"Buffett Rule" Bill is Bad for Nebraska

Newton's third law of motion says "For every action, there is an equal and opposite reaction,"[i] and while Sen. Danielle Conrad's LB532 may not be equal in scope to Gov. Heineman's proposal to eliminate income taxes, it certainly qualifies as an opposite reaction.

LB532 takes its inspiration from the "Buffett Rule," named after billionaire investor and Nebraska native Warren Buffett, whose advocacy for higher taxes on wealthy individuals has become the centerpiece of President Obama's tax policy.[ii] LB532 would create a new tax bracket for Nebraskans making over $400,000 individually or over $450,000 as a couple and tax them at a rate of 7.74 percent. This is a significant increase from the current top rate of 6.84 percent, which currently applies to individuals and couples with annual income over $27,000 and $54,000, respectively.[iii]

Increasing the state's top income tax rate would exacerbate Nebraska's already uncompetitive tax climate. Among Nebraska's neighbors only Iowa has a higher tax rate. Two of our neighbors, South Dakota and Wyoming, do not have income taxes, and last year Kansas cut their income taxes dramatically, eliminating their top tax rate and cutting the next-highest rate down to 4.9 percent. Colorado and Missouri also have better income tax rates at 4.63 percent and 6 percent, respectively.[iv] On a national scale, Nebraska's income taxes are 18th highest in the country. LB532 and its top bracket of 7.74 percent would that rank up to 13th highest.[v]

In recent years, states that are striving to improve their economic situation have made moves to cut taxes rather than raise them; in this year alone income tax cut proposals have been made by governors or legislative leaders in Kansas, Oklahoma, Ohio, Louisiana, Indiana, New Mexico, and North Carolina.[vi] Increasing Nebraska's income tax would further stigmatize Nebraska as a high-tax island in a sea of low-tax states.

Aside from the simple arguments of economic competitiveness, raising income taxes, specifically in an effort to "soak the rich" as this bill seems designed to do, is simply bad economic policy. First, the increase results in little additional revenue, only about $42.2 million the first year, which is about 2.3 percent of the revenue brought in by the income tax and only 1.1 percent of the revenue brought into the entire general fund in fiscal year 2011-2012.[vii] The revenue estimates for the second, third, and fourth years are all substantially lower than the first, at approximately $31.1 million, $32.9 million, and $34.7 million respectively. These lower amounts become more inconsequential when

one considers that general fund revenue has increased an average of 5 percent for the past thirty years, so the revenue from this tax would decrease as a percentage of the general fund almost immediately and continue to decrease in the future.[viii]

Besides the nearly inconsequential impact on state revenue, there is also the issue of where the money is coming from. Taxing an additional $42.2 million out of high-wage earners means there is less for those individuals to spend, save, or invest. Each of these activities have a positive economic benefit, even savings, as savings kept in banks or credit unions are relent out to borrowing consumers or productive investors.[ix] Reducing the money available for individuals to spend, save, or invest would result in less business activity and therefore fewer jobs, dealing a substantial blow to the private sector and economic growth.

There is also the issue that this tax would cause high-wage earners to leave the state. An estimated 4,000 Nebraskans would pay this tax,[x] yet with high-wages comes a degree of mobility, and it is possible that some of these individuals would leave the state to avoid increased taxes. Since every surrounding state except Iowa has lower taxes-including two with no income tax at all-these high earners would not have to go far. The phenomena of people fleeing high-tax states is clear: between 1997 and 2007 the nine states with the highest income taxes saw 1,100 people leave their states *every day*, many relocating to locales with lower taxes.[xi] Nebraska's population already grew slower than the national average in the 2010 census and state cannot afford increased out-migration.[xii] An exodus of high-wage earners would negatively impact income tax revenue and deprive state and local governments of revenue they would otherwise receive from taxing the sales and property of these individuals.

Finally, taxing high-earners disincentivizes others from working to become wealthy. Why work to make $400,000 if more of it is going to be taken away from you? Better for someone to make $399,999 and pay the same taxes as when they made only $30,000. An overly progressive tax penalizes people directly in proportion to their productiveness and kills the incentive to work harder and become wealthier, making society poorer from lost productivity.[xiii]

While the debate between lowering or eliminating income taxes rages on, it is clearly bad public policy to raise income taxes. States without income taxes have demonstrated higher economic growth, higher population growth, and even higher tax receipts growth, while the average among the nine states with the highest income taxes lagged behind the national average and far behind the no income tax states.[xiv] Furthermore, LB532's proposal to raise taxes on high-wage earners results in little revenue while greatly damaging Nebraska's economic competitiveness, taking money out of the general economy, disincentivizing productiveness, and encouraging high wage-earners to leave the state and

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[i] The Physics Classroom, "Newton's Third Law of Motion." Accessed February 10,

2013, http://www.physicsclassroom.com/class/newtlaws/u2l4a.cfm.

[ii] Graeme Wearden, "Warren Buffett calls for higher taxes for US super-rich," *The Guardian*, August 15, 2011. Accessed February 10, 2013, http://www.guardian.co.uk/business/2011/aug/15/warren-buffett-higher-taxes-super-rich; "The Buffett Rule," the White House. Accessed February 10, 2013, http://www.whitehouse.gov/economy/buffett-rule; Naftali Bendavid, "'Buffett Rule' Tax Plan Fails in a Senate Test Vote," *Wall Street Journal*, April 16, 2012. Accessed February 10, 2013, http://online.wsj.com/article/SB10001424052702304299304577348221678464912.html; Paul Hammel, "Senator invokes 'Buffett rule,' asks state to raise income taxes on wealthy," *World Herald Bureau*, January 24, 2013. Accessed February 10, 2013, http://www.kearneyhub.com/news/state/senator-invokes-buffett-rule-asks-state-to-raise-income-taxes/article_220269ea-662e-11e2-a93e-0019bb2963f4.html.

[iii] Joseph Henchman, "Nebraska Approves Modest Income Tax Reduction," Tax Foundation April 11, 2012. Accessed February 10, 2013, http://taxfoundation.org/blog/nebraska-approves-modest-income-tax-reduction. It should be noted that the income thresholds for the 6.84 percent bracket will increase in 2014 to $29,000 for individuals and $58,000 for couples filing jointly.

[iv] Tax Foundation, "State Individual Income Tax Rates, 2000-2012," February 16, 2012. Accessed February 10, 2013, http://taxfoundation.org/article/state-individual-income-tax-rates-2000-2012; Mark Robyn, "Not in Kansas Anymore: Income Taxes on Pass-Through Businesses Eliminated," Tax Foundation May 29, 2012. Accessed February 10, 2013, http://taxfoundation.org/article/not-kansas-anymore-income-taxes-pass-through-businesses-eliminated.

[v] Tax Foundation, "State Individual Income Tax Rates, 2000-2012," February 16, 2012. Accessed February 10, 2013, http://taxfoundation.org/article/state-individual-income-tax-rates-2000-2012.

[vi] NewsOK, "Okla. Governor pledges to seek income tax cut," *The Oklahoman*, January 23, 2013. Accessed February 10, 2013, http://newsok.com/okla.-governor-pledges-to-seek-income-tax-cut/article/feed/490879/?page=1; Francis DeLuca, "The States' Income-Tax Repeal Revolution," *National Review* January 28, 2013. Accessed February 10, 2013, http://www.nationalreview.com/articles/338875/states-income-tax-repeal-revolution-francis-deluca; John Frank, "GOP leaders suggest abolishing N.C. income tax," January 17, 2013. Accessed February 10, 2013, http://www.newsobserver.com/2013/01/16/2612085/gop-leaders-suggest-abolishing.html; "The State Tax Reformers," *Wall Street Journal*, January 29, 2013. Accessed February 10, 2013, http://online.wsj.com/article/SB10001424127887323968304578245720280333676.html; Julie Carr Smyth, "Ohio gov proposes income tax cut, hikes elsewhere," *San Francisco Chronicle* February 4, 2013. Accessed February 10, 2013, http://www.sfgate.com/business/energy/article/Ohio-gov-proposes-income-tax-cut-

hikes-elsewhere-4249552.php.

[vii] Doug Gibbs, "LB 532 Fiscal Note," Nebraska Legislative Fiscal Analyst Estimate, February 5, 2013. Accessed February 10, 2013, http://nebraskalegislature.gov/FloorDocs/Current/PDF/FN/LB532_20130207-141425.pdf; Nebraska Department of Revenue, "Monthly Report of General Fund Receipts by Fiscal Year." Accessed February 10, 2013, http://www.revenue.ne.gov/research/gen_fund.html.

[viii] Doug Gibbs, "LB 532 Fiscal Note," Nebraska Legislative Fiscal Analyst Estimate, February 5, 2013. Accessed February 10, 2013, http://nebraskalegislature.gov/FloorDocs/Current/PDF/FN/LB532_20130207-141425.pdf; Nebraska Legislature, "State of Nebraska FY2011-12/FY2012-13 Biennial Budget,"August 2011. Accessed February 10, 2013, http://nebraskalegislature.gov/pdf/reports/fiscal/2011budget.pdf.

[ix] Murray Rothbard, *The Mystery of Banking*. (Auburn, Alabama: Ludvig von Mises Institute, 2008), 2, 76. The full pdf of this book is available from the Mises Institute website at http://mises.org/Books/mysteryofbanking.pdf.

[x] Paul Hammel, "Senator invokes 'Buffett rule,' asks state to raise income taxes on wealthy," *World Herald Bureau*, January 24, 2013. Accessed February 10, 2013, http://www.kearneyhub.com/news/state/senator-invokes-buffett-rule-asks-state-to-raise-income-taxes/article_220269ea-662e-11e2-a93e-0019bb2963f4.html.

[xi] Karen Hube, "Fleeing the Tax Man," *Barron's* September 28, 2009. Accessed February 11, 2013, http://online.barrons.com/article/SB125392413369542679.html.

[xii] David Drozd, "Nebraska State/Local Population Trends," Center for Public Affairs Research, University of Nebraska at Omaha, 23rd Annual Data Users Conference, August 15, 2012. Accessed February 3, 2013, http://www.unomaha.edu/cpar/conf2012/State-LocalTrends2012.pdf.

[xiii] Henry Hazlitt, "Soak Rich and Hit Poor," *Newsweek* April 5, 1954, reprinted by the Ludwig von Mises Institute at "Soak the Rich?" October 19, 2012. Accessed February 10, 2013, https://mises.org/daily/6241/.

[xiv] Arthur B. Laffer, Stephen Moore, and Jonathan Williams, *Rich States, Poor States: ALEC-Laffer State Economic Competitiveness Index*. 4th Edition. American Legislative Exchange Council. (Washington DC: American Legislative Exchange Council, 2011), 25. Accessed February 10, 2013, http://media.khi.org/news/documents/2012/08/14/Rich_States_Poor_States.pdf.

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