

# Minnesota's Tax Credit and Subtraction for 529 Contributions

December 2019

## Federal and state tax advantages for section 529 college savings accounts

Investment income on 529 accounts is exempt from both federal and Minnesota income taxes, if the income is used for qualifying higher education expenses. Qualifying expenses include tuition, fees, room and board, books, and some other education expenses. Investment income on the accounts that is used for nonqualifying purposes is taxed as ordinary income, plus a 10 percent penalty. 529 plans also provide special estate and gift tax benefits.

Minnesota allows both a nonrefundable income tax credit and an income tax subtraction for contributions to any state's 529 plan. A taxpayer may claim either the credit or the subtraction, but not both. Any Minnesota resident who makes a contribution to a 529 plan or prepaid tuition plan may claim the credit or subtraction, as long as the individual is not claimed as a dependent. An individual does not need to be the account owner to be eligible to claim the credit or subtraction.

## Minnesota's subtraction for 529 account contributions

Minnesota offers a subtraction for contributions to any state's section 529 Plan. A taxpayer may subtract up to \$1,500 (\$3,000 for married joint filers) of contributions to any state's section 529 college savings plan or prepaid tuition plan. The subtraction excludes any amounts that are rolled-over from other college savings plans. Taxpayers who claim the credit cannot take the subtraction.

### 529 Subtractions Claimed by Minnesota Taxpayers, Tax Year 2017

Income (FAGI, married or single)	Average Subtraction Claimed	Estimated Subtractions Claimed	Share of Subtractions	Estimated Claimants	Share of Claimants
Less than \$50,000	\$956	\$456,000	0.8%	480	1.9%
\$50,000 to \$75,000	\$2,554	\$681,000	1.2%	270	1.0%
\$75,000 to \$100,000	\$1,174	\$491,000	0.8%	420	1.6%
\$100,000 to \$150,000	\$1,559	\$5,112,000	8.8%	3,280	12.7%
\$150,000 to \$200,000	\$2,173	\$15,958,000	27.3%	7,340	28.5%
\$200,000 or Greater	\$2,550	\$35,695,000	61.1%	14,000	54.3%
<b>Total</b>	<b>\$2,265</b>	<b>\$58,393,000</b>	<b>100%</b>	<b>25,790</b>	<b>100%</b>

In tax year 2017, about 25,790 taxpayers claimed the 529 subtraction. In total, taxpayers claimed about \$58.4 million in subtractions. The total revenue lost due to the subtraction is about \$4.1 million, meaning taxpayers who claimed the subtraction paid an average marginal rate of about 7.0 percent. The average taxpayer who claimed the subtraction saw a tax reduction of \$166 as a result of the subtraction.

## Minnesota's tax credit for 529 account contributions

Minnesota's Section 529 Plan Credit is a nonrefundable credit for contributions to a college savings account established by any state under section 529 of the Internal Revenue Code. The credit equals 50 percent of contributions, up to a maximum of \$500. The maximum credit is phased out as income increases with varying thresholds for individuals and married joint filers. The phaseouts for tax year 2019 are described in the table below.

For individual filers, the maximum credit is phased out by 2 percent of federal adjusted gross income (FAGI) in excess of \$78,340. FAGI is a broad definition of income defined in federal law. The credit is fully phased out for individual filers at \$103,340 of FAGI. For married couples filing joint returns, the maximum credit is phased out for taxpayers with FAGI above \$78,340. The credit is reduced by 2 percent of FAGI in two phases, and is fully phased out when FAGI reaches \$166,010.

### 529 Credits Claimed by Minnesota Taxpayers, Tax Year 2017

Income (FAGI)	Average Credit Claimed	Estimated Credits Claimed	Share of Credits	Estimated Claimants	Share of Claimants
Less than \$50,000	\$414	\$459,000	11.8%	1,110	7.4%
\$50,000 to \$75,000	\$409	\$881,000	22.6%	2,150	14.4%
\$75,000 to \$100,000	\$271	\$1,106,000	28.4%	4,090	27.4%
\$100,000 to \$150,000	\$205	\$1,421,000	36.4%	6,950	46.6%
\$150,000 to \$200,000	\$51	\$32,000	0.8%	630	4.2%
\$200,000 or Greater	\$0	\$0	0.0%	0	0.0%
<b>Total</b>	<b>\$261</b>	<b>\$3,899,000</b>	<b>100%</b>	<b>14,930</b>	<b>100%</b>

### Comparison of the credit and subtraction

The credit and subtraction differ in three main ways. First, income limits apply to the credit, but not the subtraction. Second, for the same contribution amount, the credit will typically provide a larger tax benefit than the subtraction. A credit reduces tax liability dollar-for-dollar, while the value of a subtraction depends upon the taxpayer's marginal tax rate. Third, the credit can result in a marriage penalty or bonus, while the subtraction can only provide a bonus.

### What incentives do other states offer for 529 plan contributions

States offer a wide variety of incentives for 529 plan contributions, including income tax deductions, tax credits, and matching grants. In tax year 2017:

- 29 states other than Minnesota and the District of Columbia allowed **tax deductions**
- Two states other than Minnesota (Vermont, and Utah) offered **credits** for 529 contributions
- Seven states with income taxes don't offer 529 plan deductions or credits
- Most states limit deductions to contributions to the state's own plan, but six states (including Minnesota) provide deductions for contributions to any state plan
- Ten states offer **matching grants** of some kind; seven offer matching grants and three offer onetime grants, either at the time of the child's birth or the opening of an account



**MN HOUSE  
RESEARCH**

*Minnesota House Research Department provides nonpartisan legislative, legal, and information services to the Minnesota House of Representatives. This document can be made available in alternative formats.*