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LB970 Tax Relief Package

Allowing Taxpayers to Keep More of the Money They Earn and Making Nebraska More Competitive for New Businesses and Jobs

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Nebraska's Current Tax Climate: The Need for LB970

For a Midwestern state that generally supports low taxes and restrained government spending, Nebraska taxpayers pay excessive taxes. According to the Tax Foundation, Nebraska has the 15th highest state tax burden in the nation, paying an average of $2,842 per capita to state government. When local taxes are included, the amount increases to $3,960 per capita.[1] Nebraska leads its neighbors in high tax rates.[2] LB970, Governor Dave Heineman's tax relief package which was introduced in the Unicameral by State Senator Abbie Cornett of Bellevue, is a sensible proposal to reform Nebraska's tax climate.

LB970 will:

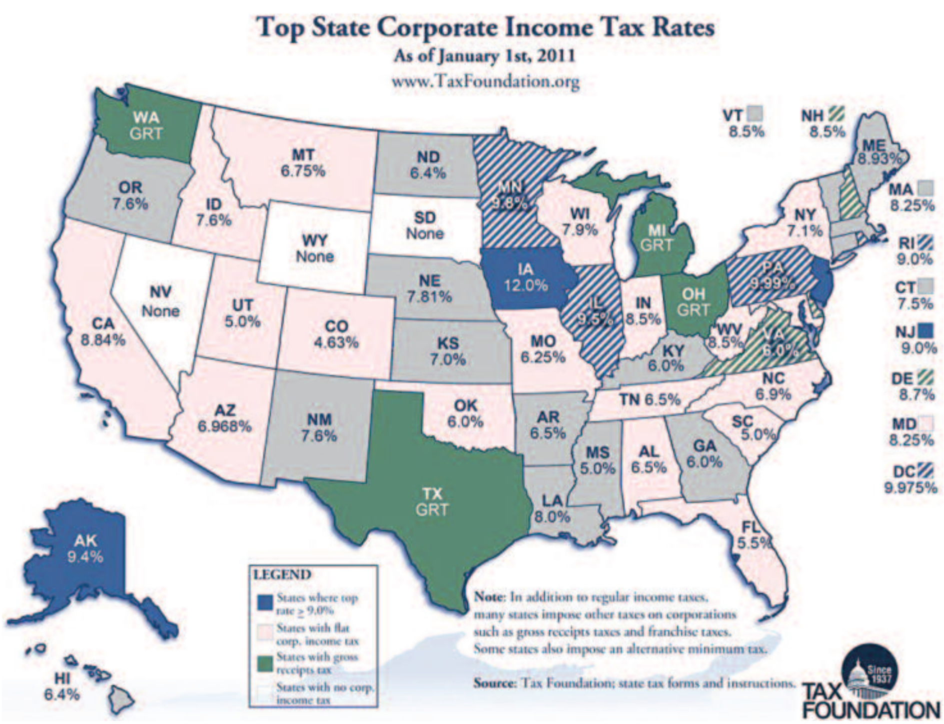
1. eliminate the inheritance tax – a key issue for family farms and small businesses
2. lower individual income tax rates by adjusting the tax brackets – providing middle class tax relief and making Nebraska more attractive to individuals and families
3. lower the top corporate income tax rate – spurring investment and new business development and creating jobs

These three reforms would provide immediate relief for small businesses and farmers and would go a long way to make Nebraska more competitive by providing a better business climate for new companies, and a better tax climate for households, both of which encourage job creation.

A Reduction in Corporate Income Taxes

One of the most arduous barriers constructed against small businesses is the corporate income tax. The United States currently has the highest income tax in the world, 35 percent.[3] On top of this, 47 states also impose their own corporate income tax, including Nebraska. Nebraska's relatively high corporate income tax puts it an immediate competitive disadvantage when compared to the surrounding states. The Cornhusker State has two separate rates for corporate income tax, 7.81 percent for corporations making over $100,000 and 5.58 percent for corporations making under that amount.[4] These rates – specifically the top 7.81 percent rate – give Nebraska the highest corporate income tax of the neighboring states with the exception of Iowa. South Dakota and Wyoming, on the other hand, are one of only three states with no corporate income tax at all (Nevada is the third).[5] This high rate is underscored by the fact that Nebraska is ranked as having only the 30th best business climate in the nation, making us less attractive for businesses looking to expand, relocate or start up, particularly when Wyoming is ranked at number one for best business climate and South Dakota at number two.[6]

Table 1: Map of State Corporate Income Tax Rates[7]



Source: The Tax Foundation

While corporate income taxes are often thought to be levied on large businesses with massive profits, the fact is that corporations do not bear the costs of the corporate income tax; those costs are instead passed down to consumers through higher prices, workers through lower wages, and investors through lower returns.

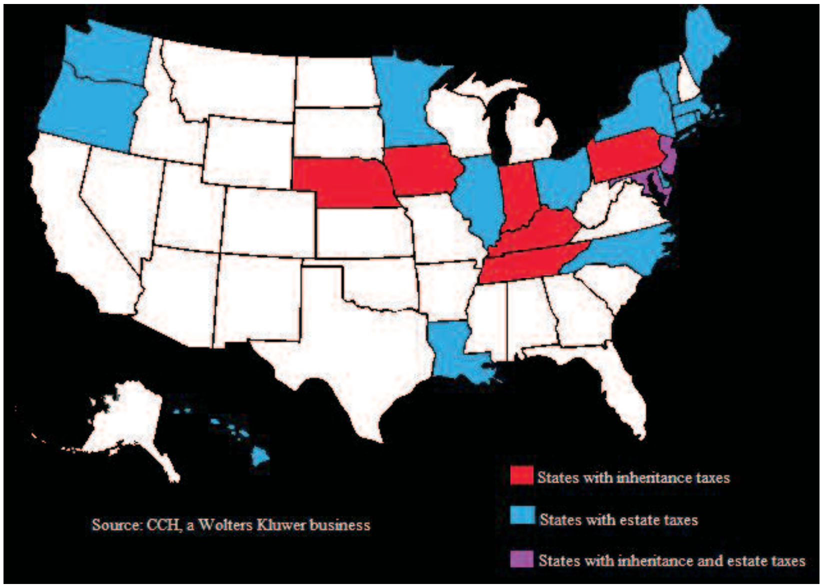
Most recent research suggests that workers are forced to pay most of the costs incurred by the corporate income tax. The Congressional Budget Office estimated that around 70 percent of the costs from the corporate income tax are passed down to workers, with the other 30 percent largely borne out by investors and consumers through higher prices.[8] The evidence that increases in corporate income taxes leads to falling worker wages is clear – for every $1 given to the state in the form of corporate income tax, the worker loses about $2.50 in wages.[9] At the same time, decreases in corporate income taxes result in increased worker wages.[10]

Additionally, examination of the effect on workers by education finds the corporate income tax actually punishes workers with more education. A one percent increase in corporate taxes has a progressively negative effect on worker wages as the level of education increases. Those without a high-school diploma see their wages decrease around 0.26 percent, those with a high school diploma (or some college) see a decrease of 0.31 percent, and college-educated workers see their wages decrease around 0.44 percent for every one percent increase in corporate income taxes.[11] As a result, corporate income taxes encourage high-skilled workers to leave the state, since states with lower corporate income taxes will likely have higher wages for those workers. Corporate income taxes also have a notably negative effect on manufacturing jobs – wages for manufacturing jobs fall about 0.8 percent for every one percent increase in the corporate tax rate.[12]

While opponents often cast proposals to reduce corporate income tax as benefitting the wealthy, the reality is that higher corporate income taxes hurt workers. Reducing the top corporate income tax by 1.11 percent, as proposed by LB970, would return an estimated $15.1 million to workers in FY2012-2013 alone, and that amount would increase exponentially in subsequent years.[13]

With a lower corporate income tax, businesses would have more capital to invest, expand their business, and create new jobs. This applies to small businesses as well – the average income for a Subchapter S small business nationally is approximately $100,436.00, just over the cutoff for the lower 5.58 percent rate.[14] Lower corporate income taxes will also mean that instead of businesses looking to relocate out of Nebraska, we can compete for new businesses to call Nebraska home.

Table 2: Map of States with Inheritance and Estate Tax[16]



The inheritance tax is a significant issue for families to maintain family farms and small family businesses. When added to the federal estate tax that was reinstituted in 2011, Nebraska has the fifth highest death tax in the nation, with 46.7 percent of inherited wealth ultimately confiscated by government in the form of taxes.[18]

Individuals hit hardest by inheritance and estate taxes are not the super wealthy – it is family farmers, small businesses, and investors. Since many of Nebraska's farms are family-owned – nationally, 98 percent of farms are family-owned[19] – the inheritance tax makes passing property from one generation to the next complicated and sometimes impossible. The United States Department of Agriculture estimated that the net income of farms is higher than the average American household; however, three-fourths of income is in farm-related assets.[20] But because farm income is, on average, higher than non-farm income, it makes family farms much more susceptible to having the family business bankrupted by death taxes. Higher death tax liability means the small or medium-sized farmers have to sell land, equipment, and in some cases, the entire operation to pay these duplicative taxes. Many family farming operations are "land rich, but cash poor."[21]

This tax reality has a negative impact on the Cornhusker State's agricultural sector – which last year contributed $17 billion to Nebraska's economy, making it the state's largest industry by a significant margin.[22] Nebraska's agricultural economy is one reason Nebraska has weathered the "Great Recession" as well as it has.[23] Repealing the inheritance tax would make it possible for family farmers and ranchers to pass property from generation to generation and would allow Nebraska's agricultural sector to become even more robust and productive, insulating Nebraska from future economic hardships.

Another group profoundly impacted by the inheritance tax is small business owners. Small family business owners face the same challenge as family farmers. Their income is heavy on assets – many of which are industry specific – but not available cash. The result is that parts and sometimes all of the business must be sold to pay inheritance taxes. If the

Repealing the Inheritance Tax

The Cornhusker State is one of only eight states that impose an inheritance tax, along with the estate tax, are often referred to as a "death tax." Fourteen other states and the District of Columbia also impose estate taxes – Ohio's estate tax will be officially repealed as of January 1, 2013 – and New Jersey and Maryland collect both an inheritance and estate tax.[15]

The inheritance tax differs from the estate tax in that it taxes specific bequests passed along to heirs and often has different rates and exemptions depending on the heir's familial relationship to the deceased (see Table 2). Estate taxes simply collect a percentage of the entire estate of the deceased.

Table 3: Nebraska Inheritance Tax Rates and Exemptions[17]

	Exemptions	Tax Rate After Exemptions
Spouses	No tax on spouses	No tax on spouses
Immediate Relatives	Amount up to $40,000	No
Remote Relatives	Amount up to $15,000	13 percent
Non-Relatives	Amount up to $10,000	18 percent

business survives, it is often much less productive, with fewer resources to expand and create new jobs.[24]

The inheritance tax also discourages individuals from saving to pass income along to their children. Individuals will save less, either because they choose to work and earn less, or because they devote a large share of their income to consumption. Less savings implies less capital for potential investment in the economy, and slower economic growth.

Death taxes also impact out of state migration. A study by the Ocean Policy Research Institute found that death taxes are a significant driver of out-state migration.[25] This is a serious concern for Nebraska, whose population growth has been stagnant. The 2010 census found that Nebraska grew by only 6.7 percent, three percent below the national average.[26] The slow growth is compounded by Nebraska's reputation as one of the "worst places to die," a reputation attributed, in part, to the inheritance tax.[27] Repealing the inheritance tax in accordance with LB970 would help stem the flow of taxpayers out of the state.

It should be noted that Nebraska's inheritance tax is structured differently than in most other states. Rather than being collected and administered by the state, the inheritance tax is collected at the county level and administered by the county court where the deceased person's property resides. The property inherited is evaluated and priced based upon the fair market value at the time of death.[28]

The inheritance tax is basically a local county tax, a fact that is proving to have a significant impact on opposition to LB970. Many county officials are condemning LB970.[29] However, for most of these counties, the inheritance tax makes up a miniscule portion of their county budget, and for a few counties, the amount is so small that they do not even budget for it, instead using the tax as a cash reserve fund. Counties need to understand that repealing the inheritance tax could actually help counties by curbing out-of-state migration, preserving property tax-paying family farms, ranches, and businesses, and freeing up capital in our overall economy. Cutting taxes and government spending increases economic growth, as such, revenues will decrease much less than opponents to this proposal claim.

Counties should not tackle how to meet their budgets without the duplicate, unfair inheritance tax, since repealing it will allow people to keep, save, and invest their money in ways that will generate economic growth, and lead to higher revenues for county governments as more people stay in those communities.

Reducing Personal Income Taxes

LB970 would make relatively moderate changes to Nebraska's individual income tax. But any effort to allow taxpayers to keep more of the money they earn is a worthwhile effort. LB970 would expand brackets so more individuals pay less, and would also lower the overall rates (see Table 4).

Table 4: Current Individual Income Tax Rates and LB970 Income Tax Rates[30]

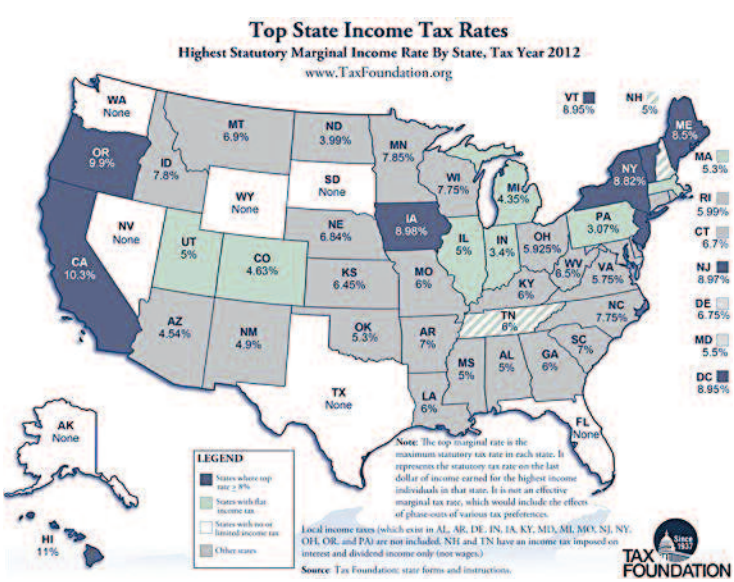
	Current Rate	LB970 Rate	Percentage Difference	Current Income Range	LB970 Income Range
Bracket 1	2.56%	2.42%	-0.14%	Single: $0-2,400 Couple: $0-4,800	Single: $0- 3,000 Couple: $0-6,000
Bracket 2	3.57%	3.40%	-0.17%	Single: $2,400-17,500 Couple: $4,800-35,000	Single: $3,000-18,250 Couple: $6,000-36,500
Bracket 3	5.12%	4.90%	-0.22%	Single: $17,500-27,000 Couple: $35,000-54,000	Single: $18,250-30,000 Couple: $36,500-60,000
Bracket 4	6.84%	6.70%	-0.14%	Single: $27,000 and over Couple: $54,000 and over	Single: $30,000 and over Couple: $60,000 and over

Much of the tax relief provided by LB970 would go directly to middle class families. For example, a married couple filing a joint income of $54,000 would see their taxes decrease by nearly 2 percent annually.

Along with achieving increased equity in Nebraska's tax code, reducing personal income taxes will have a positive effect on economic growth and attract more individuals and businesses to the state. Data from the 2010 census indicates that states with lower taxes see the greatest population growth. Between 2000 and 2010, Nevada grew its population by 35.1 percent.[31] Nevada has no income tax and a business friendly climate, with no corporate income tax.[32] Of the nine states with no income tax, seven had population growth above the national average. The other two states, South Dakota and New Hampshire, still grew the fastest in their regions.[33] Data clearly shows people choose to live in areas with lower tax rates. This fact should be concerning to Nebraska, a state with taxes higher than our neighbors; South Dakota and Wyoming are low-tax havens, with no income taxes, individual or corporate, and lower state and local sales taxes.[34]

Lower income tax rates have also spurred more economic growth than high income taxes. A comparison of the nine states with no income taxes to nine states with the highest income taxes, as well as the United States as a whole and

Table 5: Map of Top State Marginal Income Tax Rates [35]



Source: The Tax Foundation

Nebraska (see Table 6) from 1998 to 2008, highlights that higher taxes stifle economic growth, contributes to low population growth, and could even lead to lower tax receipts.

Data shows that states with low taxes attract people, businesses, and investment capital. LB970's changes to the individual income tax make Nebraska's tax code more progressive – helping the middle class – and is a step in the right direction for enticing individuals to consider making Nebraska their home.

Tax Cuts in Other States

Critics of LB970 question if the state can afford them. To answer this, it is helpful to note tax trends in other states. States across the country are considering tax relief packages:

- Kansas Governor Sam Brownback is pushing to lower the top income tax rate from 6.45 percent – a rate already lower than the potential LB970 rate – to 4.9 percent, while also ending deductions to make the plan revenue-neutral and expand the tax base.[36] His plan would also phase out the tax altogether over a ten year period[37]
- Oklahoma Governor Mary Fallin is seeking a ten-year phase out of the income tax, beginning with a reduction of their rate from 5.25 percent to 3.5 percent in the next year[38]
- Governor Nikki Haley of South Carolina is pushing for broad tax reform, including eliminating the corporate income tax over four years, cutting individual income tax rates, and consolidating brackets, as well as reforming property taxes[39]
- In Idaho, the state house approved Governor Butch Otter's $35.7 million tax cut which lowers individual and corporate income tax rates from their current 7.6 percent to 7.4 percent[40]
- Last year, Maine Governor Paul Le Page signed the largest tax cut in state history, and he aims to do that again, saying that last year's cuts where still "not enough"[41]
- New Jersey Governor Chris Christie has proposed a ten percent across-the-board tax cut over four years in order to make his state more competitive and undo the stigma of being known as one of the highest taxed states in the nation[42]

- Ohio Governor John Kasich's tax plan would restructure energy taxes to give Ohioans a revenue jump with plans to begin cutting the income tax in 2013 with the ultimate goal of phasing it out[43]

With other states taking bold steps in their approach to taxes, another question that should be asked is whether Nebraska can afford *not* to do anything to lower tax rates and develop a more business friendly climate.

Conclusion

LB970 is good public policy and is important to Nebraska's long-term economic success. Eliminating inheritance taxes will end a major reason for out-migration and will allow family farms and small businesses to survive and thrive. Lowering corporate and personal income taxes will spur business investment, make our tax climate more attractive to prospective businesses and individuals, and safeguard worker wages and consumer prices.

Table 6: Comparison of States with No Income Taxes and High Income Taxes, 1998-2008*

	Income Tax Rate†	GSP Growth	Pop. Growth*	Total Tax Receipts Growth‡
Texas	0	0.945	0.206	0.883
Florida	0	0.784	0.176	1.048
Washington	0	0.649	0.141	0.682
Tennessee**	0	0.567	0.115	0.728
Nevada	0	1.062	0.351	1.287
New Hampshire**	0	0.535	0.065	0.724
South Dakota	0	0.779	0.079	0.634
Alaska	0	1.068	0.133	1.053
Wyoming	0	1.376	0.141	1.613
California	0.1055	0.701	0.1	0.911
New York	0.105	0.666	0.021	0.605
Ohio	0.0824	0.352	0.016	0.327
New Jersey	0.1075	0.512	0.045	0.877
Maryland	0.093	0.688	0.09	0.824
Oregon	0.11	0.601	0.12	0.581
Hawaii	0.11	0.7	0.123	0.706
Maine	0.085	0.567	0.042	0.579
Vermont	0.094	0.597	0.028	0.812
U.S. average	0.0569	0.6634	0.097	0.742
States without income tax average	0	0.8628	0.1563	0.9612
States with highest income tax average	0.0992	0.5981	0.065	0.7386

Table information from Laffer, Moore, and Williams, Rich States, Poor States 3rd Edition

**Population growth from 2000-2010 Census*

***Tennessee and New Hampshire tax income made from interest and dividends, at five and six percent respectively*

†Each state's highest tax rate, with the tax rate of the largest city serving as proxy for local taxes

‡Equal weighted averages

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Director and noted north central Nebraska lawyer and water resources activist. He has practiced through-out Nebraska and South Dakota and has represented the Niobrara Council since its creation.

Michael Groene
Director and farm equipment sales representative. He is co-founder of the Western Nebraska Taxpayers Association.

Travis Hiner
Former president and chairman of Hiner Implement, Inc., and president/chairman of Hiner Lease Company. He has served as a board member of the Kosman Banking Family since 1990 (now Platte Valley Companies).

Executive Director:

John S. McCollister
He recently capped a 35 year career with McCollister & Co. and served five terms on the publically elected Metropolitan Utilities District Board of Directors.

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