

House Research Act Summary

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Analyst: Joel Michael
Nina Manzi
Karen Baker
Steve Hinze

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Article 1: Federal Conformity

Overview

Conforms Minnesota's individual income tax and corporate franchise tax to most federal changes enacted from February 13, 2008, through December 31, 2008.

The principal federal changes that Minnesota would conform to are:

- counting nontaxable combat pay as earned income for members of the military for purposes of claiming the earned income credit and working family credit
- allowance of direct transfers to charities from traditional IRAs and Roth IRAs for tax years 2008 and 2009
- extension of the special rule for contribution of conservation property by qualified farmers and ranchers
- apportioning of the exclusion of gain on the sale of an individual's principal residence for time periods after January 1, 2009, when the residence was not used as the principal residence
- extension of various provisions related to depreciation and expensing (does not affect general section 179 expensing or bonus depreciation)
- provision of preferential tax treatment within the Midwestern Disaster Relief Area and within other federally designated disaster areas
- changes requirements for employer-sponsored group health plans to qualify for the employee income exclusion,

Federal changes that Minnesota would not conform to are:

- deduction for teacher classroom expenses
- deduction for higher education tuition expenses
- deduction for qualified computer donations by corporations
- additional standard deduction for property taxes paid
- treatment of certain preferred stock losses as ordinary losses

Waives penalties and interest on employers who fail to withhold taxes on differential pay paid to employees called to active service, for calendar year 2009 only.

- 1 Update of administrative tax provisions.** Adopts federal tax administrative provisions made between February 13, 2008, and December 31, 2008, that Minnesota references for state tax administration purposes under chapter 289A. None of the four federal acts enacted between February 13, 2008, and December 31, 2008, changed federal provisions that Minnesota provisions refer to in chapter 289A.

Effective the day following final enactment.

- 2 Update to federal definition of taxable income.** Adopts all of the federal changes to taxable income effective when the federal changes became effective, for tax year 2008 and following years. The four new federal laws and important changes were:

The Heroes Earnings Assistance and Relief Tax Act, Public Law 110-245, enacted June 17, 2008, made several changes mostly relating to military personnel. Provisions include:

- making permanent the ability of military personnel to count tax-exempt combat

pay as earned income for the purpose of qualifying for the earned income tax credit (and, by reference, Minnesota's working family tax credit), effective in tax year 2008

- modifying requirements and limitations relating to contributions to and distributions from tax advantaged accounts (IRAs, 401Ks, etc.) for members of the military
- imposing income tax on unrealized gain on property as if the property had been sold for fair market value on individuals with net worth over \$2 million and over \$600,000 of unrealized gains who relinquish their U.S. citizenship or terminate long-term residency on or after June 17, 2008

Heartland, Habitat, Harvest, and Horticulture Act of 2008, Public Law 110-246, enacted June 18, 2008, which made a large number of changes to federal agriculture provisions. Provisions with tax consequences include:

- extends the special rule for contribution of conservation property by qualified farmers and ranchers, allowing deduction of contributions valued at greater than 50 percent of the donor's adjusted gross income, effective in tax year 2008
- allows deduction for site-specific actions recommended in management plans for endangered species
- changes the depreciation schedule for race horses from seven years to three years, for horses two years old or younger
- allows like-kind exchange treatment for shares in mutual ditch, reservoir, or irrigation companies (effective June 19, 2008)
- disallows excess farming losses for taxpayers who receive certain federal subsidies

Housing Assistance Tax Act of 2008, Public Law 110-289, enacted July 30, 2008, made changes to federal housing provisions. Provisions with tax consequences include:

- allows an additional standard deduction amount of \$500 for property taxes paid (\$1,000 for married joint filers), effective for tax year 2008 only (*Minnesota would not conform to this deduction; instead an addition to taxable income would be required under section 3*)
- extends the state and local bond interest exemption to bonds guaranteed by federal home loan banks
- excludes from alternative minimum taxable income interest for tax-exempt housing bonds issued for first-time home buyers, moderate income housing, and owner-occupied housing for veterans
- reforms Real Estate Investment Trust (REIT) treatment
- makes changes related to the Gulf Opportunity Zone losses and bonus depreciation

- apportions the exclusion of gain on the sale of an individual's principal residence for time periods after January 1, 2009, when the residence was not used as the principal residence

Emergency Economic Stabilization Act of 2008, Public Law 110-343, enacted October 3, 2008, extended and expanded several pre-existing tax provisions, provided tax relief for federally declared disaster areas and for a designated Midwestern disaster area, included the Mental Health Parity and Addiction Parity Act of 2008, and raised revenue by changing the tax treatment of nonqualified deferred compensation for certain taxpayers. Major provisions include:

- extends the higher education tuition expense deduction of up to \$4,000 to tax years 2008 and 2009 (*Minnesota would not conform to this deduction; instead an addition to taxable income would be required under section 3*)
- extends the additional standard deduction amount for property taxes enacted in the Housing Assistance Tax Act to tax year 2009 (*Minnesota would not conform to this deduction; instead an addition to taxable income would be required under section 3*)
- extends the teacher classroom expense deduction of up to \$250 to tax years 2008 and 2009 (*Minnesota would not conform to this deduction; instead an addition to taxable income would be required under section 3*)
- extends the authorization for individuals age 70½ or older to transfer up to \$100,000 from a traditional IRA or Roth IRA directly to a qualified charity, while excluding that amount from adjusted gross income to tax years 2008 and 2009
- extends preferential treatment of dividends of regulated investment companies to tax years 2008 and 2009
- extends the enhanced deductions for contributions of food inventory, book inventory, and computers to tax years 2008 and 2009 (*Minnesota would not conform to with regard to computers; instead an addition to taxable income would be required under section 4*)
- extends various provisions related to depreciation and expensing, including more generous rules for cellulosic biofuel plant property, refineries, energy efficient commercial buildings, qualified smart electric distribution property, certain reuse and recycling property, 15-year straight-line recovery for leasehold and restaurant improvements, including new restaurant property and improvements to retail property, advanced mine safety equipment, accelerated depreciation for business property on Indian reservations, brownfields environmental remediation costs, qualified film and television productions, and certain farming business machinery and equipment
- provides preferential tax treatment within the Midwestern Disaster Relief Area, including temporary suspension of limits on charitable contributions, and temporary suspension on limits on casualty losses. The area is defined as counties in which a disaster was declared between May 20, 2008, and July 31,

2008; this includes the Minnesota counties of Cook, Fillmore, Freeborn, Houston, Mower, and Nobles.

- allows an additional standard deduction for casualty losses occurring in a federally declared disaster area, for disasters occurring before January 1, 2010 (does not apply to the Midwestern Disaster Relief Area)
- provides more generous expensing and depreciation for 2008 and 2009 federally declared disaster areas, excluding areas in the Midwestern Disaster Relief Area and a similar Kansas Disaster Relief Area
- changes requirements for employer-sponsored group health plans to qualify for the employee income exclusion, as part of the Mental Health Parity and Addiction Equity Act

- 3 Additions to taxable income; individuals.** Requires the extended federal deductions for up to \$4,000 of higher education tuition and up to \$250 of classroom educator expenses to be added to taxable income by individuals. Minnesota did not conform to these deductions in tax year 2007 and the bill continues that treatment permanently (federal law allows these deductions for tax years 2008 and 2009).

Also requires the new additional standard deduction amount for property taxes (\$1,000 for married joint filers, \$500 for other taxpayers) to be added to taxable income. Modifies the definition of standard deduction used in limiting the addition for state income or sales taxes deducted at the federal level to include the new additional amount for property taxes.

- 4 Additions to taxable income; corporations.** Extends the requirement that taxpayers add back the amount excluded from subpart F income at the federal level for tax year 2010; EESA 2008 extended the additional subpart F exclusion to 2010. Also extends the requirement that taxpayers add back the enhanced deduction for donations of computers. Minnesota did not conform to these deductions in tax year 2007 and the bill continues that treatment (federal law allows this deduction for tax years 2008 and 2009).
- 5 Subtractions from taxable income; corporations.** Extends the requirement that taxpayers disregard the additional amount excluded from subpart F income at the federal level when calculating the allowable subtraction for decreases in that income to tax year 2010; EESA 2008 extended the additional subpart F exclusion to 2010.
- 6 Preferred stock losses treated as capital losses.** Directs individual and corporate taxpayers to treat losses on the sale or transfer of certain preferred stock as capital losses for purposes of Minnesota's regular and alternative minimum taxes, and also for calculation of Minnesota net operating losses. EESA 2008 authorized certain financial institutions to treat losses on preferred stock in the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation that was sold or exchanged between January 1, 2008, and September 7, 2008, as ordinary losses rather than capital losses, as a result lifting the limit on the amount of losses that may be recognized in tax year 2008. This section subjects those losses to the limits on recognition of capital losses for state tax purposes, with outstanding amounts carried forward to future tax years.
- 7 Update to other references to the Internal Revenue Code in chapter 290.** Adopts federal changes to federal adjusted gross income used for computing individual alternative minimum tax and determining withholding on wages. FAGI also is the starting point for

calculating household income which is used to compute the dependent care and K-12 education credit for tax year 2008 and following years. The main changes to federal adjusted gross income are described in section 2.

- 8 Household income; dependent care credit.** Adds the disallowed deductions for teacher classroom expenses and tuition expenses to the definition of household income used in calculating the dependent care credit and also the K-12 education credit.
- 9 Household income; property tax refund.** Adds the disallowed deductions for teacher classroom expenses and tuition expenses to the definition of household income used in calculating the homeowner and renter property tax refund.
- 10 Update of references to Internal Revenue Code in the property tax refund chapter.** Adopts the federal changes that affect household income, which uses the definition of federal adjusted gross income as a starting point.
- 11 Federal update; estate tax.** Changes the date through which Minnesota incorporates the federal estate tax from February 13, 2008, to December 31, 2008. Since there have not been any federal changes to the estate tax since the last update, this change does not have any substantive effect.
- 12 Withholding on differential pay; temporary prohibition on penalties and interest.** Prohibits the commissioner from assessing tax penalty or interest against an employer for failure to withhold taxes on wage differentials paid in calendar year 2009 to members of military called to active service. A wage differential is the amount by which the servicemember's civilian pay exceeds his or her military pay; some employers have chosen to voluntarily continue to pay this amount to servicemembers while they are deployed. Federal changes to the definition of "wages" being conformed to in this bill require withholding on differential pay for wages paid after December 31, 2008.

Article 2: Green Acres

Overview

This article makes the following changes to the Minnesota Agricultural Property Tax Law (better known as the “Green Acres” program):

- Allows most land in government-sponsored conservation programs (i.e. RIM, CRP, etc) to be eligible.
- Allows property owners to withdraw a portion of their rural vacant land from the program without withdrawing all of it.
- Provides that rural vacant land grandfathered into the Green Acres program is terminated from the program effective January 1, 2013; much of the terminated land will be able to transition to a new “rural preserve” program with somewhat similar tax benefits; no additional taxes will be collected from properties that transition to the new program.
- Allows rural vacant land to remain in the program until 2013 if sold or otherwise transferred to the owner’s son or daughter, as long as it continues to qualify under the pre-2008 law.
- Provides that property that was enrolled prior to 2008, but that no longer qualifies due to the 2008 changes (class 2b rural vacant land), may be withdrawn from the program prior to May 1, 2010, with no additional back-taxes due.
- Provides a list of various types of transfers that do not constitute a change in ownership and therefore, do not trigger a pay back of additional taxes (i.e. marriages, divorces, etc.).
- Establishes a new Rural Preserve Property Tax program. Requires the owner to have an approved conservation management plan for the property and it must be at least ten acres. Requires a covenant that is binding on the land. Requires land to be enrolled for at least ten years and for the property owner to notify the assessor five years in advance before terminating the covenant. Upon termination, it imposes additional taxes for the last three years the property was enrolled in the program. Effective for taxes payable in 2012 and thereafter.
- Modifies the definition of class 2a property to include interspersed non-productive land.
- Requires the commissioner of revenue to annually report to the house and senate tax committees on agricultural valuation and classification.

- 1 Requirements.** Allows land enrolled in state and federal sponsored conservation programs such as RIM and CRP to be enrolled in Green Acres (other than RIM land subject to a perpetual easement) provided that the land was in agricultural use before enrollment. Also extends the green acres eligibility to certain farm entities that are not regulated under section 500.24. This primarily includes poultry farming in which the majority of the owners are related and at least one of them either resides on the land or actively operates the land.

Effective for assessment year 2009 and thereafter.

- 2 Property no longer eligible for deferment.** Allows property owners to withdraw a portion of their rural vacant land from the program without withdrawing all of it. Allows property that was in the program prior to the 2008 changes but no longer qualifies due to those changes (i.e. rural vacant land) to continue to qualify until the 2013 assessment. This date ties in with the rural preserve program established in section 5. If it is not enrolled in that new rural preserve program within that time period, it must be removed from Green Acres. Also allows rural vacant land to remain in the program until the 2013 assessment, if sold or otherwise transferred to the owner's son or daughter as long as it continues to qualify under the pre-2008 law. Lastly, this section provides that if property enrolled in the Green Acres program is removed from that program and enrolls in the new rural preserve program established in section 5, it is not subject to any additional taxes.
- 3 Additional taxes.** Provides that property that was in the program prior to the 2008 law changes, but that no longer qualifies due to those 2008 changes (i.e. rural vacant land), may be withdrawn from the program prior to May 1, 2010, with no back-taxes due.
- 4 Continuation of tax treatment upon sale or other events.** Clarifies that certain types of property transactions are not to be considered changes of ownership in the Green Acres program, specifically:
- transfer to surviving spouse upon death,
 - divorce of a married couple when one spouse retains ownership,
 - marriage of a property owner when the owner retains full or partial ownership,
 - organization or reorganization of a farm entity if all owners retain the same interest,
 - placement of the property into trust provided the owners are the grantors of the trust and they maintain the same beneficial interest.
- 5 Rural Preserve Property Tax Program.** Establishes a new tax preference program for rural land that meets certain criteria.

Subd. 1. Definitions.

(b) "Conservation management plan" means a written document approved by the soil and water conservation district providing a framework for site-specific healthy, productive, and sustainable conservation resources. Requires the plan to include the following:

1. Conservation management goals for the land;
2. Reliable field inventory of the individual conservation cover types;
3. Description of soil type and quality;
4. Aerial photo or map of the vegetation with the conservation boundaries indicated;

5. Proposed future conditions of the land;
6. Prescriptions to meet proposed future land conditions;
7. Recommended timetable for implementing prescribed practices; and
8. Legal description of land included in the plan.

(c) Provides that the Board of Water and Soil Resources will develop guidelines for conservation management plan preparation and approval.

(d) Provides that the commissioner of revenue is the final arbiter of any disputes over plan approvals.

Subd. 2. Requirements. Provides that land classified as 2a (productive agricultural) or 2b (rural vacant) that was in Green Acres, or that is part of an agricultural homestead, is entitled to valuation and tax deferment under this section if:

1. there are at least 10 acres of land;
2. a conservation management plan has been prepared by an approved plan writer and is being implemented;
3. the land must be enrolled for at least ten years; and
4. there are no delinquent property taxes on the land.

Prohibits real estate enrolled under this section from being enrolled in the Green Acres program, the Open Space program, having a conservation easement, or in the sustainable forest incentive program concurrently.

Provides that if more than 50 percent of the acreage of an agricultural homestead is class 2b, the portion of 2b land in excess of 50 percent may not be enrolled in the program.

Subd. 3. Determination of value. Provides that the value of property qualifying under this section may not exceed the value prescribed by the commissioner of revenue for class 2a tillable property in the county. The house, garage, and surrounding acre and any minor ancillary nonresidential structures, if any, shall be valued according to their appropriate value. Prohibits the assessor from considering the presence of any commercial, industrial, residential, or seasonal recreational land use influences when determining the properties value.

Subd. 4. Separate determination of market value and tax. Requires the assessor to make a separate determination of the market value of property enrolled under this section based on the highest and best use. Also requires the tax based on that value and the appropriate local tax rate to be recorded in the county's property tax records.

Subd. 5. Application and covenant agreement. (a) Requires the application to be filed by May 1 of the year prior to the year in which the taxes are payable. Provides that any application filed and granted shall continue in effect for subsequent years until termination of the covenant agreement under (b). Requires the application

to be filed with the assessor on a form prescribed by the commissioner of revenue. Allows the assessor to require proof that the property qualifies.

(b) Requires owner to sign a covenant agreement that is filed with the assessor and recorded in the county where the property is located. Provides that the covenant must contain:

1. Legal description of area to which covenant applies;
2. Name and address of owner;
3. Statement that land described in covenant must be kept as rural preserve land, which meets requirements in subd. 2 for the duration of the covenant;
4. A statement that the landowner may terminate the covenant agreement by notifying the assessor in writing five years in advance of date of proposed termination, provided that the notice of intent to terminate may not be given before the land has been subject to the covenant for a period of five years;
5. A statement that the covenant is binding on the owner or the owner's successor or assigns, and runs with the land; and
6. A witnessed signature of the owner, agreeing to the covenant to maintain the land.

(c) Provides that after a covenant has been terminated, the land subject to the covenant is ineligible for subsequent valuation under this section for three years after the termination.

Subd. 6. Additional taxes. Requires additional taxes to be paid upon termination of the covenant agreement in an amount equal to the difference between the amount of taxes paid and the amount of taxes that would have been due based on the property's value under its highest and best use for the last three years that the property was valued and assessed under this section. Provides that no interest or penalties shall be levied on the additional taxes if timely paid.

Subd. 7. Lien. Provides that the additional tax is a lien on the property in the same manner as the other taxes that are imposed. Provides that when these additional taxes are collected, they shall be distributed in the same manner as other property taxes.

Subd. 8. Special local assessments. Defers the payment of special local assessments levied after June 1, 2011, on any real property under this section until it no longer qualifies. Requires the amounts to be recorded with the county. Requires that when the property no longer qualifies, all deferred special assessments plus interest shall be due in equal installments spread over the time remaining until the last maturity date of the bonds issued to finance the improvements. If the bonds have matured, the amount is due within 90 days. No penalty is assessed if timely paid. Special assessments levied at any time by a county or district court under chapter 116A (i.e. public waters and sewer systems) or by a watershed district under chapter 103D are not deferred under this subdivision.

Effective for deferred taxes payable in 2012 and thereafter.

- 6** **Class 2.** Modifies and further clarifies the definition of class 2a by stating that assessors “must” include (rather than “may” include) property that otherwise would be classified as class 2b, that is impractical for the assessor to value separately from the rest of the property or that is unlikely to be able to be sold separately. This includes items such as sloughs, wooded wind shelters, acreage abutting ditches, ravines, rock piles and land subject to a setback requirement. Effective for assessments in 2010 and thereafter, taxes payable in 2011 and thereafter.
- 7** **Annual report on agricultural valuation and classification.** Requires the commissioner of revenue to study and annually report to the chairs of the committees on taxes of the house and senate on:
1. Trends in market values of class 2a and class 2b properties;
 2. Green Acres value methodology and determinations; and
 3. Assessment and classification practices pertaining to class 2a and 2b property.