the remaining one-time tobacco settlement payments of $334.2 million will be diverted from the general fund to the Tobacco Settlement fund to establish the Healthy Kids Learn endowment and provide additional funding for the existing Medical Education endowment. In the next biennium (FY 2004-05), often referred to as "the tails", general fund spending is projected to be $7.4 billion.

Table 1: Health and Human Services Finance Committee
Governor's FY 2002-03 General Fund Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Governor vs. Current Law FY 02-03
Department of Human Services	5,245,168	6,037,948	6,214,292	18%	3%
Department of Health	124,612	124,320	155,084	24%	25%
Veterans Homes Board	52,995	57,120	58,978	11%	3%
Emergency Medical Services Board	5,497	3,478	7,003	27%	101%
Ombudsman for MH/MR	2,858	2,756	3,320	16%	20%
Disabilities Council	1,389	0	1,406	1%	N/A
Ombudsperson for Families	337	342	507	50%	48%
Total	**5,432,856**	**6,225,964**	**6,440,590**	**19%**	**3%**

From the Health Care Access fund, the Governor recommends spending $481.3 million, an increase of $164.1 million (52 percent) from the previous biennium. From the federal Temporary Assistance for Needy Families block grant, the Governor proposes spending $568.9 million, an increase of $83.3 million (17 percent) from the previous biennium. All amounts refer to direct appropriations.

All funds spending for Health and Human Services, which include direct and statutory appropriations, totals $15.4 billion for the FY 2002-03 biennium. Table 2 on the next page shows the total recommended spending for all funds.

Table 2: Health and Human Services Finance Committee
Governor's FY 2002-03 General Fund Recommendations (*)
(all dollars in thousands)

	Nov. Forecast FY 2000-01	Gov's Recs FY 2002-03	% Change Gov. FY 02-03 vs. November FY 00-01
General fund	5,560,088	6,530,589	17%
Federal fund	5,133,815	5,809,622	13%
Health care access fund	497,827	732,021	47%
Federal TANF block grant	485,587	568,899	17%
Special revenue fund	567,097	398,871	-30%
State government special revenue fund	71,757	78,534	9%
Medical education & research fund	56,585	66,449	17%
Tobacco use prevention fund	21,529	49,845	132%
Healthy kids fund	0	3,000	N/A
Trunk Highway fund	1,571	0	N/A
Solid Waste fund	396	0	N/A
Miscellaneous agency fund	10,275	10,496	2%
Child support enforcement fund	1,028,995	1,047,630	2%
Gift fund	2,679	2,042	-24%
General projects fund	135	0	N/A
Minnesota Resources fund	200	0	N/A
Lottery cash flow fund	2,896	2,609	-10%
Enterprise funds (CD services)	29,357	30,230	3%
Enterprise funds (State-operated services)	86,753	93,814	8%
Enterprise fund (Neuro-rehab hospital)	3,232	6,464	N/A
Total:	**13,560,774**	**15,431,115**	**14%**

* Direct and statutory appropriations.

Significant Initiatives

The Department of Human Services and the Department of Health possess the most significant changes within the Governor's proposed Health and Human Services budget. The Governor proposes substantial policy and finance changes in the areas of:

- long-term care for the elderly;
- community-based services for the mentally ill and disabled;
- health care for children under age 19 and the disabled;
- family planning services;
- TANF funding, as recipients approach their lifetime limits on receipt of "assistance";
- health disparities among Minnesota's citizens; and
- support for hospitals (especially rural hospitals) and community clinics.

New and expanded endowment funds

With the final one-time tobacco settlement payments from Minnesota's Tobacco Settlement agreement, the Governor proposes to establish the Healthy Kids Learn Endowment and expand the Medical Education endowment. The 1999 Legislature created the Tobacco Use Prevention and Local Public Health Endowment and the Medical Education Endowment. When fully endowed, the value of these investments will approach $550 million(Tobacco Use Prevention) and $352 million (Medical Education) based on the November 2000 forecast. For the FY 2002-03 biennium, statutory appropriations from the endowments are estimated to be $49.9 million for Tobacco Use Prevention and $38.7 million for Medical Education.

In addition to the existing endowments, the Governor proposes to establish the Healthy Kids Learn Endowment with $173.9 million of the remaining one-time tobacco settlement payments. The endowment is expected to generate $8.7 million annually for this new initiative (see details on page 10). The remainder of the one-time payments ($160.3 million), which will be added to the existing Medical Education endowment, will generate approximately $8.0 million annually to support medical education at the University of Minnesota's Academic Health Center. Both of these initiatives are highlighted in the narrative for the Department of Health.

Federal TANF Block Grant

From the federal TANF block grant, including the TANF reserve, the Governor proposes to increase spending by $119.0 million in the FY2002-03 biennium and $173.3 million in the FY2004-05 biennium; these amounts include proposed TANF spending across all of state government. Consequently, the federal TANF reserve balance will be reduced from a projected $317.1 million in FY 2005 to $24.8 million. While the current authorization of the federal TANF block grant expires on September 30, 2002, proposed TANF spending assumes no change to the state's annual block grant level of $267.2 million in future years.

The largest single initiative of the Governor extends TANF assistance beyond 60 months for MFIP clients determined to be in compliance with the program's requirements at a cost of $132.6 million over four years. An additional $40 million over four years is targeted to teen pregnancy prevention activities, $25.8 million to repeal current law that sunsets the provision of cash and food assistance to non-citizens, and $24.0 million to refinance the Working Family Tax Credit program with federal TANF block grant monies. These supplanted general fund dollars will be used to provide affordable housing for MFIP clients and low-income individuals.

Health Care Access Fund

The Governor proposes to spend $598.4 million from the Health Care Access fund in the FY 2002-03 biennium. Within the Health Care Access fund, there are significant changes proposed by the Governor. On the revenue side of the ledger, the Governor is proposing to maintain the provider tax at 1.5 percent, while providing exemptions from the provider tax for adult day care centers and repealing the wholesale drug tax. The Governor also proses to repeal the 1.0 percent gross premiums tax. To replenish the reduction to the fund's revenues, the Governor proposes to redirect 85 percent of the existing Tobacco excise tax into the account beginning in FY 2004.

In terms of expenditures, the Governor expands Medical Assistance eligibility for children under age 19 up to 185 percent of the federal poverty guidelines (FPG). For MinnesotaCare enrollees affected by this change, the financing of their health care will shift from the Health Care Access fund to the general fund.

For children under age 19 who remain in MinnesotaCare, the Governor proposes to repeal cost-sharing provisions and allow enrollment in the program without regard to their parent's health insurance coverage.

The Governor proposes to spend $30.0 million for the biennium on the Minnesota Comprehensive Health Association, also known as MCHA, to subsidize the program's current costs. An additional $30.0 million for the biennium will be provided to shore up hospitals with excessive charity care burdens, aid community clinics that provide "safety net" services, and finance capital improvement grants for rural hospitals.

Future Implications

As noted earlier, general fund spending on Health and Human Services is growing at double-digit rates. Expenditures are projected to grow from $5.4 billion in FY2000-01 to $6.4 billion in FY2002-03 to $7.4 billion in FY2004-05. Billion dollar biennial increases in spending might be expected when the state is experiencing troubling economic times, but when the economy is relatively strong, it is worthy of note. If the economy should slow in the near future, growth pressures on Minnesota's forecasted programs will increase.

Of course, as the state has accumulated recent surpluses -- largely the result of lower than anticipated expenditures in Health and Human Services forecast programs -- investments have been made in needed areas. For instance, cost of living adjustments have been paid to long-term care workers who have needed a boost in their pay. Also, disabled individuals who have been waiting for customized services are now receiving assistance as a result of legislation passed two years ago. Improvements in public health have been enacted to confront fetal alcohol syndrome, food safety issues, and immunizations for children. Finally, the providers of professional services have received increases in their payment rates from the state's Medicaid program. These initiatives are but a few examples of investments made in Health and Human Services over the past few years.

The Governor's budget attempts to control spending in Health and Human Services. In the area of long-term care, he emphasizes community-based care as opposed to institutional care, projecting savings in future biennia. Similarly, he proposes a community-based approach to serving people with mental illness. It remains to be seen if these ventures will actually save money in future years.

While the Governor attempts to reign in spending, he also commits to take over and forecast the non-federal share of family foster care (currently paid by county governments), expand Medicaid and MinnesotaCare coverage for children under age 19, and expand Medicaid eligibility for the aged, blind, and disabled. These proposals are potentially expensive endeavors in the coming years.

The narrative that follows highlights biennial spending contained in the Governor's proposed budget. Unless otherwise noted, proposed changes involve permanent general fund increases in direct appropriations for the FY 2002-03 biennium that begins July 1, 2001.

Department of Human Services

For the FY 2002-03 biennium, the Governor proposes a general fund budget for the Department of Human Services of $6.3 billion, a $1.2 billion increase from the previous biennium. Reimbursements from the federal government offset the Department's biennial spending by $68.2 million. In addition, the Governor proposes an appropriation of $427.4 million from the Health Care Access fund and $534.9 million from the federal TANF block grant.

Agency Management

The Governor proposes $76.0 million in spending for Agency Management, a 38.9 percent increase from the previous biennium. Specifically, the proposals for Agency Management include:

- $2.1 million to increase staffing in the Licensing Division to reduce current caseloads, inspect more facilities, and expedite investigations. Increased funding will also be used for operating the licensing division's new computer system;
- $636,000 to increase staffing in the Licensing Division to expedite maltreatment investigations;
- $7.1 million to improve public access to information contained at the Department via web-based connections; and
- $6.5 million to improve the Department's information security systems to comply with the federal Health Insurance Portability and Accountability Act (HIPPA).

Children's Services Grants

The Governor proposes an increased appropriation for the Children's Services Grant program of $201.5 million, a 72.8 percent increase from the prior biennium. An additional appropriation of $9.3 million from the federal TANF block grant is proposed to continue the Concurrent Permanency Planning project. Specific proposals include:

- $9.3 million from the federal TANF block grant to establish base funding for Concurrent Permanency Planning. The initiative is designed to reduce the time it takes to establish a permanent placement for children in the foster care system or return them to their family;
- a net increase of $20.7 million to fund anticipated growth in the Adoption Assistance ($11.5 million) and Relative Custody Assistance ($10.3 million). Savings of $1.5 million are forecasted in the Medical Assistance program as children move off the state's health insurance program and qualify for their adoptive parent's health insurance. An additional appropriation of $194,000 will be added to the Department's base to hire three staff members to administer these growing programs; and
- $67.4 million to take over and forecast the non-federal share of Medical Assistance payments -- currently paid by county dollars -- for the family foster care program. At the same time, the Governor proposes to reduce the Homestead Agricultural and Credit Aid (HACA) by a like amount in the Department of Revenue's budget request. In the same bill, the Governor proposes to increase the Family Preservation Aid grant by $10.0 million annually but decrease HACA payments by the same dollar amount.

Children's Services Management

Proposed spending on Children's Services Management totals $11.7 million for the FY 2002-03 biennium, $7.1 million higher than the previous biennium. Approximately $4.0 million of the increase is due to the exclusion of attorney general's costs from the previous biennium's expenditures.

Basic Health Care Grants

The Governor proposes a biennial budget for Basic Health Care Grants of $2.4 billion from the general fund, and $382.8 million from the Health Care Access fund, representing increases over the current biennium of $608.3 million (33.3 percent) and $116.5 million (43.7 percent) respectively.

Proposals contained within the Governor's budget include:

- $4.3 million from the general fund and $9.0 million from the Health Care Access fund to provide health insurance coverage to more low-income children. Recommendations include:
  - Establishing a gross income test at 185% of the FPG for children under age 19 ($26,178 for a family of three based on 2000 FPG data).
  - Allowing children under age 19 with income that is at or below 185 percent of FPG to enroll in MinnesotaCare without cost-sharing.
  - Allowing children under age 19 with income under 185 percent of FPG who have or had other health care coverage to enroll in MinnesotaCare. Current law dictates that families and individuals must have no health coverage while enrolled in MinnesotaCare or for at least four months prior to application and renewal.
  - Requiring the prepayment of MinnesotaCare premiums.
  - Enrolling uninsured children in MinnesotaCare if they are already enrolled in other program with similar income requirements such as Head Start, the National School Lunch Program, and the Supplemental Nutrition Program for Women Infants and Children (WIC).
  - Expanding outreach efforts in communities with high rates of uninsured individuals and limited English proficiency.
  - Reinvesting administrative savings in a new enrollment system.
- $36.8 million to shift the financing of health care to the general fund for children under age 19 in families with income under 185 percent of FPG as of July 1, 2002. Separately, the Governor proposes to expand MinnesotaCare coverage to children under age 19. If these proposals are enacted, a savings of $36.8 million in fiscal year 2003 would accrue to the Health Care Access fund;
- $1.8 million in savings to the general fund and $548,000 in costs to the Health Care Access fund to comply with federal Medicaid law. Since 1999, the Department has been in violation of federal Medicaid law, because it has treated MFIP and non-MFIP clients disparately with regard to MA eligibility. This proposal reduces eligibility for MFIP-eligible MA clients to the level of non-MFIP MA clients.
- one-time spending of $4.6 million from the Health Care Access fund to hire additional staff to reduce current caseloads and improve MinnesotaCare operations.
- $880,000 to continue cost-based reimbursement for Federally Qualified Health Centers (FQHCs) and Rural Health Centers (RHCs).

- $2.4 million to expand the coverage of clinical family planning services under MA. This expansion envisions leveraging $9.00 (federal) for each $1.00 (state) based on current family planning services models used in other states.
- $5.2 million in savings as a result of disallowing the inclusion of the hospital surcharge as part of MA hospital payment rates. Recently, Minnesota hospitals won an appeal to include the surcharge as part of their Medicare cost report. Accordingly, the federal government will compensate hospitals for the assessment. Because Minnesota already reimburses hospitals for the cost of the surcharge through disproportionate share payment rates, this change will avoid a double payment to hospitals for the surcharge payment amounts.
- $1.9 million to require the implementation of Prepaid Medical Assistance Program (PMAP) by January 1, 2002 for Minnesota counties that have not received federal approval to operate County-based purchasing plans by September 2, 2001.
- a net increase of $239,000 as a result of expanding enrollment in MA (by increasing the MA income standard to 100 percent of FPG) for aged, blind, and disabled individuals ($18.1 million increase). This change will result in declining enrollment and cost ($14.9 million decrease) in the state-only funded Prescription Drug Program, as current enrollees migrate to the MA program. A related proposal would change the way premium payments are calculated for enrollees in the MA-EPD (Employed Persons with Disabilities), resulting in savings of $3.0 million as enrollees without earned income move off the program.
- net savings of $1.5 million by collecting rebates from pharmaceutical manufacturers for drugs dispensed in outpatient facilities, reimbursing outpatient facilities at the Average Wholesale Price (AWP) less 5 percent (instead of the current AWP), and paying honoraria to members of the Drug Utilization Review Board.
- $2.9 million from the general fund, $82,000 from the Health Care Access fund, and $5.0 million from the federal TANF block grant to repeal the Systematic Alien Verification for Entitlements (SAVE) program, enacted by the 2000 Legislature and scheduled to take effect on July 1, 2001.

Health Care - Other Assistance

The Governor proposes to spend $19.8 million for Health Care - Other Assistance in fiscal years 2002-03, a decrease of $5.7 million from the previous biennium.

Health Care Management

The Governor proposes a biennial budget for Health Care Management of $44.2 million, $26.7 million higher than the previous biennium. In actuality, the increase from the previous biennium is $3.7 million, because the state share of MMIS expenditures ($22 million) are not reflected in the previous biennium's expenditures. These expenditures are reflected in a non-general fund account in the special revenue fund. Specific Governor's recommendations include:

- a net savings of $685,000 as a result of centralizing the billing and collection of Alternative Care premium payments at the state level, relieving counties of this responsibility. This change is assumed to increase the collection of premiums.

State-operated Services

The Governor proposes to spend $417.6 million on state-operated services, an increase from the previous biennium of $4.4 million. Initiatives within this program include the following:

- a net increase of $0 as a result of reallocating administrative savings of $1.1 million in FY 2002-03 and $4.7 million in FY 2004-05 from the state-operated services system to fund the expansion of the Minnesota Sex Offender Treatment program and collaboration efforts between the Departments of Human Services and Corrections regarding the treatment of sexual offenders.

Continuing Care Grants

The Governor proposes $2.8 billion for the Continuing Care Grants program, an increase of $483.6 million (21.3 percent) compared to the previous biennium. Of the increase, $84.0 million is the result of chemical dependency treatment fund expenditures that are reflected in special revenue fund expenditures and not the general fund.

- $2.3 million in savings as a result of eliminating base funding for two "narrowly-focused" grant programs -- the Social Services Supplemental Grants program ($860,000 per year) and the Minor Parent Evaluation program ($330,000 per year).
- $8.9 million in savings as a result of reallocating existing spending on people with mental illness within the Department's budget. Specifically, the initiatives include:
  - Expanding the rehabilitation option under MA to include psychiatric rehabilitation services for adult with serious and persistent mental illness in addition to those at risk of institutionalization if they do not receive these services.
  - Reducing spending on admissions to emergency rooms and inpatient psychiatric units and the utilization of day-treatment services as a result of the expansion of the services under the MA rehabilitation option.
  - Increasing staffing to administer these proposed changes.
  - Simplifying the administration of the state-operated services administrative structure.
  - Implementing earlier than planned the shift of appropriations-based services to enterprise funds.
- $862,000 to continue the implementation of the Region 10 Quality Assurance Initiative.
- A net increase of $589,000 as a result of relocating and diverting people with disabilities who reside in nursing homes who can be better served, at a lower cost, in the community.
- A net increase of $0 as a result of establishing a demonstration project called the Consumer-Directed Home Care program, designed to more flexibly serve the needs of individuals who need home care services. An estimated $30.2 million will be redirected from existing Medical Assistance home care spending to fund the initiative and its administrative component.
- $15.1 million in savings as a result of limiting enrollment in the Consumer Grants Program to 200 participants, and directing funds that would have been transferred to the Medical Assistance program for home care services to the Consumer-directed Home Care program.

- a net increase of $7.7 million as a result of restructuring the provision of long-term care services. Specific recommendations by the administration include:
  - $2.8 million to expand services under the Senior Linkage Line;
  - $1.8 million to expand Health Insurance Counseling services;
  - $8.8 million to assist communities in determining the long-term care service needs of their communities;
  - a net increase of $17.9 million to equalize payments among counties for the Alternative Care program and the Elderly Waiver, simplify the services available under these programs and other services for the disabled, and fund additional caseload growth under the Alternative Care program.
  - a net decrease of $27.9 million as a result of downsizing the bed capacity in nursing homes through planned closures. As beds are removed from the nursing facility system, new entrants to the long-term system will be directed into less expensive community-based services such as the Alternative Care program and the Elderly Waiver. A sub-component of this proposal removes the licensing of 3rd and 4th beds in multiple-bed rooms in nursing facilities.
  - $2.6 million to administer the changes proposed under this initiative.
- $23.0 million to provide a cost-of-living adjustment (COLA) increase beginning July 1, 2002 (FY 2003) to continuing care providers such as nursing homes, intermediate care facilities for people with mental retardation, waiver programs, and mental health grant services;
- $2.1 million in savings as a result of limiting to 2.0 percent the rate at which counties can approve increases for chemical dependency treatment in fiscal years 2002 and 2003. In the absence of any limitations on rate changes, the Department of Human Services forecasts county-approved rates to increase by 4.0 percent each year of the biennium;
- $1.5 million in general fund savings as a result of transferring monies from the Consolidated Chemical Dependency Treatment fund in excess of the cost of providing treatment services to Tier I (entitlement grants) and Tier II (non-entitlement grants) clients.

Continuing Care Management

Proposed biennial spending for Continuing Care Management totals $46.5 million, an increase of $11.7 million from the previous biennium. Proposals include:

- $938,000 to implement new, federally-mandated oversight and regulations for nursing facilities and intermediate care facilities for persons with mental retardation.

Economic Support Grants

The Governor proposes spending $197.5 million from the general fund and $395.8 million from the federal TANF block grant for Economic Support Grants, a decline of $107.2 million (general fund) and an increase of $100.3 million (TANF). Proposed spending in Economic Support Grants include:

- $36.4 million from TANF and a savings of $490,000 to implement policies that will respond to MFIP families who are projected to exhaust their 60 months of eligibility for TANF-funded "assistance".[1] Specific policy changes include:
  - extending the receipt of assistance beyond 60 months for MFIP recipients who are in compliance with program requirements;
  - closing cases of participants who have been in sanction more than 30 of the 60 months and are out of compliance in the 60th month;
  - modifying MFIP sanction policy to remove automatic vendoring and increasing the maximum sanction from 30 percent to 50 percent for participants who have been non-compliant for five cumulative months;
  - modifying eligibility for the Emergency Assistance and MFIP employment services programs to permit individuals who have used up their 60 months of assistance to receive aid. In addition, participants using up 60 months of assistance would be added as a target population to the Local Intervention Grants program.
- $3.8 million from TANF and $833,000 from the general fund to permanently index the MFIP exit level at 120 of FPG. As a result of this change, MFIP participants approaching the exit level will remain on the program longer than under current law.
- $6.2 million from TANF and $1.1 million from the general fund to allow up to 24 months of post-secondary education or training for MFIP participants who meet criteria in statute. Under current law, participants are allowed to complete post-secondary education or training from 13 to 24 months on an exception basis.
- $10.8 million to repeal sunset dates for legal non-citizen families receiving MFIP cash and food assistance. Furthermore, funding for the Minnesota Food Assistance Program – a program that currently relies solely upon general fund dollars -- would be shifted to the federal TANF block grant.
- $378,000 in savings as a result of reducing the base appropriations for the Injury Projection Program to the level of need.
- $496,000 in savings as a result of reducing the base appropriations for the following food stamp employment and training (FSET) grant programs:
  - $300,000 FSET start work grants
  - $96,000 FSET literacy training funds
  - $100,000 FSET literacy transportation funds.
- a net increase of $164,000 to improve the child support program by increasing paternity establishment payment rates and establishing a fee payable to institutions who fully implement federal Financial Institutions Data Match activities.

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[1] "Assistance" is defined in the federal TANF regulations to be aid that is ongoing (more than four months) for basic needs (cash, food, or housing).

Economic Support Management

The Governor proposes biennial spending of $93.0 million in fiscal years 2002-03, an increase of $71.9 million from the previous biennium. The actual increase is approximately $48.0 less or $23.9 million, because the state share of the PRISM and MAXIS computer systems are excluded from the previous biennium's expenditures.

- $400,000 to implement a shared responsibility model to calculate child support responsibilities of obligors and obligees and make improvements to the medical support statutes.
- $2.5 million from TANF to implement a new Employment Services Tracking System for MFIP participants. The cost of this initiative will be shared with the Department of Economic Security.
- $4.3 million to implement the Department's Limited English Proficiency Plan in order to make human services more accessible to individuals who lack proficiency in the English language.
- $17.8 million to increase funding for PRISM, MAXIS, and SSIS, computer systems maintained at the Department. The cost will be offset by a $24.0 million transfer from the special revenue fund from balances carried forward.

Minnesota Department of Health

The Governor proposes general fund spending for the biennium of $155.1 million for the Department of Health, an increase of $30.5 million (24.5 percent) for the biennium. The Governor also proposes $53.9 million from the Health Care Access fund, $50.7 million from the state government special revenue fund, and $34.0 million from the federal TANF block grant. Specifically, the Governor proposes:

- $1.0 million from the State Government Special Revenue fund to provide operational costs for the Vital Records System. Ongoing funding will be provided by a $2.00 surcharge on copies of birth and death records. Financing for the development of the program has been funded by a $3.00 surcharge. Under current law, the surcharge would expire on July 1, 2002.
- $4.4 million to provide grants to address workforce shortages in the health care industry. The Community/Regional Health Workforce Grants program would be established to provide funds to assist communities in identifying and addressing their local workforce needs. Also, additional funding would be made available to expand existing health professional loan repayment programs.
- $60,000 in savings as a result of eliminating funding for the Bone Marrow program, a program that develops and disseminates education materials to recruit bone marrow donors among minority communities.
- $684,000 in savings as a result of reducing base appropriations for the Minnesota Education Now and Babies Later (ENABL) program. It is assumed that the need for services will be met by additional funding for family planning services provided elsewhere in the Department's budget.
- $2.7 million to restore and increase state funding for the Poison Control System.
- $13.9 million to eliminate health disparities between white and non-white populations of the State. Specific proposals include:
  - $5.0 million for the most effective prevention services;
  - $4.5 million for Community Health Boards to support local public health efforts to eliminate health disparities;

- $1.0 million for grants to Tribal Governments to identify and implement culturally-based interventions;
- $200,000 for the Health Disparities Advisory Council to recommend effective strategies to eliminate health disparities in Minnesota, focusing on racial and ethnic disparities.
- $1.8 million for implementation of the health disparities proposal and accountability;
- $1.0 million for tuberculosis control activities and immigrants, refugee, and migrant health.
- $400,000 for attracting a more diverse public health workforce and enhancing the design and utilization of culturally and linguistically appropriate public health information.

- $400,000 in savings as a result of streamlining the Department's administration of grants to local governmental agencies and non-profit organizations.
- one-time spending of $2.0 million from the general fund and $173.9 million from the Tobacco Settlement Fund to establish a new endowment called "Healthy Kids Learn." The endowment is projected to earn revenues of $3.0 million in FY 2003 and $8.7 million each year thereafter that will be appropriated to the Department of Health to improve the health of school-aged students and their learning environment. The one-time general fund item will be used to begin the development of regional immunization information services, which will be operated in future years, from the endowment's revenues. Funds will be used as follows:
  - $1.0 million in FY 2002 and $2.0 million thereafter for grants to Community Health Boards to support the development and maintenance of a statewide immunization information services.
  - $1.0 million in FY 2003 and thereafter for eight regional school specialists, training and technical assistance and an interactive website.
  - $900,000 in FY 2003 and thereafter for nine FTEs to provide staff expertise on environmental health and public health, as well as coordination among agencies, planning, administration, and data collection and analysis. These funds will also be used to establish an interagency contract with the Department of Children, Families, and Learning to evaluate the Healthy Kids Learn initiatives.
  - $100,000 in FY 2003 and thereafter to support the Healthy Kids Learning Steering Committee. The committee will identify innovative strategies to improve the health of Minnesota students.
  - $4.7 million in FY 2004 and thereafter for public-private Health Kids Learn Initiatives to implement the strategies identified by the steering committee. Local initiatives must provide a 25 percent match from non-governmental sources.
- $2.2 million to establish base funding for Suicide Prevention activities. Non-competitive grants would be provided for community-based planning and implementation grants for suicide prevention activities and mental health improvement strategies targeted to high risk groups. The Department will also hire staff to begin implementation of their suicide prevention plan.
- $20.0 million to expand teen pregnancy prevention efforts. Specifically, the Governor proposes to spend:

- $2.4 million each year to provide grants to community-based organizations to reduce disparities in teen pregnancy rates.
- $1.4 million annually to provide non-competitive grants to Community Health Boards or tribal governments that have culturally appropriate youth development programs who add or enhance current programming aimed at teen pregnancy prevention.
- $2.5 million each year to provide grant funds to tribal governments and Community Health Boards to address the issue of teen pregnancies.
- $1.4 million each year to develop a statewide media campaign around the issue of teen pregnancies.
- $500,000 each year to expand the teen parent program operated by the Department of Children, Families, and Learning.
- $600,000 each year to fund statewide teenage pregnancy capacity building activities.
- $800,000 each year to administer and monitor these teenage prevention activities.
- $400,000 each year to conduct process and outcome evaluations.

- $810,000 in savings from the State Government Special Revenue fund as a result of deregulating occupational therapists, speech language pathologists, and audiologists.
- one-time costs of $725,000 as a result of shifting regulation of Health Maintenance Organizations from the Health Department to the Department of Commerce. The goal of the initiative is to apply more consistent regulation of managed care plans.
- one-time spending of $10.0 million from the Health Care Access fund to create the Minnesota Center for Health Quality. Funds will be used as follows:
  - $5.0 million to research, analyze, and distribute information on the overall state of health and health quality in the state.
  - $2.0 million to determine the information needs of consumer of health care, assess the effectiveness and cost of technologies and treatments, make available information and reports about quality, and evaluate the effectiveness of this initiative.
  - $3.0 million to identify costly but preventable health conditions and develop a method to track what health care services are directed at these conditions.
- one-time spending of $160.3 million from the Tobacco Settlement Fund to increase funding for the Medical Education Endowment. The additional allocation to the endowment is projected to earn revenues of $8.0 million in FY 2003 and each year thereafter. Fund will be used to support medical education activities at the University of Minnesota's Academic Health Center.
- one-time spending of $30.0 million for the biennium from the Health Care Access fund to provide additional support to hospitals and community clinics. These funds will be used as follows:
  - $10.0 million to relieve the burden of hospitals providing excessive amounts of charity care;
  - $10.0 million to provide grants to community health clinics for improved information systems, investments in primary care equipment and infrastructure, enhanced services to

the community served by community health clinics (e.g. interpreter or translation services), and to offset uncompensated care to the clinics clientele.

- ▸ $10.0 million to continue funding rural hospital capital improvement grants.

- $6.4 million in increased revenues to the State Government Special Revenue fund to recover the cost of regulating, licensing, and certifying Medicaid and Medicare programs health care facilities such as nursing homes, hospitals, boarding care homes, supervised living facilities, and ambulatory surgical centers to support this activity.
- $820,000 from the State Government Special Revenue fund to provide training to home care providers -- primarily assisted living providers -- to consult and educate providers how to deliver quality care and provider support.
- $920,000 from the State Government Special Revenue fund to meet additional requirements of the federal Safe Drinking Water Act that require more aggressive laboratory testing for contaminants in drinking water. The program changes involve no additional fee increases, simply an appropriation from the existing Drinking Water Revolving Loan fund.
- $1.3 million from the State Government Special Revenue fund to maintain Food, Beverage, and Licensing inspection services statewide and provide inspection services for Cook County. The increased appropriation will involve fee increases for currently licensed facilities. A new fee will be imposed for services in Cook County, since the State is assuming responsibility for these activities.
- $1.0 million from the State Government Special Revenue fund to provide additional resources to maintain services for the State's Well Management Program. Fee increases will accompany this change for additional appropriation authority.
- $600,000 each year in additional revenues to regulate activities under the Federal Nuclear Regulatory Commission, whose responsibilities the State assumed in recent years.
- $420,000 from the State Government Special Revenue fund to conduct food safety inspections for public and private schools. These costs would be recovered through fees assessed for inspections.
- $150,000 from the State Government Special Revenue fund to cover the current costs of Minnesota's Environmental Laboratory Certification program. The appropriation increase will be accompanied by a fee increase for laboratory services.
- $4.8 million from the general fund to strengthen the state's preparedness to identify and respond to emerging health threats. Savings of $734,000 will accrue to the State Government Special Revenue fund by refinancing core public laboratory services; this change will result in lower fees to laboratory users.
- $100,000 in savings to the general fund as a result of eliminating a staff position.

Minnesota Veterans Homes Board

The Governor proposes to spend $59.0 million for the Minnesota Veterans Home Board.

Disability Council

- $1.4 million to restore base funding for the Disabilities Council. Under current law, base funding for the council will be eliminated on June 30, 2001.

Ombudsperson for Mental Health and Mental Retardation

- one-time spending of $250,000 to establish the Center for Ombudsman Services.
- $153,000 to provide additional funding to maintain current staffing levels.

Ombudsperson for Families

- $124,000 to provide additional funding to maintain current staffing levels.

Health Occupations Licensing Boards

Board of Nursing

- $1.1 million in additional revenues to the State Government Special Revenue fund as a result of increasing nursing fees to support the boards current operations.
- $266,000 from the State Government Special Revenue fund for additional staffing at the Health Professionals Services Program.
- $360,000 from the State Government Special Revenue fund for one-time and ongoing needs.

Board of Pharmacy

- $147,000 from the State Government Special Revenue fund for the Administrative Services Unit to provide additional services to the 14 health-related licensing boards and the Emergency Medical Services Regulatory Board.
- $196,000 from the State Government Special Revenue fund to restore a previously eliminated position and union-negotiated salary and benefit levels.

Board of Psychology

- $232,000 from the State Government Special Revenue fund for additional costs of contested case hearings and union-negotiated salary and benefit levels.

Board of Social Work

- $341,000 from the State Government Special Revenue fund for additional costs associated with board member expenses, contested case hearings, negotiated salary and benefit levels, and records management capabilities.

Emergency Medical Services Regulatory Board

- $3.6 million to restore and increase, with general fund dollars, base funding from the Trunk Highway fund that was eliminated by the 2000 Legislature.

For more information on Health and Human Services Finance issues, contact Joe Flores at 651-296-5483 or Joe.Flores@house.leg.state.mn.us

Judiciary Finance

The Governor's general fund budget recommends an appropriation of $1.326 billion for the FY 2002-03 biennium, a 13 percent increase over the previous biennium. This recommended funding level is a 7.4 percent increase over the current law base for FY 2002-03. The budget for all funds in the criminal justice area increases by 4.4 percent, due mainly to an anticipated decrease in federal funds. The criminal justice budget makes up 4.9 percent of the Governor's proposed general fund budget for FY 2002-03.

Judiciary Finance
Governor's FY 02-03 General Fund Budget Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
Supreme Court	55,415	52,988	58,348	5.29%	10.12%
Court of Appeals	13,199	13,498	15,180	15.01%	12.46%
Trial Courts	177,752	201,752	243,742	37.12%	20.81%
Judicial Standards Board	511	476	509	-0.39%	6.93%
Public Defense Board	92,568	95,234	105,746	14.24%	11.04%
Tax Court	1,436	1,342	1,499	4.39%	11.70%
Human Rights Department	7,898	7,848	8,329	5.46%	6.13%
Uniform Laws Commission	75	76	89	18.67%	17.11%
Corrections Department	678,190	715,650	729,808	7.61%	1.98%
Ombudsman for Corrections	780	620	659	-15.51%	6.29%
Sentencing Guidelines Commission	1,264	996	1,075	-14.95%	7.93%
Crime Victims Ombudsman	808	758	827	2.35%	9.10%
Public Safety Department	143,362	143,420	160,282	14.87%	14.82%
Peace Officer Standards Training Board	600	600		-100.00%	-100.00%
Private Detective Board	275	280	292	6.18%	4.29%
Total:	**1,174,133**	**1,235,538**	**1,326,467**	**13.34%**	**7.71%**

Supreme Court

The Governor is recommending a biennial appropriation of $67.05 million. New initiatives include the following:

- $3.2 million for increased compensation and increases in insurance costs.
- $124,000 for an increase in National Center for State Court fees and for increases from West Law.
- $4 million is for increased funding for civil legal services.
- $3.4 million for increased costs as a result of the court takeover.

- $20 million is for the Minnesota Court Information System (MNCIS). The Governor has recommended $15 million for this request under the Department of Administration.

- $221,000 for increased costs for legal materials for the law library.

Court of Appeals

The Governor is recommending a biennial appropriation of $15.2 million. New initiatives include the following:

- $1.6 million for increased compensation and increases in insurance costs.

- $664,000 for legal research assistance. The funding will be for two staff attorneys and 2.5 law clerk positions.

District Courts

The Governor is recommending a biennial appropriation of $243.99 million. New initiatives include the following:

- $5.1 million for 9 new judge units and supplemental retired judge funding to meet the increasing caseload demand. It also includes an update of the weighted caseload methodology and referee conversions.

- $26.8 million for increased compensation and increases in insurance costs..

- $9.2 million for operation cost inflation, training funds, increase in mileage reimbursement rate for jurors, continued funding for the community courts, and an increase in 21 positions.

- $28.8 million for growing services mandated by state and federal law. These services include guardian ad litem, interpreters, Rule 20 and commitment psychiatric exams, and in forma pauperis costs.

- $1.8 million for fiscal and human resources staff to provide support previously obtained from counties and to create a administrative structure within the judicial branch.

Since the courts are separate branch agencies, the Governor treats them differently from executive branch agencies. The Governor does not make specific recommendations on their budget requests. Instead, the Governor's budget allocates a general increase of $54.5 million for the biennium for the courts to recognize caseload increases and mandated costs. This also includes the $15 million court request for their court information system which appears under the Department of Administration. The court requests are $37.4 million over the Governor's recommendations.

Tax Court

The Governor is recommending a biennial appropriation of $1.5 million. New initiatives include the following:

- $94,000 for on-going technology infrastructure support.

Board of Judicial Standards

The Governor is recommending a biennial appropriation of $509,000. New initiatives include the following:

- $12,000 for router access to state systems, e-mail and the internet.

Public Safety

The Judiciary Finance Committee is responsible for seven programs (other programs in the agency are the responsibility of the Transportation Finance Committee). The Governor is recommending a biennial appropriation of $236.25 million for the Public Safety programs in the Judiciary Finance Committee. New initiatives include the following:

Emergency Management

- $11.8 million to cover projected state match obligations for federal disaster assistance, and a reduction in funding of $385,000 for hazardous material funding.

Bureau of Criminal Apprehension (BCA)

- $2.7 million from the general fund and $715,000 from the trunk highway fund to restore base funding for DWI enforcement.

- $2 million to alleviate the suspense file problem. This is part of the Crimnet proposal.

- $3 million to work with counties to develop cost estimates and recommendations on how to best integrate local criminal justice agency systems and data with state information. This is part of the Crimnet proposal.

- $1.5 million to analyze, fill out and maintain the Crimnet enterprise model for use in all criminal justice information systems and to staff other Crimnet activities. This is part of the Crimnet proposal.

- $584,000 increase in fee revenue by charging a fee of $5 for access to public criminal history data over the internet.

Law Enforcement & Community Grants

- Eliminates the automobile theft prevention surcharge and funding for the Camp Ripley weekend camp.

- $280,000 for a racial profiling study.

Crime Victim Ombudsman

The Governor is recommending a biennial appropriation of $827,000. New initiatives include the following:

- $16,000 to maintain technology infrastructure.

- The Governor is also recommending that the Offices of the Ombudsman for Mental Health and Mental Retardation, Ombudsman for Crime Victims, and Ombudsman for Corrections be co-

located into a Center for Ombudsman Services. One time funding of $250,000 is included under the budget recommendations for the Ombudsman for Mental Health and Mental Retardation

Private Detectives Board

The Governor is recommending a biennial appropriation of $292,000. The Governor is recommending a increase in fees to cover the cost of operating the Board's functions.

POST Board

The Governor is recommending a biennial appropriation of $9.4 million (the main source of financing is from a special revenue fund). New initiatives include the following:

- The Governor is recommending that the $600,000 in base funding from the general fund for police pursuit training be moved to the special revenue fund.

Public Defense Board

The Governor is recommending a biennial appropriation of $106.55 million. New initiatives include the following:

- $9.8 million to reduce caseloads and continue the viability of the part time public defender system.
- $220,000 for a trial support team in the Office of the State Public Defender.
- $780,000 for increased funding for the public defense corporations. This would fund four additional positions, provide a grant adjustment of 3 percent, and a salary adjustment.
- $1.3 million for a redesign to the information system and to hire seven local area network administrators.

Implications

Since the Public Defender is a separate branch agency, the Governor treats them differently from executive branch agencies. The Governor makes no recommendation on their specific budget requests. Instead, the Governor's budget allocates a general increase of $6.1 million for the biennium to recognize caseload increases. The Public Defender budget request is $5.97 million more than the Governor's recommends.

Department of Corrections

The Governor is recommending a biennial appropriation of $874.9 million. New initiatives by program include the following:

Institutions

- $18.4 million reduction in funding by implementing a per diem reduction plan for the adult facilities.
- $3 million for cost efficiency projects to ensure that the facility per diem goals are accomplished.

Juvenile Services

- $3.7 million reduction in the juvenile placement grants in juvenile placement grants to offset the 35 percent reduction in fees that counties are charged for using Red Wing. This continues this

practice for an additional year.

- $545,000 for a dedicated fee increase for per diem cost increases at the Thistledew Camp.

Community Services

- $1.5 million for additional state agents and grants to counties for increased intensive community supervision.
- $3 million for an increase in the Community Corrections Act subsidy for local correctional services.
- $1.4 million to expand performance accountability and technical assistance for community services programs around the state.
- $2 million for sex offender treatment and transitional funding.
- $3.77 million for county probation officer reimbursement. This is to maintain county probation officer reimbursement at the 50 per cent level.
- $2 million for statewide probation caseload/workload reduction.
- $316,000 reduction to the general fund for probation fees now collected by the state that will go instead to the counties who pay for the services.

Management Services

- $1.5 million to develop statewide systems for tracking offenders in jail or prison, or under community supervision. This is part of the overall CRIMNET proposal.

Ombudsman for Corrections

The Governor is recommending a biennial appropriation of $659,000 a increase of $90,000 from the current spending level. The Governor is also recommending that the Offices of the Ombudsman for Mental Health and Mental Retardation, Ombudsman for Crime Victims, and Ombudsman for Corrections be co-located into a Center for Ombudsman Services. One time funding of $250,000 is included under the budget recommendations for the Ombudsman for Mental Health and Mental Retardation.

Sentencing Guidelines

The Governor is recommending a biennial appropriation of $1.1 million. New initiatives include the following:

- $32,000 to maintain current staffing levels and accompanying operating expenses.

Human Rights Department

The Governor is recommending a biennial appropriation of $8.4 million. New initiatives include the following:

- $112,000 to maintain hardware and software and for other system enhancements.

Uniform Laws Commission

The Governor is recommending a biennial appropriation of $89,000, an increase of $10,000 over the current spending level. New initiatives include the following:

- $10,000 for an increase in dues for the National Conference of Commissioners on Uniform State Laws.

Implications:

The Governor's budget does not include any funding for several legislative initiatives. For example, it appears that Driving While Intoxicated (DWI) legislation is likely in two areas with one being lowering the limit to .08 and the other being making a person's forth or more DWI a felony. The Governor's budget does not address either one.

The Governor's budget initiatives do include funding for the criminal justice information system known as CRIMNET. However, the funding the Governor proposes does not match the policy group recommendation of $41.5 million. The total funding for CRIMNET in the Governor's budget is $27 million. To further complicate matters $19 million of the Governor's recommended CRIMNET funding is in the Department of Administration. This means the State Government Finance committee may be reviewing part of the CRIMNET proposal.

For additional information on judiciary finance issues, contact Gary Karger at 296-4181 or gary.karger@house.leg.state.mn.us

Environment and Natural Resources Finance

The Governor recommends a total General Fund appropriation of $414.2 million for the state departments and programs under the jurisdiction of the Environment and Natural Resources committee. This recommended amount is an increase of $12 million from current law for FY 2002-03.

Environment and Natural Resource Finance Committee
Governor's FY 2002-03 General Fund Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Gov. FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
Pollution Control Agency	29,575	33,455	36,115	22%	8%
Office of Environmental Assistance	40,773	41,006	41,434	2%	1%
MN/WI Boundary Area Commission	304	308	322	6%	5%
MN Zoological Garden	14,438	14,458	15,113	5%	5%
Dept. of Natural Resources	289,065	274,224	281,160	-3%	3%
Board of Water and Soil Resources	43,981	36,256	37,611	-14%	4%
Science Museum	2,328	2,328	2,328	0%	0%
Academy of Science	82	82	82	0%	0%
Total	**420,546**	**402,117**	**414,165**	**-1.5%**	**3%**

Pollution Control Agency (PCA)

The Governor recommends a total budget of $238.1 million, of which $36.1 million (15.2 percent) is General Fund dollars. This is a recommended General Fund increase of $6.54 million (22.1 percent) compared to the current biennium. Changes recommended by the Governor to the agency base budget include the following:

Overall:
The PCA has traditionally been organized into "media-based" programs. Within the past three years, PCA has gone through an extensive re-design of the delivery of programs into a regionalized approach. This approach has led to an additional program at the agency called Integrated Environmental Programs (IEP), while the PCA still maintains the Land, Water and Air programs.

General Fund - Proposed Reallocations

Project	**Program**	***Increase***	**Project**	**Program**	***Reduction***
BWSR Delegated County Feedlot Permitting	Water	1,070,000	Clean Water Partnership Grants	Water	(2,470,000)
BWSR Feedlot Cost Share Grants	Water	1,400,000			
		2,470,000			

Environmental Fund - Proposed Reallocations					
Project Name:	**Program**	***Increase***	**Project Name**	**Program**	***Reduction***
Water & Storm Permitting	Water	1,173,000	ISTS Assistance	Water	(247,000)
			Solid Waste	Land	(400,000)
			Hazardous Waste	Land	(400,000)
			Underground Storage Tanks	Land	(126,000)
			subtotal:		**(1,173,000)**
Lake Superior LaMP	Water	200,000	Listed Metals	Land	(380,000)
Deformed Frog Research	IEP	180,000			
subtotal:		**380,000**			
Air Toxics	Air	400,000	Salvage Yard	Land	400,000
Basin Monitoring Information	IEP	1,000,000	Superfund	IEP	1,000,000

New Initiatives:
General Fund:

- $1.450 million increase as a part of a multi agency initiative for feedlot cost-share and permitting administration.

PCA Environmental Tax Reform:
Since the passage of the Clean Air and Water Acts, the State of Minnesota has created a web of environmental fees to pay for the myriad of environmental programs aimed at cleaning up "Point Sources" of pollution. As the pollution from Point Sources become under control, "Non-Point Source" pollution moves to center stage. As Non-Point pollution factors take center stage, the dedicated funding from traditional sources becomes scarce and unrelated to the higher priority activities. Therefore, the Governor is proposing a change in the way environmental clean-up programs are funded. The proposal eliminates the dedication of resources to specific activities and creates flexibility for the Pollution Control Agency to address issues such as animal feedlots, water quality permitting, and air toxins.

The proposal contains the following:

- Elimination of water and hazard waste permitting fees totaling approximately $5 million annually.
- Renaming of the Solid Waste Management Tax to the Environmental Tax. Proceeds from this tax would be deposited into the Environment Fund and the Solid Waste Fund would be eliminated.
- An amount consistent with the state's pollution clean-up liability would be transferred to a new fund called the Remediation Fund.

Implications:

- The Pollution Control Agency does not receive any additional funds in the FY 2002-03 biennium. The agency is able to bring forth initiatives paid for with the newly broadened, undedicated Environment Fund for Legislative approval.

- The Legislature retains control of all current direct appropriation of all funds; no additional statutory appropriations are established.
- Environmental funding moves from a "Polluter Pays" principle to a more broad based assessment.
- Simplifies the accounting structure within the environment.

Office of Environmental Assistance (OEA)

The Governor recommends a total budget of $49.2 million, of which $41.4 million (84.1 percent) is General Fund dollars. This is a recommended General Fund increase of $570,000 (1.4 percent) compared to the current biennium.

The Governor is proposing the reallocation of $200,000 from the OEA's Pollution Prevention Grant Program to a new Pollution Prevention Revolving Loan Program. The program would provide a zero percent interest loan as a 50 percent match to a bank loan. Funds would be used for the purchase of equipment designed to prevent or reduce pollution.

Minnesota-Wisconsin Boundary Area Commission

The Governor recommends a total budget of $393,000, of which $322,000 (81.9 percent) is General Fund dollars. The Governor includes a small agency operating adjustment to the original base appropriation.

Minnesota Zoological Garden (MZG)

The Governor recommends a total budget of $36.9 million, of which $15.1 million (41 percent) is General Fund dollars. This is a recommended General Fund increase of $511,000 (3.5 percent) compared to the current biennium. The majority of the Zoo budget comes from admission and membership fees ($19.2 million.)

Department of Natural Resources (DNR)

The Governor recommends a total Department of Natural Resources budget of $577.6 million, of which $281.2 million (48.7 percent) is General Fund dollars. This is a recommended General Fund increase of $51 million (22.2 percent) compared to the current biennium. Changes recommended by the Governor to the agency base budget include the following:

Overall:
The Governor has split the Fish and Wildlife program into three separate programs this budget cycle. They are Fish Management, Wildlife Management, and Ecological Services.

The table on the next two pages shows the Governor's proposed re-allocations within the DNR's base budget resources.

DNR: Proposed Reallocations

	FY 02	FY 03	FY 02-03 Total
Land and Mineral Management:			
Minerals Diversification	(10,000)	(10,000)	
Iron Ore Cooperation Agreement	(7,000)	(7,000)	
Mineral Coop Env Research	(3,000)	(3,000)	
Land and Mineral Management	(36,000)	(5,000)	
Subtotal - Land & Mineral Management:	**(56,000)**	**(25,000)**	**(81,000)**
Water Resource Management			
Lewis and Clark Water System	(25,000)	(25,000)	
Water Monitoring - Waters	(12,000)	0	
Water Resource Management	158,000	184,000	
Leech Lake Band Grant	(7,000)	(7,000)	
Mississippi Headwaters Grant	(40,000)	(40,000)	
Red River Flood Damage Grants	(150,000)	(150,000)	
Subtotal - Water Resource Management:	**(76,000)**	**(38,000)**	**(114,000)**
Forest Management			
MN Forest Resource Council	375,000	375,000	
Forest Mgmt - MCC	(300,000)	(300,000)	
Forest Mgmt	(728,000)	(744,000)	
Subtotal - Forest Management:	**(653,000)**	**(669,000)**	**(1,322,000)**
Parks and Recreation Management			
Parks Accelerated Maint.	(75,000)	(105,000)	
Parks Interpretation	(100,000)	(100,000)	
Parks Resource Mgmt.	(125,000)	(175,000)	
Parks Mgmt	(407,000)	(336,000)	
Subtotal - Parks & Recreation Management:	**(707,000)**	**(716,000)**	**(1,423,000)**
Trails and Waterways Management			
T&W Gen	(69,000)	(75,000)	**(144,000)**
Fish Management			
Reinvest in MN - F&W	(138,000)	(121,000)	**(259,000)**
Wildlife Management			
Population Survey	(13,000)	(13,000)	
Brushland & Forest Habitat	(9,000)	(11,000)	
Wildlife Habitat Improvement	(47,000)	(48,000)	
Wildlife Mgmt Area Level	(15,000)	(17,000)	
Reinvest in MN F&W	(33,000)	(36,000)	
Subtotal - Land & Mineral Management:	**(117,000)**	**(125,000)**	**(242,000)**
Ecological Services			
Rivers and Streams Restoration	(5,000)	(6,000)	
Eco General	289,000	286,000	
Subtotal - Ecological Services	**284,000**	**280,000**	**564,000**

DNR: Proposed Reallocations			
	FY 02	**FY 03**	**FY 02-03 Total**
Enforcement			
Enforcement General	(369,000)	(380,000)	**(749,000)**
Operations Support			
Operations Suppport - Gen Adm Mgmt	450,000	440,000	
Metro Greenways Grants	(45,000)	(45,000)	
Operations Support - Gen Reg Operations	430,000	524,000	
Operations Support- Gen Field Operations	(134,000)	(140,000)	
Info Tech Projects	250,000	140,000	
MIS Software Engineering Services	950,000	950,000	
Subtotal - Operations Support:	**1,901,000**	**1,869,000**	**3,770,000**
Net Total all DNR Re-allocations:			**0**

Natural Resources Fund -Snowmobile Budget Reduction
The Governor is recommending a $1.3 million reduction in spending from the Snowmobile account within the Natural Resources Fund in order to keep the balance in the account positive over the FY 2004-05 biennium. Fifty percent of the reduction will be taken form the Grants-in-aid program, with the other 50 percent coming from the agency's operating budget.

Wildlife Heritage Account/Natural Resources Fund - Lottery-in-Lieu
The Governor proposes to spend $19.6 million and $20.96 million from the Game and Fish Fund (Wildlife Heritage Account) and the Natural Resources Fund respectively. The Governor adds these expenditures to the DNR's base. He proposes to reduce the percentage of proceeds from the in-lieu-of-tax from 87 percent to 86 percent. This diverts $1 million to the General Fund annually to cover PILT payments on 102,000 acres of Con-Con land the Commissioner proposes to designate this session.

PCA Environmental Tax Reform Ramifications
If the PCA tax proposal is enacted, one appropriation from the Solid Waste Fund in the Division of Enforcement would be changed to the proposed Remediation Fund.

White Pine Blister Rust Project to University of Minnesota
The DNR is appropriated $150,000 annually to enter into a contract with the University of Minnesota for the research of white pine blister rust. The Governor proposes to transfer the $300,000 of General Fund directly to the University budget.

Federal Wallup/Breaux
The Governor recommends to reduce spending from the Game and Fish Fund by $713,000 in FY 2002 and $299,000 in FY 2003. The USFWS requires that the state allocate 15 percent of the funds apportioned to it for the payment of up to 75 percent of the costs of acquisition, development, renovation or improvement of public access facilities for recreational boating purposes.

Board of Soil and Water Resources (BWSR)

The Governor recommends a total Board of Soil and Water Resources budget of $37.9 million of which $37.6 million (99.1 percent) is General Fund dollars. This is a recommended General Fund decrease of $6.4 million (14.5 percent) compared to the current biennium. The factors that cause such a large decrease in general fund budget are: 1) $3.4 million appropriated to PCA was transferred to BWSR (delegated feedlot permitting and ISTS contracts with counties, therefore, actual spending occurs in BWSR and not PCA. 2) One time appropriations equal $3.4 million.

- A reallocation of $613,000 from the BWSR cost share program. The funds would be used for non-point feedlot engineering assistance ($113,000) and feedlot cost share grants ($500,000.) This reallocation formalizes the cost share portion already being allocated to feedlots.

Science Museum of Minnesota (SMM)

The Governor recommends a total Science Museum of Minnesota budget of $2.3 million, all of which is General Fund dollars. The recommended General Fund amount is equal to the current biennium's amount.

Academy of Science

The Governor recommends a total Academy of Science budget of $82,000 all of which is General Fund dollars. There is no change compared to the current biennium.

Legislative Commission on Minnesota Resources (LCMR)

The LCMR is recommending a total of 49 projects be funded for a total of $49.351 million.

Agriculture and Rural Development Finance

The Governor recommends a total General Fund appropriation of $130.3 million for the state departments and programs under the jurisdiction of the Environment and Natural Resources committee. This recommended amount is an increase of $3.6 million from current law.

Agriculture and Rural Development Finance Governor's FY 2002-03 General Fund Recommendations *(all dollars in thousands)*					
	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
Dept of Agriculture	119,978	112,909	115,877	-3%	3%
Animal Health Board	6,834	5,410	6,035	-12%	12%
Horticulture Society	164	164	164	0%	0%
Agriculture Utilization Research Institute	7,760	8,260	8,260	6%	0%
Total	**134,736**	**126,743**	**130,336**	**-3%**	**3%**

Department of Agriculture (MDA)

The Governor recommends a total Department of Agriculture budget of $170.1 million, of which $45 million (26.5 percent) is General Fund dollars, and of which $70.86 million is ethanol producer payments (41.7 percent General Fund - open appropriation.) This is a recommended General Fund decrease of $1.7million (-3.7 percent) and an ethanol decrease of $1.2 million (1.7 percent) compared to the current biennium. The decrease is largely due to one time appropriations of $3.5 million in the current biennium. MDA also received $18 million one time funding for farm tax relief in FY01. Recommended changes include:

Reductions

The Governor is recommending a variety of reductions to offset a portion of the increases):

- $130,000 elimination - Beaver Damage Control Grants
- $120,000 reduction (14 percent) - Bio Control Operating funds
- $80,000 elimination - Information and Demonstration Grants
- $100,000 elimination - Organic Cost Share Grants
- $100,000 reduction (50 percent) - Sustainable Ag Demonstration Grants
- $80,000 reduction (40 percent) - MISA Grants
- $10,000 reduction (25 percent) - Demonstration Grants
- $78,000 reduction (80 percent)- Family Farm Payment Adjustments

- $100,000 elimination - Passing on the Farm Grant
- $2,000 elimination - Red River Dairymen's Association Grant
- $12,000 elimination - Red River Valley Livestock Association Grant

New funds received (offset by the reductions above):

- $430,000 of general fund for the Minnesota Certification Program.
- $420,000 of general fund for the operation expense of the Quarentine Greehouse building which received bonding funds in the 2000 Legislative Session.
- $700,000 of general fund toward the Agricultural Best Management Practices (AgBMP) program to provide low interest loans to feedlot improvement projects as a part of a multi agency feedlot initiative.
- $1.250 million of general fund for the upgrade of computer systems (project unity.)

Reallocation:
$350,000 reduction from the Dairy Diagnostic Program will fund Feedlot Information Assessment teams.

Proposed Fee Increases:
- Fertilizer Inspection
- Commercial Canneries Inspection
- Dairy Inspection
- Egg Law Inspection
- Food Handler's Plan Review
- Lab Services
- Wholesale Producer Dealers License
- Grain Buyer and Storage

PCA Environmental Tax Reform Ramifications
If the PCA tax proposal is enacted, current appropriations from the Environmental Fund would be changed to the proposed Remediation Fund.

Animal Health Board

The Governor recommends a total Animal Health Board budget of $7.1 million, of which $6 million (85 percent) is General Fund dollars. This is a recommended General Fund decrease of $799,000 (- 11.7 percent) compared to the current biennium. The decrease is largely due to one time appropriations for psuedorabies eradication program. Changes recommended by the Governor to the agency base budget include the following:

- $119,000 in FY 2003 from the General Fund to investigate Avian Pneumovirus in turkeys.
- $330,000 in General Fund dollars as a base adjustment for small agency infrastructure.
- An $80,000 reallocation from the companion grants program to Johne's disease research.

Minnesota State Horticultural Society (MSHS)

The Governor
recommends a total Minnesota State Horticultural Society budget of $164,000 all of which is General Fund dollars. There is no change compared to the current biennium, nor are there any change items recommended.

Agriculture Utilization Research Institute (AURI)

The Governor recommends a total AURI budget of $8.7 million of which $8.3 million (95 percent) is General Fund dollars. This is a recommended General Fund decrease of $500,000 (-6.4 percent) compared to the current biennium due to a legislative reduction in the AURI's budget in FY 2000.

For additional information on Environment or Agriculture Finance issues, contact Peter Skwira at 651-296-4281, or Peter.Skwira@house.leg.state.mn.us.

Jobs & Economic Development Finance

The Governor is recommending General Fund appropriations of $403.4 million in the FY 2002-03 biennium for the 20 state departments, agencies, boards and councils under the budget jurisdiction of the Jobs and Economic Development Finance Committee. For all directly appropriated funds, the total recommended by the Governor is $527.4 million. This section summarizes the Governor's major budget recommendations.

Jobs & Economic Development Finance
Governor's Y 02-03 General Fund Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Governor vs. Current Law FY 02-03
Trade & Economic Development	87,319	69,926	69,999	-19.8%	0.1%
Economic Security	108,619	71,906	77,849	-28.3%	8.3%
Housing Finance Agency	114,040	79,664	103,664	-9.1%	30.1%
Commerce	59,195	46,741	57,649	-2.6%	23.3%
Bd of Accountancy	1,263	1,271	1,427	13.0%	12.3%
Architecture, Eng. et.al.	1,694	1,848	1,932	14.0%	4.5%
Barber Board	293	298	312	6.5%	4.7%
Board of Boxing (sunset 6/30/01)	149	n/a	n/a	n/a	n/a
Labor & Industry	7,649	6,948	7,228	-5.5%	4.0%
Mediation Services	4,378	4,360	4,566	4.3%	4.7%
Labor Interpretive Center	3	0	0	-100.0%	0.0%
Public Utilities Comm.	7,776	7,968	8,367	7.6%	5.0%
Public Service	6,345	6,414	0	-100.0%	-100.0%
Historical Society	50,878	51,336	53,728	5.6%	4.7%
Council on Black Minnesotans	649	658	688	6.0%	4.6%
Chicano Latino Affairs	638	648	678	6.3%	4.6%
Asian-Pacific Minn	563	572	599	6.4%	4.7%
Indian Affairs	1,118	1,134	1,186	6.1%	4.6%
MN Technology	13,850	12,210	12,210	-11.8%	0.0%
IRRRB (Region 3 - Occup Tax)	1,320	1,336	1,336	1.2%	0.0%
Total	**467,739**	**365,238**	**403,418**	**-13.8%**	**10.5%**

Notes: The Board of Electricity and Workers Compensation Court of Appeals do not receive a General Fund appropriation.
The IRRRB number show is a pass-through. The Board itself does not receive a general fund appropriation.
The Governor's Recommendations for FY 2002-03 includes a proposal to merge the remaining division of Public Service with Commerce.

Department of Trade and Economic Development

The Governor recommends a $69.99 million General Fund appropriation in FY 2002-03. The total recommendation for all directly appropriated funds is $93.1 million. The Governor's major General Fund recommendations are:

- $901,000 in increased funding for staff salary and benefit cost.

- $754,000 in increased funding for agency space/lease cost increases.

- $10 million in one-time General Fund funding for the Biomedical Innovation and Commercialization Initiative. These funds, to be matched 3:1 by private fund commitments prior to release, will be used to create a third-party entity charged with the responsibility of fully exploiting the commercial opportunities from biomedical research at the University of Minnesota.

- $155,000 per year to restore funding for the Metropolitan Economic Development Association.

- $1.5 million per year for transfer to the Metropolitan Council. Of this amount, $500,000 is for the Council's Livable Communities program, and $1 million is for an Agricultural Land Preservation pilot program. This pilot program's funding is one-time.

The Governor also recommends eliminating General Fund appropriations for the Job Skills Partnership and the Pathway programs. These programs would be funded with a single $10 million per year direct appropriation from the Workforce Development Fund. The savings to the General Fund would be $14.9 million for the biennium. The combined funding for the Job Skills Partnership and Pathway Programs would be $5.1 million higher in the 2002-03 biennium under this proposal than current law.

The Twin Cities Rise employment training program would receive a $300,000 per year direct appropriation from the Workforce Development Fund under the Governor's proposed budget. The program is currently funded with a Jobs Training tax credit which would be eliminated.

The Governor is recommending elimination of the State Dislocated Worker Program. The recommendation would result in a $41.9 million savings to the Workforce Development Fund. The Governor also recommends suspending the Dislocated Worker assessment which funds the Workforce Development Fund in calendar year 2002, saving Minnesota employers an estimated $26.3 million in 2002.

Two additional recommendations for funding programs with Workforce Development Funds are included in the Higher Education and K-12 Education portions of the Governor's budget.

- $5 million per year would be appropriated to the Department of Children Families and Learning for the Teachers for the 21st Century Program. This appropriation would fund a set of programs to attract and retain teachers in shortage areas. The program would sunset on June 30, 2005.

- $3.5 million per year would be appropriated to MnSCU to fund Regional Programs of Excellence. The funds are to implement high priority programs that address critical workforce needs of the regions.

Minnesota Technology, Inc. (MTI)

The Governor recommends that MTI receive General Fund appropriations of $12.2 million in FY 2002-03. This is the same funding level as current law, with no new programs or initiatives being recommended by the Governor. MTI, through its governing board, is considering the reallocation of existing resources to expand select existing programs and embark on new initiatives.

Department of Economic Security

The Governor recommends appropriations of general and special revenue funds totaling $79.4 million in FY 2002-03. General Fund dollars represent $77.85 million of this total. The remaining $1.55 million comes from the Workforce Development Fund. The Governor's major funding recommendations are:

- $377,000 in General Fund dollars to fund staff salary and benefit increases in the FY 2002-03 biennium.

- $66,000 from the General Fund for documented space/lease cost increases for the biennium.

- $1.5 million from the General Fund in each year of the biennium to create an emerging worker program. The program is designed to provide technical training for 11th and 12th grade students who may otherwise not pursue post-secondary education.

- $111,000 each year to satisfy a federally required hard cash state match to secure $3.9 million in federal Juvenile Accountability Incentive Block Grant funds. General Fund appropriations to the state Youthbuild program would be reduced by $111,000 each year to free-up the required match dollars.

- $1 million each year to fund a new Universal Customer program in the state's workforce development system. Universal customers are those individuals who could benefit from employment and training services but do not qualify for current targeted services.

- $250,000 each year from the General Fund to fund the Best Buddies program. The program will establish chapters on high school and college campuses to match volunteer students with individuals with mental retardation. Program funding would be one-time and requires a 1:1 match with non-state funds.

- $300,000 in FY 2002 and $8 million in FY 2003 from a new Unemployment Insurance Set-Aside special revenue account to fund Unemployment Insurance (UI) technology enhancements. Funding for this new revenue account would come from setting aside a portion of UI payments that would otherwise go into the UI trust fund. The amount of set-aside is $5 million in FY 2002 and $10 million per year through FY 2005.

The Governor also recommends abolishing the Displaced Homemakers Program. The recommendation saves the Workforce Development Fund $3.65 million in the FY 2002-03 biennium.

Department of Labor & Industry

The Governor recommends that the Department's FY 2002-03 General Fund appropriation be set at $7.2 million. The recommended direct appropriation from all funds is $51.4 million. Besides the General

Fund, the Department receives direct appropriations from the Workers Compensation Special Fund (recommended $42.6 million) and the Workforce Development Fund (recommended $1.6 million).

The Governor's funding recommendations are at the Department's current law levels with the following exceptions:

- $368,000 from the Workers' Compensation Fund to provide for systems support and front end processing supervision for the Workers Compensation case scheduling and management system. This initiative, which includes $148,000 to hire a supervisory position to direct data and image quality assurance activities, will have no new cost. It will be paid for through the reallocation of $238,000 from the Office of Administrative Hearings and $130,000 from the Workers' Compensation Court of Appeals

- $1.55 million for salary and benefit increases. The increases would be paid for with $256,000 from the General Fund, $1.26 million from the Workers' Compensation Fund and $40,000 from the Workforce Development Fund

- $167,000 for space/lease cost increases. The increases will be paid for with $24,000 from the General Fund, $140,000 from the Workers' Compensation Fund and $3,000 from the Workforce Development Fund.

- $46,000 from the Workers' Compensation Fund to fund increased Attorney General costs.

The Governor also recommends the current law requiring employment search firms to register with Labor and Industry be repealed. The registration fee these firms pay would also be abolished. This initiative will cost the General Fund $100,000 per year in lost revenue.

Minnesota Housing Finance Agency

The Governor recommends a $103.7 million General Fund appropriation in FY 2002-03. This is an increase of $24 million over the current law funding base. The $24 million is one-time money for the Affordable Rental Investment Fund. The appropriation will be used to increase the supply of low-income rental housing by 300-375 units depending on cost and the availability of other funding sources. The general fund dollars for this initiative will come from a $24 million transfer of TANF funds for the Working Family Tax Credit.

The Governor also is recommending that several of MHFA's current programs be consolidated. No new state funding would be involved in the consolidation; however, current program resources will be reallocated. The proposed consolidations are summarized below. A visual outline of the consolidation is presented in the table on the next page.

- Several development programs will be consolidated into the Economic Development and Housing Challenge Fund to help increase the production of affordable housing and leverage non-state resources.

- A number of supportive housing programs will be consolidated into the Housing Trust Fund to better develop housing for homeless and very low-income households with special needs.

- The Foreclosure Prevention and Assistance Program will be consolidated into the Full Cycle Homeownership Services Program.

- $100,000 per year would be reallocated from the ARIF and Housing Trust Fund production programs into the Nonprofit Capacity Building Grants program to fund continuum of care planning in Greater Minnesota and homeless prevention and assistance coordination in the Twin Cities area.

Minnesota Housing Finance Agency's Consolidation Proposal

Current		Proposed	
Re/development Programs		**Consolidation of Re/development Programs**	
Affordable Rental Investment Fund	$6,493,000	Economic Development Housing Challenge Fund	$12,004,000
Community Rehabilitation Program	4,900,000		
Employer Matching Grants	800,000		
MN Rural & Urban Homesteading	186,000		
Urban Indian Housing Program	187,000	Urban Indian Housing Program	187,000
Total	12,566,000	Total	12,191,000
Supportive Housing Programs		**Consolidation of Supportive Housing Programs**	
Housing Trust Fund	$1,798,000	Housing Trust Fund	$4,623,000
Housing Trust Fund – Transitional	550,000		
Rental Assistance for Family Stabilization	2,000,000		
Bridges	1,700,000	Bridges	1,700,000
Family Homeless Prevention	3,250,000	Family Homeless Prevention	3,250,000
Total	9,298,000	Total	9,573,000
Homeownership Loan Programs		**Homeownership Loan Programs**	
Housing Rehabilitation Loan Program	$4,287,000	Housing Rehabilitation Loan Programs	$4,287,000
Tribal Indian Housing	1,683,000	Tribal Indian Housing	1,683,000
Home Ownership Assistance Fund	900,000	Home Ownership Assistance Fund	900,000
Total	6,870,000	Total	6,870,000
Preservation of Federally Assisted Housing		**Preservation of Federally Assisted Housing**	
Affordable Rental Investment Fund	$10,000,000	Affordable Rental Investment Fund	$10,000,000
Resident &Organizational Support		**Consolidation of Resident & Organ. Support**	
Mortgage Foreclosure Prevention	$583,000	Full Cycle Homeownership	$858,000
Full Cycle Homeownership	275,000		
Nonprofit Capacity Building Grants	240,000	Nonprofit Capacity Building Grants	340,000
Total	1,098,000	Total	1,198,000
Agency Grand Total	**$39,832,000**	**Agency Grand Total**	**$39,832,000**

Department of Commerce

The Governor recommends that the Department's FY 2002-03 General Fund appropriation be $56.65 million. Included in the recommendation:

- $1.5 million to fund biennium staff salary and benefit increases.

- $46,000 to fund biennium space/lease cost increases.

- $3.3 million in FY 2002 and $3.35 million in FY 2003 reflecting the Governor's recommendation that the remaining Weights and Management division at the Department of Public Service be transferred to the Department of Commerce. With this recommendation, the Governor's initiative to merge Public Service and Commerce will be complete. The Department of Public Service would be abolished.

- $250,000 in FY 2002 and $250,000 in FY 2003 for three positions to support the cable regulation component of the Governor's telecommunication reform proposal. The cost will be recovered through a new fee assessment on the cable industry.

- $725,000 in FY 2002 and $1.5 million in FY 2003 as a result of the Governor's recommendation that Managed Health Care regulation be transferred to Commerce from the Department of Health. The current fees charged by Health for this regulation would also transfer and be placed in the General Fund. The fees are projected to offset Commerce's regulatory costs.

- The Governor recommends two new fees that will be deposited in the General Fund. First, a collection agency audit fee which is estimated to yield $14,000 in FY 2002-03. Second, self insurance plan certification and utilization review fees which will generate an estimated $33,000 per fiscal year.

Commerce would also receive $15 million per fiscal year from the Health Care Access Fund under the Governor's proposed budget. Of the FY 2002 appropriation, $250,000 will be used to conduct an actuarial study of establishing a private insurance access pool for the individual health insurance market. The remaining $14.75 million in FY 2002 and the entire $15 million in FY 2003 will be used to offset the losses of the Minnesota Comprehensive Health Association.

The Department will serve as the lead agency in the Governor's major telecommunication reform initiative. The proposed budget carries the major state revenue and expenditure impacts should this initiative become law. The major elements are that the department will be appropriated $94.9 million in FY 2002 and $220 million in FY 2003 to support the governor's reform plan.

These appropriations will be funded by a 5 percent universal service excise tax applied to all interstate and intrastate end user revenue derived from telecommunication services, cable and other multi-channel programming. The 5 percent excise tax, which the budget suggests will be revenue neutral to Minnesota telecommunications consumers, is estimated to raised $164.3 million in FY 2002 and $195.8 million in FY 2003. The Governor proposes that these revenues be deposited in a Universal Service special revenue fund and be statutorily appropriated to the Department.

Board of Accountancy

The Governor recommends that the Board receive General Fund appropriations totaling of $1.4 million in the FY 2002-03 biennium. The recommended budget includes:

- $40,000 in FY 2002 and $57,000 in FY 2003 to implement the AICPA computerized testing program. The fee charged by the board to individuals taking the Uniform CPA Examinations will be increased to generate the revenue to offset the increased costs.

- $25,000 for the biennium for staff salaries and benefits costs, $6,000 for documented space/lease cost, and $28,000 for the small agency operational expenses.

- $23,000 in carryover funds that were appropriated by the 1999 Legislature for the Board's IT enhancements. These funds would allow the approved projects to be completed.

Board of Architecture, Engineering, Land Surveying, Landscape Architecture, Geoscience and Interior Design

The Governor recommends a $1.9 million General Fund appropriation for the Board in FY 2002-03. This amount represents current law base funding plus $31,000 to cover salary and benefit increases, $4,000 to pay for documented space/lease costs, and $49,000 for the small agency operational expenses.

Board of Barber Examiners

The Governor recommends a General Fund appropriation of $312,000 in FY 2002-03. The funding is the Board's current law base amount plus $10,000 to cover salary and benefit increases, $1,000 to pay for documented space/lease costs, and $3,000 for the small agency operational expenses.

Board of Electricity

This agency receives no General Fund appropriations. The Governor recommends $21.8 million from the Special Revenue Fund for the Board's FY 2002-03 appropriation. The proposed budget includes funding to continue development and maintenance of the Board's IT System, including electronic business and expanded communication, and funding for additional full-time employees to monitor inspection services and investigate complaints.

Bureau of Mediation Services

The Governor recommends General Fund appropriations of $4.6 million in FY 2002-03. The recommendation includes:

- $58,000 for on-going support for technology infrastructure. The Governor has also included recommended funding to further improve BMS' technology capacity in the FY 2002-03 biennium. This recommendation is part of the Small Agency Infrastructure initiative included in the proposed budget of the Office of Technology (see State Government Finance section).

- $140,000 for salary and benefit increases.

- $8,000 for space/lease cost increases.

Public Utilities Commission

The Governor recommends that the FY 2002-03 General Fund appropriation be set at $8.4 million. The proposed budget includes:

- $281,000 for salary and benefit increases.
- $118,000 for space/lease cost increases.
- $210,000 in carryover funds that were appropriated by the 1999 Legislature for the Commission's information technology enhancements. These funds would allow the approved projects to be completed.

Department of Public Service

The Governor recommends that the Department of Public Service be abolished, and that the Department's remaining Weights and Measures Division be transferred to the Department of Commerce.

Minnesota Historical Society (MHS)

The Governor recommends that MHS receive a $53.7 million appropriation from the General Fund in the FY 2002-03 biennium. The recommended budget is at the current law level with the following exceptions:

- $1.3 million for staff salary and benefit increases.
- $1.1 million for documented rent/maintenance cost.

The Governor's MHS budget submission also includes $90,000 for a one-time appropriations from the Minnesota Natural Resources Fund to design and upgrade trails at the Forest History Center. This project's funding is recommended by the Legislative Commission on Minnesota Resources.

Council on Black Minnesotans

The Governor recommends a $688,000 General Fund appropriation for the FY 2002-03 biennium. The recommendation includes $21,000 to cover staff salary and benefit increases and $9,000 to fund small agency operational expenses.

Chicano Latino Affairs Council

The Governor recommends a $678,000 General Fund appropriation for the FY 2002-03 biennium. The recommendation includes $16,000 to cover staff salary and benefit increases, $3,000 to fund documented space/lease costs, and $11,000 to cover small agency operational expenses.

Council on Asia-Pacific Minnesotans

The Governor recommends the Council's General Fund appropriation in FY 2002-03 be $599,000. The recommendation includes $21,000 to cover staff salary and benefit increases, $1,000 to fund documented space/lease costs, and $5,000 to cover small agency operational expenses

Minnesota Indian Affairs Council

The Governor recommends the Council receive a General Fund appropriation of $1.2 million for the FY 2002-03 biennium. The recommendation includes $27,000 to cover staff salary and benefit increases and $25,000 to cover small agency operational expenses.

Workers Compensation Court of Appeals

This agency receives no General Fund appropriation and is funded from the Workers Compensation Special Fund. The Governor recommends the Court receive an appropriation for FY 2002-03 of $3.2 million. The recommendation includes:

- $96,000 for salary and benefit increases.
- $30,000 for space/lease cost increases.
- $19,000 to cover small agency operational expenses.
- $130,000 reduction in funding will be reallocated to the Department of Labor and Industry to partially fund the workers' compensation case scheduling and management system (discussed in the DLI section).

Iron Range Resources and Rehabilitation Board

The Governor recommends the Board receive the current law required General Fund open appropriation of $1.3 million for FY 2002-03. The Governor also recommends that $71.6 million be appropriated to the Board from the Iron Range Resources and Rehabilitation Fund and the Northeast Minnesota Economic Protection Plan in FY 2002-03. This is a statutory appropriation.

Departments of Trade and Economic Development and Economic Security Merger

The Governor did not include the details of the recommendation to merge the Departments of Trade and Economic Development and Economic Security with the January 23rd budget submission. The administration has indicated their intention to submit the merger proposal as a separate budget recommendation. The recommendation will be sent to the Legislature either before or in conjunction with the Governor's supplemental budget recommendations in late February.

For additional information on Jobs and Economic Development Finance issues, contact Ron Soderberg at 651-296-4162, or ron.soderberg@house.leg.state.mn.us

State Government Finance

The Governor recommends total General Fund appropriations of $791.4 million for the state departments and programs under the jurisdiction of the State Government Finance committee. This recommended amount is an increase of $75.2 million, or 10.5 percent, from current law.

State Government Finance
Governor's FY 2002-03 General Fund Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
Legislature	131,695	125,432	132,797	0.8%	5.9%
Governor's Office	8,223	8,254	8,858	7.7%	7.3%
State Auditor	18,278	18,622	19,828	8.5%	6.5%
State Treasurer	18,907	18,476	18,774	-0.7%	1.6%
Attorney General	56,455	49,967	53,090	-6.0%	6.3%
Secretary of State	21,530	12,148	12,877	-40.2%	6.0%
Campaign Finance Board	5,510	5,703	7,118	29.2%	24.8%
Investment Board	4,686	4,752	5,012	7.0%	5.5%
Administrative Hearings	400	0	168	-58.0%	
MN Planning	11,532	9,488	10,189	-11.6%	7.4%
Administration	67,654	57,362	85,062	25.7%	48.3%
Public Broadcasting	6,660	6,660	6,660	0.0%	0.0%
Capitol Area Arch. Board	1,229	612	678	-44.8%	10.8%
Finance Department	40,441	37,822	38,945	-3.7%	3.0%
Indirect Cost Receipts	(41,419)	(45,409)	(45,409)	9.6%	-0.0%
Employee Relations Dept.	21,782	20,666	22,132	1.6%	7.1%
Revenue Department	184,018	172,034	185,789	1.0%	8.0%
Revenue Open General Fund	78,532	73,589	73,189	-6.8%	-0.5%
Military Affairs	22,832	22012	27196	19.1%	23.6%
Veterans Affairs Dept.	10,492	8,712	8,685	-17.2%	-0.3%
Veterans Service Orgs.	148	148	148	0.0%	0.0%
Gambling Control Board	4,692	4,482	4,775	1.8%	6.5%
Racing Commission	792	804	840	6.1%	4.5%
MN Amateur Sports Cmsn.	2,758	2,778	2,834	2.8%	2.0%
State Arts Board	26,308	26,188	26,260	-0.2%	0.3%
Humanities Commission	1,806	1,818	1,858	2.9%	2.2%
Contingent Accounts	197	200	10,200	5077.7%	5000.0%
Tort Claims	970	550	550	-43.3%	0.0%
MN State Retirement System	11,757	13,584	13,584	15.5%	0.0%
Mpls. Employees Retirement	8,890	6,464	6,464	-27.3%	0.0%
Local Police & Fire Aid	9,269	12,690	12,690	36.9%	0.0%
Govt. Innovation & Cooperation	2,032	2,036	2,050	0.9%	0.7%
1st Class Cities - Teachers Aid	37,540	37,534	37,534	-0.0%	0.0%
Total	**776,596**	**716,178**	**791,425**	**1.9%**	**10.5%**

Constitutional Offices[1]

Attorney General's Office

The Attorney General's Office (AGO) requests $57.7 million from the General Fund for the biennium, an increase of $7.8 million from current law. The AGO's request includes two initiatives:

- $1.8 million for information technology
- $4.1 million in permanent funding for salary increases.

The Governor's recommended General Fund spending level for the AGO is $53.1 million, an increase of $3.1 million from current law. This recommendation includes $2.1 million for salary and non-salary inflation, and an additional $1 million for information technology.

Other Funds

The AGO requests $3.7 million from the State Government Special Revenue Fund for services provided to health related licensing boards. The AGO also requests $1.2 million from the Environmental Trust Fund for investigating and prosecuting environmental crime and for responsibilities associated with insurance claims settlements and recovery associated with landfills in the landfill cleanup program. The Governor concurs with the AGO's requested funding levels for its non-general fund activities.

Governor's Office

The Governor requests $8.9 million for the biennium, an increase of $604,000 over current law. This funding level includes $394,000 for salary and non-salary inflation, and $210,000 for technology. The Governor is also recommending that $88,000 be transferred from his office budget to the Department of Administration to cover the utility costs at the Governor's residence. In addition, a request for $20,000 for the Governor's portrait is included in the budget request for the Department of Administration.

Secretary of State

The Secretary of State requests $14.9 million for the biennium, an increase of $2.7 million over current law. Included in this request is one new initiative:

- $2.7 million for operating costs for the Uniform Commercial Code (UCC) system. The 2000 Legislature provided one-time funding of $4 million to construct a new statewide UCC filing and retrieval system. The Secretary of State's office is requesting new funds for the system's on-going operating costs, and estimates that if the funding is not provided, the General Fund will forgo $6.3 million in new revenues that were projected from increased filings with the state.

The Governor's recommended spending for this office is $12.9 million, an increase of $729,000 over current law. This funding level including an increase of $479,000 for salary and non-salary inflation, and $250,000 for technology.

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[1] Because of the separation of branches of government and constitutional offices, the Governor acknowledged the right of these offices to present their budgets directly to the legislature for consideration. The Governor does not comment on any specific initiatives requested by constitutional offices. However, the Governor's Budget does included recommended overall spending levels for each office, including increases for both salary and non-salary inflation, and technology initiatives.

State Auditor

The State Auditor's office requests $20.3 million, an increase of $1.7 million over current spending. Agency requested change items totaling $939,000 include:

- $451,000 for additional staff to respond to citizen requests for petition audits, and to institute a process to review local audit deposited with the office's Government Information Division. The State Auditor would recover the costs of the petition audits through fees charged to the audit clients, and deposit these revenues in General Fund. These estimated revenues are $232,000 for the biennium.
- $141,000 to add a Human Resources Director position.
- $155,000 to add one additional information technology staff person.
- $192,000 for additional staff to handle pre-need funeral trust reviews.

The Governor's recommended spending for this office is $19.8 million, an increase of $1.2 million over current law. This funding level includes of $823,000 for salary and non-salary inflation, and $382,000 for technology.

State Treasurer

The State Treasurer requests $4.8 million for the biennium, an increase of $356,000 from current law. The State Treasure is requesting $150,000 in one-time funding for continuation of its Electronic Financial Transactions initiative.

The Governor's recommended spending for this office's operations is $4.77 million, including an increase of $116,000 for salary and non-salary inflation. Because the State Treasure's office will be eliminated in January 2003, the Governor is also recommending a $90,000 reduction in the FY 2003 base for the office. This reduction reflects one-half year costs for the positions of the Treasurer and the Deputy Treasurer.

In addition to the recommendation for the Treasurer's operating costs, the Governor's budget is also tracking an additional $14 million in costs unrelated to the office's actual operations, thus increasing the total spending for the State Treasurer to $18.7 million and distorting the overall spending picture for the office. It is unclear at this time if this item will be corrected in the Department of Finance's fund balances released with the February forecast.[2]

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[2] The cause is an accounting mechanism established in FY 2000 to accommodate a legislative change made to MS 357.021, Subd.7, which directs the Treasurer to disburse surcharges on criminal and traffic offenses to the Peace Officers Standards and Training (POST) Board.

The revenue source existed prior to FY 2000, but statutory changes effective mid-FY 1999 increased the surcharge revenue. In an attempt to isolate the "new" funding stream in a method that would provide an audit trail, a General Fund appropriation account under the Treasurer's Office was established for the POST Board portion of the "new" funds. The funds were then transferred to a Special Revenue fund in the POST Board. Because the transfer is out of the Treasurer's Office General Fund receipts, it is accounted as an expense to Treasurer's Office.

Legislature

The Legislature does not participate in the executive agency budget process. Legislative budget requests will be available after their approval by House and Senate leadership.

The Governor recommends a total of $132.8 million for the Legislature, an increase of $7.4 million from current law. This recommendation includes $58.4 million for the House of Representatives, $43.6 million for the Senate, $19.9 million for the Legislative Coordinating Commission, and $11 million for the Legislative Audit Commission.

State Agencies

Department of Administration

The Governor recommends a direct General Fund appropriation of $85 million for the biennium, an increase of $27.7 million from current spending. This recommendation includes a $1 million increase for salaries and benefits[3], and $2.1 million for documented rent increases.

New General Fund initiatives for the FY 2002-03 biennium total $26.9 million. The Governor is also recommending $2.3 million in base reductions to programs within the department.

Department of Administration
Proposed General Fund Initiatives

	Base Reductions	New Initiatives
Operations Management		
Materials Management	(212)	
Comm.Media	(88)	
Office of Technology		23,953
Facilities Management		
Plant Management	(46)	2,584
Building Construction	(214)	125
Management Services		
Administration	(50)	20
Management Analysis		211
Information Policy Analysis	(400)	
State Archaeologist	(196)	
STARS	(600)	
Fiscal Agent	(520)	
Total all Programs:	**(2,326)**	**26,893**

[3]It should be noted that almost 70 percent of the Department of Administration's employees are funded through internal service funds, not through a direct general fund appropriation. The salary and benefits increases for these employees are built into the rates charged by the internal service fund.

Operations Management
The Governor is recommending base budget **reductions** to two budget activities:

- ($212,000) for the Material Management activity. This reduction would be accomplished through the reduction of two positions, and cuts to the activity's training and travel budget.
- ($88,000) reduction to the Comm.Media activity, by eliminating the funding provided to partially offset the cost of making the State Register available on-line. The total costs for this service will now be passed on to state agencies that publish in the Register through increased page charges.

These reductions would reduce the program's recommended base budget to $8 million.

Office of Technology (OT)
The Office of Technology's recommended base budget (including salary and benefits adjustments of $195,000) is $5.4 million. In addition, the Governor is recommending $23 million in new spending initiatives:

- $1 million in increased base funding for the North Star web portal. Current base funding is $936,000. The new funds would be used to cover increasing license fees for the search engine, to provide ADA compliant and multi-lingual technologies and services, and to offer digital audio and video streaming capabilities to all state agencies with sites hosted on the North Star portal.
- $1 million to create a new "Technology Enterprise Fund" or TEF. The TEF would be used to provide loans and grants for enterprise-wide technology projects and citizen telecommunications access. The TEF would be administered by the commissioner of administration, with oversight from the department of finance. In addition to the direct appropriation, the TEF would be funded through revenues collected from rental of antenna tower space, and from savings generated by information technology and telecommunications projects. All funding would carry-forward across bienniums.

  The Governor also is recommending the creation of a "Technology Advisory Board" consisting of appointed members from both the private and public sector. The purpose of the board would be to advise the commissioner, Governor and the legislature on expenditures from the TEF.

  Implications: The creation of a TEF would be a significant change in the process for funding information technology projects. The executive branch states that the TEF would help improve enterprise level oversight and reduce duplication of systems, and provide a more timely funding source for quickly-changing technology. However, such a fund would also reduce the direct role of the legislature in determining funding levels for specific projects, and would separate many funding decisions from the associated policy areas and programs.
- $864,000 to hire a total of additional Technology Analysts (3 in FY 2002 and 2 more in FY 03). These analysts would be responsible for coordination, review, and collaboration among state agencies with regard to IT initiatives.
- $300,000 for an information technology architecture initiative. This initiative would help develop a statewide framework or "blueprint" of principles, best practices, and standards that will govern the design, construction, deployment, and management of enterprise-based information systems.
- $1.5 million from the General Fund and $1.2 million from State Government Special Revenue fund for continuation of the Small Agency Infrastructure initiative. This project provides small agencies

with a funding stream for basic technology infrastructure needs, Electronic Government Services, maintenance, support, and related activities. The appropriation for this initiative would be assigned to OT . Once the small agency work plans are complete and approved by OT, funds would be transferred to the eligible small agencies. Base funding in future budgets would be directly appropriated to the small agency. The table below shows the small agencies involved in the initiative:

Small Agency Infrastructure Initiative
(dollars in thousands)

Agency	Project	FY02-03	FY04-05
Architecture, Engineering	Database Security	45	20
Amateur Sports	Technology Initiative	79	0
Campaign Finance	IT Support & Development	30	30
Campaign Finance	Real-Time On-line Contributors List	25	0
Judicial Standards	Data Program	20	0
Mediation Services Bureau	Electronic Files Project	230	40
Nursing	Electronic Government Services (EGS)	750	0
Racing Commission	Technology Infrastructure	24	24
Sentencing Guidelines	Life Cycle Replacement	46	46
Veterans Affairs	Info Technology Infrastructure	240	240
	General Fund subtotal:	**$1,489**	**$400**
Chiropractic Board	EGS Development	75	0
Medical Practices	EGS Infrastructure	824	187
Nursing	EGS Infrastructure w/ EMS	160	97
Social Work	EGS	120	400
	State Govt. Special Revenue:	**$1,179**	**$684**
	Total Small Agency Infrastructure	**$2,668**	**$1,084**

The Governor is recommending that two significant pieces of the CRIMNET project be funded through the Office of Technology. These include:

- $4 million and 3 new FTEs to complete the development of an integration backbone for the CriMNet project. The funds would be used to develop a search engine to allow criminal justice information to be shared across organizations, and to expand the bandwidth of the data network. Costs for the next biennium would be charged to users through the InterTech internal service fund.
- $15 million for the continued implementation of the Minnesota Court Information Systems (MNCIS) component of the CriMNet project. These funds may be transferred to the Supreme Court upon a determination by the Office of Technology that this project is consistent with statewide information systems requirements.
- $300,000 for a joint study by the Office of Technology and the Unemployment Insurance (UI) Branch of the Department of Economic Security to prepare for the development of a $30 million systems project.

Intertechnologies Group (InterTech)
The Governor recommends $1.7 million in General Fund spending for Intertech's computer services and telecommunications management, the same as current law. Approximately 85 percent of Intertech's spending is "off-budget" - that is, the funding is provided through state agency reimbursements to internal service funds. Estimated expenditures for the internal service funds for FY 2002-03 biennium are $152.6 million.

The Governor is requesting an increase in FY 2001 spending authority of $4 million from the 911 Special Revenue fund, for increased costs associated with wireless enhanced 9-1-1. He is also recommending an increase in the fee from 27 cents to 29 cents per telephone line.

Facilities Management
The Governor recommends base budget **reductions** to two budget activities:

- ($46,000) for the Plant Management activity, from Resource Recovery. This reduction would eliminate recycling collection and transportation for agencies located in leased space. The expectation is that private landlords will take over the recycling activities.
- ($214,000) for the Building Construction activity, through elimination of a vacant (but funded) position for a Principal Electrical Engineer.

These reductions are offset by $2.2 million in recommended base adjustments for salaries, benefits and lease increases. In addition, the Governor recommends three spending initiatives totaling $2.7 million:

- A permanent increase to the In-Lieu-of-Rent payment of $2.5 million, bringing the total amount for this activity to $13.5 million. This appropriation is for the space costs for the Capitol, State Office Building and the ceremonial spaces on the Capitol mall.
- $48,000 increase for costs associated with the Governor's residence, in addition to the recommended transfer of $88,000 in base funding for these costs from his office budget to the Department of Administration. The new funds would be used for expenses previously covered through fundraising and donations.
- One-time appropriations of $75,000 in FY 2001 and $125,000 for costs related to the Luverne lawsuit.

Management Services
The Governor recommends base reductions totaling $1.25 million in four activities:

- ($50,000) in the Administrative Management activity, achieved through staff attrition.
- ($400,000) in Information Policy Analysis. This reduction eliminates funding for the data practices training program established by the 1999 Legislature.
- ($196,000) in FY 2003 to the Office of the State Archaeologist. The Governor recommends eliminating General Fund support for the office, and allowing the commissioner the authority to charge state agencies, political subdivisions, and businesses a fee for the cost of providing archaeological services.
- ($600,000) for the biennium for the System of Technology to Achieve Results (STAR) program. This program provides technology-related assistance to individuals with disabilities. The program

was totally supported by federal funds until the FY 2000-01 biennium, when the state began to provide General Fund support to make up for a cut in federal funds. The Governor is reducing state support and recommending that the office develop a transition plan to move to complete non-state funding by FY 2004.

These reductions are offset by recommended base adjustments of $342,000, and by three spending initiatives:

- $20,000 for the Governor's portrait.
- $200,000 in FY 2003 for transition costs for the next Governor-elect.
- $11,000 in FY 2003 for transition costs for the next Attorney General-elect.

Office of Administrative Hearings (OAH)

This agency is supported by the Workers' Compensation Special Fund and revolving fund revenues, and usually does not receive General Fund money. The Governor recommends direct appropriations of $14.1 million for the biennium from the Workers Compensation Fund, which includes a base reduction of ($238,000) for a transfer to the Department of Labor and Industry related to the case scheduling management support system.

The Governor is also recommending a significant increase in OAH's fees charged to agencies and local governments for rule hearings and contested case proceedings. This fee increase - from $91/hour to $130/hour for administrative law judges, and from $50/hour to $75/hour for staff attorneys - would increase the office's revolving fund revenues to $2.9 million for the biennium. The base for this activity is $1.95 million.

In addition, the Governor is recommending a General Fund deficiency appropriation of $168,000 in FY 2002 for on-going lease costs associated with space formerly used by the child support activities that were transferred to the court system in 2000. The office was unable to renegotiate its lease agreement and is obligated to pay rental costs for this unused space.

Amateur Sports Commission(MASC)

The Governor recommends a total of $2.8 million for the biennium, an increase of $56,000 over current law. This increase is due to recommended base adjustments for salaries and benefits, and small agency operational expenses. Funding for MASC's technology initiative is included in the Small Agency Infrastructure initiative under the Department of Administration.

State Arts Board

The Governor recommends $26.3 million for the biennium, an increase of $72,000 from current law. This increase is due to recommended base adjustments for salaries and benefits, and small agency operational expenses.

Capitol Area Architectural Planning Board (CAAPB)

The Governor recommends $678,000 for the biennium to the CAAPB, an increase of $66,000 over current law. This increase includes $26,000 in recommended base adjustments for personnel and small agency expenses, and $40,000 for a base increase to cover unanticipated Local Area Network charges paid to the Department of Administration.

Campaign Finance and Public Disclosure Board

The Governor recommends a General Fund operating budget of $1.38 million, an increase of $228,000 over current law. This recommendation includes an initiative of $75,000 in FY 2001, and $155,000 for the FY 2002-03 biennium, for unfunded costs related to rising state-paid benefit costs, training expenses, and increases in postage costs.

In addition, the Governor's budget includes $7.1 million in an open general fund appropriation for the Campaign Financing public subsidy program authorized in MS 10A.

Contingent Accounts

The Governor recommends increasing the General Fund portion of the contingent accounts by $10 million, to a total of $10.2 million. This represents a 5000 percent increase in the account.

The contingent accounts are appropriations made to provide supplemental funding in emergencies. The Governor may approve expenditures from the accounts only after consulting with the Legislative Advisory Commission (LAC). However, the Governor can release funds even if the LAC recommends against the expenditure.

In addition to the General Fund increase, the Governor recommends additional $800,000 from the State Government Special Revenue Fund, $100,000 from State Airports Fund, $400,000 from the Trunk Highway Fund, $250,000 from the Highway User Tax Distribution Fund, and $200,000 from the Workers Compensation Special Fund.

Department of Employee Relations (DOER)

The Governor recommends $22.1 million, an increase of $1.5 million over current law. This funding level includes $751,000 in base adjustments for salaries and benefits, and documented lease increases. The Governor also includes two new spending initiatives:

- $2 million one-time appropriation in FY 2001for back-pay settlement costs related to the Fair Labor Standard Act. This backpay is the result of a consent agreement between the federal Department of Labor (DOL) and DOER which requires state agencies to reimburse some employees for previously unpaid overtime dating back to January 1998.
- $715,000 to renew open appropriation language for the Worker's Compensation Reinsurance. The state as an employer is self-insured for workers compensation claims, and DOER is responsible for the payment of the annual premiums to the Workers Compensation Reinsurance Association. The department is requesting that the appropriation used to pay these premium expenses become a standing open appropriation as opposed to being a biennial open appropriation in session law.

The Governor is also recommending reallocating $843,000 within the department's base to implement a new Selection and Hiring Reform Project.

Department of Finance

The Governor recommends a total of $38.9 million for the biennium, an increase of $1.1 million from current law. The agency is not seeking any new spending initiatives. The Governor is recommending one base reduction:

- ($100,000) for the elimination of the Uniform Settlement Reporting process. This process was

established by the 1995 Legislature for the purpose of providing baseline information on collective bargaining agreements. The department states that there have been very few requests for this information, and the data does not seem to be used by decision-makers.

Board of Government Innovation and Cooperation

The Governor recommends $2.1 million, an increase of $14,000 over current law. This increase is due to recommended base adjustments for salaries and benefits, and small agency operational expenses.

Humanities Commission

The Governor recommends $1.86 million, an increase of $40,000 over current law. This increase is due to recommended base adjustments for salaries and benefits, and small agency operational expenses.

State Board of Investment

The Governor recommends $5 million for the biennium, an increase of $260,000 over current law. This recommendation includes $160,000 for salary and benefits base adjustments, and an additional $100,000 to fund the increased lease costs associated with the board's move to the new pension building.

Lawful Gambling Control Board

The Governor recommends $4.78 million for the biennium, an increase of $293,000 over current law. This recommendation includes $193,000 for salary and benefits, and rent adjustments. One new initiative is included:

- An additional $100,000 permanent base increase for a computer maintenance and infrastructure. In the previous two bienniums, the agency received one-time appropriations for information technology infrastructure, including $178,000 in FY 2000-01 through the Office of Technology's Small Agency Infrastructure project.

Minnesota Racing Commission

The Governor recommends a General Fund appropriation of $840,000, and increase of $36,000 over current law. In addition, the Governor is recommending that funding to improve the agency's information technology infrastructure be included in the Office of Technology's Small Agency Infrastructure initiative.

The Department of Military Affairs

The Governor recommends $27.2 million for the biennium, an increase of $5.2 million over current law. This funding level includes $649,000 for base adjustments for salaries and benefits, and rent increases. In addition, the agency has three new spending initiatives:

- $200,000 one-time appropriation for special assessments from local governments for improvements benefitting state-owned property.
- $206,000 for lease costs associated with the new Mankato Training and Community Center.
- $4.1 million to fully fund the tuition reimbursement program. Currently the department is authorized to reimburse national guard members for up to 75 percent of tuition at the University of Minnesota and other state colleges and universities. However, the base funding level of $4.7 million has only allowed the department to reimburse 50 percent of costs.

Political Contribution Refunds

The Governor recommends doubling the amount of the refund that an individual can receive under this program, from $50 to $100, beginning in FY 2003. The recommended change would increase the projected cost of the program to $14.4 million from a current law level of $9.79 million. The Political Contribution Program is funded through an open appropriation administered by the Department of Revenue.

Public Broadcasting

The Governor recommends maintaining base level funding for Public Radio and Public Television. Total base funding for all activities is $6.66 million for the biennium.

Public Radio: The total funding level of $1.63 million is split evenly between the Association of Minnesota Public Educational Radio Stations (AMPERS) and Minnesota Public Radio (MPR). Specific funding levels are:

- $640,000 in AMPERS community service grants
- $174,000 in AMPERS equipment grants, and
- $814,000 in MPR equipment grants.

Public Television: $1.2 million for equipment grants, and $2.9 million for matching grants, for a total of $4.1 million.

Legislative Television: appropriations would remain at base spending levels of $882,000.

Public-Local Employees Retirement

Four public retirement programs under the State Government Finance committee's jurisdiction receive either direct or open General Fund appropriations. The funds include:

- MN State Retirement System - $13.6 million for benefits paid to former legislators and elected officials.
- Local Police-Fire Amortization Aid - $12.7 million for regular and supplemental amortization aid, and the firefighter supplemental benefit tax reimbursement.
- First Class City Teachers State Aid - a $37.5 million open appropriation to reduce the unfunded liabilities of the Minneapolis, St. Paul and Duluth teachers' retirement funds.
- The Minneapolis Employees Retirement Fund (MERF) - $6.5 million to reduce the plan's unfunded liability. The 2000 Legislature reduced the FY 2002-03 base for MERF by $3.8 million because actuarial figures showed that the state's base appropriation exceeded the amount needed to amortize the fund's deficiencies.

Department of Revenue

The Governor recommends $185.8 million for the biennium, an increase of $13.8 million over current spending. This funding level includes $5.5 million for base adjustments for salaries and benefits, and a reduction of $293,000 for rent. New spending items total $9.3 million:

- $5.4 million in additional funding to complete the individual income tax re-engineering project. This project received $12.6 million in the 1999/2000 legislative sessions. The additional funds would add a scanning and imaging component, allowing more taxpayer data to be captured

electronically. The department states this will speed up processing times and improve compliance activities.

- $1.2 million for newly identified re-engineering operational costs associated with the need to retain and scan copies of federal income tax returns. The original re-engineering project design included plans to eliminate the requirement for Minnesota taxpayers to attach copies of their federal returns. Instead, the department would obtain federal tax return information from the IRS. However, both the Legislature and some staff at the Department of Finance raised concerns about the reliability of the IRS data samples, and a interim study group concluded that the paper federal returns must be retained.
- $570,000 base increase for new operating costs associated with changes made in the tax laws in previous sessions. One-third of this amount would cover additional printing and mailing costs for expanded tax forms and booklets.
- $2.2 million for the Non-Filer initiative, to fund 17.5 additional FTE to identify and collect taxes from both individuals and corporations that owe the state taxes but do not file returns. The department estimates that focusing additional staff resources on this activity would bring in new General Fund revenues of $20 million in FY 2002-03, and $37 million in FY 2004-05.

The Governor also recommends changing funding for the non-tax revenue recapture program from a direct general fund appropriation to a "performance-based" special revenue fee system. The department's base would be reduced by $826,000 in exchange for allowing it to retain $2.55 of each of the current $10 revenue recapture offset fees now fully returned to the General Fund.

Office of Strategic and Long Range Planning (Minnesota Planning)

The Governor recommends $10.2 million for the Office of Strategic and Long Range Planning, an increase of $701,000 over current law. This funding level includes $456,000 for base adjustments for salaries and benefits, and rent increases. Three new spending initiatives are included:

- $170,000 to complete the General Environmental Impact Statement (GEIS) on animal agriculture (feedlots). This project has received $2.8 million in appropriations to date.
- $230,000 base increase for local planning assistance grants. The funds would support two positions to respond to requests from local governments for information and technical assistance with planning efforts. These two positions have been (partially) funded in the past biennium with funding provided for the Community Based Planning Act, which sunsets on June 30, 2001.
- $180,000 for a base increase to create an information technology unit, staffed by part-time IT staff. The agency's intent is to share Chief Information Officer (CIO) and web staff with another state agency.

The Governor is also proposing to partially offset this new spending with a base reduction of $335,000, achieved through the elimination of positions in the document production and administrative activities.

Tort Claims

The Governor recommends $550,000 from the General Fund.

The Department of Veterans Affairs

The Governor recommends $8.87 million for the biennium, an **decrease** of $27,000 million from current

law. The Governor has recommended reducing funding to three veterans grants programs by a total of $218,000:

- ($26,000) for the Bronze Star Marker program
- ($100,000) to the County Veterans Service Office grant program, and
- ($92,000) to the Vinland National Center contract for rehabilitation services.

Veterans Service Organizations

The Governor recommends a total of $148,000 for three veterans service organizations. This funding level is the same as current law.

- **Disabled American Veterans (DAV)** -$26,000 for the biennium.
- **Military Order of the Purple Heart** - $40,000 for the biennium.
- **Veterans of Foreign Wars (VFW) Claims and Service Office** - $82,000 for the biennium.

For more information on State Government Finance issues, contact Helen Roberts, 651-296-4117 or Helen.Roberts@house.leg.state.mn.us .

Transportation Finance

Governor Ventura's proposed budget for the Department of Transportation is very similar to the budget he put forward two years ago. The Governor includes increases for rural and metro transit, several small agency initiatives, and increases road construction funding to reflect the growth in revenue collections from motor fuel tax and motor vehicle registration taxes. Also similar to two years ago, the Governor proposes a large rail transit project and cuts in motor vehicle registration taxes or "tab fees". The major difference in the budget put forth this year is several base reduction items by proposed by agencies as a tradeoff for increases in other areas.

Transportation Finance
Governor's FY 02-03 General Fund Budget Recommendations
(all dollars in thousands)

	November Forecast FY 00-01	Current Law FY 02-03	Governor's Recs FY 02-03	% Change Governor FY 02-03 vs. November FY 00-01	% Change Gov. vs. Current Law FY 02-03
MN/DOT	366,622	31,960	36,140	-90.1%	13.1%
Metropolitan Council	113,602	106,202	136,202	19.9%	28.2%
Public Safety	23,514	22,883	35,617	51.5%	55.6%
MN Safety Council	267	0	0	-100.0%	0.0%
Total	**504,005**	**161,045**	**207,959**	**-58.7%**	**-100.0%**

Minnesota Department of Transportation

- $15.3 million in base reductions including $4.8 million annually in payments for sales tax from the trunk highway fund. Other reductions include $4 million annually in general workforce reductions and $3 million annually in consultant services.

- $500,000 annually from the state airports fund to increase grants to local governments for repair and maintenance of municipal airports.

- $600,000 annually from the airports fund to implement Global Positioning System (GPS) navigation aids at airports throughout the state.

- $3.1 million for the biennium to preserve service levels of transit systems in greater Minnesota.

- $500,000 annually for a new office of passenger rail in MN/DOT's transit program.

- $47.8 million annually from the trunk highway fund for highway construction and program delivery.

- $100,000 annually to develop design-build methods of construction.

- $1 million for the biennium for scientific equipment.

- $2.75 million per year from the trunk highway fund to increase MN/DOT's budget to maintain buildings and other facilities.

- $3.25 million per year from the trunk highway fund to purchase and maintain vehicles and equipment.

- $3 million annually for additional pavement striping costs. The department is responding to surveys that show drivers demand bright easy to see pavement markings and hopes to provide better pavement marking and use costlier, more durable epoxy paints.

- $8.6 million annually from the trunk highway from for information technology programs. $6.6 million per year for Information Technology Infrastructure and $2 million per year for Information Technology Development.

- $7.7 million from the trunk highway fund for MN/DOT building projects that include various truck stations, salt shed and rest areas.

Implications

The largest implication on transportation is included in the Governor's capital budget requests. Governor Ventura recommend $115 million from general obligation bond proceeds to be spent on commuter rail in the Northstar corridor. Commuter rail uses existing freight rail track to transport commuters. Dollars would be used for final design, stations and track upgrades needed to make the system work. The 80 mile line would run from St. Cloud to downtown Minneapolis and link up with the Hiawatha light rail near the Target Center. The project anticipates 50 percent of the total $283 million project to come from the federal government and the remaining 10 percent from local, non-state sources. The recommendation of commuter rail is to coincide with the Governor's theme of giving people transportation choices.

There is no provision, however, for increased levels of highway financing in Governor Ventura's plan as was proposed by Ventura in 2000. During the 2000 session the Governor had then called for a dedication of motor vehicle sales taxes to transportation purposes and infuse funds to meet growing needs. The Legislature did not agree with the Governor's plan one year ago and used the dollars to fund other priorities, but did include $360 million of one-time cash from the general fund.

In the one-third budget deal agreement, the governor chose to reduce vehicle registration taxes and "backfill" the loss to the highway funds with a dedication of 32 percent of motor vehicle sales tax leaving a smaller pot of dollars that could be dedicated to transportation projects in the future. The Governor has introduced two proposals that could shrink the availability of motor vehicle sales taxes in the future. The Governor proposes both a reduction in the sales tax from 6.5 percent to 6 percent, and further cuts in vehicle registration taxes backfilled with an even greater percentage of motor vehicle sales tax revenues.

The Department of Transportation maintains that highway construction costs have escalated at a rate of about 10 percent per year for the last several years. The Governor recommends a construction increase of about 9 percent from the previous base level. The increase in construction dollars is from un-appropriated dollars in the fund balance. These are highway trust fund dollars that represent growth in

revenues over collections from the previous biennium. One year after the Legislature infused $277 million in cash from the general fund in the 2000 session for state road construction, the road construction budget reverts back to the pattern of slipping against inflation as demands on the highway system continue to increase.

Metropolitan Council

The Governor recommends a $15 million annual increase for Metropolitan Council transit services. The increase would maintain current service levels, and extend some transit services outside the metro taxing district. Of the increase, $2.1 million per year would go to increase the budget for Metro Mobility transit services for the disabled. The Governor also provide $10 million in general obligation bond proceeds in his capital investment recommendations for Metropolitan Council bus garage facilities.

Implications

The major implications for transit in the Governors proposal would be the recommendation of a fare increase of twenty-five cents per ride across the board. The fare increase is neessary to generate the revenues needed in the Metropolitan Council's plan for increased service. The Governor also recommends increased levy authority of $11.5 million inside the seven county area but outside of the current transit taxing district in order to provide extended service to communities outside of the current taxing district.

Public Safety

The Governor's recommendations for the transportation related components of public safety contain radical departures from previous years. The Governor recommends that appropriations for license plate production, license and ID card production and driver licensing be made open and standing appropriations. The fees collected by these functions had produced revenues intended to equal the cost of the services provided. The dollars were deposited into the trunk highway fund and highway user tax distribution fund, and were then appropriated by the legislature. The Governor recommends depositing the revenues into special revenue accounts and giving the department direct access to the funds rather than seeking legislative authority to spend the dollars. The department hopes to be more responsive to customer demands with the open appropriation.

The Governor also recommends a one-time permanent utility trailer registration and an increased fee of $55 per trailer. This would create a short term gain to the highway user fund but a long run loss realized beginning in about eighteen years. The goal is to change the fee from $10 every two years to the one-time fee of $55 and cut down on the staff time to deal with the registrations and benefit the owners of the trailers with the one-time fee.

The Governor recommends an appropriation of $11.725 million from the general fund to the highway user tax distribution fund for reimbursement of motor vehicle registration tax refunds. The refunds were made by Public Safety for June 2000 registrations that were not anticipated in the Governors plan for "tab fee" cuts made in the 2000 legislative session. The Governor had recommended that the cuts in vehicle registrations begin in July of 2000, but due to some ambiguous language, the refunds were extended to those renewing registrations in June. The un-anticipated refunds totaled $11.725 million and the appropriation makes the highway user fund whole with respect to this particular oversight.

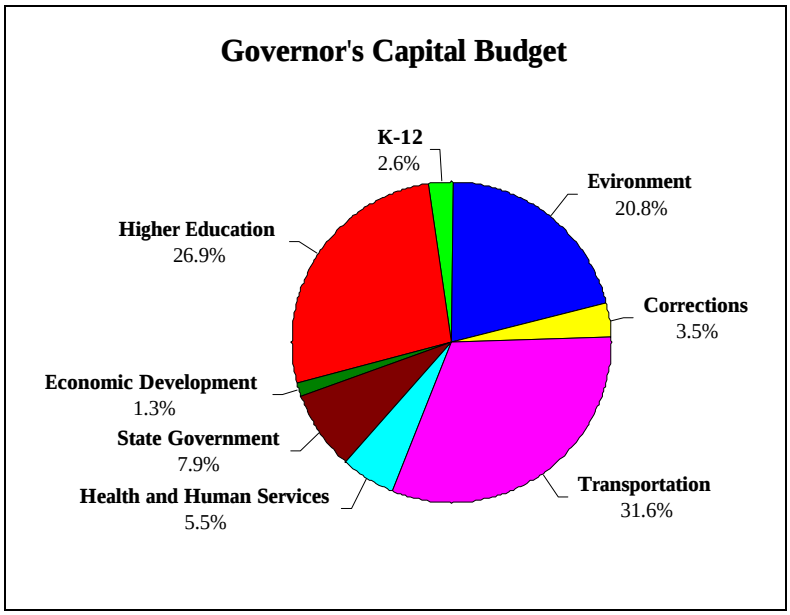
Governor Ventura also provides an additional $4.3 million for the biennium for the State Patrol to pay the costs of running trooper training academies and adds salary money to bring on sixty-five troopers that the agency states their budget can no longer provide for. The request would have a biennial cost of $10.2 million in future biennia. The department argues that increases in fuel cost and health care have eroded its budget and require the additional dollars to fund troopers the Patrol feels are necessary for adequate enforcement statewide.

For further information on Transportation Finance issues contact John Walz (651) 296-8236 or John.Walz@house.leg.state.mn.us

Governor's Capital Budget for 2001

In order to advance his "one session per biennium" agenda, Governor Ventura has introduced a complete capital budget package one year after last year's $607 million dollar capital investment bill. In past years, the odd-year session has been used to pass smaller capital budgets and deal with projects of an urgent nature. This year, however, the Governor is recommending $576 million in new capital budget spending. The Governor also issued an ultimatum for the legislature to pass a full capital budget package and adjourn *sine die*, or he threatened he would veto any other capital budget bill passed during the 2001 session.

The size and scope of the Governor's budget comes as a surprise to many. The process used to assemble the capital budget also did not follow the same procedures Governor Ventura used last year to compile his recommendations. Rather than require submissions of long detailed budgets from state agencies and higher education institutions, the Governor focused on the deferred maintenance needs of the state and relied on information on needs from the 2000 capital budget documents. He also added a few new construction projects that were, for the most part, unfunded projects from last years requests.



Minnesota currently has slightly over $2.5 billion in outstanding general obligation bonds. Under the "3 percent guideline", our state has the capacity to issue an additional $1.2 billion in bonds each biennium and still stay within the voluntary guideline. The guideline states that the required amount of debt service needed in a given biennium should not exceed 3 percent of non-dedicated general fund revenues. The rule was adopted several years ago to help restore the state's AAA bond rating and lower borrowing costs. During the rapid growth of state revenues in the recent economic expansion, the rule has become less of a limiting factor on capital budget size. Our current required debt service amounts to 2.29 percent of current non-dedicated general fund revenues, and the Governor's proposed budget would bring debt service to 2.42 percent.

Of the $576 million in new spending recommended by the Governor, over $365 million was dedicated to asset preservation and repair of existing facilities. Of the $210 million set aside for new projects, a full $115 million was recommended for one project, commuter rail in the Northstar corridor. Listed below are the highlights of the budget recommendations by issue area.

Higher Education

In keeping with his theme of asset preservation the Governor dedicates $126.5 million of the $154 million set aside for higher education for asset preservation and renewal.

University of Minnesota
The University of Minnesota received $68.3 million in the proposal, with $50 million dedicated to HEAPR or Higher Education Asset Preservation and Renewal. In addition, $2 million was set aside for design of a new science laboratory building to meet the growing science needs at the University campus in Duluth. Another $16.3 million was provided to finish the second phase of plant growth facilities at the St. Paul campus. Phase one received $5.9 million in last year's capital bill. Both new initiatives require one third of the debt service to be paid by the institution.

MNSCU
For asset preservation needs, MNSCU was granted $75 million for HEAPR to devote to their backlog of deferred maintenance. Phase two of the Normandale science facility was funded at $9.9 million in addition to the $11.4 million they received in the 2000 capital bill. Lastly, $1.5 million was set aside for lab renovations at campuses statewide. The lab renovations and Normandale facility carry a one third debt service requirement.

K-12 Education
After receiving $83 million to fund several projects in the 2000 capital investment bill, the Governor set aside $14.7 million for K-12 needs. The 2000 bill funded several maximum effort capital loans, magnet schools, renovations and grant programs. This year, $1.7 million is earmarked for completion of the East Metro Magnet School in Woodbury. The Perpich Center for the Arts was granted $1 million for asset preservation. The Minnesota State Academies were granted $1 million for asset preservation and $5 million to complete the renovation of Noyes Hall. The Governor also funded $5 million to the Department of Commerce for energy investment loans to school district that wish to undertake projects that improve school energy efficiency.

Health and Human Services
The Department of Human Services was budgeted to receive $10 million for asset preservation needs. In addition, the Governor recommends $8.9 million to upgrade Shantz Hall at the Saint Peter Regional Treatment Center.

The Veterans Home Board will continue to preserve the facilities in Hastings with an infusion of $7.5 million. The dollars will be used to continue work on underground steam and utility tunnels , for upgraded windows and heating and cooling replacements. Another $4.4 million was budgeted for upgrades at other veterans homes, and $600,000 was set aside for a storage building at Silver Bay.

Environment
The Governor put an emphasis on environmental programs, dedicating over one sixth of his capital budget, $119 million, to environmental needs. The governor set aside $4 million to continue road and pathway enhancements at the Minnesota Zoo, and $20 million to the Department of Agriculture for Rural Finance Authority (RFA) loans. The RFA program makes low interest loans to farmers for refinancing debt and to improve farm management practices.

The Public Facilities Authority of the Department of Trade and Economic Development was granted $8 million for wastewater and drinking water treatment through the Water Pollution Control Revolving Loan Fund. These dollars match federal dollars for loans to improve drinking water and wastewater

treatment throughout Minnesota. Each state dollar matches five dollars from the EPA. The Pollution Control Agency's Clean Water Partnership program received $2 million to improve water quality.

The Department of Natural Resource will get $35 million, all for asset preservation and renovations, under the Governor's plan. Of this amount $8 million is dedicated for field office improvements throughout the state. An additional $5 million is set aside for Metropolitan Regional Parks.

The Governor recommends $50.7 million to the Board of Water and Soil Resources for the Conservation Reserve Enhancement Program or CREP. The state dollars are used to match up to $163 million federal dollars and purchase permanent easements along the Minnesota River. The easements will prevent farm runoff from entering the river and improve the river's water quality. Of the total, $43 million of GO bonds will be used to purchase easements, and the Governor recommends a statutory change to allow $7.76 million to be used from the Solid Waste Fund to pay for implementation costs.

State Government

For asset preservation the Governor provides $2.5 million to the Department of Military Affairs and $2.25 million for the Minnesota Historical Society. The Department of Administration was granted $42.5 million, almost all for existing facilities. The Governor included $10 million for CAPRA and an additional $10 million for asset preservation. For completion of the utility work on the capitol complex, $2.5 million was included. In addition, Governor Ventura recommends $4 million for improvements at the Governor's Mansion and $3 million for renovations at the state capitol.

For future building needs, $10 million was set aside for property acquisition and design of facilities. To move agency personnel to new facilities, $1.9 million was included for agency relocations. The Governor also recommends $1 million for the demolition of the current BCA building when the new facility is completed.

Judiciary Finance

The Governor recommends $20 million for asset preservation for correctional facilities statewide.

Economic Development

Governor Ventura recommends $3 million for redevelopment grants. The grants are used to cleanup industrial sites, demolish obsolete buildings, and make site improvements to attract development in communities throughout the state. The Governor also provides $2.5 million to the Minnesota Housing Finance Agency for transitional housing loans. The loans are used to purchase or construct publicly owned transitional housing for persons in need for up to twenty four months.

Transportation

The Governor sets aside over a quarter of the funding in his bill for transportation projects. The Metropolitan Council would receive $10 million for bus garage facilities in addition to the $10 million in the 2000 capital investment bill. The dollars would be used to build garages to house buses as the Met Council increases its fleet in future years.

The largest project in the Governor's recommendation comes with a $115 million price tag. The dollars would fund a commuter rail project in the Northstar corridor. Commuter rail uses existing freight rail track

to transport commuters. Dollars would be used for final design, stations and track upgrades needed to make the system work. The 80 mile line would run from St. Cloud to downtown Minneapolis and link up with the Hiawatha light rail near the Target Center. The project anticipates 50 percent of the total $283 million project to come from the federal government and the remaining 10 percent from local, non-state sources.

The Governor also recommends three other MN/DOT request totaling $57 million. He proposes $30 million in general obligation bonds for local bridge matching funds. For MN/DOT building needs , he earmarks $14.6 million from the trunk highway fund for a consolidated operations support facility, and a new Mankato headquarters building with $12.6 million from the trunk highway fund.

For further information on Capital Budget issues contact John Walz (651) 296-8236 or John.Walz@house.leg.state.mn.us

A spreadsheet of the Governor's capital budget is available at www.house.leg.state.mn.us/fiscal/fahome.htm

Governor's Tax Proposals – The Big Plan

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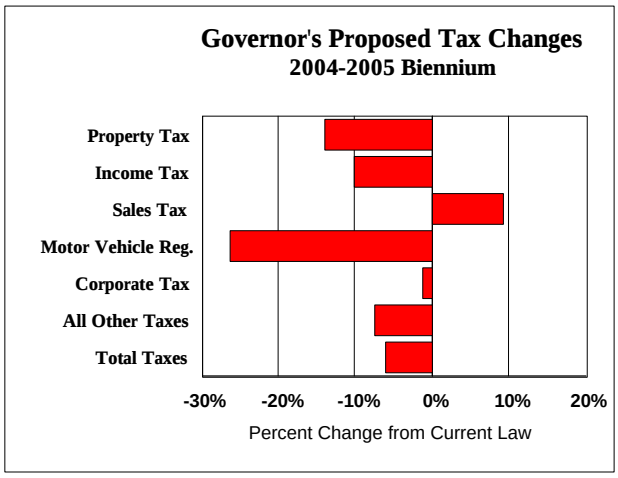
Governor's Tax Proposals – The Big Plan

Overview: Impact on the structure of Minnesota's overall tax system. In addition to a sales tax rebate to return the FY 2001 end-of-year surplus to taxpayers, the Governor proposes major permanent changes in Minnesota's combined state and local tax system. As summarized in Figure 6, the Governor's tax recommendations would reduce the General Fund by $915 million in FY 2001, $1.7 billion in FY 2002-03, and $2.6 billion in FY 2004-05. Because some of those changes would be phased in over several years, it is most revealing to examine the magnitude of the tax changes after they would be fully effective.

Figure 1



In the 2004-05 biennium, the Governor's proposals would:

- Reduce property taxes by 13.9 percent.
- Reduce individual income tax revenues by 10 percent.
- Increase sales tax revenues by 9.4 percent.
- Reduce motor vehicle registration tax revenues by 26.2 percent.
- Reduce corporate tax revenues by 1.2 percent.
- Reduce all other tax revenues by 5.4 percent.

Sales tax revenues would increase even though the tax rate would fall from 6.5 percent to 6 percent, because more goods and services would become taxable. By increasing sales tax revenues while reducing both income and property taxes, the Governor's proposal would increase the relative importance of the sales tax, moving it past property taxes and making it the second largest source of tax revenue (after the income tax).

As shown on Figure 2, prior to FY 1997 the property tax was the primary source of state and local tax revenue. It was surpassed by the income tax in 1997, but would remain in second place under current law. Under the Governor's proposal, the property tax would fall to third place starting in FY 2003, with the sales tax taking over second place and the income tax retaining the number one rank it has had since FY 1997.

Figure 2
Ranking of Tax Shares:
Current Law and Governor's Proposal
(Sales tax includes motor vehicle sales tax)

Rank by Total Tax Revenue	FY 1991 to FY 1996	FY 1997 to FY 2002	FY 2003 to FY 2005	
			Current Law	Governor's Proposal
First	*Property Tax*	Income Tax	Income Tax	Income Tax
Second	Income Tax	*Property Tax*	*Property Tax*	**Sales Tax**
Third	**Sales Tax**	**Sales Tax**	**Sales Tax**	*Property Tax*

Figures 3 and 4 show how the tax mix would differ in FY 2005 under the Governor's budget, compared to current law. The sales tax share would rise by 4 percentage points (from 24.6 percent to 28.6 percent of the total). The shares of the other taxes would fall. The property tax share would fall by 2.1 percentage points, the income tax share would fall by 1.5 percentage points, and the share for motor vehicle registration taxes would fall by 0.6 percentage points.

Figure 3

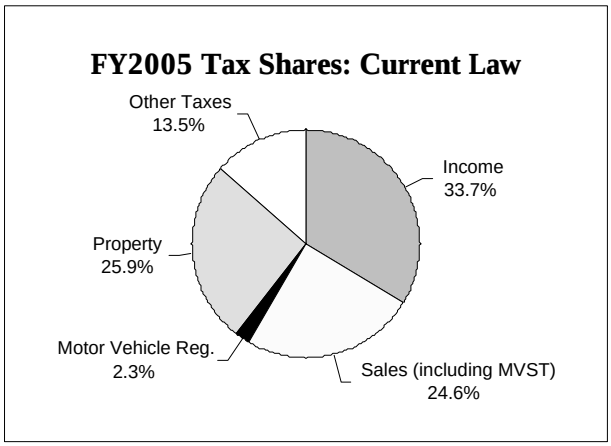


Figure 4

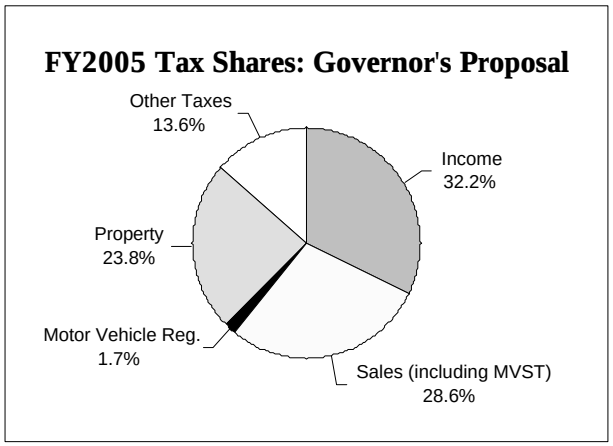
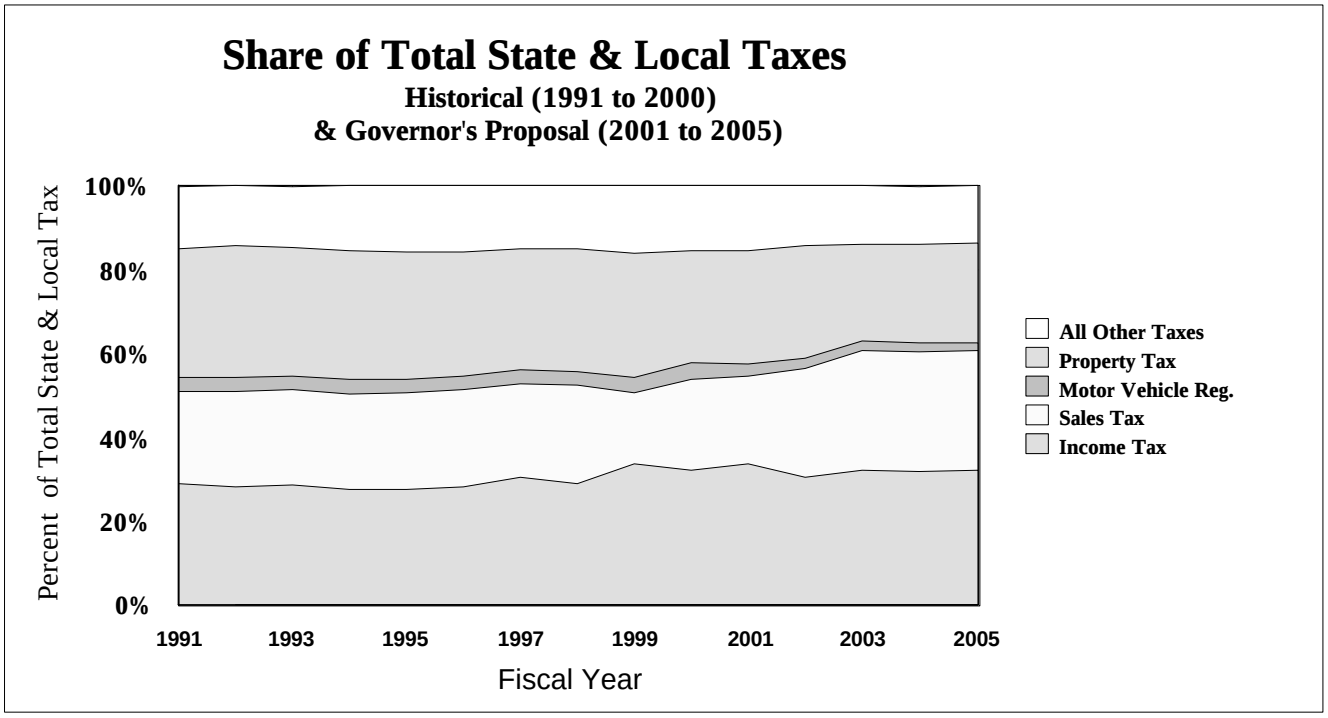


Figure 5 shows the history of tax shares from 1991 to 2000, along with the tax shares under the Governor's proposal from 2001 to 2005. If there had been no sales tax rebates, the sales tax share would have held constant at 23 percent from 1991 to 2001. The shrunken sales tax share 1999, 2000, and 2001 is just the result of sales tax rebates. Those rebates reduced the share to 17 percent in 1999 and 22 percent in 2000, and the proposed 2001 rebate would reduce it to 21 percent.

Figure 5



The shift in the tax burden away from income and property taxes and toward consumption taxes is a major component of the Governor's tax proposals. More detailed discussion of the Governor's proposals for tax reform and tax relief is provided below.

Summary of Impact on the General Fund

Figure 6

Income, Corporate, Sales, Property, Motor Vehicle, and Other Taxes
Impact on General Fund
(dollars in thousands)

Tax Type	**FY 2001***	FY 2002	FY 2003	**FY 2002-03**	FY 2004	FY 2005	**FY 2004-05**
Sales tax rebate	**($911,014)**						
Income tax	**(200)**	($628,200)	($495,900)	**($1,124,100)**	($717,450)	($806,660)	**($1,524,110)**
Corporate tax	**(3,800)**	(27,730)	(12,600)	**(40,330)**	(12,800)	(10,800)	**(23,600)**
Sales tax		35,800	445,900	**481,700**	478,300	478,300	**956,600**
Propety tax aids and credits	**0**	(480)	(886,832)	**(886,952)**	(755,411)	(770,623)	**(1,526,034)**
Motor vehicle		(41,000)	(85,000)	**(126,000)**	(120,000)	(156,000)	**(176,000)**
Excise taxes					(141,300)	(141,300)	**(282,600)**
Gambling taxes		(5,505)	(6,010)	**(11,015)**	(6,010)	(6,010)	**(12,020)**
Miscellaneous taxes and exp.		(9,477)	(9,025)	**(18,502)**	(9,000)	(8,995)	**(17,995)**
Total Change in Revenue:	**($915,014)**	($676,592)	($1,049,107)	**($1,706,697)**	($1,283,671)	($1,422,088)	**($2,605,759)**
Rebate admin. costs	**($500)**	($1,232)		**($1,732)**			
Other admin. costs		(6,840)	(4,945)	**(11,785)**			
Total admin.	**($500)**	($8,072)	($4,945)	$(13,517)			
Total for General Fund	**($915,514)**	($684,664)	($1,054,052)	**($1,720,214)**	($1,283,671)	($1,422,088)	**($2,605,759)**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state.
*Income and corporate tax changes in FY2001 are due to Federal update provisions.

2001 Sales Tax Rebate

The Governor's budget proposals include another one-time sales tax rebate of $925.4 million to be paid in the summer of 2001. The Department of Revenue and State Treasurer would receive appropriations totaling $2.01 million to administer the sales tax rebate. As was true with previous rebates, these sales tax rebates would be subject to "revenue recapture." It is assumed that 1.5 percent of the total dollars in sales tax rebate will be retained by the Department of Revenue to offset tax debts or other debts affecting the General Fund. As shown in Figure 7, the net cost of the sales tax rebate provisions is $913 million.

Figure 7

FY 2001 Sales Tax Rebate

	FY2001	FY2002
Sales Tax Rebate	($925,414)	
Sales Tax Rebate – administration	($500)	($1,232)
Sales tax rebate recapture (@ 1.5%)	+ $13,900	
Sales Tax Rebate	**($911,514)**	**($1,232)**

To be eligible for the rebate, a taxpayer must meet one of the following criteria:

- Paid income tax (before credits) in 1999 and was not claimed as a dependent on another tax return;
- Received social security or railroad retirement benefits – and was at least 18 years old – in 1999;
- Paid no income tax in 1999, but filed an income tax return to receive (i) a refundable income tax credit or (ii) a refund of taxes paid through withholding or estimated tax, and was not claimed as a dependent on another taxpayers' return;
- Received a property tax refund (homeowner or renter)for property taxes paid in 2000 or rent paid in 1999, and was not claimed as a dependent on another taxpayer's return;
- Claimed as a dependent on another return in 1999, but paid income tax (before credits) in 1999 and had some wage income; or
- Non-resident who paid no Minnesota income tax in 1998, but paid at least $10 in Minnesota sales tax on non-business purchases and has receipts for those purchases.

Only the last group – non-residents with Minnesota sales tax receipts – would need to apply for the rebate. All others would receive their rebate automatically. To be eligible, 1999 tax returns would have to be filed by November 30, 2001.

The proposed rebate amount would equal 42.85 percent of what the Department of Revenue estimates the household paid in sales tax in 1999. As in past years, rebate amounts would be larger for those with higher incomes, but would be capped at a maximum of $1,750 for singles and $3,500 for others. There would be no adjustment for family size, but married taxpayers and heads of household would receive larger rebates than single persons with the same income. Income would be defined as federal taxable income plus "Minnesota additions" (primarily state income taxes claimed as itemized deductions on the federal tax return). The rebate schedule for the proposed $925 million rebate is shown in Figure 8.

Figure 8.

Sales Tax Rebate for Minnesota Residents (assuming $925 million rebate)

(Note: Dependents who paid income tax will receive 35 percent of amount shown)

Income	Single	Others	Income	Single	Others
Less than $2,500	$ 138	$ 242	$ 70,000 - $ 79,999	$ 627	$ 755
$ 2,500 - $ 4,999	168	312	$ 80,000 - $ 89,999	627	810
$ 5,000 - $ 9,999	197	333	$ 90,000 - $ 99,999	627	894
$ 10,000 - $ 14,999	265	365	$100,000 - $119,999	755	968
$ 15,000 - $ 19,999	303	396	$120,000 - $139,999	755	1,061
$ 20,000 - $ 24,999	329	431	$140,000 - $159,999	912	1,147
$ 25,000 - $ 29,999	343	449	$160,000 - $179,999	912	1,228
$ 30,000 - $ 34,999	374	487	$180,000 - $199,999	912	1,304
$ 35,000 - $ 39,999	374	533	$200,000 - $399,999	1,237	1,669
$ 40,000 - $ 44,999	419	571	$400,000 - $599,999	1,627	2,195
$ 45,000 - $ 49,999	419	601	$600,000 - $799,999	1,750	2,634
$ 50,000 - $ 59,999	494	641	$800,000 - $999,999	1,750	3,020
$ 60,000 - $ 69,999	494	686	Over $1,000,000	1,750	3,500

Note: "Income" is 1999 federal taxable income plus Minnesota additions to income – line 4 on the Minnesota income tax return. (This is not the same as total income; nontaxable income is excluded, and personal exemptions, the standard deduction, and any itemized deductions other than state income tax have all been subtracted.) "Others" include married couples filing joint returns, plus those filing as head of household or surviving spouse. Dependents who paid income tax in 1999 will receive 35 percent of what is shown on the table. Part-year residents and non-residents who filed Minnesota income tax in 1999 will receive a fraction of these totals based on the portion of their income apportioned to Minnesota. These amounts may be adjusted by the Department of Revenue as needed so that total rebates sum to the target of $925 million.

The total rebate amount ($925 million) equals the surplus forecast for the end of FY2001 in the November 2000 forecast. Although the checks may not be mailed until after June 1, the rebate appropriation is for FY2001. The proposed rebate amount will presumably be changed if the February forecast shows a different surplus for FY2001.

Comparison to the 1999 and 2000 Sales Tax Rebates

The Governor's proposed 2001 rebate is approximately 45 percent larger than the 2000 rebate ($925 million compared to $636 million in 2000), but about 30 percent smaller than the 1999 rebate ($1,300 million). The population eligible for the proposed rebate is roughly the same as for the 2000 rebate. The groups newly eligible in 2000 (social security recipients, dependents who paid income tax, and those receiving refundable tax credits) would continue to be eligible under the Governor's proposal. So those who receive a rebate in 2001 would receive a rebate about 45 percent larger than their 1999 rebate, if their income is unchanged. Figure 9 compares the three sales tax rebates.

Figure 9.

Comparing the 2000 Sales Tax Rebate to the 1999 Sales Tax Rebate			
	2001 Rebate	2000 Rebate	1999 Rebate
Total dollars	$925 million	$636 million	$1,300 million
Total checks	2,495,000 (est)	2,392,000	1,956,000
Average check to core population			
Single filers	$270 (est)	$187	$412
Joint or head of household filers	$544 (est)	$377	$840

Two important differences in the proposed 2001 rebate:

- **Eligibility is not based on receiving a property tax rebate**: In the previous two sales tax rebates, those receiving a property tax rebate (claimed on the 1997 or 1998 income tax returns) were automatically eligible. There was no property tax rebate in 1999, however, and some who qualified for past rebates only because they received such a rebate will not qualify for the Governor's proposed rebate. To address this problem, the Governor proposes to expand the eligible population to include all who received a Property Tax Refund (PTR) in 1999. The PTR is the property tax "circuit breaker," which provides property tax relief to those whose property taxes are high compared to their income. Nevertheless, despite this expansion, the Department of Revenue estimates that about 65,000 households who received rebates in 1999 and 2000 would not qualify this year.
- **Reduced rebate for those qualifying only as social security recipients:** In the 2000 rebate, these social security recipients each received a rebate equal to the minimum rebate for a single person. As a result, some married couples received twice the minimum rebate for singles, which exceeded the minimum rebate for a married couple. This year, the Governor proposes to rebate an amount equal to half the minimum married rebate ($121) rather than the minimum single rebate ($138).

As in past years, taxpayers will pay no federal income tax on their sales tax rebate.

Individual Income Taxes

Compared to current law, the Governor's proposals would reduce individual income tax revenues by 8.5 percent in the 2002-03 biennium and by 10 percent in the 2004-05 biennium. Figure 10 summarizes the Governor's proposed changes to the state's individual income tax.

Figure 10.

Permanent Income Tax Reductions
($ in Thousands)

Tax Provision	FY 2002	FY 2003	**FY 2002-03**	FY 2004	FY 2005	**FY 2004-05**
Reduce tax rates	($601,000)	($483,000)	**($1,084,000)**	($628,000)	($717,000)	**($1,345,000)**
Increase working family credit	(26,500)	(26,600)	**(53,100)**	(101,700)	(103,300)	**(205,000)**
Repeal alternative minimum tax	0	(29,600)	**(29,600)**	(31,800)	(33,400)	**(65,200)**
Repeal Child/Dependent Care Credit	0	+12,000	**+12,000**	+12,000	+12,000	**+24,000**
Reduce K-12 Education Credit	0	+15,100	**+15,100**	+15,800	+16,600	**+32,400**
Restrict K-12 Education Subtraction	0	+$2,000	**+$2,000**	+$2,100	+$2,200	**+4,300**
Federal Update	(700)	(1,200)	**($1,900)**	(1,600)	(1,800)	**(3,400)**
Penalty Reform	0	(5,100)	**(5,100)**	(5,400)	(5,800)	**(11,200)**
Interaction effect: Property tax cuts	0	+18,200	**+18,200**	+18,800	+19,200	**+38,000**
Interaction effect: Motor vehicle registration tax cuts	0	+2,300	**+2,300**	+2,350	+4,640	**+7,120**
Total: Individual Income Taxes	($628,200)	($495,900)	**($1,124,100)**	($717,450)	($806,660)	**($1,524,110)**

Note: Negative changes represent a cost to the state and positive numbers represent a gain.
*Federal update would also have a ($200) revenue impact in FY 2001.

Reduce Income Tax Rates – The Governor proposes an equal reduction in each of the three income tax rates – 0.4 percentage points in tax years 2001 and 2002, followed by an additional 0.1 percentage point reduction in both 2003 and 2004. Figure 11 shows the resulting tax brackets in each of the four years. In 2001, of all Minnesota resident tax filers who have tax liability (before tax credits), 42 percent would pay 4.95% tax on their last dollar of income, 51 percent would pay 6.65% tax on their last dollar of income, and 7 percent would pay 7.45% tax on their last dollar of income.

Figure 11.

Tax Rates Before and After Governor's Proposed Changes, by Filing Status						
Ranges of Minnesota Taxable Income*			**Tax Rates**			
			Current Law (all years)	**Governor's Proposal**		
Joint Return	**Single Filer**	**Head of Household**		**2001 & 2002**	**2003**	**2004**
$1 - $26,480	$1 - $18,120	$1 - $22,300	5.35%	4.95%	4.85%	4.75%
$26,481 - $105,200	$18,121 - $59,500	$22,301 - $89,610	7.05%	6.65%	6.55%	6.45%
$105,201 and over	$59,501 and over	$89,611 and over	7.85%	7.45%	7.35%	7.25%

*Income ranges are for 2001 tax year. The ranges are indexed for inflation in later years. Taxable income is income after subtracting personal exemptions and either the standard deduction or itemized deductions. The alternative minimum tax rate would also be reduced by 0.4 percentage points in 2001 (to 6.0%).

Repeal the alternative minimum tax – The Governor proposes to repeal the alternative minimum tax, effective for the 2002 tax year. This tax is currently paid by taxpayers who have a substantial amount of income that would otherwise not be subject to tax. This "tax preference" income includes tax-exempt interest, itemized deductions (home mortgage interest and charitable contributions), and tax-preferred forms of business income. The alternative minimum tax is designed to guarantee that relatively high-income taxpayers whose income is largely exempt under the regular income tax will pay some tax, though at a lower rate, on that income.

The alternative minimum tax is a very complex tax, and compliance rates are quite low. Its repeal is proposed as a major step toward tax simplification.

Figure 12 provides some information on the 10,000 filers who paid the alternative minimum tax in 1997. The tax raised $16.6 million in 1999. Because the tax is not indexed for inflation, tax revenue is forecast to grow rapidly in future years. The Governor's budget assumes a growth rate of 12 percent per year. Taxpayers with unused AMT credits from earlier years will be allowed to claim these credits in tax years 2002 and 2003.

Figure 12.

Alternative Minimum Tax (AMT) Paid in 1997		
Gross Income*	% of AMT filers	% of AMT dollars
Less than $50,000	4.9%	1.0%
$50,000 to $99,999	30.1%	7.5%
$100,000 to $249,999	41.0%	21.4%
Over $250,000	24.0%	70.1%

*Gross income includes nontaxable as well as taxable income. This exceeds federal adjusted gross income (which excludes some of the preference income).

Increase working family credit – The Governor proposes a major increase in the working family credit, roughly doubling the total amount of credit by tax year 2003, when the changes are fully phased in. The credit would be increased in two distinct ways:

- Starting in the 2001 tax year, increase the credit amount for all qualifying taxpayers with qualifying children – by $100 for those with one child and by $200 for those with two or more qualifying children. The number of taxpayers eligible for the credit would not change, and there would be no increase for those with no children.

- Starting in the 2003 tax year, increase the first tier credit rate for all eligible taxpayers. This will result in higher credit amounts for all those eligible under current law. The additional amount for those with children would also be raised to $200 for those with one child and $400 for those with two or more children. The number of taxpayers eligible for the credit would not change.

Figure 13 shows how the Governor's proposal would increase the maximum credit, depending on the number of children in the family. In 2003, the maximum credit would increase by 63 percent for those with two children and by 55 percent for those with one child. Because about half of the increased cost is due to the added $200 per child (up to two children), those with smaller credit amounts would see an even larger percentage increase. The average credit amount – and the total dollars paid in credit – would almost double compared to current law.

Figure 13.

Increase in Working Family Credit Proposed by the Governor								
	2001 Tax Year				**2003 Tax Year**			
Maximum Credits	Current Law	Gov's Proposal	Dollar increase	Percent increase	Current Law	Gov's Proposal	Dollar increase	Percent increase
Two Children	$1,404	$1,604	$200	14%	$1,464	$2.387	$923	63%
One Child	728	828	100	14%	759	1,175	416	55%
No Children	90	90	0	0%	91	136	45	49%
Total Dollars of Working Family Credit	$103.1 million	$129.6 million	$26.5 million	26%	$107.3 million	$210.6 million	$103.3 million	96%

The large proposed increase in the credit in tax year 2003 can be seen by comparing Figure 14(current law) with Figure 15(Governor's proposal). Note that the proposed credit would have a "cliff," where earning a few more dollars would result in losing $400 (two children) or $200 (one child). Although the expansion of the Working Family Credit would qualify for funding from TANF (Temporary Assistance for Needy Families) funds, the Governor would fund it with General Fund dollars. There is uncertainty about the future levels of TANF funding, and the Governor does not want to finance a permanent expansion of the credit using that uncertain source of funding.

Figure 14

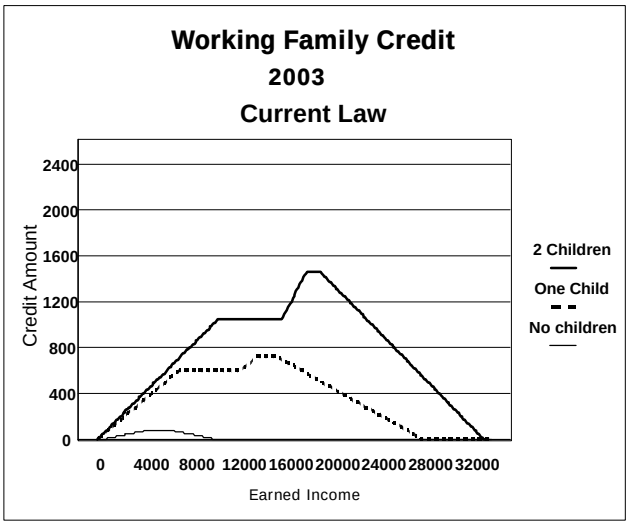
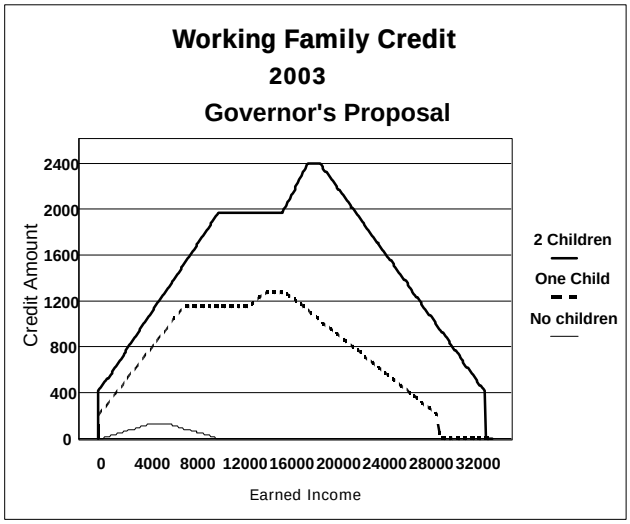


Figure 15



Repeal Child and Dependent Care Credit (CDCC), and use the money to fund direct child care subsidies – The Governor proposes to repeal the CDCC, which currently provides $12 million in child care subsidies to about 36,000 households with incomes below $31,700. The maximum credit amounts are $720 (one child) and $1440 (two or more children), but the average credit was only $330 in 1999. Unlike the federal credit for child care, Minnesota's credit has been refundable, so even those who owe no tax would receive the credit. The amount of credit paid has been steady at about $12 million dollars in recent years, and is not expected to grow in the future.

The Governor proposes shifting these dollars to the newly-consolidated system of direct child care subsidies for low-income working families. This will consolidate all child care subsidies – including the money formerly spent on tax subsidies – in one program. With the advent of welfare reform, direct subsidies for child care were greatly expanded, but the credit remained unchanged. Current law appropriates almost $200 million for direct subsidies in FY 2001, so the existing child care tax credit currently accounts for only one out of every 18 dollars of state subsidy. It is argued that placing all child care funding in one program will better target the dollars toward those with greatest need.

The populations served by the dependent care credit and the consolidated child care subsidy program are somewhat different. Some who receive the dependent care credit will be ineligible for the consolidated credit. Until more is known about the parameters of the new consolidated credit, an estimate of the number of such families is unknown.

K-12 Education Tax Credit – Restrict eligible expenditures and reduce the credit rate from 100 percent to 75 percent. The Governor proposes to leave the maximum credit amount unchanged, but to reduce the cost of the credit in two ways:

- Allow the credit *only* for (a) textbooks, (b)purchases of computer hardware (up to $200) for use at home, and (c) instructor fees or tuition for classes or instruction taken outside the normal school day or school year. No longer eligible would be expenditures for other materials used during the normal school day, educational software, or fees paid to transport a child to or from school. This change is proposed in response to audits showing a high proportion of credits improperly claimed

for these categories of expenses. In recent audits, between 70 and 80 percent of claimed amounts have been disallowed.

- Reduce the credit rate from 100 percent of eligible expenditures to 75 percent. The maximum credit amount ($1000 per child for up to two children) would remain unchanged. This will generally reduce the amount of credit received. The proposal is based on a belief that a 100 percent credit results in careless spending because it reduces the cost of eligible items to zero. With a 75 percent credit, the taxpayer will have to pay 25 percent of the cost.

This would reduce the credit amounts by an estimated $15.3 million in the 2002 tax year. About $24 million of credit was claimed in the 2000 tax year, so the Governor would cut the current law credit by about half (after adjusting for higher participation rates). The reduced credit would only affect families with total income (including nontaxable income)below $37,500; families with higher incomes are not eligible.

The Governor's proposed flat $100 per child addition to the working family credit (rising to $200 per child in 2003) is intended in part to offset the reduction in the K-12 credit. The proposed increase in the working family credit is roughly twice as large (in total dollars) as the cut in the K-12 credit in FY 2003, but some families would still lose more in the K-12 credit than they gain in the additional working family credit. Families who have no earned income, for example, can receive the K-12 credit but do not qualify for the working family credit.

K-12 Education Subtraction – Restrict eligible expenditures. Under the Governor's proposal, expenditures for transportation, computer software, and materials (other than textbooks) for use during the regular school day would no longer be eligible for this subtraction. The total tax benefit from the subtraction would fall by roughly 10 percent.

Federal Update – Conform to new federal tax laws. The Governor proposes to adopt the changes made in three federal tax bills passed by the 2000 Congress. Conforming to these federal changes is proposed for purposes of simplicity. Any deviation from federal rules complicates the calculation of state tax liabilities.

Most of the cost of conforming to these provisions shows up in corporate (rather than individual) income tax collections. See the discussion of federal update in the corporate tax section for a description of the federal bills and their tax provisions.

Reform Tax Penalties – The Governor proposes significant changes in the penalties levied for late payment or failure to pay taxes. Penalties would generally be reduced for taxpayers with relatively minor violations, and the penalties for late payment would accumulate less rapidly.

Interaction Effects – The Governor's proposals to reduce property taxes and motor vehicle registration taxes will result in higher income tax collections, because those taxes can be claimed as itemized deductions (or business expenses) for income tax purposes.

Implications of Income Tax Changes

Impact on Representative Households – Figure 16 illustrates how lower tax rates and increased working family credit would affect some typical households in 2003. The examples assume that those with incomes of $50,000 or less take the standard deduction, and that those with higher incomes claim itemized deductions equal to 17 percent of gross income. Households with children are assumed to claim the working family credit at incomes of $10,000 and $25,000.

On average, the Governor's proposal would cut income tax liability by 9.7 percent in 2003, but the tax reductions would vary by income and household type. Married couples and heads of household with incomes of $10,000 and $25,000 see larger gains due to the increase in the working family credit. At higher incomes ($50,000 or more), the percentage cut in taxes falls with income. For example, the tax cut for married couples falls steadily from 9.2 percent (at $50,000) to 6.7 percent (at $500,000). Although each tax rate is cut by the same 0.5 percentage points, that represents a larger reduction – in proportional terms – for the bottom tax rate. The bottom bracket tax rate falls by 9.3 percent (0.5/5.35 = 0.093), while the top bracket rate falls by only 6.4 percent (0.5/7.85 = 0.064).

The Governor's tax proposals would increase the progressivity of the individual income tax, because they would reduce taxes by a larger proportion for low-income taxpayers than for high-income taxpayers. However, the income tax would raise a smaller share of total state and local taxes, with more regressive taxes raising a larger share. Without a detailed analysis, it is not clear whether the overall tax burden would be more or less regressive.

Figure 16.

Governor's Proposed Income Tax Changes in Tax Year 2003

Married couple with two dependents (spouses have equal incomes)

Adjusted Gross Income	Amount of Tax		Change in Tax	
	Old Law	New Law	Dollars	Percent
$ 10,000	(1,000)	(1,900)	(900)	n/a
25,000	(599)	(1,339)	(740)	n/a
50,000	1,610	1,462	(148)	(9.2)%
75,000	3,037	2,786	(251)	(8.3)%
100,000	4,400	4,045	(355)	(8.1)%
250,000	14,292	13,278	(1,015)	(7.1)%
500,000	31,792	29,663	(2,129)	(6.7)%

Head of household with one dependent

Adjusted Gross Income	Amount of Tax		Change in Tax	
	Old Law	New Law	Dollars	Percent
$ 10,000	(632)	(1,149)	(516)	n/a
25,000	389	21	(367)	(94.5)%
50,000	2,107	1,929	(178)	(8.4)%
75,000	3,570	3,289	(281)	(7.9)%
100,000	5,033	4,648	(385)	(7.6)%
250,000	15,228	14,185	(1,043)	(6.8)%
500,000	32,284	30,155	(2,129)	(6.6)%

Single filer with no dependents

Adjusted Gross Income	Amount of Tax		Change in Tax	
	Old Law	New Law	Dollars	Percent
$ 10,000	98	75	(22)	(22.8)%
25,000	923	837	(86)	(9.3)%
50,000	2,393	2,200	(193)	(8.0)%
75,000	3,856	3,559	(296)	(7.7)%
100,000	5,462	5,062	(400)	(7.3)%
250,000	15,709	14,656	(1,053)	(6.7)%
500,000	32,610	30,481	(2,129)	(6.5)%

Distribution of Income Tax Cuts by Income Level in 2003 – Figure 17 shows the distribution of tax filers, tax liability under previous law, and tax cuts by income level. As shown on the table, the 56 percent of tax filers with incomes under $50,000, paying 13 percent of all income taxes under current law, would receive 26 percent of total tax cuts. The top 14 percent of all tax returns, with incomes over $100,000, paying 57 percent of all income taxes under current law, would receive 47 percent of the total income tax cut.

Figure 17

Percent of Filers, Tax Liability, and Income Tax Cuts, by Level of Income in 2003

Adjusted Gross Income	Percent of All Filers with Tax Cut	Percent of Tax Liability (before tax cut)	Percent of Total Tax Cut
Under $30,000	36%	3%	17%
$ 30,000 to $ 49,999	20%	10%	9%
$ 50,000 to $ 99,999	30%	30%	27%
$100,000 to $249,999	12%	29%	25%
$250,000 and Over	2%	28%	22%
Total	100%	100%	100%

Corporate Taxes

Although the Governor proposes some significant changes in the corporate income tax, the net impact on tax collections would be small. Provisions that increase revenue would roughly offset provisions that reduce tax revenue. The net tax cut would be only two percent in the 2002-03 biennium and one percent in the 2004-05 biennium. The Governor's proposals include provisions that would – by themselves – cut revenues by about 15 percent, but they are offset by other provisions that would raise revenues by nearly as much.

Figure 18 summarizes the corporate tax changes recommended by the Governor.

Proposals that reduce the corporate tax by a combined total of about 15 percent.

- **Increase sales apportionment factor to 90 percent** – For multistate companies, Minnesota's share of corporate income is calculated as a weighted average of the shares of a corporation's sales, payroll, and property that are located in Minnesota. Under current law, the Minnesota share of sales is weighted at 75 percent, while the Minnesota shares of payroll and property are each weighted at 12.5 percent. Raising the sales factor to 90 percent (and reducing the payroll and property shares each to 5 percent)would generally reduce taxes for companies that produce more in Minnesota than they sell here, while raising taxes for companies that sell more in Minnesota than they produce here. The increased weight on the in-state share of total sales is designed to increase the competitiveness of Minnesota-based production facilities. It would mirror the national trend as other states are also placing a heavier weight on the sales factor.

Although this change would reduce total corporate tax collections by about $50 million per year – by about six percent – it would increase taxes for some corporations, including some non-headquartered companies with substantial payroll and property in Minnesota.

Figure 18

Proposed Changes in Corporate Franchise Taxes
($ in thousands)

Tax Provision	FY 2002	FY 2003	**FY 2002-03**	FY 2004	FY 2005	**FY 2004-05**
Sales apportionment to 90%	($54,900)	($46,300)	**($101,200)**	($50,700)	($52,600)	**($103,300)**
Reduce tax rate to 9.4%	($39,500)	($33,600)	**($73,100)**	($36,800)	($38,400)	**($ 75,200)**
Repeal alternative minimum tax	($14,400)	($12,200)	**($26,600)**	($13,400)	($13,800)	**($ 27,200)**
Exempt insurance companies who pay insurance premiums tax	($10,100)	($ 8,600)	**($18,700)**	($ 9,400)	($ 9,700)	**($ 19,100)**
Net income definition	($ 5,300)	($ 4,500)	**($ 9,800)**	($ 4,900)	($ 5,100)	**($ 10,000)**
Federal update*	($18,800)	($16,300)	**($35,100)**	($16,700)	($16,600)	**($33,300)**
Reform penalties	0	($ 1,000)	**($ 1,000)**	($ 1,000)	($ 1,000)	**($ 2,000)**
Repeal foreign operating company provisions	+ $34,600	+ $29,300	**+ $63,900**	+ $32,000	+ $33,200	**+ $65,200**
Repeal foreign royalty income deduction	+ $56,300	+ $47,500	**+ $103,800**	+ $52,100	+ $54,100	**+ $106,200**
Modify research credit	+ $18,100	+ $15,600	**+ $ 33,700**	+ $17,700	+ $19,700	**+ $ 37,400**
Modify contributions deduction	+ $ 6,070	+ $ 5,200	**+ $11,270**	+ $ 5,700	+ $ 5,900	**+ $ 11,600**
Repeal job training credit	+ $ 200	+ $ 100	**+ $ 300**	0	0	**0**
Interaction effect: Property tax cuts	0	+ $12,200	**+ $12,200**	+ $12,800	+ $13,500	**+ $26,300)**
Corporate Tax Changes	($27,730)	($12,600)	**($40,330)**	($12,800)	($10,800)	**($23,600)**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state.
*Federal update would also have a ($3,800) impact on revenues in FY2001.

- **Reduce tax rate to 9.4 percent** – The reduction in tax rate from 9.8 percent to 9.4 percent would – taken alone – reduce corporate tax burdens for all who pay the tax by a little more than four percent.

- **Repeal alternative minimum tax** (AMT) – Repeal of the corporate AMT would substantially simplify this tax both for tax filers and for the Department of Revenue. The AMT increases tax for those with a substantial amounts of preference income. AMT tax collections (net of the AMT

credit) tend to smooth out corporate tax payments over the business cycle, so repeal might increase the volatility of the corporate tax. Those with unused AMT credits would be allowed to use those credits to offset tax only for two additional years (2003 and 2004). The amount of accumulated credit that would remain unclaimed is unknown.

- **Exempt insurance companies who pay insurance premiums taxes** – The Governor would eliminate the corporate tax for insurance companies. The change would make Minnesota insurance companies more competitive with foreign (e.g. non-Minnesota) insurance companies. Only a few other states subject insurance companies to their corporate tax.

- **Change definition of net income** – The Governor would simplify the corporate tax by eliminating a number of adjustments made to income as defined by federal law. These include adjustments for depletion, dividends received, pollution control facilities, enterprise zones, and border cities. The depletion adjustments represent about two-thirds of the total tax reduction from these provisions.

- **Federal Update – Conform to new federal tax laws.** The Governor proposes to adopt the changes made in the three federal tax bills passed by the 2000 Congress.
    - The Consolidated Appropriations Act of 2001 included the following: fair market deduction for donation of computers to schools; the expensing of brown field cleanup costs; an increase in the volume of private activity bonds that can be sold by state and local governments; the creation of new empowerment zones; and allowing a dependent exemption for children who have been kidnaped.
    - The Installment and Tax Correction Act of 2000 repealed a 1999 law that precluded accrual-based taxpayers from using the installment method of reporting sales.
    - The FSC Repeal and Extraterritorial Income Exclusion Act of 2000 repealed the special tax preferences for Foreign Sales Corporations (FSCs), instead excluding from tax net income attributable to sales made outside the U.S. This Act was in response to a trade dispute between the United States and the World Trade Organization.

  Most of the revenue impact for corporations is from the last of these -- the repeal of the FSC provisions. Conforming to these federal changes is proposed for purposes of simplicity. Any deviation from federal rules complicates the calculation of state tax liabilities.

Proposals that increase the corporate income tax by a combined total of almost 15 percent

- **Eliminate foreign income provisions** – The Governor proposes to repeal two special provisions for foreign income. This would increase corporate taxes by an average of about $80 million per year. These provisions were adopted in the early 1980s, when Minnesota adopted unitary apportionment. Adoption of unitary apportionment resulted in substantial tax increases for corporations whose "unitary group" included a foreign operating company (FOC) that itself had no nexus with Minnesota. An FOC is defined as a U.S. corporation with at least 80 percent of its payroll and property either in Puerto Rico or outside of the United States, and which is part of a unitary group with Minnesota nexus. Current law allows Minnesota corporate taxpayers to deduct

80 percent of the income earned by these 80-20 corporations, either as royalty income or as a "deemed dividend."

Repeal of these provisions for foreign income will particularly affect high tech corporations. According to the Department of Revenue, only two percent of all corporations receive a benefit from the current foreign income provisions. For those companies, though, the impact may be substantial.

- **Modify the research credit** – The research credit reduces tax liability for corporations that increase their research expenditures over a base amount. Under current law, the base amount is defined as average research expenditures in the years 1984 to 1988, measured as a percentage of gross receipts in those years. The Governor's proposal would change the definition of the base years from 1984 through 1988 to the most recent five years. Only corporations whose Minnesota research expenditures were higher this year than their average over the past 5 years would receive the revamped credit. This change would reduce the amount of the research credit by an average of $17 million per year. According to the Department of Revenue, this would cut the value of the credit roughly in half.

- **Modify contributions deduction** – Current law limits a corporation's charitable deduction to (a) contributions to organizations located in and carrying on substantially all their activities in Minnesota or (b) a proportion of contributions (equal to the Minnesota share of charitable expenditures) given to foundations that carry out most of their activities outside of Minnesota. The Governor proposes adoption of the federal charitable deduction instead. The share of a corporation's total charitable contributions that it could deduct would equal the share of its total income that was taxed as Minnesota income. Although some companies would receive a larger deduction than under current law, the proposal would increase net corporate tax collections by about $5.5 million per year. According to the Department of Revenue, this would cut the value of the current-law deduction by about 25 percent.

- **Repeal job training credit** – The Governor proposes to replace this tax credit with a direct appropriation to the same organization. The recommended appropriation -- $300,000 per year for four years -- is four times as large as the value of the lost tax credit. In future years, this training program would be reviewed in the same manner as other state subsidies for job training.

- **Interaction effect with property tax cuts** – The reduction in property taxes for commercial and industrial property, utility property, and apartments will reduce corporate costs by (roughly) an equal amount. This will result in higher profits and higher corporate taxes.

Implications of corporate tax changes – The Governor's corporate tax proposals would simplify the tax and eliminate almost half of the 31 special adjustments to income under current law. Corporate tax collections would remain essentially unchanged in the aggregate, however. Revenue-raising provisions would roughly balance revenue losing ones. If the federal update provisions are ignored (such provisions are usually enacted), there would be no net cut in corporate taxes. The relative share of the corporate tax in total state tax collections would rise slightly as a result (from 4.4 percent of total 2004-05 taxes under current law to 4.7 percent under the Governor's proposal). There will be some corporations with large gains under the proposal, but there will also be some with large losses.

Sales and Use Tax (including Motor Vehicle Sales Tax)

The Governor's sales tax proposals include (a) a lower sales tax rate and other tax-cutting provisions that would – by themselves – *reduce* tax revenues by 13.3 percent and (b) tax base expansion that would – by itself – *raise* sales tax revenues by almost 22 percent. In combination, they would raise state sales tax revenues by 8.6 percent in the 2004-2005 biennium. Figure 19 summarizes the effects of changes to the state's sales and use.

Provisions that would reduce the sales tax by a combined total of 13 percent

- **Reduce the tax rate from 6.5 percent to 6.0 percent** – The reduced rate applies to both the general sales tax and the motor vehicle sales tax. The motor vehicle sales tax accounts for between 11 and 12 percent of the reduction in revenue. By itself, the lower tax rate would reduce total sales tax collections by 7.7 percent.

- **Repeal the special add-on tax rate for rental cars** – The total state tax now levied on rental cars is 12.7 percent, an additional 6.2 percent on top of the current 6.5 percent general sales tax rate. Under the Governor's proposal, rental cars would pay the same 6 percent sales tax as other taxable goods and services.

- **Exempt state and local government purchases (including motor vehicles)** – The Governor proposes to exempt all purchases by state and local governments. Government purchases have been subject to the general sales tax since 1987 (state purchases) and 1991 (local government purchases except for school districts, hospitals, nursing homes, and some purchases by libraries). However, vehicle purchases by state and local governments have been taxed since the inception of the motor vehicle sales tax in 1971. By itself, exempting all state and local purchases would reduce sales tax revenues (including motor vehicle sales tax) by 3.0 percent.

  The Governor's proposal goes beyond restoring the tax status that existed before 1987 (for state government) and 1991 (for local governments). First, it extends the exemption to motor vehicles. Second, it extends the exemption to include construction materials purchased by a contractor for use in a government building. Third, it extends the exemption to include the purchase of meals and lodging.

Figure 19

Sales and Use Tax
(includes Motor Vehicle Sales Tax)
(dollars in thousands)

Tax Provision	FY 2002	FY 2003	FY 2002-03	FY 2004	FY 2005	FY 2004-05
Reduce tax rate from 6.5% to 6.0% (includes motor vehicle sales tax)	($148,300)	($384,500)	($533,100)	($404,600)	($425,700)	($830,300)
Repeal add-on 6.2% tax on rental vehicles	(5,400)	(13,400)	(18,800)	(13,800)	(14,300)	(28,100)
Exempt state and local government purchases (@6%)	(54,900)	(136,400)	(191,300)	(141,400)	(146,600)	(288,000)
Repeal June accelerated payments (@6%)	(134,000)	(9,900)	(143,900)	(8,100)	(8,500)	(16,600)
Up-front exemption for capital equipment (@6%)	(39,000)	(47,500)	(86,500)	(31,100)	(33,800)	(64,900)
Expand exemption for business inputs (@6%)	(36,600)	(91,100)	(127,700)	(94,500)	(97,700)	(192,200)
Modify exemptions for non-profits(@6%)	(8,400)	(20,800)	(29,200)	(21,600)	(22,400)	(44,000)
Miscellaneous (@6%)	(4,700)	(11,700)	(16,400)	(12,200)	(12,800)	(25,000)
Provisions that cut tax	($431,500)	($715,300)	($1,146,800)	($727,300)	($761,800)	($1,489,100)
Expand sales tax to many services* (@6%)	$384,500	$959,200	$1,343,700	$995,000	$1,031,900	$2,026,900
Repeal exemptions (@6%)	54,000	132,000	186,000	136,000	141,000	277,000
Telecommunications (@6%)	22,100	54,600	76,700	57,900	61,400	119,300
Miscellaneous including non-profits (@6%)	6,600	15,800	22,400	16,300	16,900	33,200
Provisions that raise tax	$467,200	$1,162,400	$1,629,600	$1,206,000	$1,252,200	$2,458,200
Subtotal: Sales and Use	**$35,800**	**$445,900**	**$481,700**	**$478,300**	**$478,300**	**$956,600**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state. All provisions are effective starting January 1, 2002. Columns may not add to totals due to rounding.
*Does not include services sold to state and local government, which would be exempt, but does include previously exempt installation and shipping charges.

- **Repeal June accelerated payments** – Since 1983, venders with annual sales and use tax liability of $120,000 or more have been required to make an early payment of a portion (currently 62 percent) of their June tax liability. Because payment is due two business days before the end of June – rather than the 14th of the following month, as is typical for these taxpayers – these

payments are shifted to an earlier state fiscal year. This "fiscal year shift" was originally used to balance the state budget in years when tough budget choices were required. The Governor proposes to reverse that fiscal shift. Eliminating this complication would be required by Minnesota's participation in the Streamlined Tax System, which is discussed below.

The cost of repeal is largely a one-time cost in FY 2002, because $134 million of sales tax revenues would be received in the first month of FY 2003 rather than the last month of FY2002. However, there is also an ongoing cost in later fiscal years, because the size of the existing fiscal shift grows slightly larger each year (with the growth of sales tax revenues).

The net revenue loss for FY 2003 (the first of the out-years) would be calculated as follows:

Gain:	$134.0 million in July 2002 (shifted from June 2002 in FY 2002)
Lose:	$143.9 million in June 2003 (shifted to July 2003 in FY 2004)
Net loss:	$ 9.9 million for the fiscal year.

- **Up-front exemption for capital equipment** – Current law provides for a refund of taxes paid on certain capital equipment purchased (or leased) by businesses engaged in manufacturing, fabricating, mining, refining, or on-line data retrieval. Tax must be paid at the time of purchase, but the taxpayer can apply for a full refund. The Governor proposes to replace the refund application process with an exemption at time of sale. This would eliminate both the administrative costs of the refund mechanism and the delay in receiving refunds. The complexity of the refund process also means that some who are eligible for the refunds fail to apply for them. The on-going cost of an up-front exemption (over $30 million per year) is due to the higher proportion of eligible purchases that benefit. Under current law, about 15 percent of allowable refunds are not received.

- **Expand exemptions for business inputs** – The Governor proposes to exempt some currently taxable purchases of business inputs, reducing the sales tax burden by an additional $90 million per year. These include:
    - Inputs used in producing currently taxed services. The benefits would go primarily to producers of amusement and cable TV services. Hotels, restaurants, motion picture theaters, and landscaping companies also benefit.
    - Interstate trucks would be exempt.
    - Farm tires would be exempt, as would machinery and equipment for use in growing plants.
    - Pollution control equipment would be exempt.
    - Inventory control equipment would be exempt.

- **Expand exemptions for non-profit organizations** – The Governor proposes significant changes in the sales tax exemptions for non-profit organizations. Some of those provisions will benefit non-profits; some will hurt non-profits. A description of those changes and their impact on particular types of non-profit organizations can be found on pages 25-26.

- **Miscellaneous provisions that reduce tax** – The Governor also proposes to:
  - Expand the exemption for occasional sales ($6.9 million in FY 2003).

- Change the "sourcing rules" that determine whether services are taxable in Minnesota. Under current law, services may be subject to tax if the service is provided in Minnesota. By basing taxability on the location of the consumer (rather than the location of the provider), the proposal would create a level playing field for Minnesota service providers who compete in the national market. ($4.6 million in FY2003).
- Provide a use tax credit for taxes paid to local governments in other states ($0.2 million in FY 2003).

Provisions that increase the sales tax by a combined total of 22 percent

- **Expand tax base to include most services** – The Governor proposes to increase sales tax revenues by over $2.1 billion in FY 2004-05 by expanding the tax base to include most services. However, services would be exempt if they are (a) used or consumed directly in the industrial production process or (b) used or consumed in providing taxable services. Newly taxable categories of services would include:

  - Legal services
  - Computer & data processing
  - Real estate commissions
  - Warehousing & storage
  - Engineering, architecture, & surveying
  - Motor vehicle repair
  - Construction – special trades
  - Accounting
  - Management, consulting, & public relations
  - Intra-state transportation
  - Advertising
  - Investment counseling & brokerage fees
  - Personnel services
  - General repair
  - Personal services (including beauty & barber)
  - Sewer services
  - Research & development/testing
  - Funeral services

Figure 20 summarizes who will pay the tax on these newly taxable services. Of total purchases of these services, governments buy four percent, consumers buy 26 percent and businesses buy 70 percent. All of the government purchases would be exempt under the Governor's proposal, and about one-third of business purchases would be exempt as business inputs. So 36 percent of the tax paid on these newly taxable services would be paid by consumers and 64 percent would be paid by businesses. This $600 million increase in tax on business inputs is substantially larger than the reduced sales taxes paid by business due to all of the other provisions of the Governor's tax plan. This would represent a substantial increase in total tax paid on business-to-business purchases.

Figure 20.

Newly Taxable Services in Governor's Budget (FY 2003)							
	Total Purchases		Exempt		Taxable Purchases	Tax Liability (@6%)	
Purchaser	%	Dollars	%	Dollars		%	Dollars
Government*	4%	$ 0.8 billion	100%	$0.8 billion	$ 0.0 billion	0%	$ 0 million
Consumers	26%	$ 5.7 billion	0%	$0.0 billion	$ 5.7 billion	36%	$341 million
Businesses	70%	$15.2 billion	34%	$5.2 billion	$10.0 billion	64%	$600 million
Total	100%	$21.7 billion	24%	$6.0 billion	$15.7 billion	100%	$941 million

Note: Does not include installation or delivery services.
*Include s some services purchased by non-profits as well.

- **Tax all shipping and installation charges** – For tax purposes, the Governor proposes to include all transportation and installation charges in the price of a product. Under current law, these charges are not taxed if they are shown separately on the bill.

Taxation of construction materials and services – Under current law, construction materials are generally taxable, but construction labor services are not. If a building's construction costs include materials (40 percent)and construction labor (60 percent), current law would tax only the materials. In this case, only 40 percent of the total construction costs are subject to tax.

The Governor proposes to tax general contractors and special trades contractors differently. For both types of contractors, construction materials would be purchased exempt as "purchases for resale." Subcontractors would collect tax on the total price they charged – both what they charged for materials and what they charged for their labor. For subcontractors, this would result in full taxation of both labor and materials. In contrast, the Governor proposes that general contractors charge tax only on the construction materials. Labor services provided by general contractors would not be taxed.

The proposal would result in the taxation of all materials, plus labor services by subcontractors. This disparate treatment of general contractor labor and subcontractor labor would create an incentive to restructure the provision of construction services. Switching labor from subcontractors to the general contractor (or successfully reclassifying oneself as a general contractor) would result in lower tax liability. The extent to which this would occur is unknown.

Repeal existing exemptions – The Governor proposes to repeal a large number of existing exemptions, raising tax revenue (at the proposed 6 percent rate) by $139.6 million in FY 2003. Repealing each of the following exemptions would increase sales tax revenue by at least on million dollars in FY 2003:

- Publications ($43.4 million) – Under current law, publications issued at least once every three months (including newspapers, magazines, journals, seasonal catalogs, shoppers guides) are exempt from tax, except for magazines and periodicals sold over the counter.

- Institutional meals ($24.1 million). Meals served *by* schools, colleges, and universities would remain exempt, but catered meals served *at* educational facilities would not.
- Water for residential use ($18.6 million).
- Nonprescription analgesics and therapeutic devices, such as wheelchairs, hospital beds, and blood glucose monitoring machines ($10.0 million). Prescription medicines, insulin, and prosthetic devices would remain tax exempt.
- Certain interstate telephone service on WATS lines ($9.2 million).
- Advertising materials ($6.9 million).
- Caskets and burial vaults ($4.7 million).
- Feminine hygiene products ($2.7 million).
- Repair and replacement parts for airplanes ($2.0 million).
- YMCA, YWCA, and JCC memberships ($1.5 million).
- Television commercials ($1.1 million).

- **Telecommunications –** The Governor's proposal includes adoption of language developed by the National Telecommunications Tax Reform Initiative, a joint state-industry working group. The proposed definition of telecommunications includes cable television, satellite TV, and electronic information services. The changes would make Minnesota law consistent with the recently passed federal Mobile Telecommunications Act in defining sourcing for tax purposes. Phone calls either originating or terminating in Minnesota would be taxable if billed to an address in Minnesota. This change would increase the number of interstate phone calls subject to Minnesota tax, increasing tax revenue by $54.6 million in FY 2003. (This is in addition to the $9.2 million raised by ending the exclusion for certain interstate service on WATS lines, which is listed above.)

Other miscellaneous changes that increase tax – These include the following:

- Several provisions that reduce tax exemptions for certain non-profit organizations. ($9.0 million in FY 2003). See pages 25-26 for a description of these changes.
- The exemptions for interstate truck parts and ready mix truck chasses would be repealed ($3 million in FY 2003).
- Some definitions would be modified to conform to Streamlined Sales Project ($3.8 million in FY 2003).

Implications of sales tax changes

Streamlined Sales Tax Project – Some of the sales tax changes proposed by the Governor (and described above) will be required if Minnesota is to continue to participate in this project. The required changes include some definitional changes, new rules for sourcing services, and repeal of June accelerated payments. As authorized in the 2000 Tax Bill, Minnesota has joined 26 other states as an official "participant" in the Streamlined Sales Tax Project, a national effort to radically simplify state sales taxes. Participating states

include all of Minnesota's neighboring states. An additional 14 states are represented as "observer" states. The project is supported by the National Conference of State Legislatures, the National Governors Association, and the Federation of Tax Administrators.
The project's goal is to radically simplify payment of sales and use taxes by multistate companies. Companies with sales in many states now face high administrative costs. They must file separate returns in each state, and the definitions used to identify taxable purchases vary greatly. Administrative rules and payment dates and procedures also vary. Tax exemption certificates issued by one state are not recognized by other states, and the treatment of bad debts and rounding rules differ from state to state. Adopting uniform definitions and uniform administrative rules would greatly simplify tax filing while allowing tax rates and the tax base to vary by taxing jurisdiction.

The Streamlined Sales Tax Project hopes to move toward a "zero burden" sales tax system. Companies would use either their own certified automatic payment technology or a certified service provider to send tax payments to every state that adopts the streamlined system, and the states would help pay the costs of developing and using that technology. A pilot project is currently underway in four states – Kansas, Michigan, Wisconsin, and North Carolina. Following a competitive bidding process, three private companies have been selected to develop prototype computer systems that allow automated tax payments while fully protecting consumer privacy.

The Streamlined Sales Tax Project is largely a response to the rapid growth of e-commerce, which is likely to substantially increase sales by out-of-state sellers who are not legally required to collect tax. *Quill v. North Dakota* (1992) concluded that out-of-state companies can only be required to collect sales tax if they have employees or property in the state (thus creating *nexus*). Given the complexity of the tax system now facing multistate sellers, requiring other companies to collect sales tax would impose an "excessive burden on interstate commerce." When taxes are not collected by the out-of-state seller, those buying such products (businesses or consumers) are legally required to pay "use tax". However, few consumers pay use tax on purchases from out-of-state companies, and compliance rates for businesses are less than 100 percent.

If the Streamlined Sales Tax Project can significantly reduce the administrative costs for multistate companies, some out-of-state companies might agree to pay the tax voluntarily. Even if that does not occur, courts may be willing to require out-of-state companies to withhold taxes if administrative costs are minimal. Alternatively, Congress might be persuaded to enact legislation requiring such payments to any state that has adopted the streamlined sales tax system.

The potential revenue implications for Minnesota are uncertain, but two recent estimates for 2003 are summarized in Figures 21 and 22 below. The first study, by the U.S. General Accounting Office (GAO) provides a range of estimates. Minnesota's total revenue loss from all remote sales (e-commerce along with catalog, telephone, and home shopping network sales) is estimated at between $129 million (3.0 percent of general sales tax revenues) and $489 million (11.5 percent of general sales tax revenues).

Some e-commerce sales simply replace other remote sales, which would not be taxed anyway. E-commerce results in less tax revenue only to the extent that untaxed e-commerce sales replace taxable sales by the "bricks-and-mortar" sector. The incremental revenue loss due to e-commerce represents $19 million of GAO's $129 million "low estimate" and $232 million of their $489 million "high estimate" for all remote sales in 2003. Thus e-commerce is estimated to reduce Minnesota's 2003 general sales tax revenue by

between 0.4 percent and 5.5 percent. Another recent study by Donald Bruce and William Fox at the University of Tennessee estimates the Minnesota's incremental e-commerce impact in 2003 at $220 million (5.2 percent of projected general sales tax revenues).

Figure 21

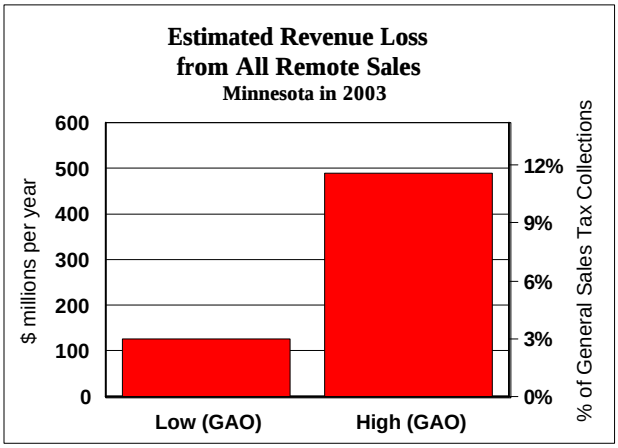
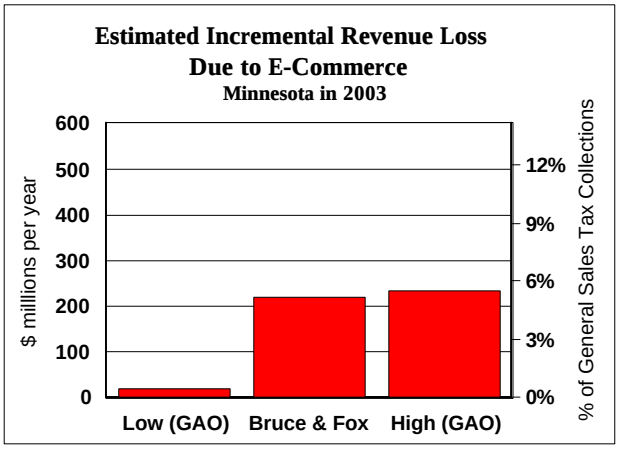


Figure 22



How do the proposed sales tax changes affect nonprofit organizations?

The Governor's changes in the sales tax provisions affecting non-profits are complex. Some are beneficial to non-profits, while others are harmful. Changes are separated into those dealing with purchases by non-profit organizations and those dealing with sales made by non-profits.

1. *Purchases* by nonprofit organizations

- *Current law:*
  - Eligible organizations: Nonprofits that are exclusively educational, religious,or charitable, along with nonprofit senior citizens' groups, veterans' organizations, and cemeteries.
  - Exempt purchases: Most purchases other than motor vehicles, meals, and lodging. (Purchases are not exempt if made by a contractor.)
- *The proposal:*
  - Eligible organizations: Expand eligibility to include any 501(c)(3) organization. Newly eligible would be nonprofit organizations whose purpose is scientific, literary, testing for public safety, fostering amateur sports competition, or preventing cruelty to children or animals.
  - Exempt purchases: Expand to include motor vehicles (purchase or lease), meals, and lodging. Purchases by a contractor would also be exempt.
- *Net change:* Net reduction in FY2003 tax would be $11.6 million (net of a $0.3 million increase for veterans' groups). Nonprofit senior citizens' groups would generally lose their exemption, however, along with veterans' organizations and cemeteries.

2. *Sales* by non-profit organizations:

- *Current law:*

  Eligible organizations: Nonprofits and government-sponsored groups operated for charitable, religious, educational, civic, fraternal, senior citizens' or veterans' purposes.

  Exempt sales include: admission tickets to artistic events sponsored by a nonprofit;

  admission to charitable golf tournaments;

  admission to school-sponsored events (elementary and secondary);

  admission tickets and sales of personal property, food, meals, and drink at Minnesota Amateur Sports Commission events;

  camp fees for youth camps operated by a 501(c)(3) organization;

  fundraising candy sales by organizations that primarily serve youth;

  fundraising sales by a youth or senior citizen organization if annual receipts are less than $10,000;

  fundraising sales at events (other than bingo or gambling) sponsored by charitable, religious, and educational nonprofits if the events occur no more than 24 days per year; and

  memberships at YMCA, YWCA, and JCCs.

- *The proposal:*

  Eligible organizations: Groups sponsored by governmental units other than public schools lose the exemption.

  Exempt sales: First $25,000 of taxable sales per year. The $25,000 limit is applied separately to each individual organization of elementary or secondary school students. Would now include bingo and gambling fundraising events. Removes time limits on days spent in fundraising,

- *Net change:*

  Some nonprofit organizations gain by the changes, but others lose because all of their sales are currently exempt. Taxing admission tickets to artistic events would increase tax by $4.1 million in FY2003. This includes currently exempt tickets to large concerts by for-profit companies that have paid nonprofits to become cosponsors, thereby claiming the tax exemption. Taxing YMCA, YWCA, and JCC memberships would add another $1.5 million. The combined impact of the other changes would result in a net reduction in tax of $4 million.The tax increase for camp fees (Girl Scouts and others) is not broken out separately, but is included in the overall totals.

Summary: The total value of all exemptions for nonprofit organizations would increase by as much as 15 percent. Nevertheless, there are many categories of nonprofits that would pay higher sales tax under the Governor's proposals. Nonprofit organizations are also affected by other provisions in the Governor's proposal, of course, including the reduction in gambling taxes and local option taxes in lieu of property tax.

Property Tax Aids and Credits

The Governor proposes comprehensive changes to the property tax system having a net General Fund cost of $877.5 million in FY 2003 when most provisions would first become effective. The proposed changes fall into three broad categories, including:

- K-12 education finance, including a state takeover of general education funding, changes in how school operating referendum levies and debt levies are funded, and creation of a new statewide property tax on businesses and cabins;
- class rate reform and general property tax relief, including continued reductions in business and apartment class rates and the creation of two new property tax credits; and
- state aid reform including the elimination of a variety of local government aid programs and replacing the existing local government aid (LGA) program with a new formula.

K-12 Education Finance Reforms

Reforms to K-12 education finance are the center-piece of the Governor's overall tax reform initiative, including:

- eliminating the existing state-determined but locally collected property tax for the general education formula and replacing it with a state appropriation;
- requiring that existing and future voter approved school operating referendum levies be collected only from residential homestead and apartment property owners while also increasing state referendum equalization aid to reduce tax base disparities and offset the shift in tax burdens on to home and apartment owners;
- increasing state debt service equalization aid for voter approved school bonding (capital) levies; and
- establishing a new statewide property tax on businesses and cabins to offset, in part, the cost of state assumption of the general education levy.

None of the proposed reforms in how K-12 education is financed would increase or decrease funding for education.

Proposed reforms would not increase or decrease funding for K-12 education.

As summarized in Figure 23, the K-12 education funding reform provisions, including revenue from the new statewide property tax, would result in a net increase of $452.5 million of state appropriations in FY 2003. Those costs would be largely offset by the additional revenues collected through the Governor's proposal to expand the sales tax base and reductions in other aids as discussed below.

Figure 23

Fiscal Summary: K-12 Finance Changes

Provision	FY 2002	FY 2003	FY 2004	FY 2005
General Education Aid	0	($1,331,000)	($1,331,000)	($1,331,000)
90/10 metering adjustment	0	87,547	0	0
Eliminate Education Homestead Credit	0	399,824	403,825	407,863
Eliminate Ag Education Credit	0	55,705	55,705	55,705
Referendum Equalization Aid	0	(128,360)	(137,536)	(148,465)
90/10 metering adjustment	0	12,836	918	1,093
Debt Service Equalization Aid	0	(19,471)	(20,960)	(20,210)
New Statewide Property Tax	0	470,401	484,513	499,048
Subtotal	**0**	**(452,518)**	**(544,535)**	**(535,966)**

State Takeover of General Education Levy

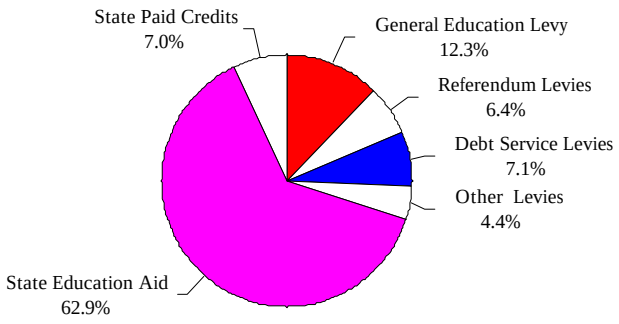
As illustrated by Figure 24, total statewide funding for K-12 education for the 2002-2003 school year (State FY 2003) is estimated to be $6.9 billion, not including federal funds or school district fee revenue, such as food service charges and extra-curricular activity fees. The Governor proposes to eliminate the general education levy, which reflects 12.3 percent of total state-local education spending for 2002-2003, and replace it with a $1.3 billion General Fund appropriation.

The existing general education levy amount is set by the state and collected uniformly throughout the state. That means that every property owner in the state will pay a general education tax rate of 32.41 percent in 2002 but because tax capacity varies across school districts, the uniform rate will generate more property tax revenue for some school districts than in others. Under the proposal, funding levels for individual school districts would be unchanged since the $1.3 billion appropriation would be distributed based on the same per pupil formula.

Local property taxpayers would continue to pay school taxes for a variety of levies, including voter approved operating referendum levies, debt service levies, and other special school levies.

Figure 24

Current Law State-Local Share of K-12 Education School Year 2002-03 ($6.9 billion)*



*Does not include local fees or federal funds.

Elimination of Education Homestead and Ag Education Credits

As also illustrated by Figure 24, the existing 69.9 percent state share of total state and local funding includes the amounts paid to school districts for both the educational homestead and the agricultural education credits since these credits reduce the amount of general education levy paid by homeowners and farmers. The amount of educational credit is equal to a percentage of the general education tax these property owners would otherwise pay up to a maximum for the homestead credit. There is no maximum for the Ag credit.

The elimination of credits would not increase property taxes for homeowners or farmers.

However, because the Governor is eliminating the general education tax for all property owners, the General Fund amounts attributable to payment of these two credits will now instead be used to fund the cost of the state aid payments to school districts. The property tax owed by homeowners and farmers will not increase as a result of this change because the tax they were receiving the credit for will no longer exist. However, homeowners, as well as farmers and other property types do pay other types of school taxes.

Operating Referendum Levies

Under current law, voters may approve the collection of additional property taxes to fund school operations and those taxes are levied on the market value of all classes of property, with the exception of homestead farmland.[1] The Governor proposes that both existing and future operating referendums instead be levied only on the adjusted net tax capacity of apartment and residential homestead property, including the house, garage, and one acre for farm homesteads.

To offset the shift onto homeowners and apartment owners that would otherwise occur for existing levies, as well as to reduce tax base disparities among school districts for future levies, the Governor proposes to increase equalization aid for school operating referendums by $115.5 million beginning in taxes payable in 2002 (FY 2003). To do so, the Governor proposes a two tiered equalization formula that would:

Homes and apartments would pay the full cost of operating referenda.

- increase the amount of operating levy per pupil qualifying for equalization from $415 to $600 per pupil with those amounts continuing to be equalized at $6,400 of adjusted net tax capacity per pupil; and

- create a second tier of equalization revenue for operating levy from $600 to $1,125 equalized at $4,265 of adjusted net tax capacity per pupil.

For school year 2002-2003, 306 school districts have voter approved operating referendums totaling $602.3 million in revenue. Of this amount, $432.8 million, or 72 percent, is funded by property taxes and $169.5 million, or 28 percent, is funded by state equalization aid. Based on existing voter approved operating referendums, the Governor's proposal would reduce the share funded by property taxes to $304.4 million, or 51 percent, and increase the share funded by state equalization aid to $297.9 million, or 49 percent.

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[1] Voter approved operating referenda are levied on tax capacity multiplied by 100 for farmland having a class rate of less than 1.0.

Debt Service Equalization Aid

Under current law, local property taxpayers bear the full burden of capital referendum levy up to the first 12 percent of adjusted net tax capacity. Debt service levy amounts that exceed 12 percent of adjusted net tax capacity are equalized at $4,000.

To reduce disparities in tax burdens between property wealthy and property poor school districts, and to reduce the burden on districts with high debt loads, the Governor would also increase General Fund expenditures for debt service equalization aid by $26.5 million beginning in FY 2003 by making the following two enhancements:

- For levy amounts between 12 percent and 20 percent of adjusted net tax capacity, the equalizing factor would increase from $4,000 to $5,000 per pupil. This enhancement is included as part of the Governor's tax package and, as shown in Figure 23, would increase General Fund expenditures by $19.5 million in FY 2003.

- In addition, a second tier of equalization would be created to assist districts with unusually high levels of debt relative to tax base by providing that levy amounts that exceed 20 percent of adjusted net tax capacity be equalized at $9,000 per pupil. This enhancement is part of the Governor's K-12 education finance proposal and would increase General Fund expenditures by $7.0 million in FY 2003.

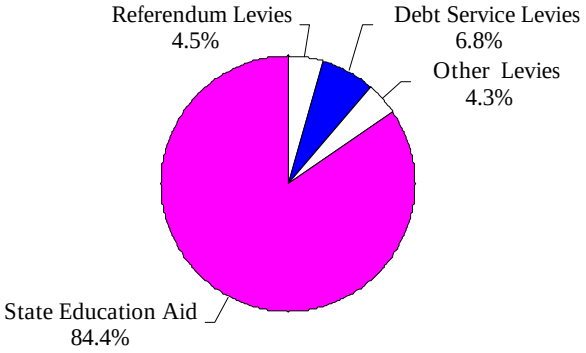
Debt service referendums would continue to be levied on all properties based on tax capacity.

State Share

State assumption of the general education levy combined with the increases in operating referendum and debt service equalization aid would substantially increase the state share of state and local K-12 education funding. A comparison between Figures 24 and 25 illustrates that the Governor's proposal would increase the state share to 84.4 percent of state and local funding in FY 2003, not including local fee revenue or federal funds.

Figure 25

Gov. Recommendations: State-Local Share of K-12 Education School Year 2002-03 ($6.9 billion)*



* Does not include local fees or federal funds.

Statewide Property Tax on Businesses and Cabins

A new state property tax on businesses and cabins would partially offset the cost of eliminating the general education levy.

The elimination of the general education levy and the requirement that operating referendums be levied only against apartment and residential homestead properties would substantially reduce local property tax burdens for businesses and cabins. As shown in Figure 23, the Governor proposes a new statewide property tax on businesses and cabins that would increase General Fund revenues by $470.4 million to partially offset the cost of eliminating the general education levy and increasing equalization aid payments to school districts. The new tax would become effective for taxes payable in 2002 and would be levied on commercial and industrial property, public utility real property and power transmission and distribution lines, resort properties, golf courses and unmined iron ore, as well as cabins. Utility attached personal property would be exempt from the tax.

While the amount of tax would be equal to a uniform statewide tax rate–based on the levy amount–multiplied by the assessed value of the property, the tax may have some disparate impacts throughout the state because it would be spread on local assessed values rather than equalizes values. Cabins would receive an exemption equal to 50 percent of their taxable value up to a maximum of $400 of tax.

Property assessment and collection of the tax will continue to occur at the local level but the revenues from the tax would be deposited into the General Fund. The proposal submitted by the Governor also calls on the levy of $470.4 million in 2002 to increase annually by the rate of inflation with a two-thirds super-majority of the Legislature being required for larger increases.

Figure 26

Fiscal Summary: Class Rate Reform and General Tax Relief
(Dollars in thousands)

Provision	FY 2002	FY 2003	FY 2004	FY 2005
New Homestead Credit	0	($362,372)	($382,030)	($393,491)
New Ag Land Credit	0	(20,953)	(22,067)	(22,729)
Increase PTR Payments	0	(23,100)	(24,100)	(26,000)
TIF Grant Aid	0	(65,600)	(65,600)	(65,600)
Eliminate TIF Aid Penalties	0	(5,400)	(5,400)	(5,400)
Other Interactions:				
PTR Targeting Offset	0	1,100	1,200	1,400
PTR Offset	0	15,300	15,500	15,300
Disparity Reduction Aid	0	2,376	2,546	2,643
Subtotal	**0**	**(458,649)**	**(479,951)**	**(493,877)**

Class Rate Reform And General Property Tax Relief

The Governor proposes a total of $407.0 million in net General Fund expenditures in FY 2003 to continue reforms begun by the Legislature several years ago to reduce the disparity between the class rates for different types of property. As summarized in Figure 26 on the previous page , the Governor would create two new tax credits to provide an estimated $362.4 million to homeowners and $21.0 million to farmers in FY 2003 to offset shifts in taxes that would otherwise result from the class rate changes, as well as to provide general property tax relief.

Property Tax Refund (PTR) payments to homeowners would increase by $23.1 million and $65.6 million would be placed in a grant fund to reimburse tax increment finance (TIF) districts for lost revenues due to the reductions in the tax base of existing TIF districts.

As also shown in Figure 26, the interaction of these and other property tax recommendations would reduce General Fund expenditures for three programs due to expected reductions in the tax liabilities of the property taxpayers eligible to receive benefits under those programs. Increases in income tax collections resulting from reduced deductibility is included with income tax provisions.

Class Rate Reforms

Under current law, each parcel of real property is assigned to a class of property with each class of property subject to different class rates and credits depending on the usage of the property. As a result, property tax burdens vary for properties having the same value but different uses, such as business property and residential property.

As summarized in Figure 27 on the next page, the Legislature has been adjusting these class rates and the valuation tiers within property classes to reduce the disparities between the classes. The Governor proposes to continue the compression of class rates to both reduce the number of class rates, as well as to increase the tier valuation limit for residential and cabin properties from $76,000 to $200,000 and for business properties from $150,000 of value to $200,000. All tier valuation limits would be annually adjusted for inflation beginning in July 2001.

Changes to class rates and valuation tier limits alter the relative proportion of total tax base for each class of property. As a result, tax burden shifts away from classes of property that become a smaller proportion of the tax base, such as businesses and cabins, and onto classes of property that become a larger proportion of the tax base, such as lower valued homes. Actual shifts in tax burdens for individual jurisdictions depend on their relative mix of property.

Figure 27

Class Rate Schedule
Tax Payable Years 1997-2002

Property Type	Payable 1997	Payable 1998	Payable 1999	Payable 2000	Payable 2001	Gov. 2002
Residential-Single Family						
Residential homestead and Farm HGA:						
< $76,000[1]	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
$76,000-200,000	2.00	1.85	1.70	1.65	1.65	1.00
> $200,000						1.50
Residential non-homestead single unit:						
<$76,000[1]	2.30	1.90	1.25	1.20	1.20	1.00
$76,000-200,000	2.30	2.10	1.70	1.65	1.65	1.00
>$200,000						1.50
Seasonal recreational residential						
<$76,000[1]	1.75	1.40	1.25	1.20	1.20	1.00
$76,000-200,000	2.50	2.50	2.20	1.65	1.65	1.00
>$200,000						1.50
Residential-Multi-Family						
2-3 Units					2.40%	1.50%
Market-rate apartments (4 or more units)	3.40%	2.90%	2.50%	2.40%	2.40	1.50
Market-rate apartments (small city)	2.30	2.30	2.15	2.15	2.15	1.50
Low-income apartments Class 4d	–	–	1.00	1.00	1.00	0.80
Agricultural						
Agricultural land & buildings:						
<$115,000	0.45	0.40	0.35	0.35	0.35	0.60
$115,000 - $600,000	-.-	-.-	-.-	0.80	0.80	0.60
>$600,000	-.-	-.-	-.-	1.20	0.20	1.00
Non-homestead/Timber	1.50	1.40	1.25	1.20	1.20	1.00
Business Properties						
Commercial/industrial/public utility:						
<$150,000[2]	3.00%	2.70%	2.45%	2.40%	2.40%	1.50%
$150,000-$200,000	4.60	4.00	3.50	3.40 [4]	3.40 [4]	1.50 [4]
>$200,000						2.00

1 First tier limit was $72,000 for payable 1997, $75,000 for payable 1998 and 1999.
2 First tier limit was $100,000 for payable 1997.
3 Class eliminated – properties assigned to other classes.
4 Utility personal property moved from class 5 to class 3a, 2nd tier.

New Residential Homestead and Farm Homestead Credits

To continue a policy of relatively lower property tax burdens for lower valued homes and farms, the Governor proposes two new homestead property tax credits to offset shifts on to homes, particularly lower valued homes, when class rates are reduced disproportionately, including:

- For homesteaded farmland, a credit equal to .0025 multiplied by the market value of the farm up to a maximum of $288. A farm would reach the maximum credit at a market value of $115,200. The credit would increase General Fund expenditures by $21.0 million beginning in FY 2003. The credit would apply to all local taxes and county auditors would certify the credit amounts to the Commissioner of Revenue.

- For all residential homesteads, including the house, garage, and one-acre of farm homesteads, a credit equal to .005 multiplied by the market value of the home up to a maximum credit amount of $330 but with the additional caveat that the amount of credit cannot reduce the total property tax liability below .0085 times the market value. The credit would increase General Fund expenditures by $362.4 million beginning in FY 2003. The credit would apply to all local taxes and county auditors would certify the credit amounts to the Commissioner of Revenue.

How the Residential Homestead Credit Works:

- The maximum credit eligibility is equal to the lesser of .005 multiplied by the taxable market value of the home or $330.

- The minimum tax is equal to .0085 multiplied by the taxable market value of the property.

- A homeowner's property tax liability is reduced by the maximum credit for which they are eligible unless doing so would reduce their final tax liability to below the minimum tax level, in which case the tax liability is reduced to the minimum tax.

The amount of homestead credit would vary by both the market value of the home and the local tax rate. For example, under the Governor's proposal, a home valued at $60,000 would have a taxable value of $30,000. As shown in Figure 28, if the local tax rate was 0.020 the tax liability before credits for this home would be $600. The home would be eligible for a credit up to $300 (market value multiplied by .005 up to a maximum of $330). However, because the credit cannot reduce the final tax amount to below .0085 times the market value, or $510 for a home valued at $60,000, this home would only receive a $90 credit reducing its after-credit tax amount to $510.

As a result of the minimum tax threshold in the Governor's proposal, the owner of a $60,000 home with a tax rate of 0.02 (100% under current law) would pay no additional taxes until the tax rate reached 0.024 (135 percent under current law). While that circumstance may provide an incentive to increase local tax collections to fully capture all available credit eligibility, such an incentive would be limited since once homes reached their maximum credit eligibility then all future tax increases would be born fully by local property taxpayers. In general, as suggested by the examples in Figure 27 on the next page, the circumstance of unused credit eligibility is most likely to occur in areas with both low home values and low tax rates.

Figure 28

Examples of Proposed Homestead Credit

Example 1 – $60,000 Home*
Credit Eligibility = $300
Minimum Tax = $510

Current Law Tax Capacity Rate	Proposed Law Tax Rate Equivalent	Tax Before Credit	Credit	Tax After Credit	"Unused" Credit
100%	.020	600	90	510	210
120%**	.024	720	210	510	90
135%***	.027	810	300	510	0
180%	.036	1,080	300	780	0

Example 2 – $100,000 Home*
Credit Eligibility = $330
Minimum Tax = $850

Current Law Tax Capacity Rate	Proposed Law Tax Rate Equivalent	Tax Before Credit	Credit	Tax After Credit	"Unused" Credit
100%	.02	1,000	150	850	180
118%***	.0236	1,180	330	850	0
120%**	.024	1,200	330	870	0
180%	.036	1,800	330	1,470	0

Example 3 – $150,000 Home*
Credit Eligibility = $330
Minimum Tax = $1,275

Current Law Tax Capacity Rate	Proposed Law Tax Rate Equivalent	Tax Before Credit	Credit	Tax After Credit	"Unused" Credit
100%	.02	1,500	300	1,200	30
107%***	.0214	1,605	330	1,275	0
120%**	.024	1,800	330	1,470	0
180%	.036	2,700	330	2,370	0

* Assumes the homestead is not subject to limited market value and has no value excluded under the this old house program so that market value equals taxable value.
** approximate average statewide tax capacity tax rate for pay 2001 expressed in mills.
*** Reflects the tax rate at which the example property maximizes its credit eligibility.

NOTE: For comparison purposes, average local tax rates for pay 2001 were 118.3% statewide, 115.8% in the metro area, and 122.1% non-metro. Elimination of the general education tax rate would reduce each of these average rates by about 32 percentage points.

Increased Homeowner Property Tax Refunds

The Property Tax Refund (PTR) program provides property tax relief to renters and homeowners whose property tax is high relative to their incomes. Under current law, homeowners and renters who meet certain income limits may apply for refunds equal to the amount of property taxes (defined as 19 percent of rent for renters) that exceeds a certain percentage-of-income less a percentage of that excess (a co-payment amount) which must be paid by the claimant, up to certain maximum refund amounts. For FY 2001, the current law maximum household income limit is $41,820 for renters and $71,700 for homeowners. The maximum refund amounts are $1,190 for renters and $510 for homeowners.

The Governor proposes enhancing the program for homeowners by increasing the maximum refund schedule to be the same as for renters. As a result, the maximum refund amount for homeowners would increase from $510 to $1,190. Because income thresholds and maximum refund amounts are indexed to inflation, maximum refund amounts for both homeowners and renters would increase to $1,230 by the time the proposed change would become effective. The additional homeowner PTR would increase General Fund expenditures by an estimated $23.1 million beginning in FY 2003. No changes would be made to the renter PTR program.

TIF Grant Aid

Elimination of the general education tax rate and the reductions in class rates for businesses would significantly reduce the revenue captured by tax increment finance (TIF) districts throughout the state. For example, the Department of Revenue estimates that TIF revenues would decline by about $119 million statewide in FY 2002.

To help offset reductions in the increments anticipated when districts were created, the Governor proposes an annual appropriation of $65.6 million to the TIF Grant Fund established in 1998. TIF authorities could apply to the Commissioner of Revenue for grants. Grant amounts would be equal to the amount of lost increment for each TIF district that is attributable to the elimination of the general education tax rate and the changes in class rates minus any amount of pooled excess increment available from other districts certified by June 2, 2001. To maintain a consistent level of funding for the Office of State Auditor (OSA) tax increment enforcement responsibilities, the percentage of increment dedicated to the Office would increase from 0.25 percent to 0.34 percent.

Eliminate TIF Penalties – Under current law, TIF districts–for which certification was requested after May 1, 1990–are required to contribute, either from general funds or by reduced state aid payment, a certain percentage of tax increment to offset the impact captured tax capacity has on the distribution of state aids. The percentage of penalty depends on the type of district and penalty amounts are used to adjust statewide aid appropriations before certification and distribution. The Governor eliminates this penalty provision in light of the state aid changes being proposed and the overall reduction in TIF revenues resulting from class rate changes and the elimination of the general education tax rate.

State Property Tax Aids

Approximately $1.1 billion in aid will be paid to local governments in FY 2001 through a variety property tax aid programs intended to reduce the amount of property tax revenue that would otherwise be collected to fund local services. Two programs–the Homestead and Agricultural Credit Aid (HACA) program and Local Government Aid (LGA) program–account for over 80 percent those aid payments. In FY 2001, HACA payments all local jurisdictions will total $501.7 million. Payments to cities and towns under the LGA program will total $395.0 million in FY 2001.

More specifically, the Governor proposes:

- eliminating HACA payments to all local governments except for counties;
- reducing county HACA in exchange for the state agreeing to assume the cost of funding services in two areas; court administration and child out-of-home placement;
- eliminating the existing LGA program and replacing it with a new LGA funding formula.

The Governor also proposes eliminating the attached machinery aid program and increasing low-income apartment aid.

Homestead and Agricultural Credit Aid (HACA)

As summarized in Figure 29 on the next page, the Governor proposes reducing HACA payments by a total of $355.1 million in FY 2001 of which: $84.7 million of county HACA would be offset by state expenditure increases in other programs; $53.6 million of the city HACA eliminations would be added to the LGA payments; $14.6 million would be used to increase town LGA payments; and the remaining $202.2 million would help offset the cost of state assumption of the general education levy and other proposed changes.

HACA payments are not related to a jurisdiction's fiscal need or fiscal capacity. Rather, HACA was created in 1990 to replace the homestead credit program and payment amounts are derived from the credit amounts paid under that program, as well as subsequent adjustments that have been made to hold taxpayers harmless from shifts due to tax base restructuring throughout the 1990's. Virtually all non-school taxing jurisdictions and some school districts receive HACA but HACA payment amounts are frozen with the exception of county HACA which increases annually based on a county household growth factor.

HACA Eliminations – Under the Governor's proposal, HACA payments to all jurisdictions other than counties–including both regular HACA and mobile home HACA–would be eliminated. While increases in other aid programs for some jurisdictions may partially offset reductions in HACA, the fiscal impact of the proposed changes is likely to vary widely for individual jurisdictions.

- School Districts – All HACA payments to schools would be eliminated beginning in FY 2003. The change would reduce school revenues by a total of $11.9 million statewide, including $8.0 million in regular HACA and $3.9 million in mobile home HACA. Under current law, as reflected by the declining HACA amounts for schools in Figure 27, HACA payments to school districts is already being phased out.

- Cities – The elimination of all HACA payments to cities beginning in FY 2003 would reduce city revenues by a total of $200.8 million statewide, including $199.4 million for regular HACA and $1.4 million in mobile home HACA. Those reductions would be somewhat offset for certain cities by an overall increase of $53.6 million in city LGA payments. For nonmetropolitan cities the amount of HACA exceeding 8 percent of each city's tax capacity would be added to that city's LGA payment. If a nonmetropolitan city's HACA payment is 8 percent or less of the city's tax capacity then all HACA would be eliminated and no change would be made to the city's LGA aid base.

- Towns – The elimination of all HACA payments to towns beginning FY 2003 would reduce town revenues by a total of $29.3 million statewide. Those reductions would be partially offset by an increase of $14.6 million statewide in increased town LGA payments.

- Special Taxing Districts – The elimination of all HACA payments to special taxing districts beginning in FY 2003 would reduce special taxing district revenues by $28.3 million. As a result, special taxing districts would receive no general purpose state aid.

In estimating the impact that these and other local government aid changes would have on local property taxpayers, the Department of Revenue assumed that any reduction in state aid revenue would increase the property tax levy for that district on a dollar for dollar basis. Correspondingly, any increase in aid revenue was assumed to result in a decrease in the property tax levy for that local government on a dollar for dollar basis.

Figure 29

Fiscal Summary: Homestead and Agricultural Credit Aid (HACA)

(in thousands)

Provision	**FY 2002**	**FY 2003**	**FY 2004**	**FY 2005**
Eliminate School HACA	0	$7,972	$5,973	$3,944
Eliminate City HACA	0	199,374	199,374	199,374
Eliminate Town HACA	0	29,259	29,259	29,259
Eliminate SD HACA	0	28,713	28,713	28,713
Eliminate Mobile Home HACA	0	5,072	5,460	5,464
County HACA Reduction	0	84,676	84,867	85,060
Family Preservation Aid Increase	0	(10,000)	(10,100)	(10,201)
Subtotal	0	345,066	343,546	341,613
Related Non-Tax Bill Provisions:				
Increased Court Appropriation	0	(9,100)	(9,100)	(9,100)
Increased DHS Appropriation	0	(67,364)	((67,364)	(67,364)

County HACA Reductions

Consistent with his preference for eliminating undesignated transfers in favor of state assumption of costs for services required by the state and/or federal government, the Governor proposes reducing county HACA payments by $84.7 million in FY 2003 in exchange for state assumption of court costs, family foster care costs, and an increase in Family Preservation Aid.

Court Costs – As enacted by Chapter 243, 1999 Laws of Minnesota, the state has already agreed to assume funding responsibility for various court services in all judicial districts, including costs for guardians *ad litem*, court interpreters, Rule 20, civil commitment examinations and hearings, and in forma paupers costs. However, because state assumption of those functions for counties in judicial districts one through four,

six, and ten do not become effective until July 1, 2001, the funding necessary to effectuate the takeover was not included in Chapter 243. The Governor proposes appropriating an additional $9.1 million to the state court administrator beginning in FY 2002 and reducing HACA payments to the relevant counties by equivalent amounts beginning in FY 2003.

Child Family Foster Care – The Governor also proposes to have the state assume funding responsibility for child family foster care services. To fund the state takeover, the Governor appropriates an additional $67.4 million beginning in FY 2003 to the Department of Human Services (Language in the Health and Human Service Finance Bill) with county HACA being reduced by equivalent amounts. As proposed, the DHS appropriation does not include any growth even though it appears the provision would become a forecasted item with costs likely to grow. The amount of HACA reduction for individual counties would be equal to the state court administrators estimate of county expenditures on the relevant court services for 2001 plus the county's 1999 non-federal expenditures for child family foster care.

Family Preservation Aid – Because Family Preservation Aid must be used for dedicated purposes–out-of-home placement and family preservation services–the Governor proposes reducing undesignated HACA payments by $10 million beginning in FY 2003. The exchange would reflect a dollar-for-dollar exchange for the affected counties.

The increase in state expenditures exceeds the total of all county HACA reductions by $1.8 million because two counties–Koochiching (about $200,000) and Beltrami (about $1.6 million)–receive too little HACA to fully offset the takeover of expenditures for child family foster care services. As a result, these counties will realize a net benefit from the takeovers since their county expenditures will decline by more than their HACA revenues.

Local Government Aid (LGA)

The Governor recommends eliminating the existing LGA program for cities and towns and replacing it with a new LGA program. As summarized in Figure 30 on the next page, these changes would result in a net increase in LGA payments of $68.2 million in 2002 (FY 2003), including an increase $14.6 million in payments to towns and an increase of $53.6 million in payments to cities. However, those changes must be considered in the context of various other changes proposed to other aid programs, including the elimination of county and city HACA and the conversion of a portion of city HACA for nonmetropolitan cities into LGA.

In addition, as also shown in Figure 30, the Governor proposes a one-time shift forward in the timing of LGA payments. Specifically, the first one-half of a city or town's LGA payment would be made on June 20 rather than July 20 as under current law. The change would result in a one-time expenditure shift of $255.2 million from FY 2004 into FY 2003. The payment date for second-half payment would change from December 20 under current law to December 15 but would have no state fiscal impact.

New City LGA Formula

Cities are expected to receive $418.3 million in LGA and $200.8 million in HACA in 2002 (FY 2003), or $619.1 million together. The Governor proposes eliminating HACA and increasing LGA payments to $472.0 million in 2002 (FY 2003) but changing how those funds are distributed.

Figure 30

Fiscal Summary: Local Government Aid (LGA)

(in thousands)

Provision	FY 2002	FY 2003	FY 2004	FY 2005
Eliminate City LGA	0	$418,340	$429,213	$442,201
Eliminate Town LGA	0	3,856	3,956	4,059
New City LGA	0	(471,963)	(491,393)	(511,850)
New Town LGA	0	(18,464)	(18,953)	(19,450)
Subtotal	*0*	*(68,231)*	*(77,177)*	*(85,040)*
LGA Payment Schedule Shift	0	(255,200)	0	0
New Subtotal	*0*	*(323,431)*	*(77,177)*	*(85,040)*

Under current law, the $418.3 million appropriation for cities in 2002 (FY 2003) would be distributed through a two-part mechanism. The first part, referred to as the city aid base or "grand fathered" aid, distributes $328 million to cities in the same amount as in the previous year. The second part, referred to as "formula" aid, will distribute the remaining $90.3 million based on a somewhat complicated formula in which the aid amount is equal to a percentage of the difference between a "city's need" and its "ability to pay," each of which are described more fully in various publications available from House Research.

A new "sprawl factor" for qualifying nonmetropolitan cities, including Duluth, would enhance aid amounts based on the population of cities, towns, and unincorporated areas within 5 miles.

The Governor proposes to divide the $472.0 million appropriation into three pots, including: $184.1 million distributed among Minneapolis, St. Paul, and Duluth; $51.9 million distributed among all other metropolitan cities; and $236.0 million distributed to all nonmetropolitan cities other than Duluth. By comparison, under current law, Minneapolis, St. Paul, and Duluth would receive $156.9 million; other metropolitan cities $53.0 million; and nonmetropolitan cities $213.9 million. Each pot would be distributed according to a new formula with the appropriations increased each year based on the existing inflation factor–the implicit price deflator for government services but not more than 5% or less than 2.5%–plus a new household growth factor.

In general, formula aid for all cities would be equal to a percentage of the difference between an average basic expenditure amount per capita for the core services of streets and public safety and a minimum required tax rate of 17 percent of each city's tax capacity per person, multiplied by its population. Average basic expenditure amounts were derived from an analysis of 1998 data collected by the Office of State Auditor with separate amounts proposed for: Minneapolis, St. Paul, and Duluth; all other metro cities; all nonmetropolitan cities having populations of 5,000 persons or more; and all other nonmetropolitan cities except for Duluth. The average expenditure amounts are subject to an annual inflation factor.

The first class cities of Minneapolis, St. Paul, and Duluth and all other metropolitan cities will receive aid strictly on the basis of the formula beginning in 2002. None of these cities would receive any "grand fathered" aid after 2001.

Non-metropolitan cities will continue receiving "grand fathered" aid but the amounts of such aid will be recalculated and will be phased out by 2007. The new grand fathered aid for nonmetropolitan cities will be equal to the sum of 90 percent of each cities total 2001 LGA (both the grand fathered portion and the formula portion) plus the portion of its HACA payment that is greater than 8 percent of the city's tax capacity. Fifteen percent of the new grand fathered aid amount would be phased out each year for 6 years with all nonmetropolitan aid being distributed via the new formula by 2007.

Metropolitan cities, not including Minneapolis and St. Paul, would also be subject to a new "density factor," that would be used to adjust the average expenditure amount for metro cities. The density factor would have the effect of reducing aid for metropolitan cities that have an average residential density below the metropolitan average, not including Minneapolis and St. Paul, and would increase aid for metropolitan cities have an average residential density greater than the metropolitan average, not including Minneapolis and St. Paul.

A new "density factor" for metro area cities, other than Minneapolis and St. Paul, would reward more densely populated cities and diminish aid for less densely populated cities.

Nonmetroplitan cities having a population of 5,000 or more would be subject to a new "sprawl factor" which would increase aid for communities that have higher population levels near their borders.

Finally, it should be noted that the Governor's proposal eliminates all special law permanent adjustments that have been made to the city aid base for selected cities.

New Town LGA Aid

Under current law, in calendar year 2002 (FY 2003), towns are expected to receive $29.3 million in HACA and $3.9 million in LGA, or $33.2 million between the two aid programs. The Governor proposes to eliminate all HACA payments to towns but to increase LGA payments to $18.5 million in calendar year 2002 (FY 2003).

Currently, the aid a town receives is equal to its aid in the previous year multiplied by the appropriate inflation rate. Under current law, a town only receives LGA payments if it had levied in the previous year a tax rate of at least .008. Under the Governor's proposal any city that did not levy a tax rate of at least .008 in 1993 is permanently excluded from receiving aid under the LGA program.

The new formula proposed by the Governor would allocate the Town LGA appropriation among eligible towns based on a two-part formula:

- 50 percent, or $9.238 million in 2002, would be distributed on a per capita basis with each eligible town receiving $9 per person; and

- 50 percent, or $9.238 million in 2002, would be distributed according to a formula intended to ensure that the citizens of each town make a minimum contribution toward town services based on the towns relative tax capacity per person–specifically, each town would receive an amount equal to $81, less 10 percent of the town's non-agricultural tax capacity per person, multiplied by the population of the town.

If the amounts to be allocated under the two parts of the formula were to exceed the total appropriation for town LGA, the amounts distributed through the tax capacity part of the formula would be reduced as necessary. The amount a town receives in aid would increase annually by the appropriate inflation rate plus a household growth factor.

Based on the eligibility criteria, eight townships would not qualify for aid. Six townships would not qualify because they were levying less than .08 of tax capacity in 1993, including: Lima and Wahnena Townships in Cass County; LaPrairie Township in Clearwater County; Schroeder Township in Cook County; unorganized Marshall County; and Hickory Township in Pennington County. Two townships and any existing unorganized areas would not be eligible for aid payments because they did not exist in 1993, including Little Elbow Township in Mahnomen County and Camp 5 Township in St. Louis County.

Only towns that levied a tax rate of at least .008 in 1993 would be eligible for town aid.

Other Aid Programs and Miscellaneous Provisions

As summarized in Figure 31, the Governor proposes changes to two other General Fund aid programs.

Figure 31

Fiscal Summary: Other Aid Programs

(Dollars in thousands)

Provision	FY 2002	FY 2003	FY 2004	F 2005
Eliminate Attach. Mach. Aid	0	$3,218	$3,218	$3,218
Low-income Apt. Aid	0	-70	-106	-141
Subtotal	***0***	***3,148***	***3,112***	***3,077***

- Expansion of Low Income Apartment Aid for New Construction–To provide additional incentive for the construction of new low-income housing, the Governor proposes increasing low-income apartment aid for new construction by $70,000 in FY 2003. Aid levels would increase from 1.5 times the tax capacity of qualifying new construction to about 2 times the tax capacity of qualifying new construction. The aid applies only to new low-income housing for which construction began after January 1, 1999, and does not apply to low-income housing aid also provided in law to qualifying housing that existed prior to that time.

- Elimination of Attached Machinery Aid–The Governor proposes eliminating this program which would reduce General Fund expenditures by $3.2 million in FY 2003. Of the $3.2 million, $0.8 million is paid to a variety of school districts and $2.4 million paid to 13 counties.

This aid program was originally established to hold communities harmless from the elimination of the personal property tax on attached machinery and primarily affected jurisdictions with large paper milling operations. The amount of attached machinery aid a school district or county receives has been frozen.

As shown in Figure 31, while the aid amounts to less than 1 percent of general fund revenues for most counties, for three counties the aid represents a substantial component of their overall funding. Counties, however, may use the aid amounts received under this program for any purpose.

Finally, the Governor seeks $480,000 in FY 2002 and $448,000 in FY 2003 for ongoing appropriations for the Department of Revenue to enhance property tax education efforts and to ensure assessment uniformity, to measure the quality of assessments, and implement minimum assessment accountability standards.

Figure 31
Attached Machinery Aid by County and Percent of County GF Revenue

County	2000 Aid	% of 2000 GF Revenue
Anoka	90,099	0.13%
Blue Earth	65,317	0.37
Carlton	490,939	3.72
Clay	72,233	0.62
Crow Wing	52,568	0.28
Dakota	375,772	0.63
Itasca	409,373	2.93
Koochiching	487,627	11.08
Mower	49,748	0.45
Polk	65,167	0.93
Scott	76,204	0.31
Stearns	46,227	0.46
Washington	100,513	0.16
Total	2,381,787	0.74

Property Tax Provisions With No State Cost

- *Non-Profits Public Safety Fee* – Cities and counties would be authorized to assess a fee on property owned by institutions of purely public charity--other than burial grounds, public and private schools and post-secondary institutions, churches, and church property--to help offset the cost of providing public safety services to those properties. The fee, if adopted, could not exceed 75 percent of the local city or county tax rate multiplied by the ratio of the jurisdictions public safety expenditures to its total expenditures and would need to be uniform throughout the city or county and;

- *Transportation Utility Fee* – Municipalities would be authorized to impose a transportation utility fee the proceeds of which could only be used to fund road and bridge projects listed in a master plan. Fee amounts must be uniform and based on trip generation rates for each type of property.

- *Metropolitan Council Transit Levy Authority* – The metropolitan council's levy authority for transit purposes is increased by $17.4 million for 2002 only and then permanently increased by $11.5 million beginning in 2003.

- *Limited Market Value (LMV) Sunset* – Under existing law, limited market value for homesteads, cabins and farmland sunsets after assessment year 2001 (taxes payable in 2002). The Governor allows the sunset to become effective but specifies that any market value being excluded from taxable value under current law be added back to the properties taxable value in three equal installments in assessment years 2002 through 2004 (taxes payable years 2003 through 2005).

- *Local Fiscal Impact Note Costs* – Under current law, the chair or ranking minority members of the Senate and House Tax Committees can request that the Department of Finance work with local governments to develop an estimate of the local fiscal impact of proposed state legislation. Further, the costs of completing such notes, up to a maximum of $200,000, is deducted evenly from city and

county HACA payments before distribution amounts are certified. Because city HACA is being eliminated, the Governor proposes having all administrative costs up to $200,000 deducted from county HACA.

- *Mill Rates* – the Governor proposes to replace the existing system of tax capacities and tax rates, with assessed value rates and mill rates.

- *Pollution Control Equipment Exemption* – The Governor would expand the definition of pollution control equipment that may qualify for an exemption from the personal property tax paid by utilities.

In-Lieu of Property Taxes - Motor Vehicle Registration Tax

Proceeds from the motor vehicle registration tax (MVRT), sometimes referred to as 'tab fees," are constitutionally dedicated to the Highway User Tax Distribution Fund (HUTDF). The Governor recommends:

- phasing in further reductions in the MVRT for passenger vehicles until all vehicles pay a maximum of $75 beginning in calendar year 2004;

- beginning the dedication of motor vehicle sales tax revenues to the HUTDF–enacted last session to replace lost MVRT revenues due to the tax cut–in FY 2002 rather than FY 2003;

- increasing the percentage of motor vehicle sales tax revenues dedicated to the HUTDF to reflect the Governor's proposal to reduce the sales tax rate from 6.5 percent to 6.0 percent; and

- further increasing the dedication percentage of motor vehicle sales tax revenues to the HUTDF to replace expected MVRT revenue losses due to the additional tax reductions.

Prior to FY 2001, the amount of MVRT tax for passenger vehicles was equal to a base tax of $10 plus an ad valorem tax amount equal to 1.25 percent multiplied by the original value of a vehicle subject to a depreciation rate based on the age of the vehicle and a maximum tax of $35 for vehicles older than 10 years. As enacted by Chapter 490, 2000 Laws of Minnesota, the tax was reduced to the lesser of the ad valorem tax amount or a maximum of $189 for the first renewal or $99 for any subsequent renewal.

Under the Governor's proposal, the maximum for any initially registered vehicle prior to the end of its first year of vehicle life would be $189–no vehicle would pay more than $189 under any circumstances–and after the first year of vehicle life the maximum tax would be reduced from $99 to $89. Those provisions would become effective beginning December 31, 2001. Further, on January 1, 2004, the maximum tax for every vehicle would become $75. Note however, that a vehicle could pay between $75 and $35, the current minimum tax, if the amount they would owe under the ad valorem tax was less than $75.

Figure 32 summarizes General Fund and HUTDF impacts of the various Governor initiatives. While making sense of the changing percentages of dedicated motor vehicles sales tax revenues to the HUTDF can be somewhat tricky, the general concept is as follows:

- In FY 2002, the 39 percent dedication reflects the level needed replace the $161.7 million General Fund transfer appropriated under existing law to the HUTDF related to passenger vehicle tab reductions enacted last session plus the amount needed to offset the costs of 6-months of additional tab fee reductions recommended to begin after December 31, 2001, or the second-half of the fiscal year.

- In FY 2003, the percentage increase reflect the full fiscal year MVRT revenue losses attributable to the tab reductions which become effective after December 31, 2001.

- In FY 2004, the increase from 50 percent to 55 percent reflects the additional cost for one-half fiscal year for the final stage of the proposed reduction to a maximum tax of $75.

- In FY 2005, the increase from 55 percent to 61 percent reflects the full fiscal year cost for the final stage of the proposed reduction to a maximum tax of $75.

Figure 32

Fiscal Summary: Local Government Aid (LGA)

(in thousands)

General Fund Provisions	**FY 2002**	**FY 2003**	**FY 2004**	**F 2005**
Repeal Current Appropriation	$161,723	0	0	0
Increase MV Sales Tax Transfer to HUTDF	(202,723)	(85,000)	(120,000)	(156,000)
Net General Fund Impact	(41,000)	(85,000)	(120,000)	(156,000)
HUTDF Provisions	**FY 2002**	**FY 2003**	**FY 2004**	**FY 2005**
Repeal Current Appropriation	($161,723)	0	0	0
New Tax Reduction	(41,000)	(85,000)	(120,000)	(156,000)
Increased MV Sales Tax Transfer from GF	202,723	85,000	120,000	156,000
Net HUTDF Impact	**0**	**0**	**0**	**0**
Dedication Percentage	**FY 2002**	**FY 2003**	**FY 2004**	**FY 2005**
Current Law	n/a	32%	32%	32%
Proposed Law	39%	50%	55%	61%

All of these percentages are based on the November 2000 forecast for motor vehicle sales tax revenues, as well as the Governor's proposal to reduce the sales tax rate from 6.0 percent to 6.5 percent, and may change when the February 2001 forecast is released. Finally, it should be noted that Transportation Finance proposal includes $11.725 million General Fund transfer to the Highway User Tax Distribution Fund (HUTDF) to cover a deficiency resulting from the motor vehicle registration tax reductions enacted during the 2000 legislative session being implemented one month earlier than intended due to an inconsistency between effective date specified for implementing the reduction and existing statutes.

Excise Taxes

The Governor proposes to transfer 85 percent of all cigarette tax revenues to the Health Care Access Fund, beginning in FY 2004, as well as to make changes in how the Mortgage Registry and Deed Taxes are calculated.

Figure 33

Excise Taxes (dollars in thousands)						
Tax Provision	FY 2002	FY 2003	**FY 2002-03**	FY 2004	FY 2005	**FY 2004-05**
Transfer 85% of cigarette taxes to Health Care Access Fund	$ 0	$ 0	**$ 0**	($141,300)	($141,300)	**($282,600)**
Total: Excise Taxes	**$0**	**$0**	**$0**	($141,300)	($141,300)	**($282,600)**

Mortgage Registry Tax

The Governor proposes amending existing law to specify that the amount of tax owed is equal to the tax rate of .0023 multiplied by the value of the debt secured by the mortgage rather than 23 cents per $100 or fraction of the debt secured. Under current law, this tax is collected by counties which retain 3 percent of the proceeds and remit 97 percent of the proceeds to the state General Fund. In FY 2000, the Deed and Mortgage Registry taxes together generated $141.4 million for the state General Fund. The proposed revision will not change the amount of tax owed or collected.

Deed Tax

The Governor proposes amending existing law to specify that the amount of tax owed is equal to tax rate of .0033 multiplied by the net consideration rather than $1.65 for each $500 or fraction of the net consideration. Under current law, this tax is collected by counties which retain 3 percent of the proceeds and remit 97 percent of the proceeds to the state General Fund. In FY 2000, the Deed and Mortgage Registry taxes together generated $141.4 million for the state General Fund. The proposed revision will not change the amount of tax owed or collected.

Gambling Taxes

Figure 34 summarizes changes to gambling taxes. The old and new tax rates are shown in Figure 35.

The combined receipts tax brackets have remained unchanged since the tax was enacted in 1989, so the bracket changes are proposed to offset the impact of inflation. The reduced tax on bingo is proposed because it is the most expensive form of gambling to operate. The shift of paddlewheel and raffles to the combined receipts tax is proposed to eliminate any tax-induced shift from other forms of gambling toward these forms.

Figure 34

Gambling Taxes						
Tax Provision	FY 2002	FY 2003	FY 2002-03	FY 004	FY 2005	FY 2004-05
Reduce tax on bingo from 8.5% to 5%	($485)	($540)	($1,025)	($540)	($540)	($1,080)
Subject paddlewheel & raffle games to combined receipts tax (not 8.5% tax)	480	530	1,010	530	530	1,060
Raise each of the gross receipts tax brackets by $200,000	(5,500)	(6,000)	(11,500)	(6,000)	(6,000)	(12,000)
Subtotal: Gambling Taxes	($5,505)	($6,010)	($11,015)	($6,010)	($6,010)	($12,020)

Figure 35

Changes in Lawful Gambling Taxes		
Type of Tax	Previous Tax Rate	New Tax Rate
Bingo	8.5% of gross profit	5.0%
Paddlewheel and raffles	8.5% of gross profit	Subject to combined receipts tax
Pulltabs and tipboards	1.7% of ideal gross	No change
Combined receipts tax* 1.8% of receipts between plus 3.4% of any additional receipts between plus 5.1% of any additional receipts over	 $ 500,000 $ 700,000 $ 900,000	 $ 700,000 $ 900,000 $1,100,000

*For example, the tax paid by an organization with gross receipts of $1,500,000 would fall from $41,400 to $31,200.

Other Miscellaneous General Fund Taxes and Expenditures

Solid Waste Management Tax

The Governor proposes imposing a use tax liability on generators and self-haulers where the waste management tax is either not charged or not received because the waste is either hauled out of state or the service is being provided by an out-of-state hauler. The Commissioner of Revenue would have the authority to assess generators and self-haulers according to existing tax rates.

Under current law, the greater of $22 million or 50 percent of the proceeds from this tax are deposited into the Solid Waste Management Fund administered by the Public Utilities Commission and the remainder is deposited into the state General Fund. The proposed change is estimated to increase both General Fund revenues and Solid Waste Management Fund revenues by $83,000 each in FY 2002. In FY 2000, this tax generated a total of $53.5 million.

Mining Taxes

The Governor would make changes to two minerals taxes, including revising the occupation tax rate to ensure parity for any new mining companies that might locate to the state and reducing the taconite production tax by a level commensurate with the property tax relief proposed for other business properties in the state.

Taconite Production Tax

The Governor proposes reducing the taconite production tax rate from $2.173 per taxable gross ton, which would increase by an appropriate inflation rate in 2002, to $1.956 per taxable gross ton. The expected reduction in production tax revenues would be offset by having the state General Fund distributions to qualifying iron range school districts rather than production tax revenues. The school aid distributions being taken over by the General Fund are not subject to statutory inflation and would increase General Fund expenditures by $8.8 million annually beginning in FY 2003.

The taconite production tax is a severance tax paid on the annual tonnage of taconite concentrates or pellets produced by taconite mining companies. The tax is paid in lieu of property taxes on taconite and lands containing taconite. However, mining companies remain subject to *ad valorem* (property) taxes on land and structures not part of active mining operations, such as properties adjacent to active mines, as well as on the value of unmined iron ore and taconite. Nonetheless, the taconite production tax clearly dwarfs other mining company tax liabilities. For example, in 1999, taconite production taxes totaled $93.1 million or 92.9 percent, of the $100.2 million in taxes paid by mining companies.

Occupation Tax

The state constitution requires that the state impose an occupation tax on the business of mining. The tax is in lieu of, and is be computed in accordance with, the corporate franchise (income) tax. The revisions proposed by the Governor would reduce the tax rate from 9.8 percent to 2.45 percent but would change the definition of in-state sales to subject a more of the mining tax base to tax liability. However, the two changes offset each other resulting in non net change in tax amounts for existing mining operations but is intended to ensure a level playing field for any new mining companies that may move into the state.

Under current law, the tax base for the occupation tax begins with the value of the mine subject to changes in mine value, mine depletion, and apportionment according to the same formula as used for the corporate franchise tax–75 percent based on sales, 12.5 percent payroll, and 12.5 percent property–and corporate income tax rate (9.8 percent).

However, because existing mining companies have no in-state sales now, only 25 percent of the tax base is apportioned to Minnesota. By changing the definition of in-state sales to include all sales, all of the tax base would now be subject to the tax but because the tax rate is also being reduced to 25 percent of the previous law (9.8% / 4 = 2.45%), the amount of tax will remain the same. The primary purpose of the change is to encourage new mining initiatives by treating in-state sales and out-of-state sales the same.

In 2000, General Fund revenues from the occupation tax amounted to approximately $2.2 million with only three companies having occupation tax liability. Fifty-percent of those revenues are dedicated to education, including 40 percent for elementary and secondary schools and 10 percent for the University of Minnesota, and of the remaining 50 percent an amount equal to 1.5 cents per taxable ton is appropriated to Carlton and Koochiching counties for property tax relief.

Other

In addition, the Governor would make the following changes:

- Insurance premiums taxes would be paid on a quarterly basis, on the same schedule as other taxes. Current law provides for payment in April, June, and December.
- The automobile self-insurance tax would be repealed.
- The 1-cent bottle tax on distilled spirits and wine would be repealed.
- The petroleum inspection fee would be imposed on the first licensed distributor receiving the petroleum product in Minnesota. Current law allows products originating in other states to avoid this tax.

Figure 36

Other Miscellaneous General Fund Taxes
(dollars in thousands)

Tax Provision	FY 2002	FY 2003	**FY 02-03**	FY 2004	FY 2005	**FY 04-05**
Aid to offset reduced taconite tax	($8,800)	($8,800)	**($17,600)**	($8,800)	($8,800)	**($17,600)**
Waste management use tax	83	95	**178**	100	105	**205**
Pay insurance premiums tax quarterly	(500)	(20)	**(520)**	0	0	**0**
Repeal automobile self insurance tax	(100)	(100)	**(200)**	(100)	(100)	**(200)**
Repeal 1-cent bottle tax	(460)	(500)	**(960)**	(500)	(500)	**(1,000)**
Reform petroleum inspection fee	300	300	**600**	300	300	**600**
Total: Other Miscellaneous Taxes	**($9,477)**	**($9,025)**	**($18,502)**	**($9,000)**	**($8,995)**	**($17,995)**

State Tax Changes Affecting Other Funds

Environmental Fund

As summarized above, the Governor's recommendation to establish a use tax on out-of-state solid waste services provided to Minnesota residents would increase revenues for both the General Fund and the Environmental Fund. Figure 37 reiterates the impact on the Environmental Fund.

Figure 37

Environmental Fund
(dollars in thousands)

Tax Provision	FY 2002	FY 2003	**FY 02-03**	FY 2004	FY 2005	**FY04-05**
Waste management use tax	$83	$95	**$178**	$100	$105	**$205**
Total: Environmental Fund	**$83**	**$95**	**$178**	**$100**	**$105**	**$205**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state.

Highway User Tax Distribution Fund (HUTDF)

The Governor proposes additional reductions to the motor vehicle registration tax for passenger vehicles affecting both the General Fund and the HUTDF. The provisions are discussed above and the cost implications affecting the HUTDF are reiterated in Figure 38. In addition, the Governor also proposes the following changes that would affect the HUTDF.

- Reducing the shrinkage allowance from 3 percent to 2.5 percent, because the current allowance exceeds the actual rate of shrinkage. By making a slightly larger proportion of petroleum subject to tax, this raises revenue.
- Eliminating the up-front exemption for farmers' gasoline purchases. Farmers would still be allowed to file for a refund for off-road gasoline use, just like other businesses.
- Making a one-time appropriation of $140,000 to the HUTDF to administer these two provisions.

Figure 38

Highway User Tax Distribution Fund
(dollars in thousands)

Tax Provision	FY 2002	FY 2003	**FY 02-03**	FY 2004	FY 2005	**FY04-05**
Repeal existing appropriation	($161,723)	0	**($161,723)**	0	0	**0**
New Tax Reductions	(41,000)	(85,000)	**(126,000)**	(120,000)	(156,000)	**(276,000)**
Increased MVST dedication	202,723	85,000	**287,723**	120,000	156,000	**276,000**
Reduce shrinkage allowance	($2,500)	($2,540)	**($5,040)**	($2,590)	($2,640)	**($5,230)**
Repeal up-front exemption for farmers' gasoline purchase	0	0	**0**	0	0	**0**
One-time appropriation to Department of Revenue	($140)	0	**0**	0	0	**0**
Total: Highway User Fund	**($2,640)**	**($2,540)**	**($5,040)**	**($2,590)**	**($2,640)**	**($5,230)**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state.

Health Care Access Fund

The Governor proposes to reduce health care taxes and transfer cigarette taxes to the Health Care Access Fund to replace some of the lost tax revenues.

Figure 39 details the provisions affecting the Health Care Access Fund.

- Repeal the 1 percent premiums tax on nonprofit health plans – Under current law, this tax is zero until January 1, 2003, so there is no revenue impact until FY 2003.
- Repeal the wholesale drug tax – This tax can be avoided by consumers if they purchase drugs from sources outside Minnesota. It adds complexity to the administration of the provider taxes, because they must deduct revenue received from drugs already taxed at the wholesale level. Repeal of this tax will reduce the drug deductions taken by providers, partially offsetting the revenue loss, as shown in Table 28.
- Exempt adult day care centers from the provider tax.
- Transfer 85 percent of all cigarette tax revenue from the General Fund to the Health Care Access Fund, beginning in FY2004.

Figure 39

Health Care Access Fund (dollars in thousands)						
Tax Provision	FY 2002	FY 2003	**FY 2002-03**	FY 2004	FY 2005	**FY 2004-05**
Repeal 1% premium tax on nonprofit health plans	$ 0	($17,594)	**($17,594)**	($33,727)	($35,144)	**($68,871)**
Repeal wholesale drug tax	(16,000)	(34,000)	**(50,000)**	(35,000)	(37,000)	**(72,000)**
Reduction in drug deductions	4,000	10,000	**14,000**	11,000	12,000	**23,000**
Freeze provider taxes at 1.5% rate	(28,000)	(59,000)	**(87,000)**	(62,000)	(64,000)	**(126,000)**
Exempt adult day care centers from provider taxes	(300)	(380)	**(680)**	(400)	(420)	**(820)**
Deposit 85% of cigarette taxes in HCAF beginning FY2004	0	0	**0**	141,300	141,300	**282,600**
Total: Health Care Access Fund	**($40,300)**	**($100,974)**	**($141,274)**	**$21,173**	**$16,736**	**$37,909**

Note: Negative changes represent a cost to the state and positive numbers represent a gain to the state.

Implications for the Health Care Access Fund – The balance in the HCAF is projected to fall under current law. With $141 million less revenue during the 2002-2003 biennium, the balance in the Health Care Access Fund would fall by even more – from a balance of $268 million at the end of FY 2001 to $62 million at the end of FY2003. The Governor proposes to set a required reserve equal to 20 percent of the annual direct appropriation for MinnesotaCare. This would replace the current "federal reserve" (currently set at $150 million)and would equal $39 million in FY 2003.

Starting in FY2004, the influx of cigarette tax revenue would result in an increase the total balance to slightly over $110 million at the end of FY 2005. Cigarette revenues are not expected to grow in future years, however, while MinnesotaCare program expenditures are likely to grow each year. Nevertheless, the balance in the HCAF remains above the amount needed to meet the 20 percent reserve for many years into the future. This is partly due to other changes the Governor proposes on the expenditure side. For example, the Governor proposes to make more low-income children eligible for Medical Assistance, which will reduce the number covered by MinnesotaCare.

For additional information on income, corporate, sales, and health care taxes contact Paul Wilson at 651-296-8405 or paul.wilson@house.leg.state.mn.us. For additional information on property aids and credits, motor vehicle taxes, and other taxes contact Matt Massman at 651-296-7171 or matt.massman@house.leg.state.mn.us