

Nebraska's long struggle with high reliance on property taxes to fund K-12 education has been well documented. It's been noted in every major study of Nebraska taxes since 1962 and continues to frustrate taxpayers, legislators and school officials alike. A local option income surtax – such as that proposed in LB 182 -- could reduce our reliance on property taxes by bringing more income tax revenue into the way schools are funded.

What is a local option income surtax?

A local option income surtax is a tax levied by local governments based on the amount of state individual income tax due and generates revenue that goes directly to those local governments. In most cases, the local option income surtax amount cannot exceed a certain percentage of tax liability and voter approval only lasts a certain number of years. With a majority vote of the school board, an income surtax may be put to the ballot in a primary, general or special election. The local income surtax in Iowa is used by 85 percent of the state's public school districts.¹

How does a local option income surtax work?

A local option income surtax is an additional percent of tax applied to tax liability. For example, if a resident of School District A has a state income tax liability of \$1,000² and School District A has imposed a voter-approved local option income surtax of 1 percent, the local option income surtax amount is \$10. The new surtax revenue would be collected along with their income tax and returned to the district to support property tax reduction or to preclude the reliance on more property tax revenue to pay for building construction, remodeling or site acquisition.

The impact of local option income tax on property taxes

A local option income surtax would have varying effect throughout the state in terms of reducing property taxes. For example, a 20 percent surtax could allow the Bennington Public School District to lower its property tax levy by about 39 cents while the Sioux County Public School District could only lower its levy by 1.2 cents. According to the fiscal note for the 2018 iteration of the bill (LB 911),³ a maximum 20 percent income tax surtax levied statewide could lower school district property taxes by 15.6 percent, ranging from 1.9 percent to 35.3 percent for individual school districts.

Local option income surtax and the school funding formula

A local option income surtax wouldn't impact the existing school funding formula but instead provide districts with a separate local funding stream to reduce or preclude

¹ For more information, visit <https://www.legis.iowa.gov/docs/publications/FT/14439.pdf>

² After refundable credits are applied.

³ Nebraska Legislature, "LB 911 Fiscal Note," downloaded from https://nebraskalegislature.gov/FloorDocs/Current/PDF/FN/LB911_20180213-110518.pdf on Feb. 13, 2018.

reliance on property taxes. State support through the Tax Equity and Educational Opportunities Support Act (TEEOSA) would remain the same, regardless of whether schools enact an income surtax. School districts also would still be subject to existing restrictions intended to keep property taxes down, such as property tax levy limits, spending caps that limit how much their budget can grow annually and limits on how much districts can hold in reserve.

If the intended use for a local option income surtax is building construction, remodeling and/or site acquisition, new revenue would be deposited in a Special Building Fund, as currently used when a district decides to acquire or improve sites and/or to erect, alter or improve buildings.⁴ If the intended use is property tax reduction, new revenue would be deposited in a district's General Fund, subject to existing budget authority limits.

Local option income surtaxes can make school funding less regressive

Property taxes are more regressive than income taxes, meaning that low- and middle-income residents pay a greater percentage of their income in property taxes than in income taxes. By introducing a local option income surtax, lawmakers can help reduce our reliance on a regressive tax. This would lighten the K-12 funding load for low- and middle-income Nebraskans.

Conclusion

Property taxes make up the majority of revenue used to support schools in Nebraska and our high reliance on property taxes has long been a sore spot for many in the state. A local option income surtax would give school districts another resource for funding education and help reduce the need to rely so heavily on property taxes. It also would help make school funding more progressive and take some of the load of funding our schools off the plates of low and middle-income residents.

⁴ Nebraska Department of Education, "Program Budgeting, Accounting, and Reporting System for Nebraska School Districts 2017 Users' Manual," <https://2x9dwr1yq1he1dw6623gg411-wpengine.netdna-ssl.com/wp-content/uploads/2017/07/2017UsersManual.pdf>.