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LB 314 – which will be the focus of a Revenue Committee hearing today – would help reduce Nebraska's reliance on property taxes while also protecting our investments in K-12 education and other vital services. By generating about $640 million in new revenue[1] to provide property tax relief and maintain vital investments, LB 314 presents a responsible approach to addressing Nebraska's high reliance on property taxes.

LB 314's sales tax changes

Nebraska's sales tax is out of date and isn't keeping pace with household consumption. Created nearly half a century ago, the state sales tax applies to a wide range of goods but exempts many consumer services despite the fact that our economy has become largely service based.[2] Treating goods different than services has led to inconsistencies in Nebraska's tax code, gives some services preferential treatment over others, and treats goods differently from many services. LB 314 expands the sales tax to include more services. The bill also would increase Nebraska's sales tax rate one half cent from 5.5 cents to 6 cents per dollar.

Income tax changes

Previous tax changes, many of which were income tax reductions, have contributed to the erosion of Nebraska's tax base and increased our reliance on property taxes to fund K-12 education and other services. LB 314 would make multiple income tax changes including eliminating all itemized income tax deductions except for medical expenses. The state increased its standard deduction in response to 2018's federal tax changes but Nebraskans can still reduce their taxes dramatically by itemizing those remaining deductions. This can contribute to higher reliance on property taxes.

LB 314 also would eliminate the s-corp and LLC non-Nebraska income exclusion, which allows Nebraskans to avoid paying income tax on earnings from S-Corporations and Limited Liability Companies that are generated from goods or services sold outside Nebraska, even when the income isn't taxed in another state.[3] LB 314 also eliminates the special capital gains and extraordinary dividends election, which is a one-time tax exclusion that allows Nebraskans to sell stock in their employers' companies without paying state income taxes on the capital gains.[4]

LB 314 would reinstate Nebraska's alternative minimum tax, which was eliminated in 2013, and add a surtax of 7.84 percent on income tax liability for taxpayers with federal

[1] Nebraska Legislature, "LB 314 Fiscal Note," accessed at https://www.nebraskalegislature.gov/FloorDocs/106/PDF/FN/LB314_20190213-133552.pdf on Feb. 14, 2019. The $640 million is the projected amount of revenue that would be generated in FY21.
[2] Nebraska Legislature, "Nebraska Revenue Act of 1967, see Neb. Rev. Statute 77-2701," accessed at https://nebraskalegislature.gov/laws/statutes.php?statute=77-2701 on Dec. 18, 2018.
[3] Nebraska Legislature, "Nebraska Revised Statute §77-2716 (4)," accessed at https://www.nebraskalegislature.gov/laws/statutes.php?statute=77-2716 on Dec. 26, 2018.
[4] Nebraska Legislature, Nebraska Revised Statute §77-2715.09, accessed at https://www.nebraskalegislature.gov/laws/statutes.php?statute=77-2715.09 on Dec. 26, 2018).

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adjusted gross income in excess of $250,000 for individuals and $500,000 for married couples filing jointly.

Property tax expenditure changes

LB 314 would end the personal property exemption, which allows taxpayers to exempt the first $10,000 of tangible personal property value for each tax district in which a personal property return is filed. Tangible personal property is personal property possessing a physical existence, excluding money, and includes trade fixtures, such as machinery and equipment, used directly in commercial, manufacturing, or processing activities conducted on real property.[5] The measure also would repeal the property tax exemption for fraternal benefit societies.

Taxing emerging goods and services

Nebraskans today purchase goods and services that didn't even exist 15 years ago, much less in 1967, when our state's sales tax was implemented. LB 314 would extend Nebraska's sales tax to services like Uber and Lyft and electronic cigarettes, all of which have become more prevalent in Nebraska in recent years.[6] The bill would also close a loophole that allows online travel companies like Priceline and Expedia to remit less in sales tax than hotels do for a room that costs the same to consumers.

Consumption tax changes

Nebraska's tax on cigarettes is below the national average (10th lowest in the nation[7]) and LB 314 would bring it closer to that average while generating a considerable amount of revenue. LB 314 also would increase our taxes on alcohol, which haven't changed since 2003.[8]

Real estate transfer fees

LB 314 would slightly increase the documentary stamp tax, which is a real estate transfer fee. Real estate transfer fees are charged when the title of a property changes hands (unless exempt) and are usually structured as a surcharge imposed by the state or local government that processes the title transfer. The documentary stamp tax started at a rate of $0.55 per each $500 of value in 1965 and has risen gradually to $2.25 per each $1,000 of value.[9] LB 314 would raise it to $2.75.

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[5] State of Nebraska, "Information Guide: Personal Property Exemption, June 2018," accessed at http://www.revenue.nebraska.gov/PAD/infoguide/per_prop_info_guide.pdf on November 7, 2018.
[6] NET Nebraska "Vaping on the rise in Nebraska (October 25, 2013)," accessed at http://netnebraska.org/article/news/vaping-rise-nebraska on Dec. 26, 2018.
[7] Tax Policy Center, "State Cigarette Tax Rates: 2001-2018, August 10, 2018," accessed at https://www.taxpolicycenter.org/statistics/state-cigarette-tax-rates on Dec. 7, 2018.
[8] Nebraska Legislature "LB 759 (2003)," accessed at https://www.nebraskalegislature.gov/FloorDocs/98/PDF/Slip/LB759.pdf on Dec. 22, 2018.
[9] Ibid.

Large portion of revenue goes into the property tax credit while K-12 funding study ensues

LB 314 measure calls for the majority of the new revenue to be added to the Property Tax Credit Fund while a study would be undertaken to review the current system of funding K-12 education in Nebraska. Funding for the study also is included in LB 314. The study would be similar to the one enacted in the late 1980s to help address property tax and school funding concerns. That study led to the creation of our current school finance system -- the Tax Equity and Educational Opportunities Support Act or TEEOSA -- which in its initial years did help reduce property taxes as a share of the economy. Many tweaks have been made to the formula over the years that have contributed to Nebraska again finding itself faced with high reliance on property taxes to fund K-12 and other services. A comprehensive review of school finance can help Nebraska again find a strategy to meaningfully and sustainably address property taxes.

School finance changes include increasing the allocated income tax, special education funding

LB 314 would increase the rate at which Nebraska reimburses school districts to educate special education students from 51 percent to 80 percent. It also would increase the allocated income tax from 2.23 percent to 20 percent. Allocated income tax is state income tax revenue that is diverted back to the district in which it was paid in the form of K-12 aid.

EITC increase, renters credit help low and middle-income earners

LB 314 would increase the Nebraska Earned Income Tax Credit (EITC) – which helps many low- and middle-income earners with children -- from 10 percent to 15 percent of a recipient's federal EITC. This change would lead to an average $118 increase in the refundable tax credit for those who receive it.[10] Increasing the EITC would help offset the regressive effects of other tax changes in LB 314, such as the sales tax rate increase. LB 314 also would provide renters with a credit to help them receive property tax relief and also offset some of LB 314's regressive tax changes.

Conclusion

Nebraska's school funding formula has been adjusted many times since it was implemented in the early 1990s. Most of the adjustments reduced state school funding and resulted in a greater share of Nebraska's K-12 funding load to be shifted onto property taxes. Ironically, the school funding formula was initially implemented to alleviate the state's high reliance on property taxes. Also during this time, the state enacted many tax cuts. The revenue losses caused by these tax cuts led to budget

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[10] U.S. Internal Revenue Service, "Statistics for Tax Returns with EITC," accessed at https://www.eitc.irs.gov/eitc-central/statistics-for-tax-returns-with-eitc/statistics-for-tax-returns-with-eitc on May 7, 2018. To provide this estimate, the average federal credit for NE in 2017 ($2,360) was multiplied by 10 percent to obtain the average state EITC estimate.

issues that lawmakers addressed, in part, by altering the funding formula and reducing state funding for K-12 education. These changes, in turn, contributed to increased property taxes. By increasing state revenue and distributing it in the manner detailed in LB 314, policymakers can substantially reduce our reliance on property taxes to fund schools. Furthermore, by undertaking the school finance study, we can get a comprehensive overview of what is and isn't working regarding our school finance system and we can also determine what changes need to be made to truly alleviate our state's long-running overreliance on property taxes.