HOUSE RESEARCH

Bill Summary

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Subject: Income tax subtraction for discharge of student loan indebtedness

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Overview

H.F. 882 provides a state income tax deduction for student loans forgiven under certain federal student loan forgiveness programs. The bill is effective beginning in tax year 2017.

Background: Forgiven loans are generally subject to federal income taxes, because discharged debt is included in the Internal Revenue Code definition of gross income. Minnesota conforms to this federal definition, meaning that discharged debt that is subject to federal taxes is also subject to state taxes. Student debt discharged under some federal and state programs is explicitly excluded from the federal definition of gross income, so those programs already qualify for an exemption from state and federal income taxes.

The Pay as You Earn (PAYE) and Revised Pay as Your Earn (REPAYE) programs are income-contingent repayment plans offered by the federal government. Both programs require monthly payments equal to ten percent of a borrower's discretionary income. The PAYE program caps monthly payments at the amount a borrower would owe under a standard, ten-year repayment plan; the REPAYE program does not.

Both programs forgive any remaining balance on a borrower's loan after a borrower makes payments for a certain number of years. In the PAYE program, all loans are forgiven after a borrower makes 20 years of payments. In the

Section

REPAYE program, undergraduate loans are forgiven after 20 years, while graduate loans are forgiven after 25 years.

1 **Discharge of indebtedness; education loans.** Allows a subtraction for student loan indebtedness discharged by the lender following the borrower's completion of an income-driven repayment plan that sets monthly payments based on the borrower's income and family size. Programs covered include the income-based repayment plan, the income-contingent repayment plan, and the PAYE or REPAYE programs.

2 **Definitions.** Allows the same subtraction as is provided in section 1 for the purposes of the state alternative minimum tax.