MN HOUSE RESEARCH

Memorandum

To   Tax committee members

From   Sean Williams, Legislative Analyst

Subject   Income tax modeling; Rate cut proposal (H1040DE1)

Executive summary

This memo contains modeling results for H.F. 1040, the delete everything amendment (H1040DE1), which allows a subtraction for 100% of Social Security benefits for individuals with adjusted gross income below $80,000 (married joint) or $62,500 (single/head of household). The subtraction is reduced by 10% for each $4,000 above the phaseout. The amendment additionally allows taxpayers to continue to claim the subtraction allowed under current law, if that amount is greater.

My modeling estimates that the bill would reduce revenues by about $140.8 million in tax year 2023. About 286,600 returns would see an average tax decrease of about $524. These results are based on the November forecast assumptions.

Background: House modeling capabilities

House Research can model some individual income tax proposals using the House Income Tax Simulation (HITS) model, version 7.2. The model uses a stratified sample of 2019 individual income tax returns, and forecasts changes in tax years 2021 to 2027 based on the February forecast from Minnesota Management and Budget (MMB).

The House, Senate, Department of Revenue (DOR), and MMB all use the same model to estimate certain income tax proposals, but DOR has a broader sample of high-income returns than the other agencies. This may result in differences between House Research modeling and DOR revenue estimates.

The model can only estimate tax policy changes if the data needed to model the provision is included on a tax return. All of the data used by the model comes from amounts that taxpayers entered on a state or federal income tax return.

HITS model estimates are not precise and are subject to several sources of error. The model relies on a sample of income tax records, which introduces sampling error into the estimates. Estimates for years outside of the sample year are based on the February economic forecast produced by MMB—this introduces forecasting error into the model. For some tax system components for which the model does not have precise data, the model uses imperfect assumptions about taxpayers to interpolate missing numbers; this process also introduces error.

House Research modeling results are preliminary, and cannot replace formal estimates from the Department of Revenue.

Modeling results

The HITS model estimates that the bill would reduce revenues by about $140.8 million in tax year 2023. About 286,600 returns would see an average tax cut of about $524. These results are based on the February forecast assumptions.

Tables 1 and 2 show the distribution of tax decreases by income and size of change.

Table 1: H1040DE1, Distribution by Income
Tax Year 2023

Income (AGI)	Decreases in tax			
	# of Returns	Total ($1,000)	% of Total Decrease	Average Decrease ($)
Under $50,000	70,900	19,800	14.0%	279
$50,000 to $100,000	169,000	113,500	80.7%	672
$100,000 to $150,000	28,700	7,500	5.3%	261
$150,000 to $250,000	0	0	0.0%	0
$250,000 to $500,000	0	0	0.0%	0
$500,000 and above	0	0	0.0%	0
Total	268,600	140,800	100.0%	524

Table 2: H1040DE1; Distribution by Size of Change
Tax Year 2023

$ of Change	Tax Increases		Tax Decreases	
	Returns	% of Total Returns	Returns	% of Total Returns
1 to 25	0	0	8,300	0.3
26 to 50	0	0	5,200	0.2
51 to 100	0	0	14,600	0.5
101 to 250	0	0	46,500	1.6
251 to 500	0	0	65,700	2.2

$ of Change	Tax Increases		Tax Decreases	
	Returns	% of Total Returns	Returns	% of Total Returns
501 to 750	0	0	55,200	1.9
751 to 1000	0	0	39,100	1.3
1001 +	0	0	34,000	1.1
Total Change	**0**	**0**	268,600	9.1

SW/mc