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With Nebraska facing a $1.2 billion shortfall through FY 21,[1] figuring out how to close it will be one of biggest challenges for the Legislature. In order to prepare for the budget debate ahead, OpenSky has prepared three policy briefs to help inform the discussion. The first policy brief examined how previous large shortfalls were addressed. This second brief explores the contribution of past revenue measures to the current shortfall. The third and final brief will discuss three recent reports that highlight future budget uncertainty as additional factors to be taken into consideration as the Legislature begins its work.

Annual impact of past decade's tax changes could approach $900 million

Last fall, the Legislative Fiscal Office (LFO) released a list of tax changes passed by the Nebraska Legislature over the past decade that have reduced state General Fund revenue by about $755 million in this fiscal year alone. While these tax changes have certainly contributed to the $1.2 billion shortfall facing Nebraska, new data shows the impact of some of these and other tax changes made over the past decade may be even larger than the original fiscal notes indicate and that the overall fiscal impact of all of these changes could be closer to $900 million annually.

Cost of several tax changes appear to be larger than original fiscal notes

Not included on LFO's list of tax changes was the Nebraska Advantage Act, which a November report from the Legislature's Performance Audit Committee[2] shows reduced revenue by about $108 million in 2013 after being originally projected to cost between $24 million and $60 million annually.

Other tax changes from the past decade that appear to be having a larger impact than their original fiscal notes projected include:

- A transfer of revenue from motor vehicle lease sales to the state highway funds, which was projected to reduce General Fund revenue by $10 million in FY 08-09. State accounting data[3] shows the transfer reduced the General Fund by $15 million in FY 16;
- A transfer of sales tax revenue from motor vehicle sales above 5 percent from the General Fund to cities and counties, which was estimated to reduce General Fund revenue by $15 million per year. Department of Revenue data[4] shows the transfer reduced the General Fund revenue by $20 million in FY 16;

[1] Nebraska Legislature, "General Fund Financial Status," downloaded from http://www.nebraskalegislature.gov/FloorDocs/Current/PDF/Budget/status.pdf on Dec. 28, 2016.
[2] Nebraska Legislature, "Nebraska Advantage Act Performance on Selected Measures," downloaded from http://nebraskalegislature.gov/pdf/reports/audit/naa_2016.pdf on Dec. 22, 2016.
[3] Nebraska Department of Administrative Services, "Fund Summary by Fund Report (June, 2016)," downloaded from http://das.nebraska.gov/accounting/nis/reports/062016/Fund_Summary_by_Fund_Report.pdf on Jan. 18, 2017.
[4] Nebraska Department of Revenue, "Nebraska Motor Vehicle Sales Tax Collections by County," downloaded from http://www.revenue.nebraska.gov/research/net_taxable_sales/monthly_mv_sales.html on Jan. 18, 2017.

- A 2012 measure that provided a sales tax exemption for youth development programs, which was projected to have "minimal fiscal impact" and was not included on the LFO list. The 2016 Tax Expenditure Report[5] estimates the measure reduced revenue by about $3 million in FY 16; and
- A measure that passed in 2014 that exempted the purchase of agricultural machinery repair parts and service from sales tax, which was projected to reduce state revenue by $9.7 million annually. The Tax Expenditure Report estimates that the measure reduced revenue by $15.6 million in FY 16.

New data do indicate some tax changes are having a smaller General Fund impact than projected but those are more than offset by changes that appear to cost more than originally projected. It's also worth noting that tax changes passed in the 2016 Legislative Session, which largely consisted of new tax breaks and transfers to the Property Tax Credit, are estimated to reduce the General Fund by $62 million in the upcoming biennium.[6] These measures were not reflected in the LFO list nor in the state data used in this report.

Review of past tax changes could help address current shortfall

Significant tax changes have been made over the last decade and they are contributing to the state's $1.2 billion budget shortfall. This point is an important reminder that once tax changes are enacted, they are rarely reviewed again, unlike state spending, which is reviewed every two years. This means tax changes can become more costly than originally projected and can act as unnoticed drains on revenue that is vital to support schools, roads, public safety and other services that are important to Nebraska and its economy.

As the Legislature grapples with how best to close the current shortfall, particularly one that could grow and span several years,[7] a review of past tax changes should be considered as part of the solution. Not doing so could result in a growing structural budgetary gap, one that could have major and long-lasting effects on our state and its economy.

[5] Nebraska Department of Revenue, "2016 Tax Expenditure Report," downloaded from http://www.revenue.nebraska.gov/research/tax_expenditure_rep/2016/2016_Tax_Expend_Report_1.pdf on Jan. 16, 2017.
[6] State of Nebraska, "FY15/16 & FY16/17 Biennial Budget as Revised During the 2016 Session", downloaded from http://www.legislature.ne.gov/pdf/reports/fiscal/2016budget.pdf on Jan. 3, 2017. Page 26, Table 10.
[7] OpenSky Policy Institute, "Big-picture approach, not quick fix, need for budget shortfall," accessed at http://www.openskypolicy.org/5781-2 on Jan. 16, 2017.