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As the Nebraska Legislature looks for ways to close the state's current budget shortfall, LB 373 provides an opportunity to examine revenue reductions passed by prior Legislatures in the same way lawmakers review appropriations through the biennial budget process. The measure also would increase General Fund revenue by $859 million over the FY18-19 biennium, which could help the state balance the budget and address pressing issues like corrections reform and our high reliance on property taxes to fund K-12 education.[1]

If approved, LB 373 would reverse several revenue reducing measures passed since 2005 that cost more than expected when passed or that reduce General Fund revenue by more than $5 million annually. These measures include several tax credits, exemptions and earmarks targeted for select groups of Nebraskans, as well as some tax rate and base changes and the elimination of the state's estate tax.

Along with reversing tax changes passed since 2005, LB 373 also would eliminate two income tax exclusions – the Special Capital Gains Election and the Multi-State S-Corp or LLC Exclusion – which were passed in 1987. Both measures reduce revenue significantly each year, provide large income tax cuts to wealthy Nebraskans and have questionable benefit for the rest of the state's residents.

Special Capital Gains Election -- a one-time, big-time tax break

The Special Capital Gains Election is a one-time tax exclusion that allows Nebraskans to sell back stock in their employers' companies without paying taxes on the money earned from the sales. No other state appears to have a similar exclusion. The initial election passed in 1987 as part of the LB 775 tax incentive package. It was expanded in 2007 to extraordinary dividends and again in 2013 to allow Employee Stock Ownership Programs to participate as shareholders. According to the Department of Revenue's Tax Expenditure Report, the exemption reduced revenue by $25.6 million in 2014.[2] The election was claimed on only 740 Nebraska tax returns, 80 percent of which were filed by taxpayers with annual federal Adjusted Gross Income (AGI) of $1 million or more.[3] In contrast, Nebraska's Earned Income Tax Credit in FY14 reduced revenue by about $29 million and was claimed on more than 129,000 Nebraska tax returns. About 97 percent of the EITC benefit went to Nebraskans with $40,000 or less in AGI. In 2016, the Special Capital Gains Election reduced revenue by $20.8 million. Data regarding who used the exclusion are not yet available.[4]

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[1] Nebraska Legislature, "LB 373 Fiscal note," downloaded from http://www.nebraskalegislature.gov/FloorDocs/Current/PDF/FN/LB373_20170321-102302.pdf, on March 21, 2017.
[2] Nebraska Department of Revenue, "2014 Tax Expenditure Report," downloaded from http://www.revenue.nebraska.gov/research/tax_expenditure_rep/2014/Section_B.pdf, on March 22, 2017
[3] Department of Revenue, "Nebraska Statistics of Income," accessed at http://www.revenue.nebraska.gov/research/statistics_of_income/stat_2014/stat_2014_excel.html on March 21, 2017.
[4] 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.

Multi-State S-Corp or LLC Exclusion provides major tax cuts to a few wealthy residents

The Multi-State S-Corp or LLC Exclusion was passed in 1987 and allows Nebraskans to avoid paying income tax on earnings from multistate S-Corporations or Limited Liability Companies that are not connected with Nebraska sources. According to the Tax Expenditure Report, this exclusion reduced revenue by $59 million in 2014. About 85 percent of the exclusion was claimed on 620 tax returns that were filed by taxpayers with at least $1 million in AGI. Furthermore, 60 percent of the exclusion was claimed on about 90 returns from taxpayers who had AGI of at least $5 million. It is unclear if any other state has a similar tax exclusion. In 2016, the Multi-State S-Corp or LLC Exclusion reduced revenue by $84 million. Data about who claimed the exclusion are not yet available.

Many tax cuts and loopholes benefit a few Nebraskans

Like the two examples above, many of the tax breaks and loopholes that would be reversed by LB 373 are used by relatively small segments of Nebraska residents. They also significantly reduce revenue that could help close our budget shortfall, enact needed corrections reform or reduce our high reliance on property taxes to fund K-12 education.

LB 373 would give the Legislature an opportunity to understand the impact of prior revenue measures and reverse and eliminate tax cuts and loopholes that don't serve the state's interest. Such steps can help ensure Nebraska's tax dollars are used to provide the biggest benefit to the state and all of its residents, not just some select Nebraskans.