***NEBRASKA TAXPAYERS FOR FREEDOM* ISSUE PAPER:**

NTF WHITE PAPER: PRINCIPLES FOR STATE TAX REFORM AND RELIEF.

PART I: TAXATION.

BACKGROUND. The NE Unicameral legislature for years has not mustered enough votes to pass comprehensive tax reform and relief. Instead, it occasionally has voted through individual "Band-Aid bills" to lighten the tax load on subsets of taxpayers. The only sure way to accomplish comprehensive tax reform and relief is to bring irresistible taxpayer pressure on sitting senators and elect additional fiscal conservatives in future election cycles. That is why it is crucial that taxpaying citizens search, find, volunteer for, and elect such candidates. Then, it is incumbent upon individual citizens and citizen groups to provide these senators ideas for comprehensive tax relief and spending reform as presented by this NTF White Paper.

THE TREND WE ENDORSE. Examining the tax structure of other states, we see a gradual shift from state income and local property taxes to consumption taxes, like sales, use, and excise taxes. Georgia, Kansas, Oklahoma, Ohio, and North Carolina have introduced or passed legislation that reduces state income tax rates and property taxes while increasing tax revenue from consumption taxes. States have found that shifting to consumption taxes accrues sufficient revenues to adequately fund both state and local governments. These taxes comprise more than the sales tax. They include excise taxes, nuisance taxes like occupation taxes, sin taxes like cigarette and liquor taxes, and user fees and charges. The Fair Tax is one form of consumption tax but not one that we recommend (see NTF issue paper). Subsequent property and income tax relief guaranteed every year, permanently, relief for every parcel of residential and commercial property and wage earner. Former Federal Reserve Chairman Alan Greenspan has endorsed this trend.

IMPROVES SAVINGS. Putting money into savings is important, because it allows people to prepare for emergency situations and adequately financially nurture their future lives. Consumption taxation avoids double taxation and penalties on savings, because the saver not taxed on the amount saved but taxed only on future consumption financed by the saving. Under a consumption tax, a NE taxpayer who earns $50,000 and saves $25,000 a year would pay taxes on whatever spent on goods and services. However, under our state income tax, the same taxpayer would pay taxes on the full $50,000, whether saved or spent. By allowing savings carried forward tax-free, NE taxpayers will save more of their income. Economic theory suggests that with a higher level of savings, the productivity of the economy will increase and improve living standards for families. Economists propose that individuals would likely save more of their income because of the expected increased savings under a consumption tax. Consumption taxation encourages saving and investment, whereas income taxation penalizes savers. The former eliminates taxes on interest, dividends, and capital gains. Taxing these three penalizes thrift by taxing sums reserved to savings. At the shareholder level, a consumption tax does not add a second layer of tax because of no capital gains taxes or dividend taxes. The economic benefits to Nebraskans at all income levels would blossom. More citizens could put money away for retirement, vacations, or other purposes.

EVERYONE PAYS. Everyone pays taxes with a consumption tax. The tax base is larger, because all consumption taxed. Honest taxpayers fume at individuals working off the grid or working in illegal industries and who do not file income tax returns and pay their fair tax share. There are individuals who take cash-only jobs not logged on the books; whatever money they earn going untaxed. They do not pay an income tax on that money, because it is not documented as real employment in the system. If the IRS can prove that an individual has collected income without paying taxes on wages, it can retroactively charge that person for tax money due the government. Those who peddle drugs on NE streets or engage in other illegal activities, such as working with contraband, would less likely do so, if the state income tax abolished. Illegal aliens would pay this tax whenever they purchased something. Taxed are non-residents who visit the state as shoppers or tourists. If the tax rate sets at the same level for all purchases, individuals who buy more or more expensive goods will pay more than those who buy fewer or less expensive goods. Larger-ticket items for those who can afford finer consumer goods would have a higher rate, if the tax is progressive. A frugal shopper who buys only the basics will pay less tax than formerly.

ECONOMIC BOOM. Empirical data show that a consumption tax could increase the size of the NE economy by about 15% over 10 years. This impressive growth largely would arise from investment now suppressed under our current tax system. One of the biggest reasons for replacing our current hybrid tax system with a consumption tax is a tremendous boon for the economy, because it would eliminate the heavy taxation that the current system places on investments. Investment would rise, because a consumption tax would remove the existing steep disincentives for business to make new investments and for investors to take the risk to fund them. Higher investment in the economy would create new jobs and increase productivity, which would increase wages. Those benefits would help many Nebraskans. Consumption tax has a positive effect on incentive to work. Workers taxed only when they consume. Abolishing or lowering our state income tax is equivalent to placing a small pay increase in each paycheck. Such will motivate employees to work harder and save more. An increase in private savings theoretically would increase the amount of capital available for companies to borrow and use for investments in improved facilities, equipment, and employees. Increases in the amount of capital available to firms then would increase productivity and lead to increased economic output in the future. Researchers have found that switching to a consumption tax could increase total economic output by 5% to 10% compared to an income tax. A consumption tax also would encourage individual investment, because profits on the sale of stock or other assets taxed only if spent and not reinvested. A consumption tax mostly removes tax on business investment. At the business level, it allows businesses to expense their investments in capital. Thus, they can deduct the entire cost of an asset from their taxable income at the time they purchase it rather than over many years as specified under current depreciation rules. Businesses have many more options when it comes to deducting under consumption taxes. Taxes incurred in operating a business (other than federal income taxes) are deductible business expenses. Included are sales tax paid on items bought for business daily operations, sales tax paid on items like office supplies, and sales tax paid on capital assets, such as a business vehicle, added to the vehicle cost basis. Excise taxes paid on ordinary and necessary business expenses also deductible. If paying an excise tax when buying items for business daily operations, they are either deductible as part of the item cost or added to the item cost basis. In some instances, excise tax for business claimed as a credit on an individual tax return.[1]

SIMPLE AND EFFICIENT. Convenience of payment encourages compliance. Compliance and administration costs minimized. This tax is efficient and simple for a state revenue department to implement, even if over several years during a transition. It eliminates loopholes and the many exceptions and complexities in our current state tax system. Compliance costs presently are quite substantial. If NE abolished or replaced part of the income tax with a consumption tax, it would significantly decrease compliance costs.[2]

BETTER REVENUE SOURCE. Consumption taxes can provide a significant and stable source of financing for our state government at a fairly low rate. Taxes on final consumption can raise more revenue at lower rates than income taxes. In economic recessions, consumption activity tends to decline less than incomes, so state governments that rely more on revenue from consumption taxes feel less pressure to run significant deficits.[3] Consumption tax, by taxing actual expenditures, thus more closely tracks long-term average income.

LESS STRESS. No one likes to hear a warning that they owe more money to the state government when they have been working hard and paying diligently out of their paycheck all year long! Taxpayers no longer will dread so much the month of April, when state income taxes due. A large percentage of our population would avoid tax nightmares and live within their means. We will see an increase in the privacy and freedoms upon which this country was founded. Audits would almost disappear. Perhaps business audits to ensure that all sales correctly accounted for and all consumption taxes collected and remitted, but at the individual level, no reason for state revenuers to visit you and demand to examine every item listed on your bank account statements.[4]

FRUGALITY INCENTIVES. Changes in buying behavior would occur. Taxed on consumption, people will think twice before making a purchase and more intelligently monitor their consumer behavior.

EXEMPTIONS. Consumption taxes would have the following basic life exemptions: food, health insurance and medical costs, transportation, housing, religious categories, and several business expenses.

STRATEGIES TO PURSUE. Comprehensive tax relief will present a multi-year task with short-range objectives and a long-range plan. It would proceed by increments over several legislative sessions. Necessary to produce a chart of steps and years it will take to accomplish these objectives. The taxpaying public will feel immediate trepidation and worry

[1] A Flat Consumption Tax Would Be Fair and Efficient, by Curtis Dubay, Nov. 16, 2015. Dubay is a Research Fellow, Tax and Economic Policy, at the Heritage Foundation and Senior Economist at the U.S. Chamber of Commerce.
[2] 10 Reasons to Abolish Income Tax and Replace it With a Consumption Tax, by Dave Anderson, January 26, 2020.
[3] "Income Taxes Are More Volatile Than Sales Taxes During an Economic Contraction" Tax Foundation, Mar. 17, 2020, https://taxfoundation.org/income-taxes-are-more-volatile-than-sales-taxes-during-recession/.
[4] Is it Time to Switch to a Consumption Tax? by Bonnie Lee, Fox Business, Jan. 11, 2016.

upon hearing about a movement to shift the tax load, fearing having to pay more tax than currently. Therefore, it is necessary to calm the public by clearly showing specific steps and outcomes. The tax shifting plan must plainly show tax reduction, not merely a tax shift. The objective is to lower property and income taxes and substitute consumption taxes in a way that will both shift and *lower* the tax load on individuals and businesses. Inform citizens how much property/income tax they would save. Revision must produce permanent tax relief for both urban and rural citizens and produce urban-rural unity. The first step would eliminate most state sales tax exemptions. The second step would eliminate most state income tax exemptions. Consult with the public education establishment for input regarding education funding, because public education funding must become an integral element in this tax reform. Find and elect additional fiscally conservative state senators with whom to work.

ROUND TABLE. Utilize a Round Table procedure and its building blocks, including state senators, other elected officials, and taxpaying citizens. Group solutions into categories, then narrow their number (see NTF issue papers ntfpropertytax14 and 14.1). Break down proposed solution(s) into single elements on which participants can discuss and find consensus. Single elements will formulate a solution on how to proceed.

SPREADING THE WORD. Following introduction of tax and spending reform bills in the 2023 legislature, town hall meetings across the state could publicize and gain public input for this legislation.

ELIMINATING STATE SALES TAX EXEMPTIONS. This first step would eliminate state sales tax exemptions in place from the first inception of the state sales tax to present. Exemptions have multiplied over the years, e.g., zoo, seed. Utilize staggered elimination, e.g., 25% first year, 50% second year, etc.

SALES TAX EXTENSIONS. The state sales tax gradually would encompass services, while the total sales tax rate would drop. Exemptions for food, clothing, housing, religious categories, and health and medical expenses. Utilize staggered extension, e.g., 25% first year, 50% second year, etc. Typically, sellers collect sales tax from the consumer at the point of purchase or service. As of January 1, 2021, 45 states and the District of Columbia collect state sales taxes.

EXCISE TAXES. Increase reliance upon consumption excise taxes, the main federal revenue source prior to income taxation. Examples include taxes on airline tickets, bus tickets, ship passenger tickets, fuel, environmental pollution, communication, and manufacturer taxes applied to coal and tires. Excise taxes on luxury items, such as expensive furs and jewelry, luxury cars, personal aircraft, and yachts. Sin taxes include levies on cigarettes, alcohol, gambling devices, confiscated illegal drugs, and pornography. Nuisance taxes on movies, sports events, plays, concerts, and amusement parks.

FEES. Increased concentration on fees. Adjust fee structures to meet cost of services given. If state government seeks to achieve full cost recovery for a service, it may create a separate fund to account for the service. This enables the state to segregate the revenues and expenses for the service, much like a private company handles a particular product line. User fees for public use of facilities and services, like parking garages, stadium seating, at state parks and recreation areas, grazing livestock. License and permit fees, e.g., hunting, trapping, fishing, cable TV. Franchise fees. Inspection fees. Law enforcement and court fees. Library fees. Tourism fees.

ELIMINATE STATE INCOME TAX EXEMPTIONS. Accomplish it incrementally by percentages over several years during a tax transition period.

INCOME TAX. As our state transitions to consumption taxes, the legislature can lower and merge the income tax brackets for both individual and commercial sectors of the population. Consider a flat state income tax or, alternatively, abolish it entirely. Businesses are not expanding or locating in NE because of our high corporate taxes, and both productive workers and retired senior citizens are leaving the state for lower income tax states. As years pass, our state income tax code becomes more complex, and it takes more time and money to ensure full compliance with state income tax regulations. (See NTF issue papers taxplan17, taxplan18, taxplan20, and taxplan24).

NONPROFIT TAXATION. Abuse of the nonprofit system in NE is flagrant. Many nonprofit businesses like hospitals and medical clinics enjoy tax exempt status for their entire facilities, although many of their services and facility areas compete with private enterprises for clients and customers. Nonprofits use infrastructure services like streets and sewers and public safety services as does private commerce. Institute the Payment in Lieu of Taxes (PILOT) system to tax the profit-earning parts of non-profit businesses to share the property tax burden with local property taxpayers. Specific nonprofits already offer substantial voluntary payments. Require nonprofits to prove eligibility for exemption. The legislature must take steps to reform our state nonprofit law. (See NTF issue papers taxplan19, cwatch17, douglascounty142, and NTF propertytax23 PP).

RESTRICT TAX INCREMENT FINANCING. Restrict TIFs to the original intent of the legislation, applied to actual blighted rural and urban areas otherwise not sustainable for redevelopment and restoration. Implement TIF benchmarks, audits, and penalties. (See NTF issue papers legwatch153.doc, tif.doc, and tif2.doc).

SHIFT SERVICES TO THE STATE. Most other states provide state funding for more local services than in NE, such as community colleges and all court and prison systems, and provide the bulk of funding for K-12 public schools. Consumption tax revenue would provide such funding and relieve our local property tax burden. The State would assume financial responsibility for the imposition of now unfunded or underfunded state mandates on local governments or share responsibility. (See NTF issue paper: unfundedmandates.pdf).

PUBLIC EDUCATION FUNDING. The funding of K-12 public education must become included in the transition process. The state would provide a specific percentage of state aid to K-12 schools, a % of total education costs per pupil, so that every school district receives 30% base state funding. Peg state aid to schools to decreases in their spending derived from property taxes. Limit public school district spending increases to CPI increases + growth in student numbers and expansion of facilities. Change state aid formulas, so that farmers and ranchers do not pay the highest percentages of school taxes in their areas.

PROCESS CONSULTANTS. While state senators are formulating a tax reform and relief plan together with spending reform, it is crucial to involve individuals who have definitive academic and professional backgrounds to offer guidance and assistance. We believe that the following individuals could offer critical knowledge to this effort:
Katherine Loughead, Senior Policy Analyst at the Tax Foundation.
J. David Aiken, UN-L Dept. of Agricultural Economics.
Dr. Ernie Goss, Professor of Economics, Creighton U.
Dr. John Bartle, Dean of UN-O Dept. of Public Affairs.
Dr. Craig Maher, School of Public Administration, UN-O Dept. of Public Affairs.
Cathy Lang, former NE Property Tax Administrator and former Director of NE Dept. of Labor.

TAX-FREE DAYS. Join other states in implementing tax-free days during which shoppers can purchase select items in preparation for providing for their schoolchildren in the coming school year. Implement another tax-free time during the winter holiday season for all taxpayers. (See NTF issue paper taxplan3).

CANDIDATES. Recruit and campaign for fiscally conservative candidates in the 2024 and future legislative elections who will assist the tax relief and spending control effort.

IMPLEMENTATION. The NE Dept. of Revenue must determine how much revenue needed from consumption taxes to raise sufficient revenue to replace current state and local taxes eliminated or reduced. As consumption taxes phase in, income tax brackets would lower in stages. A levy limit capping property taxes would become implemented that allows a degree of permitted growth annually and requires voter approval for proposed increases above that limit. The phased-in consumption taxes would reduce the total amount of property tax revenue collected by local governments. Taxpayers then will see clearly a reduction in property tax bills and income tax levies.

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PART II: SPENDING. Spending by our state legislature is out of control, particularly from welfare services and education funding that consume a greater portion of our state budget annually. Senators regularly set new sunset dates for program spending. Time to limit annual state budget growth increases to the Midwest consumer price index (CPI) increases + population growth or real economic growth. Other suggestions as follows:

- Implement across the board % strategic cuts in state spending.
- Cut state dept. and agency budgets by a specific percentage for a specific number of fiscal years.
- Specific targeted cuts in personnel and operations.
- Tie appropriations to dept. budget cuts.

- Prohibit altering sunset provisions on spending bills.
- Adopt accrual accounting for state finances.
- Eliminate entire agencies, e.g., NE Arts Council, education service units.
- Offer incentives to merge government entities in and between counties.
- Tie appropriations to higher education to trimming administration costs and unnecessary programs.
- End duplicative programs among NE college campuses.
- Move several university programs, resources, and students to community college settings.
- Utilize bonds for highway construction and repair.
- Most public employees enjoy defined benefit insurance plans, more expensive than costs incurred from defined contribution plans, which the state should adopt.
- Welfare recipients must start health savings accounts (HSAs) and become locked in for services.
- Rigorous financial auditing.
- Performance audits at all levels of government.

ZERO-BASED BUDGETING. Require every state department and agency to implement zero-based budgeting each fiscal year. Surpluses returned to the General Fund or re-appropriated. (See NTF issue papers legwatch16 and zerobased1.doc).

DESK AUDITS. Analyze every state employee position to analyze its necessity and possible elimination. Determine if a position could become part-time or merged with another position. Vacant positions not filled unless absolutely necessary.

PRIVATIZATION. Scrutinize state government to find places to privatize. Utilize outsourcing to the maximum extent to cut administrative and personnel costs.

PART III: LOWERING THE PROPERTY TAX.

Moving the state tax structure from heavy reliance on property and income taxes to consumption taxes will mean the gradual lowering and capping, even perhaps eliminating the tax on real property. Below, we offer suggestions for decreasing the reliance on property taxes and reforming the property tax system.

Offer equal urban and rural property tax relief.
Value farmland by income produced and soil quality.
Property taxpayers must understand how many dollars or what % they will save in property taxes.
There exists a fixed infrastructure of services in all 93 NE counties, yet population is declining in many of these counties. Counties should establish interlocal agreements and share services to lower the property tax. South Sioux City & Stromsburg areas have interlocal agreements and therefore have seen 20% property tax savings.
Public school districts likewise could share services and utilize interlocal agreements.
Merge taxing authorities.
Lower by steps property valuations, e.g., to 80% of market value, then lower.
Peg valuation hikes to annual area inflation rate + growth or only at a specific increase, e.g., 2%, 3%.
Exempt a specific percentage of property valuation from property tax.
Reform criteria for assessing real property.
Consider depreciation in homes from normal wear and tear. Do not raise valuations for replacement of necessities like roofs, plumbing, furnaces, air conditioning units.
Consider only major remodeling in a home in increasing valuation.
Eliminate the Tax Equalization Review Commission and allow local boards of equalization to set final valuations.
Our NTF preferred formula:
Require a formula to lower property taxes in order to neutralize a property tax increase caused by a valuation increase on a property.

PART IV: WARNING! AVOID THE VALUE-ADDED TAX.

There are many disadvantages in the Value-Added Tax (VAT). It is one form of consumption tax, placed on a product whenever value added at each point in the supply line, from production through distribution to sales point. The tax assessed and collected at each stage. A consumer pays VAT on the cost of the product, minus costs of materials already taxed. VAT, unfortunately, is a regressive form of the consumption tax that puts more economic stress on poor taxpayers. This taxation at every stage leads to higher consumer prices, a burden to all consumers. Although VAT is simple to maintain, it costs revenue departments more to implement. A VAT burden for the business community in the form of higher costs and higher bureaucratic loads. Because VAT calculated at each step of the process, accounting results in a larger corporate burden, and companies then pass along additional costs to consumers. VAT encourages tax evasion. Businesses can evade paying VAT by asking customers if they want a receipt, stating a lower price for a product or service if no official receipt given. The underground bartering economy would flourish. Prior to VAT adoption, European countries had average tax burdens of less than 30% of Gross Domestic Product (GDP). Now, VAT tax burdens gobble almost 40% of their GDP. Greedy elected officials see the VAT as a convenient tax to hike, viewing it as a money machine, irresistible income for politicians seeking more money to fund new spending programs. VAT also would erode welfare reform, because politicians gradually would increase the tax to finance pledged benefits. The fat VAT revenue certainly would escalate to finance a surge of new state spending, resulting in a stagnating economy, high deficits, and fewer jobs for Nebraskans. Gravitating towards a VAT would yoke another burden on our already fragile post-pandemic economy.[5]

PART V: WARNING! THE FAIR TAX IS UNFAIR.

There are numerous disadvantages in the FAIR Tax consumption tax. Several sources like Forbes state that overall taxes would rise for 90% of citizens, only the top 10% of incomes enjoying a tax cut. The Fair Tax attempts to protect poor people from paying a higher tax by implementing a huge cash transfer program called a prebate. As an offset, every eligible household would receive a periodic cash transfer equal to the amount of tax that a family would spend on necessities according to the federal poverty level, which itself changes periodically. Illegal aliens could become eligible. Prebates are very expensive, difficult to manage, susceptible to widespread fraud, and complex for a revenue department to administer; actually another welfare benefit. The FAIR Tax would create many enforcement and compliance problems. Black markets would explode overnight, creating an underground economy, and citizens would accelerate bartering exchanges for goods and services to avoid monetary purchases. For example, one neighbor could offer computer installation services, and the service recipient could reciprocate with accounting services. Businesses could declare purchases as business expenses to avoid the tax. NE businesses would have incentive to purchase their goods and services in adjacent and other states, hurting our state economy. Consumers and merchants would have many incentives to evade this tax, enforced only by aggressive measures reminiscent of the Prohibition Era. To account for such massive tax evasion, the consumption tax percentage would increase. FAIR Tax establishes a 100% tax base on consumption. NE taxpayers would pay tax on items that may not seem like “consumption” or which never before subjected to taxation. This long list includes purchases of food, water, new homes and vehicles, rent, mortgages, interest on credit cards, vehicle loans, doctor bills, medical supplies and equipment, prescription drugs, hospital bills, health insurance, nursing care, child care, private or parochial school tuition, utilities, gas at the pump, in addition to current fuel taxes, and accounting, legal, and funeral services. Despite most Nebraskans having health insurance, a major surgery taxed would deflate savings and cause financial distress. No more credit for child and dependent care, education credits and deductions like college savings plans, and student loan interest. The earned income credit for lower earners would disappear. A new $200,000 house might cost $245,000, plus the tax paid on mortgage interest. Allowing exemptions would require an increase in the tax rate. Fair Tax proponents often brag about eliminating much work for a revenue department. However, our state revenue dept. would have to determine tax rate application, mail out prebate checks monthly or quarterly, settle quarrels about taxed items and services and who qualifies for prebates, decide how much of new local taxes must transfer to the state, enforce tax payments, and pursue cheats. Compliance will become very expensive to monitor and enforce. Because this tax would apply only to new goods and services, Fair Tax boosters claim that Nebraskans will save money by buying used articles. A stronger demand for used goods actually will escalate price hikes for these items. Consumers will buy used vehicles, destroying new car dealers. Consumers will purchase homes a year old or older, killing the new housing market and home-building industry. The Fair Tax definition of “new” is vague. Therefore, the consumption tax could degenerate into a value-added tax used in many socialist European nations, a tax that increases the cost of all consumer items. Example: A company in Podunk, NE. sells new nuts and bolts to a lawn mower manufacturer in Wahwah, NE. The manufacturer pays a consumption tax on the “new” nuts and bolts. Manufacturer sells “new” lawn mowers to a retail store in Omaha. Retail store pays tax on “new” lawn mowers. Customer comes to retail store and buys a “new” lawn mower. Customer pays a tax on his “new” lawn mower. The end product always will become more expensive at the end of the line. Fair Tax would eliminate tax incentive programs like the NE Advantage Act that bring new companies,

[5] Mitchell, Daniel J. The Case Against the Value-Added Tax, 7-26-2011.

employees, and tax revenue to NE. This tax would hamper state economic growth. No state or local government has adopted the FAIR Tax, with good reason.

CONCLUSION. Nebraska stands at a taxation crossroads. We can either continue as a high tax state or transition to consumption taxes to retain younger workers and retired folks and boost both our savings and economy. The 2023 legislative session will provide a battleground fought between those who want to continue to push NE into high tax and reckless spending socialism and those who seriously want to reform our outdated and confiscatory state tax system. Using the content above, lobby your state senator to work with other senators to enact consumption state taxes that will attract business location and expansion and provide a more financially secure home state for all taxpaying Nebraskans. Email netaxpayers@gmail.com to join our NTF *Legislature Watch Project*.