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Tax Policy Reform Commission  
August 30, 2007

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The Tax Policy Reform Commission met at 1:30 p.m. on Thursday, August 30, 2007, in Room 2102 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing. Commission members present: John Anderson; Richard Baier; Senator Carroll Burling, Doug Ewald, Don Freeman, Matt Jedlicka, Senator Gail Kopplin, Senator Vickie McDonald, Senator Rich Pahls, Senator Arnie Stuthman. Commission members absent: Senator Deb Fischer, Mike Hybl, Senator LeRoy Louden, Milo Mumgaard, Mark Munger, and Senator Ron Raikes. Also present: Pat Martin. []

SENATOR BURLING: (Recorder malfunction)...the others come after we start, but we need to get started. And so I want to welcome all of you and thank you, those of you who are here, for coming to this, another important meeting of the Tax Reform Commission, and I will ask Amanda at this time to call the roll. []

AMANDA JOHNSON: (Roll call taken.) []

SENATOR BURLING: Thank you. We're trying to transcribe these proceedings and so some of you may have to share microphones. Try to talk into a microphone when you talk as much as you can, as much as possible. And we've complied with the Open Meetings Act, posted the notice on the door and published the meeting at the Nebraska Public Meetings Calendar. Did you all have a chance to look at the minutes? Any discussion anyone has of the minutes, or questions? They were sent to you sometime back, I understand. Anybody that did not get them? Any questions on the minutes? I have an addition. After the minutes were sent out, we noticed a word had been omitted and need to, if you have the minutes in front of you, it's the second paragraph, third line. We need to insert the word "relief" after "tax." Just...it's just a typo, and so...it says: "Members discussed how circuit breakers can benefit taxpayers by providing tax, generally through the income tax." Well, it should say "providing tax relief" and we just need to add the word "relief" to that, if someone would want to make a motion to do

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that. []

SENATOR KOPPLIN: So move. []

SENATOR BURLING: A second? []

DOUG EWALD: Second. []

SENATOR BURLING: Thank you very much. Discussion? All in favor of doing that say aye. Opposed? Thank you very much. Any other questions or corrections to the minutes? Is there a motion to approve as corrected? []

SENATOR STUTHMAN: So move. []

SENATOR BURLING: Motion by Stuthman, seconded by Kopplin, to approve the minutes, as corrected. Discussion? All in favor say aye. Opposed, same sign. Carried. Thank you very much. I hope you either...let's see...I'm the one that didn't bring...no, here, I have my packet. There we go. Hopefully, you all received the material that our facilitator has prepared for us and will elaborate on shortly. If you didn't have that, if you didn't bring it today we do have, right, another copy or two of these? []

AMANDA JOHNSON: Yes. I have one copy left. []

SENATOR BURLING: Okay. So hopefully you've had a chance to look over it and be able to ask questions and make comments, because we have come to the time in our deliberation where we need to start making some decisions. I'll remind you that the final report is due November 15. We're planning a meeting two weeks from today and then again about a month after that, and so we need to start to make some decisions about what goes in that final report. So, with that, are there any questions before I turn it over to Mr. McManus? Okay, Bob, it's all yours. []

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ROBERT McMANUS: Thank you, Senator. During the summer months, we did hold two public hearings in...one in North Platte and one in Lincoln. We held those in June. The North Platte hearing was...13 or 14 people spoke. We heard a lot about property tax and how it affects the rural areas of Nebraska. And I incorporated some of the North Platte comments into the paper, into the draft. And in Lincoln was just one speaker, was from Omaha, and he spoke primarily on the personal income tax, and he was representing the Omaha Chamber and setting forth the view that we needed to be careful that our top rank in income tax doesn't get so high that it's driving away people we want to be in the state. And then the rest of the...I spent quite a bit of time putting together, from all of the presentations we've had, some initial drafts which are, in some sense, merely a data dump of what the commission is seeing. They have not been reviewed by the department or by anyone really but George, so they're very rough. But I did, in going through the mandate that was given the commission, I realized that there was one area we were asked to look at which I hadn't looked at, and that was the incentives, business incentives that are available now. And so I put that as the first item on the agenda and Richard Baier will...has agreed to talk about that a little bit. []

RICHARD BAIER: Hopefully, this will not be a new topic to many of you in terms of Nebraska Advantage. I did want to walk through our programs quickly and also talk briefly about what we're seeing out there in terms of our competitiveness. And obviously, it continues to be a battle every day. We've made some great strides. This past year Ron Pollina, who is sort of the "godfather of economic development," picked us in the top ten states in the country. We just came out with a rating in the last couple days, the Milken Institute, lowest cost state for doing business. We're in the top...I think we're number seven on that one. So we're starting to get some national recognition. We feel pretty good about that. Well, what I might do quickly is kind of just walk you through some of the programs and then talk a little bit about what the trends are. And if Doug has thoughts or comments, I'd ask him to jump in. But let me just flip through it. There's some slides in there and, rather than trying to find a screen and show them up, I just

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printed them off for you to take a quick look. Again, in terms of what we're talking about, in terms of incentives in economic development, you know, we use the acronym on the front page there, the CREATE (phonetic), because what we find is some of our communities define economic development a lot of different ways. I had a community recently who was building a new hospital that was their economic development project. What I actually found is it was more of a public liability because they didn't have enough funding to keep the hospital open once they got it up and running. But same thing, (inaudible) a new city hall at one of our Panhandle communities was their economic development project for the year, and they didn't figure out what to do with the old one. So they were paying utilities on the old one, and insurance, and they built the new one that they couldn't afford. So we try to remind people that this really is about creating jobs, it's about creating wealth. And a couple of other things I want to separate on the third slide, top of page 2, is a definition we use in terms of primary versus secondary employment. And I see John shaking his head, so maybe I hit the economist button, which is a good thing. One of our challenges is really to create jobs that are primary sector jobs, because one of the challenges that we have in Nebraska, we (inaudible) periodically and I've had the conversation with some of you about why don't we provide incentives for the small downtown retailer. Well, the challenge with that is that Nebraska's pot is only so big and if we create one more nail salon downtown, all we do is give everybody a smaller piece of the pie. And so in terms of defining primary jobs, we're really looking at those that are manufacturing or processing or researching, that are bringing in dollars from outside the state. That makes the pot bigger, and that's really part of our challenges, is we separate those out of there. The bottom of that page is, again, from my perspective, and I put this on there more to remind myself than anything else, is how we look and evaluate our programs and policies in Nebraska, and do we grow stronger communities, do we stimulate primary jobs, do we create additional wealth, do we track (inaudible) financial capital, which right now is probably the hottest button that we have? And then we deal with the labor force on the bottom one. Top of page 3, and again, hopefully, this is some of...I don't want to spend a lot of time, but some of you have asked during our conversations what industries have a

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propensity to grow in Nebraska over the next five or ten years, where do we have competitive advantages, and this is kind of a breakdown of those factors before we talk specifically about the incentives. Again, value-added agriculture continues to be part of the trend that we're seeing and we feel pretty good about where that's headed, both in terms of opportunities for food and fortified foods, and we continue to see we're dealing with more and more small, startup food companies that are injecting products into the food supply. They're adding vitamins, they're doing this, they're doing that. And we just had the largest private investment announcement in the history of the state up at BPI up in South Sioux City. They've actually created a product that injects nutrients into, what I'd call, less quality grades of beef and makes it really great stuff. And so I think...and in their case it's almost all automated and they literally got to (inaudible) \$100 million plant with less than 100 people. And the people that are there, the inside of this control room looks more like NASA than it does any kind of thing that's related to a food processing location, and we're seeing more of that activity. Transportation logistics continues to be an opportunity for us, information, financial services, advanced manufacturing. You may have seen the story this morning. We actually created some manufacturing jobs in the state of Nebraska last year, one of the few that did that in the country. And then a couple of more specialized (inaudible) value-added tourism or experiential tourism, whatever you'd like to call it; defense in Omaha; and then the area of biotech. Let me move quickly to what I would call the important parts of the Nebraska incentives, and I've included this flier for you. It makes it a little easier for people if you can kind of look through the process. I'm not convinced it's a perfect format, but it's at least something to take a look at. What I will tell you, in a perfect world there wouldn't be business incentives. I wish Senator Raikes was here because he and I have this ongoing conversation. You know, the reality is, Senator Raikes, I agree with you, in a perfect world we wouldn't have incentives and, you know, as soon as the other 49 states agree not to do that, we'll go next. We sure wouldn't want to be the first ones out of the gate not to do that. Senator Stuthman, you and I were just up in Columbus for Katana Summit. You know exactly how important that was in that process. Nebraska Advantage really is performance-based, and that's a couple of things I want to hit on, in general.

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The nice thing about Nebraska's incentives is that we do require that you meet certain investment levels, certain job creation levels before you receive any kind of benefit from the state of Nebraska. I will tell you that's not the case in some other states. Texas, right now, is the worst competition we have. Iowa is not much farther behind because they have pots of money and they're just writing a check. They sit down with the Governor and they negotiate. It makes things interesting when you're having to negotiate against, you know, I like to play poker, but that's not a good hand to have. Sometimes you have to bluff your way with a two and a three against an ace and a king but...sometimes we have to play that game, but it is a challenge for us. So in terms of ours, again, requires investment, requires job creation. It also has some magic thresholds and you'll see those up there on the top. You'll also see them on your slides, in terms of minimum levels of investment and incentives. We also limit the kinds of businesses that qualify. You know, I think we made some changes under Nebraska Advantage that made us more competitive in terms exportable service businesses, people that are doing work for the defense industry, those kinds of folks. In terms of our overall program, we really focus on three or four types of credits. It's investment credit, so you get a tax credit for your investment, and you'll see that I'm going to use the 3 and 30 tier, which is Tier Two, as an example. That's the most prominent of all the tiers that we have. You'll see there again the types of qualifying businesses. We hit just about everybody that's defined as a primary employer. The investment credit in that case, if you're investing \$5 million, you're going to get a tax credit equal to 10 percent of that amount. That can then be used to offset your income and your sales tax liability. Under Nebraska Advantage, we (inaudible) changed the way we handle wage credits and you can now, based upon your average wage at your project, be eligible for, and you'll see it there, 3 to 6 percent in terms of wage credit. I think that's been a nice addition because it allows us to reward companies that are paying higher wages and higher salaries. Also has a minimum. If you're not paying at least 60 percent of the Nebraska average wage, you don't qualify for incentives. I will tell you, some of your rural towns, if you're a senator, yell at me probably about six or seven times a month that maybe that shouldn't be there, because we have some folks not meeting those requirements. The third component, in addition

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to investment and wage credits, then is the refund of sales tax on capital purchases related to those projects. And then the only other difference that you will see there is that, if you look at under Tier Four, is where we make the change at, under Tier Four, companies that would apply at 10 and 100--again, that's a minimum of \$10 million investment, 100 new jobs--qualify for a personal property tax exemption on certain items, and you'll see those listed there. They're aircraft, what's--these are old fliers, so that's kind of the reason you get the pretty color ones--mainframe computers, which you changed last session to include computer systems, ag processing machinery, and also property used in distribution facilities, again, targeting those target industries for us--how do we support those target industry growth opportunities. We also have, clear on the right-hand side, the Nebraska Rural Advantage for counties of less than 25,000. Under that scenario, a minimum of five new jobs and \$250,000 investment. []

JOHN ANDERSON: Is the investment tax credit structured at all like the federal investment tax credit was where you have to be...it has to be investment above some benchmark level, some historic average or that sort of thing? []

RICHARD BAIER: No, in this case it's tied to that project level. If they apply at 3 and 30, once they get to that \$3 million, then they go ahead and then they qualify, and all the expenses up and to and including that period. []

JOHN ANDERSON: Okay. []

RICHARD BAIER: Application fee is not a big deal. I will mention briefly recapture, and that's a topic, especially those of you that are sitting around the table in terms of legislative discussion, we do in Nebraska require and have what we call a recapture provision. If you're a company and you file for tax incentives and you maybe, the first year, get to \$4 million and you have 35 employees, but in year two you drop down below that magic 30 level, you begin to be subject to recapture some of those tax credits. And Doug's group does a great job of doing the audit process, getting out there

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and enforcing that recapture provision. It lets us hold the feet to the fire of the companies. The problem that we have is that our program right now is really kind of set up as a long-term, 15-year program. What we're seeing, as a lot of the new companies come in and out so quickly, you know, if you imagine back...if you've been watching the PayPal story, in 2003 they didn't exist. So things are changing (inaudible) rapidly than some of our programs are. We've got a new company right now that we're working with that's an Internet company called LinkedIn. A year ago they didn't exist, and now they've got 200 people working in Sarpy County, again, using that Internet face as part of that. Just a couple of other things: In terms of the bottom of page 5, talks about the Rural Advantage, and the numbers on page 5. As a whole, we feel pretty good about the numbers of projects that we've had. You'll see those there. When we put Nebraska Advantage together, and a lot of you were part of that package, we really felt it was important to try and get a good mix of industries. It was also important to get a mix of locations. I think we've been able to do that. Now the ethanol has helped us a great deal in that process, but we've been pretty fortunate to be able to spread that mix out. The only other two notes: the R&D credits, we're really kind of just in our first year of implementing those, the way the statute was structured. It's a 15 percent credit based upon your federal R&D credit. We in Nebraska are one of the few that does do a refundable R&D credit, so if you get research and development tax credits and you don't have a tax liability, you still get a check back from the state. We're one of only four states in the country we can find that offer their R&D tax credit that way. And the other piece would then be microenterprise, and microenterprise was set up sort of a way to help small projects in some of our more distressed counties. What I'll tell you is that our microenterprise pot of funds this year...I think was it March 8? []

DOUG EWALD: March, yes. []

RICHARD BAIER: March 8, we had used up the 2007 allotment of credits, and so we are looking at how those credits are being implemented for those small companies in more of those distressed counties, and trying to get a handle on that. Just in terms of

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general trends in what's going on in the incentive industry, and I'm going to call it the business industry. One of the folks, Bob, asked me originally is, can you tell me where that compares with other states? Well, it's kind of hard to do because, as we fluctuate tax rates and a variety of other things, it's real hard to get a year-to-year comparison. We did it with--prior to Nebraska Advantage, we had not done it since--with a national accounting firm. We have done some internal calculation. We think that what we have with Nebraska Advantage still probably puts us somewhere in the middle of the pack, definitely not towards the top. Part of that is a reflection of our high tax rates in Nebraska, because basically what you're doing is providing credits for somebody to offset their high taxes to start with. So it's a bit of that reflection. In terms of other things we're hearing, labor is a big issue. Every project that we see right now we've had four or five in the state in the last couple of weeks, and it's all about labor: Is it available? What's the skill set? What's it going to cost me? And it's very, very scientific, and that's probably the other challenge that we see in creating incentive programs that are complicated, because I would argue ours is a bit too complicated. If you take a look at...we had a company in Omaha--it's a pretty nice prospect--they came to us and said, look, we've already done all of our site work. It's a company called Mintax (phonetic). They're a consulting firm out of New Jersey. Mintax (phonetic) was a consultant that came in and said, look, we've looked all over the world, in this case; we've narrowed it to five cities in the world and Omaha is one of those that's going to get look. Okay, that's kind of a nice phone call to get. But they had done so much research that they literally knew how many people we had unemployed in certain sectors, how many graduates we were producing in so many sectors, and they could also tell me, based upon Bureau of Labor statistics, that for certain computer programmers we were 75 cents an hour higher than Tulsa, Oklahoma, who was one of the other five, I'm assuming, because that's where the airplane came from. It's the only reason we know that, but...so that labor issue is out there. The technology is making it more and more complicated because also what we find is that people go online and look at available buildings and available space and do a lot of their labor research before they ever get to us. So it's important that as we do incentives that we have things that are simple, easy to

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understand, and very efficient. The other piece of that...and again I wish Senator Raikes was here because he and I have an ongoing discussion about looking at factors in terms of technology companies and entrepreneurial companies. Their life cycles typically are much shorter than our programs. They're also more intense up front in terms of capital. And so our programs maybe aren't structured as much as they should be to help encourage those kinds of industries. Training is expected. Again, more focus on cash. Companies would rather see the cash up front into the project and tax credits over a 15-year deal. If we're all sitting in Don Freeman's office in York, he's thinking the same thing. Everybody is going to be in that situation. The other areas that are challenges for us: commercialization, research and development. We continue to rank, through the university this year, thanks to their aggressive efforts on federal research, we're about 9th in the country in terms of per capita R&D. []

JOHN ANDERSON: A hundred and seventy-five million this year. []

RICHARD BAIER: Yeah. It's a big number. The problem that we have is that we're 39th in number of companies that we spin out of that research. So we're working very closely with President Milliken and his staff to figure out how we may increase that connection, because right now we're getting killed at it. UNMC, to their credit, just came out with a proposal last week that literally will allow you to identify technologies that the Med Center has developed but they haven't used. They're basically sitting on the shelf at the Med Center. You can start your own Nebraska company, use their technology, without having to pay a royalty until you begin to make a profit. That's pretty creative thinking and I applaud the Med Center for that, but we've got some work to do there. The final piece of this is in terms of international trade. A lot of these companies, and we're seeing more and more of it all the time, have some sort of an international part-ownership, whatever it is, and you can look around Lincoln and see the reflection, whether it's Kawasaki, Yasufuku, Daitron, kind of go down the list. We have 32 Japanese-owned companies, and there are places like Hastings with Hastings Foods, where it's wholly owned now by the Japanese. Many times they don't have a lot of tax

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liability in Nebraska. So in terms of an incentive program like ours, it's based upon tax credits to offset your tax liability. Well, we don't always compete as well. So as we begin to look at trends and, you know, I know the Governor made a commitment when we passed Nebraska Advantage that we ought to do this every three years and step back and relook at it. We're about six months to a year away from probably needing to really take a deep look. And that's some of the things that we are starting to hear that's out there. I think we're more competitive now than we were. We still have a ways to go. []

SENATOR BURLING: Thank you. []

SENATOR PAHLS: The only question I had, and I think is when we were looking at...on the floor,... []

RICHARD BAIER: Uh-huh. []

SENATOR PAHLS: ...the training aspect. When this was...when I first really bought into this, I thought the community colleges were going to be more involved. []

RICHARD BAIER: Uh-huh. []

SENATOR PAHLS: Are they? []

RICHARD BAIER: Well, Senator, in terms of where we've been, we have about \$12 million under contract and they are tied to about, roughly, 3.5, 3, \$3.5 million. There are a couple things that I'll share with you in terms of...and yet, maybe we talked about it during the session. We had some of the community colleges thought it was a blank check and started building new buildings to do training in. That was not the intent of this money and so we turned down some proposals from the community colleges. []

SENATOR PAHLS: Okay. []

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RICHARD BAIER: The other thing is we have met with all the community college presidents on an ongoing basis, trying to get them more engaged in the business community. Because when I go to an Omaha or I go to...wherever I'm going, if it's Hastings or Columbus, if there's a business project you'd hope like heck the community college was at the table. They rarely are because... []

SENATOR PAHLS: Still today? []

RICHARD BAIER: Still today. They're getting much better, but still today it's a challenge. The challenge that we have is that a lot of their folks want to think about it like a community college and not like the needs of the business, and that's part of the challenge. []

SENATOR PAHLS: Yeah. Okay. []

RICHARD BAIER: And it's getting better. I mean, we've got some presidents now who have said, we will do a better job of this. []

SENATOR PAHLS: I'm assuming the one at Metro is probably more proactive, is she not? []

RICHARD BAIER: Yes. []

SENATOR PAHLS: Because I know they have the trucking thing... []

RICHARD BAIER: Yeah, doing nice things on the trucking program, is a good one. We're doing an ethanol training program at Northeast Community College where they're developing a curriculum for the entire state, and we're helping to support that. So there's a couple of those that are coming along, but it's been...it's not been an easy process. []

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SENATOR PAHLS: So, in other words, you're giving some of the credit for not being as successful at the administration level at the community colleges then. []

RICHARD BAIER: Yeah. And I think they would take some of that credit as well. []

SENATOR PAHLS: Okay. []

RICHARD BAIER: That's why we're working...trying to do a better job of working closely with them. But that training is a big issue. It's been able to help us close some projects. []

SENATOR PAHLS: Okay. Thank you. []

SENATOR BURLING: It's a process. []

RICHARD BAIER: It is a process. []

SENATOR BURLING: Okay. []

ROBERT McMANUS: Thank you, Richard. []

RICHARD BAIER: Uh-huh. Supposed to ask Doug some questions. (Laugh) []

ROBERT McMANUS: Okay, before we get into the drafts, I've drafted all of the sections of the paper of the report, the beginning sections, except for an overall section where we're looking at the overall Nebraska taxes compared to other states, and one of the reasons I've delayed that is that we need to have some discussion about whether there's...for instance, if the commission concludes that we need to increase one tax and decrease another, I need to have that discussion so that I can start drafting the overall

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piece. But in your folder today there's a piece called "DC Tax Burden Study," and I wanted to...this relates to the overall issue, and I just want to touch on this briefly. This is a new study that's just come out in June and the DC Tax Burden Study is done periodically and what that study is, is a study where they look at the largest city in each state and they look at the tax burden on individuals at various tax...at various income levels. And they look at both the state and local tax burden, and then they also look at the combined tax burden, and by the combined tax burden, it's when you take into account the deductions that you get for state taxes at the federal level. And this study just came out and I'll just walk through pieces of it. What it shows is that at a \$25,000 income level Nebraska would rank 16th highest in tax on people at that income level, and at a combined state level it also is 16th. At \$50,000, Nebraska ranks 22nd, which means...and at a combined level, 21st, which means that between \$25,000 and \$50,000 some states are more progressive in that range than Nebraska is. When you get to \$100,000, then Nebraska drops back to 15th, which means that between \$50,000 and \$100,000 Nebraska is more progressive than some other states, but the combined state/local rate drops to 8. And this is the point that I wanted to bring out, that from...once you get into these upper income levels, the combined state/federal rank is kind of unique for Nebraska. And in the write up on this, they talk about...there's a number of states, so it goes the opposite direction that the combined rate is very lower. And California is the...(inaudible) California's state and local tax burden ranks 9th, but the combined federal and state tax burden is 32nd. So they go from 9 to 32nd, largely due to high mortgage interest and property tax deductions on the federal income tax return. And it says in the opposite direction, Nebraska's state and local taxes rank 15th, but a large fraction of those are nondeductible sales taxes and, because mortgage interest deductions are modest in Nebraska, the combined tax (inaudible) ranks 8th. So it's kind of a unique...well, it's not a good thing (laugh), but it's kind of unique that...and the reason being at the federal level you are allowed to deduct property taxes, you're allowed to deduct state income taxes, you can...you can only deduct sales taxes if the sales taxes are higher than the income tax. And so, in general, states that have a personal income tax, taxpayers can't deduct the sales tax. And so we need to, in

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working out what we're concluding, work into the...take into account the federal consequences of all these things too. []

JOHN ANDERSON: So the major issue is modest house prices in Omaha... []

ROBERT McMANUS: That's right. (Laugh) []

JOHN ANDERSON: ...relative to either coast. []

ROBERT McMANUS: Right. []

RICHARD BAIER: Yes. []

ROBERT McMANUS: That's right. []

JOHN ANDERSON: That's the real driver. []

RICHARD BAIER: It may change a year from now. (Inaudible) housing (inaudible). []

ROBERT McMANUS: Well, that leads me into the...to talk about the drafts. What I attempted to do was to take all the information the commission has looked at and to draft, for each tax, a background and a finding section there. The findings did not...it was not intended to reach conclusions and so, in some cases, things that are of equal...some things that, in my opinion, might be more important than other things, I didn't try to weight the importance. I just tried to lay things down. And an example would be in sales tax. I don't think that the concept of sales tax holiday is as important a thing overall as some of the other issues, but I didn't try to weight that, so that everything is just kind of laid out for you to consider. The other two sections...so I did that for sales tax, property tax, personal income tax, corporate income tax, and then I did a section on demographics and a section on tax administration. And I think, the Chairman of the

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Property Tax Subcommittee isn't here today, but I want to use property tax as an example of how I see things, at least in my own mind, beginning to coalesce and I've put that down in this one-page piece. But when I put together the demographics and look at the state's history, what I find is that in some degree the problems that Nebraska is facing today in property tax go all the way back into the 1880s, because what happened back then was there was a large migration in the 1880s through 1900 because of free land, primarily because of free land. There was no overarching government structure that dictated where people were settling or how, and what was happening was any time that a mass of people would get together, they'd form towns, they'd form school districts, and it was all being done...it was also being done at a time when...the 1880s was a very wet decade and the people thought that that was the norm; that western Nebraska was very wet in that decade. And local government was being funded, not by taxes, but by land sales, and over 7,000 school districts were formed, and every school district had available a tremendous amount of cash from these land sales. There was surplus cash. And so basically the local structure that came into the twentieth century was this enormous local structure that to this day is one of the highest...one of the biggest in the country among the states. And then it, going into the twentieth century, there was pronounced and continuous rural population decline. The drought, the Depression, there was a steady eroding of population. There was consolidation of local governments, especially school district, due almost entirely to demographics. In other words, that it was due to higher tax and these things were shutting down because people were leaving and, once again, it wasn't an overarching plan to change it. And at the same time, there was population growth in Omaha and Lincoln, so that sets up the demographic that you have today of primarily a rural state with two population centers. But the original county structure and the original local structure remains basically in place. And while many steps have been taken to consolidate operations, in 1992, at the end of the century, Nebraska ranked 3rd highest in local government employment per capita. And the two states that rank higher are two states with populations of less than 500,000, which that does it. You have to have a certain critical mass. Hi, Senator. []

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AMANDA JOHNSON: I think you may have (inaudible) your seat. []

SENATOR BURLING: Over here is a...you can sit over here. []

SENATOR McDONALD: (Inaudible) chair. []

SENATOR PAHLS: But she's at the top of the class. []

SENATOR BURLING: Yeah. Doug, that's her name right there, I think. []

ROBERT McMANUS: And so the situation that exists today is that the local government structure has downsized over the years, but there are still 93 counties and there are still over 500 school districts, and compare this to states, like the state of Florida has less than 100 school districts. I think Nebraska's ranks above this. It's in the paper, but they're in the top three, I think, in terms...still, in terms of number of school districts. The other factor is that Nebraska is at or near the bottom in terms of state aid to local government and, consequently, property tax burdens are high. The state us giving over \$1.2 billion to local government, but compared to what other states do, at least one study I saw shows them at the very, very bottom. But the dilemma, I mean the paradox to me is that you can't...you've got a local government structure that's unwieldy and if you give money to that government structure you're rewarding bad behavior. And somehow you've got to increase aid to the local governments, but it has to be in a way and a fashion that rewards good behavior, which, I don't know, it's going to take somebody smarter than me to do. Any...I'd like some reactions because this is a non-Nebraskan now, after six months looking at the state, and that's what I concluded. []

SENATOR PAHLS: You know, I have a question because, unless I'm interpreting this wrong, you know, it sounds like we have an awful lot of government people per capita, but, see, do you classify OPPD government, MUD government? Would they be

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classified government? []

ROBERT McMANUS: Well, I looked at the electric utility and it didn't make any difference. You take up...you took a few...you take out, I think it was, 6,000 employees, but when I looked at the real numbers, it didn't change it. []

SENATOR PAHLS: Really? Take that many employees out, it would not drop the rate that much. []

ROBERT McMANUS: No, it didn't drop it that much at all. []

SENATOR PAHLS: Oh, okay. It's good to know. []

RICHARD BAIER: Senator, we're still at, full-time state and local government employment per 10,000 residents, 8th in the country, 8th highest. []

SENATOR PAHLS: See, that's why I thought if you take out the MUD, because they basically, you know, pay for themselves, I mean, it's not like a... []

RICHARD BAIER: Yeah, it... []

SENATOR PAHLS: All those people, I thought that would help drop that, but it's amazing. []

ROBERT McMANUS: It's a hard issue to talk about because the Legislature has been doing everything they can over the years to carve it back, but at the end of the day it's still...the situation is still, to me, it's one of the fundamental problems. I mean the property taxes are high and they're high in rural Nebraska, but it's...it's almost, you know, that the structure that rural Nebraska has mandates that. []

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SENATOR BURLING: Any comments? []

SENATOR McDONALD: In looking at we are the 8th highest, can you give us 1, 2, 3, 4, 5, 6, 7, to let us know that it just takes X amount of people to run government, regardless of the amount of population? Are those other rural states also with low population, or are we just out (inaudible)? []

RICHARD BAIER: Yeah, I got them by alphabetical, but I sure can. Alaska was 3rd. Delaware was 2nd. Kansas was 5th. Louisiana is ahead of us at 7. Mississippi at 4. New Mexico at 6. []

SENATOR McDONALD: And then the surrounding states, South Dakota, North Dakota.  
[]

RICHARD BAIER: Wyoming is number 1. []

SENATOR BURLING: Low population. []

ROBERT McMANUS: Yeah, Wyoming and Alaska are both under 500,000. []

RICHARD BAIER: South Dakota is 21. []

JOHN ANDERSON: How about Iowa? []

SENATOR McDONALD: And they only meet every other year, I think, and (inaudible) staff. []

JOHN ANDERSON: What about Iowa, Rich? []

RICHARD BAIER: Iowa, I'm sorry, (inaudible) to keep up, 20th. They have an average

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of 523 state and local employees per 10,000, and we have 576. []

ROBERT McMANUS: And some of the data I've seen is not state/local but just local. []

RICHARD BAIER: Uh-huh. []

ROBERT McMANUS: And it's worse. []

RICHARD BAIER: Yeah, it is. []

SENATOR KOPPLIN: Excuse me. But those are for per capita. []

RICHARD BAIER: Per 10,000, yep. []

SENATOR KOPPLIN: So Iowa may have just as many jobs, but they have a lot more people. []

RICHARD BAIER: Correct. []

SENATOR KOPPLIN: So they have the same amount of jobs. []

JOHN ANDERSON: There's 4.5 million people in Iowa. That's three times as many people. []

MATT JEDLICKA: Yeah, but (inaudible) by the size of the state, the population, they've got fewer. The whole point (inaudible). []

SENATOR BURLING: I think what this does is just points out part of our job, is...you know, it's a factor in what we're here to do about tax code is considering this very fact. []

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SENATOR KOPPLIN: Don't have enough people. []

SENATOR BURLING: Yeah, not enough people. []

MATT JEDLICKA: I guess I'll point out something a little bit along those lines, Bob, but I guess I don't know much about what...our state employee situation, and that's kind of disheartening to hear. But when we're looking at our school side, and this is one thing I guess that I've dwelled on lately with agriculture paying so much toward schools, with some data that is stuck in one of the attachments that Bob put out, it's information from the annual survey of local government finances, Table 11. It shows Nebraska's rank is 23rd per pupil for funding nationally. And this information is from '04-05. And I guess the feeling I get from a lot of this, when we're looking at sales, property, and income, is we can't expect a lot because we have a lot of services to pay for, but if we're middle of the road everywhere maybe that's kind of maybe what we're looking to do. So actually, on school spending, we are near middle of the road. We're 23rd highest, between Virginia and West Virginia. But still, when you break that down to funding from local sources as opposed to the state, we are 10th in the country from local sources and 48th from state sources. So you could say we have a problem with our local government, but really, in school, we don't right now, but we're still paying for it with a large amount of local funding. And then the table that I guess really gets me is Table 5, that's also with those others, and that is overall funding for schools. So of all of our sources of income for elementary, secondary, public school system, we are the absolute highest on funding from local sources, at 58.5 percent; and the absolute lowest amongst all states with state sources of 31.1 percent. So I guess as I hear this and, like I said, on the county side that's...or on local government or state employees, that's disheartening to hear, but really our problem, we have a great imbalance of how we're funding schools, and I guess that's one thing that really captures my eye. []

JOHN ANDERSON: Well, in a political sense, if what people want is local control, they've got it, right? I mean that's what the number says. And so it's...the political

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problem is do you want to trade off the local control for greater state participation, more money through the state aid formula? And the usual debate there is, right, people want it both ways, but they can't have it both ways. And so that's the political conundrum that's involved in trying to solve this, is to what extent are you willing to give up some local control, reduce your reliance on property taxes, have higher state aid, and lose the control you've got over the local schools? And this debate goes on and on and on. So it's not something we're likely to resolve here, but what your numbers are essentially telling us is that the political decision that's been made is that we prefer local control over anything else. []

MATT JEDLICKA: And, yeah, that's a very good point. And I guess where those other states stand as far as local control when they're getting more state aid, I, you know, can't answer that. I guess I don't know. []

JOHN ANDERSON: Inevitably, if you give up local control, the more state aid you disperse the more control the state has got in setting your standards and mandates and so on. And then you give up some control and that's...and politically, Nebraskans have been reluctant to give up local control. []

SENATOR PAHLS: John, do you think they would be willing to give up local control if they understood that your property taxes, changes are, would go down, but you're going to lose...I mean, there will be consolidation and things like that. Do you think...are we ready for that? []

JOHN ANDERSON: I don't know. I mean I'm not the politician. I don't read the political winds to know whether that's the case. I mean it's a legitimate question as to whether increased state aid would really result in lower property taxes. I mean it could result in lower property taxes, or it could result in higher expenditures per pupil, or some combination of the two, right? And that's the interesting question. I mean, we've gone through this exercise before in Nebraskan history. You know, in the last 20 years we've

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put caps on levies and we've observed, you know, what happens to expenditures as a result and property tax rates. And I don't think anybody is satisfied that property tax rates fell sufficiently in that whole exercise. And some of you may have more direct history with this. As I've looked at the numbers, you know, of course what happens is you get a combination of increased expenditure and lower property tax rates to some extent. But people are still saying they want lower property tax rates, through all of this. So, you know, nothing we've done has very substantially reduced the property tax rate overall. And there's still discontent. []

SENATOR BURLING: Well, I think, Senator, I've maybe got a very recent example of I don't think we're ready for that yet in this state. About three years ago, when the Hastings Correctional Center building closed down, there's all this talk about county jails around the state overflowed, we could have made a multiple county overflow jail out of that building. Everything was there. Security was there, everything was there. And I spent a lot of time, my staff spent a lot of time talking to people all over the state. Community corrections, you know, went out and looked at the building, said, yes, that will work for county jail, multiple county jail. and the bottom line was every county wanted their own. So they build a new one, send the taxpayers the bill, and there sits an empty building. I think that's...I'm not being critical. I'm just saying I think that's an example of maybe an answer to your question. I don't think we're...I think we still enjoy paying the bill for local control. []

SENATOR McDONALD: In looking at the schools, and we have a couple superintendents here, outside of forced consolidation what local control is there in the schools versus the state requirements and the state No Child Left Behind and all the things that are covered, requests from the state versus...or basically saying (inaudible) support of education and we adopt? Is there any flexible things in some local control that they really can do without that they're not doing without? And that's to Senator Kopplin and Senator Pahls. []

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SENATOR KOPPLIN: Probably not. Local school boards really don't...I mean I think they have a lot of power, but they don't. They set a budget which is controlled by a lid, and they set a mil levy, or whatever you want to think, which is controlled by a lid. After that, you know, they may decide on some curriculum issues, which are being directed from the state. What do you think, Rich? []

SENATOR PAHLS: Yeah, but also the demands, to be honest with you, put on by parents is just intense, you know, in so many kids, you know, class sizes. And any time you add another individual, you know, that's where the money is. I mean 80 percent of the budget is people. So they want their kids to have the special, if they have special needs, you know. []

SENATOR McDONALD: And that you can't take away. I mean those kids have to have the care and the... []

SENATOR KOPPLIN: That's directed to you. []

SENATOR PAHLS: By law. But again, it's a mandate to some degree, some of our mandates, you know. I mean class size is...I don't think right now is, but again, you start adding a few individuals, I mean that's...you know, a starting teacher may make \$30,000, but you add all the other stuff, it ends up closer to probably \$40,000. I mean, they don't get that money. It's just all the other stuff that goes with it. So I...but all I know is the people I'm listening to right now and I tell them on a group such as this, and they say, all you're going to do is just talk a lot and you're not going to do anything. They want to see some major changes, and I don't know what those are, but they think that we are going to be in trouble. We're going to get back to the tax thing. I mean they're even bringing up California, because I happen to be in a metropolitan area and some of those are... []

JOHN ANDERSON: What California issue is that? []

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SENATOR PAHLS: Well, Prop 13. []

JOHN ANDERSON: Prop. 13. []

SENATOR PAHLS: Yes. And hell, actually I think it's been probably detrimental in many ways in the state. []

JOHN ANDERSON: Do they know what's happened to per pupil expenditures in (inaudible) public schools since Prop. 13? []

(MAN): They don't care. []

SENATOR PAHLS: Yeah, they don't care. If you don't...see, so many of (inaudible) people do not have children in school anymore. Look around this table. If you don't have a child in school, you're probably not as attuned to it as, for example, Doug, since you have children, I know, in school. I'm not insinuating the rest of you don't, but I do know that he does. []

(UNKNOWN): I do. []

SENATOR PAHLS: You have children in school? Well, you're probably more concerned about making sure of those class sizes and you have certified teachers. Because, see, we mandate that you, you know, you can only have so many gigs in a school district. []

(UNKNOWN): Rule 10. []

SENATOR PAHLS: Yeah. See, so those are our mandates. See, I always say to the people, I cop out, I say, no, that's at the local level. They set the property tax. Then they come back to me, say, right Rich, but the Legislature sets the mandates, or the state

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does. A lot of them, that's how they feel. []

ROBERT McMANUS: And my sense is that this goes beyond the schools, but that if you look at the phone book of state...of local employees in the state, it's huge. And every county has...duplicates what every other county does. It's...this is the one thing that just...where Nebraska really seems to stand up among, when you look at all the data, among the other states, is in this area of very, very bottom of state aid to local government and very, very large local government. []

SENATOR KOPPLIN: That's true, but when you start talking about the county levels, we should combine counties, but you start talking about central, western Nebraska, you're talking about miles and miles of travel, which maybe outweigh the need for reducing that tax (inaudible) because people can't (inaudible) to get to their service is miles. We're a very large state so...you know, back to my statement before, we look bad because we don't have a lot of people, but it takes the same amount of roads people and per mile of road repair or whatever in Iowa as it does here, but if you look at it and compare it to population, my, they're not spending so much money on...per person, but it's costing the same amount and it takes the same amount of people. We just don't have enough people. []

MATT JEDLICKA: I guess the argument I make for agriculture, rural areas, is that I don't mind paying a lot, or whatever it'd need to be, for all those things because we get a direct benefit from those, from our NRDs, from our county roads, county fair, anything that's itemized on our tax bill. But when it comes to schools, that's just a strong imbalance, and I echoed this last time to a lot of the same people that were here, and that's why I guess I'm dwelling on these school costs and not everything else. I mean, if we have a lot of employees in Colfax County, that's our problem. But, by God, I benefit from that so I don't mind paying that so much with my ag land taxes. But where we're paying so much for schools...and it's happening again this October. Schuyler is going to try to pass a bond issue to build a K through 3 school and to shuffle kids around

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amongst the other schools. And just trying to explain to some people what somebody in agriculture is going to pay for that that's a 1,000-acre farmer, as opposed to somebody that owns a \$200,000 home in Schuyler, you know, it's very eye-opening to them. You know, the person in town is going to pay \$120 a year on that home; that ag producer is going to pay \$1,100 on his 1,000 acres of farm ground, whether he's owning or renting. I mean, it's going to get passed on to him one way or the other. So, you know, I guess I'm really focusing on education here. []

SENATOR McDONALD: And we can always close half the courthouses. How popular would that be? You know, that idea has always come up, you know, we don't need all the courthouses. We could consolidate. Get rid of some of the county employees. That doesn't fly. []

SENATOR BURLING: That's what I say, they're not ready for that yet. []

SENATOR McDONALD: They're not ready for that yet. []

JOHN ANDERSON: Well, the hope for a long time has been that with technological advance we'd be able to effectively make it easier for people to do their business with local governments on the Internet, electronically, and be able to gain some benefits through those means, and then potentially to eliminate some of the brick-and-mortar presence in every county. But, for the most part, those possibilities haven't been fully realized yet. We haven't...we haven't gotten to the point where you can do most of your business with the local government through your Internet connection from home. []

SENATOR McDONALD: And I think most of the generation are touchy-feely people, you know? Maybe the next generation will be more apt to do it on computer, but most of the people that go into the courthouses at this point in time are probably 50 and over, they do a lot of business there, they're touchy-feely people and they want somebody to talk to and see them and ask about the weather and that kind of stuff. So they're not really

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interested (inaudible). []

JOHN ANDERSON: At the university, we run a whole MBA program online with students all over the world, and they never come to campus. So that's, you know, from my perspective, that's...why can't you run e-government in that sort of way? Potentially, there are lots of possibilities, but the reality of people's demand for local services is they want to be able to go to the courthouse, they want to be able to talk to a person and conduct their business, even though there are great potentials to save money through advances in e-government. But if we get back to this question: How are you going to fund the schools? If schools are a public good that provide benefits for the whole community, and I would argue they are, whether you've got a child in school or not there are benefits to having educated people in your community, that's through. But then the question is, what's the economic base there to support that? The next question is what's the tax base, of course. But what's the economic base to support public goods in the first place? And if it's an ag oriented community, I just don't know what the alternative is other than relying on the agricultural industry in some sense. Now, there ought to be balance there. If there are other industries, of course, you know, we need to think about (inaudible). But in ag communities, where's the other economic base that we could point to, to ask them to shoulder a greater share of the burden of providing the public services that benefit the whole community? []

MATT JEDLICKA: Yeah, shucks, that's the hard part. []

JOHN ANDERSON: Yeah. []

MATT JEDLICKA: You know, I've been studying Proposal 8 a little bit, from Michigan, and they increase their sales tax from 4 to 6,... []

JOHN ANDERSON: Right. []

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MATT JEDLICKA: ...and the people chose that over an increase in income tax. And we're already at 5.5. You really can't go much higher with that. So, you know, that's one man's opinion. And I disagree, I guess, with the Omaha Chamber. I don't feel our income taxes are that far out of line. I don't know if we have room there to raise them. And in this...if I'm reading this right, this right here shows that we're not very progressive compared to other states at all; that we're in line or maybe behind a little bit when it comes to... []

ROBERT McMANUS: What you can't tell, though, is whether it could be that all...that all states are progressive. []

MATT JEDLICKA: Right. Yes. But comparing our sales to other states, we're not more progressive by any means. []

ROBERT McMANUS: It looks like you're more progressive at the higher rates. []

RICHARD BAIER: Yeah, we are much more (inaudible). []

GEORGE KILPATRICK: We're more progressive than most. []

MATT JEDLICKA: Okay, yeah, because we go from 22 to 17, basically. Okay. []

GEORGE KILPATRICK: Yeah, it gets higher as the income (inaudible). []

JOHN ANDERSON: We're moving up in the rankings as you go (inaudible). []

RICHARD BAIER: And the question is, if you look at where's your potential growth and your economy sectors, you know, long term, as farms consolidate, there will be less of you doing the same amount to have the same economic benefit. The real opportunity is in the income tax side, as the people move to the cities, and that may be our economic

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driver. And right now we're in a pretty tough position. I would encourage you, if you've not done that, to drive up to Dakota Dunes and drive through the neighborhoods. So many Nebraska plates are frequenting the houses there. There's a lot of folks that do that. They've already made that choice. []

GEORGE KILPATRICK: Actually, what we're hearing is everybody in Nebraska is driving with South Dakota plates, but that's a different issue. []

SENATOR STUTHMAN: I think, you know, we continually think about, you know, counties, you know, counties should combine services, and the closing of the courthouses, that was brought up here. You know, I look at that as that's totally the wrong direction that we should be looking at because what we will be doing there will be unemploying people and what we need in Nebraska, in my opinion, is to attract the people to come and work here. We need more. You know, we just talked a little bit about, you know, Iowa, the population base. If you have more bodies, if you've got 40 people paying the bill compared to 20, and then you want to shrink the 20 to 15 to pay the total bill, because those bills in the courthouses, unless you completely shut the thing down, you know, there's still going to be expenses. You know, if you have one guy out five miles on the road and he's paying all the taxes, or you got ten guys living on that same road, that's where we...that's where the emphasis we (inaudible). In my opinion, we have to continually work on striving to get people back to the state of Nebraska, and that is a tough, tough sell. But, you know, we continually got to work on, you know, our main product is agriculture. You know, we have value-added agriculture. We got to continue to strive on that. Bring people, bring young people back to hog units to work; you know, build homes in those communities. I mean that's the way I... []

SENATOR PAHLS: But, Arnie, don't you think....I mean we're...you guys, in your area, you're getting larger. You actually...are not the farms and the ranches getting larger? []

SENATOR STUTHMAN: Definitely. []

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SENATOR PAHLS: So they're getting larger, and I just don't know how you can bring the people back...I mean, I'm from a small town, so I'm not against it, but I don't see how you can bring it back because everybody is...you guys are becoming too good at what you do. You know, it used to...you need a bunch of people to help you do your work. You don't need them because of your efficiency, see, which is good. So I'm thinking maybe we ought to take a look at western Nebraska and let you guys grow, make sure you're making money out there so we can get our share of the taxes from you, but I don't know if you can populate some of those areas anymore. []

SENATOR STUTHMAN: Some of those areas, you know, driving out to Valentine, stuff like that, there is, in my opinion, there's no future to try to add population to those areas. []

SENATOR PAHLS: Yeah. Yeah, that, but, like, there may be regions, but I just don't see how we're going to...you guys are too good at what you do. []

SENATOR STUTHMAN: But yet, yeah, we can produce...one man can produce a lot more than we've ever done before. []

SENATOR PAHLS: And we want you...we want you to do that. Actually, we want you guys...to me, logic says get larger, make more money off that farm. The small farmer, I just don't think, or rancher is... []

SENATOR STUTHMAN: But are we going to have to tax that operation more just to pay the whole bill, or are we going to try to attract people to live in communities? You know, Columbus is a very unique community where we have manufacturing coming there, but, you know, you get further out, hundred miles west, and that makes a difference, northwest. []

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SENATOR PAHLS: Yeah. []

MATT JEDLICKA: You know,...oh, I'm sorry, Senator. []

SENATOR STUTHMAN: No, go ahead. []

MATT JEDLICKA: I, you know, this is a big concern for agriculture and it, per acre, if you look at us compared to other states, it's a big burden. Can I think we can get down to other states? No, not at all, because we're a different state. I mean, more cattle, less people. So I don't think that. I just think if we look at our per acre, per producer local property tax, I think it's fair and I don't think anybody in this room, if you sat down with me and I showed you the data I'm looking at, could disagree with me that we need to lower that a little bit. Where it comes from, I don't know. Yes, efficiency is going to play into this. That's also going to, if you look at it at a per producer standpoint, it's going to increase their property tax burden more and more. But that's just the way it's going and I don't think there's any way around that either. []

SENATOR PAHLS: No. No, and I don't know if there should be. I mean, I just think that's fine. []

MATT JEDLICKA: Yeah. []

SENATOR PAHLS: You want property tax to be lowered, so something has to be given up. Because, see, and I'll just be, you know, sort of...because then I, the city dweller, my sales tax and all that probably will go up or...and then somehow the money has got to...you know. So the money will probably come from maybe, what, a half a dozen counties? Isn't that what we have? Don't we have about a half dozen counties who really produce a lot of sales and income tax? []

GEORGE KILPATRICK: Well, there's more than that, but... []

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DOUG EWALD: Well, have four counties with 90 percent of the population today. []

SENATOR PAHLS: Okay. Well, 90 percent of the population tells me then the income and sales has got to be coming an awful lot from those people. []

GEORGE KILPATRICK: Sure. []

SENATOR PAHLS: I mean, if you have 90 percent. []

GEORGE KILPATRICK: There's a correlation between revenue generated in the area and the population in the area. []

SENATOR PAHLS: Yeah. []

GEORGE KILPATRICK: Yes. []

SENATOR PAHLS: So...you say 90 percent in four counties? []

DOUG EWALD: Yes. []

SENATOR BURLING: Bob, you indicated to me that the property tax debate was input; you weren't seeking any decisions on that today. Is that right? []

ROBERT McMANUS: Well, here's what...(inaudible). What I'm hoping to get accomplished, there are a couple of these papers today of the drafts that we may be able to come to closure on, but what I'm hoping is that...our next meeting is going to be October 12? []

SENATOR BURLING: No, September 14. []

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ROBERT McMANUS: Sorry, September 14, and at that meeting we really need to...the commission needs to start making decisions to promote where they want to go, and especially in terms of the more global shifting between taxes. The final report of the commission is due November 15? And so we really...I think the critical decisions need to be made by the next meeting. And then (inaudible) property tax (inaudible), but what we found in property tax is, by any measure, it's high, and all the studies show it's high. When we went to North Platte, that's all we heard was property tax. I mean people...people don't complain too much about the sales tax, but people are all complaining about property tax. The state funding to local government is at the very bottom and so that's the dilemma that I see, is if that (inaudible) was just stated, if you don't cut local government and you do increase state funding for property taxes, then you're simply going to raise another tax. But if all the...of all of the taxes that we've looked at, the property tax does seem to be the one that is...where we are the most out of line. And also, state funding to local government is one of the most out of line. And in both cases, you know, I kept going back to the 1988 Syracuse Study,... []

DOUG EWALD: The Syracuse Study. []

ROBERT McMANUS: ...and that's exactly what they found. They said you're way out of line on both of those so...and, really, nothing has changed on that. []

DOUG EWALD: I have a question on that. When you were at North Platte--I wasn't out there--when they talked about property tax, were you able to ask them if they were talking to their local people about property tax as well, in addition to, you know, this forum? Were they talking to their city, you know, city/county people as well? Do we ask them that? []

GEORGE KILPATRICK: Somebody did. []

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DOUG EWALD: And I guess that if we...and if that question was asked then, what was their response? []

ROBERT McMANUS: That question was raised at one point, but I'd say that the thrust of at least four of the testimonies was to...that property tax in rural Nebraska is killing the ranchers and farmers who are saying we pay no income tax because we don't make any income, but we're paying the property tax. And they were generally advocating...I mean, it was clear that they wanted some other tax, some state assistance of an...I mean, what I kept hearing is a broad excise tax would be preferable and...but they were definitely looking for state assistance. But, no, nobody was saying that we're putting pressure and we're critically asking our local people to look at their budgets. []

DOUG EWALD: I was going to say, it's easy to call your state senator and pick up the phone as opposed to go present in front of a school board or county board or something like that anyway. It's real easy to pick up the phone and get in the ear of your state senator. []

GEORGE KILPATRICK: You know, there was some of that. But the other thing about that particular hearing was there was a...is that's sort of where you get the hard edge that the taxes are just too high; it is fundamentally unfair and must be eliminated. So there was that, as well. []

RICHARD BAIER: Think the other thing we heard out there was in terms of the sticker shock when people do valuation increases. It's interesting, because that is a common thread among rural and urban, you know. And again, I use Lincoln's example. We went through this in Lancaster County and increased everybody's valuation last year. I think it was just about everybody in town. When they got through with the protest and got their numbers more consistent, you're down to, what, 28 or 29 or whatever the number was, wound up having, you know, sizeable valuation increases. All we did in the middle was create a great deal of work for the assessor and the people that had the protests in the

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middle. []

DON FREEMAN: And regarding the cost of education, what can be done to make school boards more efficient? How can you do...what do you, put a lower lid? Make them work within a restricted budget? Can that be done? We've got a district by York that vote the...over the lid every time to keep the school open and...but I don't know what else can be done. They have mandates from federal and state that we want done, and rightly so, but at the same time can you make a district more efficient? I was on the school board for almost 12 years in York and very frustrating. I mean, you just...of course, most of the cost is teachers, is people, and so how do you make a district more effective, more efficient? Very difficult to do. Our district in York had to get rid of its 15-passenger vans because of roll over. Now they're buying 7-passenger SUVs, I guess. All of those things just keep on adding on to the cost of education. And at one time we talked about not using bussing within, I think it was, a five-limit within the district. We tried to talk about that to cut down on transportation costs. Of course, that didn't...and we wanted to cut sports programs. That didn't work. And so it's very difficult to force a district to be efficient; same with county government and city government. What can be done there to make government more efficient? To me, that's...instead of more taxes, less cost. And I don't know how we're going to do that or how we can recommend that. But something has to be done to...if you're in business, you just can't keep on adding on sales, your price, as a tax increase to cover your costs. You can't. You've got to become more efficient, get more taxpayers? How do we do that? Make the state grow. How do you make the state grow? Lower the taxes. And it's something that's...I...it's very frustrating to sit here and try to go through this. It's a very complicated procedure and it just seems to me that I don't see any real long-range program--maybe we can't do it--to rotate our taxes then to be more competitive, rotate our taxes into getting away from property tax. And it's...I don't know how it's going to happen. It's going to have to happen someday. I don't know how. []

SENATOR STUTHMAN: You know, I think...I think one of the main things, and I've been

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a county supervisor and then...and a senator right now, and as we heard last year, you know, all the people that were campaigning, you know, property tax was the number one issue that they wanted the senators to take care of. You know, as far as I'm concerned, you know, the property tax is assessed locally, collected locally, and spent locally, and we really don't have much to do. The only thing that we can help, as a state, is to give, you know, incentives or subsidy to counties, local governments, roads department or something like that. And I think once the people understand, you know, that it's the local board is one that's in control of it, and I always say, you tell me what program you want to give up or want to have cut; then we can...then we can adjust the property taxes. And they seem to back up then. They say, well, you know, I don't want to cut this. I don't want to cut education for our kids. We don't want to cut that. But yet, when they get their bill once a year and the thing that just almost blows my head off is when they get their revaluation, they say, I got a letter my taxes are going up. He says, no, your valuation went up, you know? []

DON FREEMAN: Right, but. []

SENATOR STUTHMAN: But, you know, your taxes may be up a little bit, but that's the mill levy, is where that is set by. So it's a real...it's a real situation that I don't know...you know, we worked at that on the county level. You've got...you've got, you know, county jails and everything like that what, you know, the county has to pay. It's a tough road to hoe. And the schools, schools, schools take up, what, 80, 70-80 percent of your property taxes, and 70-80-90 percent of that is salaries, to start with. So, you know, are you going to tell the teachers to take less or cut down on teachers? []

DON FREEMAN: Well, you want good teachers, you know, and... []

SENATOR STUTHMAN: Yeah, you want good teachers, and I've got two of them in my family, so... []

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JOHN ANDERSON: Well, the salary structure, I mean, we have among the lowest teacher salaries in the country, according to the data I've seen. So it's not that the salaries are high. It may be that we've got...that doesn't mean we've got low costs per pupil in terms of administrative cost and other things. But I was interested in Richard's observation about the...part of the difficulty in economic development is in attracting or, well, firms that move in and they know the local labor market conditions very well, you said. They know exactly what kind of workers are here. Part of the problem seems to be the slowness of adjustment in labor markets to the local conditions. We are blessed with relatively low unemployment rates in Nebraska, fairly tight labor markets, but that doesn't translate into rising wages, attracting workers to come in and fill those jobs. What do you think the impediments are? Why this persistent problem of relatively low wages on a national level, low unemployment, and not rising wages attracting more workers and in-migration? []

RICHARD BAIER: That is a complicated question. (Laughter) []

JOHN ANDERSON: But I mean that's at the heart of much of what we're talking about. []

RICHARD BAIER: Yeah, and you get at all sorts of things. In terms of, and I would argue right now in Nebraska we could tolerate (inaudible) exactly what you're talking about. I did a Panhandle tour in early August. We have probably right now 1,500 good-paying openings in the Panhandle. Our challenge may not be out there, and I've suggested to some of our communities you really probably shouldn't be doing economic development for awhile; you might want to be doing labor and housing, because that's part of the challenge that we've got out there. If you've got a ton of openings going unfilled, when can you be able to bring those bodies? I think we ought to, as a state, one of my concerns is looking at the income tax numbers in that \$50,000 to \$100,000 range, because in terms of the companies that I'm looking at, whether it's Burlington Northern or Union Pacific or Lehman Brothers in the communities that growing, they're

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creating opportunities in those income ranges. []

DON FREEMAN: You talk about lower wages. In manufacturing, when you're paying up to \$1,000 a month for employee healthcare, workmen's comp rates of over 8 percent, some place you've got to be competitive and the first thing you do is try to get as much for the hour pay for the employee as possible, and it makes it very difficult, retirement fund, sick leave, all those things. And...but at the same time, I think that our cost of living is a little bit less here in Nebraska, at least now in the state of Nebraska it is, so I think that helps the employee. And most of them have...maybe have a half job, too, or their wife works. That's another reason. But it's very difficult to keep your price down in order to sell it, yeah. []

JOHN ANDERSON: So we're in competitive markets for the products that limit your ability to pay higher wages... []

DON FREEMAN: Could be. []

JOHN ANDERSON: ...to attract more workers. []

DON FREEMAN: That's right. It's a Catch 22. []

JOHN ANDERSON: Yeah. []

RICHARD BAIER: And some of that, John, in especially the more rural areas, one of the things we struggle with is just a lack of leadership and willingness to grow their communities. I mean I will tell you I've been a big believer for a long time and along Highway 2, the area that Senator (inaudible) was just talking about, one real opportunity we have along parts of Highway 82 is in the tourism area, and I would argue that the best thing we could do is plant a national park out there--personal belief, before you start throwing sticks, because... []

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JOHN ANDERSON: So that's federal money. []

RICHARD BAIER: ...I about got chased out of town in the Sandhills because they're...to really drive that economy, the farms are not getting smaller. Well, to keep people there, you're going to have to have other kinds of activities. We've got to be willing to step outside of our own boxes. The other thing we did is we sold for a long time on the theory that we were a good location for branch plants, and that was part of our...going clear back to before Bob Kerrey and, you know, we got pretty good at that. And what we don't always have is a lot of people who own those businesses locally and do the local patents and those kinds of things. And so we need to do a better job of those startups as well. That will help those communities and create different kinds of opportunities. []

JOHN ANDERSON: Well, there we've got to solve some of the problems we've got of the intellectual property rights questions, the things that are coming out of the university system, converting those into products that can generate employment. []

RICHARD BAIER: Exactly. []

ROBERT McMANUS: Well, this might segue into the corporate income tax discussion, which is a paper which I think is more complete than the others and one that we'd like to be able to reach some discussions on. So, John, I'm going to...we'll turn to corporate income tax and, John, I'm going to kick it off and then turn it to you. []

JOHN ANDERSON: Okay. []

ROBERT McMANUS: What we found on corporate income tax, Nebraska used what they called the standard three-factor apportionment formula until the 19...it got phased out between 1988 and 1991, and at which time Nebraska went to a single factor formula. The corporate income tax has been declining in importance over time, and it's

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been attributed primarily to two factors, but one is the single factor sales formula was put in, and the second is the incentives, business incentives, that are being put in, so that today it's just producing slightly over \$200 million a year, which is less than you'd get from a 1 percent sales tax. And yet, when you look at the data, we're right in the middle of the pack among the states for corporate income tax, and what we've been seeing has been happening across the nation, that all state corporate income tax is becoming less and less important. And so, as I put in the paper, there are...some of the leading commentators...and it's happening across the states for the very same reason. And the Syracuse Study back in '88 recommended (inaudible) into the single factor formula and staying with the double weighted sales factor, something not quite as extreme, but Iowa at the time had a single factor formula and Nebraska really was almost having to. At the time, what we were seeing is any state that has a single factor formula, all the states around it pretty soon adopt it. But in any event, what's happened since the Syracuse Study came out saying don't adopt it, well, Nebraska did adopt it, but then a whole series of other states have also adopted it, and so it's a...and more states every year consider it, and it could very well be that in another ten years the single factor formula may be in every state, or at least in a majority of them. And a final point is that those commentators looking at corporate income tax, there are a number of them who are now saying that it's probably that, in some sense, you could just do away with corporate income tax because corporations pay taxes in a lot of other ways, in a lot of other taxes. However, it does...you can't...you can't really have personal income tax without having a corporate income tax as a backstop, because if you did corporations...or individuals could incorporate and shelter some of their income from the personal tax. So those are the...that's the data that I saw, and I'll turn it over to John. []

JOHN ANDERSON: Yeah, so we're in this relatively odd situation where we've got a tax on corporations, which is effectively a tax on capital. But we're apportioning it as if it were essentially a sales tax. It's based on, you know, your sales in this state. So it's an odd combination. In a perfect world, you probably wouldn't do this. You wouldn't design a tax this way. In terms of tax policy, it doesn't make much sense, and the Syracuse

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people understood that and recommended against going to sales-only apportionment because that doesn't really fit corporate income tax, which is essentially a capital tax. But I don't think we're going to go back to a world in which we've got, you know, three-factor apportionment in all the 50 states so everything adds up appropriately and every dollar of corporate income is taxed once and only once, depending on what state it's attributed to. The reality is, you know, we've got single factor apportionment, and with Iowa next door taxing on that basis, we probably don't have any choice, but the state is single factor apportionment. So it's...from a policy point of view, it's an odd situation. It's certainly not a perfect remedy to the situation, and we're left with relatively little revenue coming from the tax, but that's true at the national level, although in the last, what, last fiscal year and this fiscal year, at the federal level corporate income tax revenues have been higher than they have been in recent years. The federal corporate revenues have been coming in above expectations the last two years. That, you know, that may be due to particular circumstances, and changes to the federal tax law is driving that more so than an overall trend of increasing a reliance on corporate income taxes. The long-term trend for the states has been declining corporate income taxes, and if it weren't for the issue, as Bob pointed out, that it's (inaudible) personal income tax, you might be tempted to swap the corporate income tax revenues for all the incentive programs, for example. That idea has been around for some time. What kind of economic development punch could you get by advertising that you have no corporate income tax? But then we'd have to find some remedy to the issue that it would be harder to collect personal income tax revenue if we didn't have a corporate income tax. So that's the difficulty in going that route. And so the policy question is, are we better off in this circumstance with a corporate income tax that generates a relatively small amount of revenue, keeping it just to make sure we maintain the integrity of the personal income tax system, because that's so important to the revenue structure of the state; keep it as a necessary piece to maintain the personal income tax revenue even though in the overall picture it's not doing much for us in terms of revenue, especially when we offset that with incentives, you know, where the incentives may be worth as much or more as the revenue we're generating from the corporate income tax? So that's

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the policy question for the commission: Do we recommend any change from this sort of status quo situation, keeping the corporate income tax with relatively modest revenue for the benefits it gives us on the personal side, rather than recommending some kind of radical solution that eliminates it and then gives us the problem of figuring out how we're going to collect some of our personal income tax that may disappear without corporate income tax? []

DON FREEMAN: Help me with this. If we would eliminate the corporate income tax, that is forever. That's not for two years, five years, ten years (inaudible). []

JOHN ANDERSON: Well, it's as permanent as any tax law change. []

DON FREEMAN: Yeah, I understand, but assuming that we could withhold...uphold that,... []

JOHN ANDERSON: Yeah. []

DON FREEMAN: ...it would be forever. And wouldn't that be very attractive for companies wanting to expand, wanting to migrate to Nebraska, knowing they would not have income tax, corporate income tax? And it would probably eliminate...it could eliminate some of our incentives. I don't know. []

RICHARD BAIER: Well, it'd have significantly less an impact. []

DON FREEMAN: Sure. []

RICHARD BAIER: Sure, of the incentive cost. []

DON FREEMAN: So it'd seem to me that would be...regarding the personal income tax, what is the problem between the two? []

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JOHN ANDERSON: I think George can articulate the problem. What's...if we eliminated the corporate income tax, what does that make vulnerable on the personal side? []

GEORGE KILPATRICK: It just gives some people some opportunities to incorporate businesses. For example, you would never set up another LOC, not in Nebraska anyway, because it would be subject to income tax. It (inaudible) be subject to the corporate income tax if you didn't have one. So the corporation retains the earnings and can retain the earnings (inaudible) out to owners, (inaudible) have any tax. []

DON FREEMAN: So that could be changed by...that could be changed by legislative action, couldn't it? Could that...you could protect against that loophole? []

GEORGE KILPATRICK: No. I mean a corporation is a different entity. []

DOUG EWALD: Well, you could go to some sort of a franchise tax then,... []

GEORGE KILPATRICK: You could go to a franchise... []

DOUG EWALD: ...franchise tax instead of income tax, which goes to more of your tax on capital, from that standpoint. []

GEORGE KILPATRICK: Well, it could be, and if that's the case then what you're going to do is subject it over providerships or LCs or whatever the form is. []

DOUG EWALD: Yeah. []

GEORGE KILPATRICK: But then you're not eliminating it; you're changing it to something else. (Laugh) []

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DOUG EWALD: Then you lose some of the benefit of getting rid of corporate income tax. []

DON FREEMAN: Yes, right. Indeed, yeah. Well, I don't mean...to me, it would only be an option that should be examined, anyway. []

RICHARD BAIER: Yeah, the challenge that we have, Don, is a lot of our projects right now are tied to companies that aren't C corps. I don't remember what the mix is and I'd have to go back and look, but, you know, like the BPI at South Sioux City is privately owned. So we get a lot of that, and we still get UPs (inaudible) and the Cabela's and those kinds of folks, but a lot of the new projects, especially the small startups, are LLCs or... []

JOHN ANDERSON: They're not C corps. They're S corps. []

RICHARD BAIER: They're S corps or LLCs or... []

DON FREEMAN: Uh-huh. []

ROBERT McMANUS: But the other reality is that with this one-factor formula, sales formula, corporations in a state which manufacture in the state and have payroll in the state and have plants in the state like it. They like that one-factor formula because they're not being taxed on their plant and employees. So I don't detect that there's any corporations really complaining other than a corporation which does purely sales in the state. []

JOHN ANDERSON: Well, it's good for the companies that produce their products here and sell them outside. It's great for them. []

GEORGE KILPATRICK: The other thing...the other thing...point that I wanted to make,

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Don, is in terms of the economic incentive. If somebody is actually moving to the state, then they're going to be tax incentive qualifying. They're not going to be paying corporate income tax for the entitlement period anyway. []

DON FREEMAN: Right. Yeah. Yeah. []

DOUG EWALD: Well, I guess one thing, to follow up on what John said, it looks like we might be a little bit out of whack, the states, as compared to what's happening at the federal level right now with all-time record corporate income tax receipts at the federal level. And a lot of that is due to the special...the bonus depreciation in 2000, 2001, 2002, the 30-50 percent that a lot, many states, Nebraska included, decoupled from. Which means that we didn't allow companies the deduction at the state level that they were able to take at the federal level. They've burned through that at the federal level so now they have less expense on their books at the federal level, but now they're getting the deduction at the state level. It's just a deferred deduction compared to when it was...when that whole program came together. []

JOHN ANDERSON: Yeah, and some of it may be one-time (inaudible) from foreign subsidiaries and so on, so there's lots of reasons why the federal corporate revenues are at all-time record highs and the states' are not. So I think the overall trend, as Bob has said, is downward--declining reliance on the corporate income tax relative to other tax sources for states, for the most part--and that's not likely to change. But it puts us in a position of having this tax and you get to the point where you have to ask the question: What's it doing for us in terms of the overall picture? Is it generating sufficient revenue to maintain it? There are administrative costs, of course, but then there are the difficulties of...potential difficulties getting rid of it in terms of a loss of personal income tax revenue. So it's a difficult policy question and...but the commission has the opportunity to speak to that issue, if it cares to and has a view on whether we ought to make a recommendation on modifying the corporate income tax, either eliminating it or changing into a franchise tax or a gross receipts tax or something else, if we think that's

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appropriate. []

SENATOR BURLING: Does the subcommittee have a recommendation? []

JOHN ANDERSON: We haven't brought a recommendation along those lines, no. []

ROBERT McMANUS: We...it didn't seem to us that it should be looked at as a source of new revenue, because that's counter to what...everything else we're trying to do in this state. And so the question was, do you eliminate it, which has its difficulties, or, in this case, do you just say that this one is working and, coupled with the incentive programs, is not scaring off businesses and, in fact, may be attracting businesses? []

SENATOR BURLING: So the corporate income tax should be an issue looked at in connection with business tax incentives? []

ROBERT McMANUS: Oh, absolutely, because the business tax incentives impact the amount of corporate income tax that comes in. []

SENATOR BURLING: I understand that, but I mean, you know, if we're going to take a...next time we take a look at business tax incentives, that should be...whether or not we continue the corporate tax should be part of that discussion? That could be a recommendation of the commission. []

RICHARD BAIER: I wouldn't even mind a recommendation to go in as part of this incentive review every three years, if you want to build it in as part of your recommendation. []

JOHN ANDERSON: It would give you the bigger picture of the incentives as they're, in part, delivered through the corporate income tax mechanism, whether that's the right mechanism to deliver incentives. []

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RICHARD BAIER: Yep. []

SENATOR BURLING: Comments? []

ROBERT McMANUS: Do we want to make a motion on that? []

SENATOR BURLING: Well, are we ready? I mean that's why I asked for comments. Are we? []

DOUG EWALD: I think that's fair. You're not tying your hands. []

SENATOR BURLING: Is somebody ready to make a motion of some kind that Bob can build something on to either bring this to closure or this issue to closure, or bring it back in two weeks for continued...? []

JOHN ANDERSON: Well, let's see, maybe we can articulate what we just said. I'll make a motion that the commission recommend review of the corporate income tax and its role as a delivery mechanism for business incentives. That make sense? Is that complete enough. You want to read back what I just said? []

SENATOR BURLING: Do you know what he said? []

AMANDA JOHNSON: I don't have it all. (Laughter) I was wondering if Bob did. []

JOHN ANDERSON: That we recommend that the commission...well, I think... []

ROBERT McMANUS: A review of corporate income tax and its role as a delivery method for business incentives... []

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JOHN ANDERSON: Is that broad enough? I mean... []

ROBERT McMANUS: ...at the next time that the Legislature looks at business incentives. []

JOHN ANDERSON: Okay. []

SENATOR BURLING: But then you want some more in there. []

RICHARD BAIER: That's good. []

SENATOR BURLING: You just want to leave it? []

RICHARD BAIER: Yeah. That would be fine. []

SENATOR BURLING: You don't want to tell us to do it in three years. []

RICHARD BAIER: (Inaudible) be almost nice, but that's no big deal. We'll just make it happen. []

SENATOR BURLING: Comments? []

SENATOR STUTHMAN: Second. []

SENATOR BURLING: Been seconded. Discussion? Everybody understands what they're voting on? Okay. Call the roll. Thank you. []

AMANDA JOHNSON: John Anderson. []

JOHN ANDERSON: Aye. []

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AMANDA JOHNSON: Richard Baier. []

RICHARD BAIER: I'd abstain. []

AMANDA JOHNSON: Senator Burling. []

SENATOR BURLING: Yes. []

AMANDA JOHNSON: Doug Ewald []

DOUG EWALD: Aye. []

AMANDA JOHNSON: Senator Fischer. Don Freeman. []

DON FREEMAN: Yes. []

AMANDA JOHNSON: Mike Hybl. Matt Jedlicka. []

MATT JEDLICKA: Yes. []

AMANDA JOHNSON: Senator Kopplin. []

SENATOR KOPPLIN: Yes. []

AMANDA JOHNSON: Senator Louden. Senator McDonald. []

SENATOR McDONALD: Yes. []

AMANDA JOHNSON: Milo Mumgaard. Mark Munger. Senator Pahls. []

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SENATOR PAHLS: Yes. []

AMANDA JOHNSON: Senator Raikes. Senator Stuthman. []

SENATOR STUTHMAN: Yes. []

AMANDA JOHNSON: Nine ayes. []

SENATOR BURLING: Motion is carried. Thank you. Bob. []

ROBERT McMANUS: Okay. The personal income tax paper I want to withhold for the next meeting because it's not complete. What's missing from that paper is the analysis, the work that the Department of Revenue did recently this year on how...the burden of the tax, how it falls on Nebraskans. And so I'm going to fold that information into the next draft and we'll talk about that at the next meeting. And that moves us to... []

SENATOR BURLING: Administration you want to go? []

GEORGE KILPATRICK: Demographics? []

ROBERT McMANUS: Yeah, tax administration. []

GEORGE KILPATRICK: Okay. []

ROBERT McMANUS: Which I can't find my copy of. Oh, there is it. Back in March, we took a look at state tax administration and this is really looking at the fairness of the hearing process from the taxpayers' point of view. In the last 20 years, there's been a considerable movement towards taxpayers' rights and taxpayers have been advocating across the states for a fair hearing process. And we looked at the American Bar

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Association's model tax act and brought in the committee...representatives of the Committee of State Taxation who evaluate the fairness of the tax process across all the states. And the...when COST examined Nebraska's appeal system, they found it to be fundamentally fair and sound; and in their ranking system, which went from A to F, with some states getting F, they gave Nebraska a solid B grade. And they found a number of...a question that Senator Burling and I had, George, was can the hearing administrative judge in the...is within the Department of Revenue? []

GEORGE KILPATRICK: Yes. []

DOUG EWALD: Hearing officer? Yes. []

ROBERT McMANUS: And the commissioner would have to sign and approve of that hearing decision? []

DOUG EWALD: The hearing officer performs the formal hearing function and brings a recommendation to the commissioner for approval or denial, is the way it works today. Now that hearing officer (inaudible) is an employee of the Department of Revenue. []

GEORGE KILPATRICK: It's in-house, always has been. []

ROBERT McMANUS: Well, notwithstanding that, COST gave it a grade of B, and what they...and then what they recommended were some very minor tweaks to some statutes that would get you to A, and those were mainly related to times for appeals and things, which...so...but they recommended that the current period for protesting sales tax assessment of 30 day be extended to 60 days; the date for filing state income tax returns is currently the same as for filing the federal returns, that that be at least 30 days later, which is the case in most states. []

SENATOR BURLING: Do you know why that recommendation was made? Yeah, that

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one you just read, why? []

ROBERT McMANUS: Because if you're doing your federal return, a lot of people doing...a lot of corporations, people doing the federal return are also doing the state return, and the numbers change and you find out the day of filing that it's just administratively they can't do it. It's very difficult for a corporation (inaudible) to do their state returns on the same...the reason being that at a corporate level the state return is based upon your federal tax return. []

DOUG EWALD: That's right. []

SENATOR BURLING: Do you concur with that, Doug? []

DOUG EWALD: I concur with that. I mean federal adjusted gross income at the individual level is the starting point for Nebraska, so it might (inaudible) with...at the corporate level, your federal taxable income is your starting point for Nebraska corporate taxable income. []

SENATOR BURLING: So the 30-day delay makes sense to you. []

DOUG EWALD: It...there's some merit to that. []

SENATOR BURLING: Apparently there's some nonmerit to that too. (Laughter) []

DOUG EWALD: Well, no, I mean...no, there is some merit to that. It's just a matter of do you want to change your process? Yeah, we can change it, if it's backing it up two weeks or a month. I know Iowa is at April 30 maybe or something along those lines, just to give them a couple more weeks or something to be able to react to that. []

ROBERT McMANUS: And I think this recommendation pertained only to corporate

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income tax. []

GEORGE KILPATRICK: Not individual? []

ROBERT McMANUS: At least...well, at least the COST... []

GEORGE KILPATRICK: I guess I thought it was both, but... []

DOUG EWALD: I think...well, it would probably be...most corporate returns are extended anyway, so it's really the impact would be on individuals, and some of those are extended, but more corporations are extended. []

GEORGE KILPATRICK: Although I think COST would want it to be (inaudible) exempted extended date as well. []

DOUG EWALD: Probably. Yeah, it probably would. []

ROBERT McMANUS: Right. Because usually your corporate is extended because your federal is extended. []

DOUG EWALD: Yes. []

GEORGE KILPATRICK: Yes. []

DOUG EWALD: That's automatic in Nebraska here. []

ROBERT McMANUS: And then the final recommendation was the administrative hearing officer should not have offices within the Department of Revenue and should be moved to a neutral state office site. []

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DOUG EWALD: Now there's a couple things there that we've acted on already, and I believe it's public knowledge. I am eliminating a hearing officer position within the Department of Revenue. The timing of that has not been determined yet, and we will contract that out with an attorney or firm, somebody on the outside. And I look at what dollars are going to hearing; I'm appalled (inaudible). (Inaudible) get \$135,000 issue, taxpayer has offered to settle for 70 percent, 70 cents on the dollar; we've countered at 85. I say, you can't tell me we can't get together for \$20,000. We have certain issues we have to stand on, but I'm trying to move us towards more credible assessments and reasonable settlements so that we tie things up for a shorter period of time, taking that outside the Department of Revenue, and I think we can get a better result there and save some money for the state as well. The other thing that we'll be running some...and our cleanup legislation for next year will be to mirror the extension in the amount of time they have to file a protest. Today you talked about sales tax is 30 days; income is 90. The proposal is to make them both 60 so that, either way, they know what it is, whether it's income or sales and use. So those are a couple things that have happened and what we'll propose for next year. []

SENATOR BURLING: I guess this leads me to ask, Doug, you doing this administratively I think is great. Where then does that leave us as far as recommendation in our document? How much should we say about appeal and... []

DOUG EWALD: Well, you can confirm my (laugh). No. []

ROBERT McMANUS: Yeah, right. []

GEORGE KILPATRICK: Say you recommend that he does (inaudible). []

ROBERT McMANUS: (Inaudible) his recommendations. Doug, are you able to change all of the dates (inaudible) legislation? []

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DOUG EWALD: No. Mean, the dates would take legislation. []

ROBERT McMANUS: So that's the piece. []

DOUG EWALD: Yes. Mean, that's the piece where you can have a definitive recommendation from that standpoint. []

SENATOR BURLING: Well, you know, if you're eliminating the hearing officer from your department then, number three, to move that person physically to a neutral place is irrelevant. []

DOUG EWALD: That's going to happen. Right. []

SENATOR BURLING: That was the source of my question, you know. []

DOUG EWALD: Sure. []

SENATOR BURLING: We wouldn't even need to mention that. []

DOUG EWALD: Right. That's true. I mean we will either provide space in a conference room in the State Office Building or something like that, but it won't physically be held within a hearing room in the Department of Revenue, and we may actually even do it off site, depending on what type of arrangement we enter into. []

ROBERT McMANUS: So it would seem to me that we could still include that as a recommendation, unless it's already done. []

DOUG EWALD: It's not. It will be. The timing is to be determined here. Hopefully it will be done by the end of the year. []

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SENATOR BURLING: Comments? []

JOHN ANDERSON: We might as well still make the recommendation. []

GEORGE KILPATRICK: I would leave it in the recommendations. When you're keeping score at the end, it will look better. []

ROBERT McMANUS: Yeah, something was done. []

DOUG EWALD: We get one, he gets one. []

ROBERT McMANUS: We call this low-hanging fruit. (Laughter) []

DOUG EWALD: That's kind of the way I saw it too. []

SENATOR BURLING: Yeah, it won't hurt anything. Any other comments on...Bob, did you have...so are you wanting a motion on...? []

ROBERT McMANUS: I would. I would like a motion (inaudible). []

SENATOR BURLING: That the commission approve this particular recommendation right here? Is that...? []

ROBERT McMANUS: I'd like a motion that the commission approve a recommendation that would recommend that the three COST items that are listed on the last page be put into place. []

SENATOR BURLING: Part of our report. Okay. []

SENATOR STUTHMAN: I so move. []

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SENATOR BURLING: Senator Stuthman moved. []

AMANDA JOHNSON: (Inaudible). []

SENATOR BURLING: What's that? []

AMANDA JOHNSON: Who made that motion? []

SENATOR BURLING: No, I didn't make it. []

AMANDA JOHNSON: Who made the motion? []

ROBERT McMANUS: I made that (inaudible). []

SENATOR BURLING: Senator Stuthman... []

GEORGE KILPATRICK: Senator Stuthman moved. []

AMANDA JOHNSON: Oh, okay. []

SENATOR BURLING: ...made the motion. []

GEORGE KILPATRICK: Is there a second? []

SENATOR BURLING: Seconded? Who? []

JOHN ANDERSON: Second. []

SENATOR BURLING: Seconded by John Anderson. Any more discussion? []

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SENATOR STUTHMAN: I think it's important that we do leave that in because as of now, you know, that position is still there yet, isn't it? []

DOUG EWALD: That's correct. []

SENATOR STUTHMAN: So I think that's important that we leave that in there because, when that does take place, then you know that can be handled at that time, so... []

MATT JEDLICKA: I don't have that document in front of me. Were we moving back that tax date a month? Is that what the recommendation was, for out-of-state businesses? []

ROBERT McMANUS: Thirty days. []

MATT JEDLICKA: Or for multistate, 30 days then? []

ROBERT McMANUS: For any business. []

SENATOR BURLING: Did you have a problem with the 30 days, you wanted to change it to...? []

MATT JEDLICKA: Somebody threw out...or maybe, Doug, maybe it was you, two weeks, and I just wanted to make sure that that's what the motion was, since I didn't have it in front of me. I failed to print off that part of it. []

SENATOR BURLING: Okay. Yeah, the motion says 30 days. []

MATT JEDLICKA: Yep. []

ROBERT McMANUS: Although I think what...the way that I would conclude it, and we

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could always revisit this again after you see the paper, would be to recommend that the Legislature relook, just in a more general term, at the time and adopt a protest date that provides more time for taxpayers, such as the 30 days that was recommended. []

SENATOR BURLING: You see... []

DOUG EWALD: Now you said protest date. Is that...I hear you say one thing with the protest date, but are you talking about 30 days for filing? []

ROBERT McMANUS: Right, for filing. []

DOUG EWALD: For filing a protest or filing a return? []

ROBERT McMANUS: Um... []

DOUG EWALD: I thought we were talking returns, correct? []

ROBERT McMANUS: Yeah. []

DOUG EWALD: Correct. []

SENATOR BURLING: Yeah, returns. []

GEORGE KILPATRICK: Income tax returns. []

DOUG EWALD: Yes. []

JOHN ANDERSON: Good point. []

SENATOR BURLING: I think, Matt, what we're doing here is making a recommendation

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and we're not passing law. The Legislature could look at that and say, well, the recommendation here is 30 days and we're going to make it 15 or 60. But it's a guideline for the Legislature to look at and say, well, there must be something we ought to do there but we don't agree with the 30. We'll go 20 or 10 or...okay. Any other comments? Are you ready to vote? Call the roll. []

AMANDA JOHNSON: Richard Baier. []

RICHARD BAIER: Yes. []

AMANDA JOHNSON: Senator Burling. []

SENATOR BURLING: Yes. []

AMANDA JOHNSON: Doug Ewald. []

DOUG EWALD: Yes. []

AMANDA JOHNSON: Senator Fischer. Don Freeman. []

DON FREEMAN: Yes. []

AMANDA JOHNSON: Mike Hybl. Matthew Jedlicka. []

MATT JEDLICKA: Yes. []

AMANDA JOHNSON: Senator Kopplin. []

SENATOR KOPPLIN: Yes. []

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AMANDA JOHNSON: Senator Louden. Senator McDonald. []

SENATOR McDONALD: Yes. []

AMANDA JOHNSON: Milo Mumgaard. Mark Munger. Senator Pahls. []

SENATOR PAHLS: Yes. []

AMANDA JOHNSON: Senator Raikes. Senator Stuthman. []

SENATOR STUTHMAN: Yes. []

AMANDA JOHNSON: Nine ayes, no nays. []

SENATOR BURLING: That's carried. Thank you. []

ROBERT McMANUS: Okay, the last paper today is the sales tax paper. The subcommittees met several times and what we find is that Nebraska is in the norm on sales tax. Our 5.5 percent rate is slightly above the norm. The highest rate is Vermont at 9 percent; California is at 9 percent; there's a (inaudible) 9.5 percent. Even it's...the sales tax is regressive in nature, but it seems to be the tax that most people view, at least in the literature that I've seen, that most people view as the most fair tax because if you don't consume, you don't spend. Because it is regressive though, because the very poor spend all of their income, most states give exemptions for food and all states give exemptions for medicines. What's interesting about the food exemption is that there's a movement now towards trying to isolate the food exemption to the very poor, which has not been possible really in the past, but it's...I shouldn't say that...but it's...some of the commentators believe that taxing...allowing all food to be taxed...to not be taxed actually increases the regressivity of the tax. And so the two methods that are being advocated are a debit card method, which is still probably about five years away but at some point

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that the very poor could have a debit card which would allow them to buy food where tax would not be looked at, and it seems to me that we ought to keep our eye on that technology, but the other method is a credit mechanism where the very poor would...well, you would tax food, but you give a tax credit to the poor, who can recover it through the income tax. And what's interesting is that's precisely the type of tax that Nebraska originally had. And they did away with that, well, it's in the paper, but it's been some time ago. []

DOUG EWALD: Yeah, quite awhile ago. []

ROBERT McMANUS: Quite awhile ago. And then I'm going to turn this to Don here, but we looked...we looked a lot at exemptions, and what we found is that in Nebraska about 50 percent of the taxable items that could be taxed are exempt, which is right about the norm for all the states too. That's about the norm. We looked at taxing services, and there are clearly a couple of states who have a lot more horsepower out of their sales tax because they do tax very broadly, South Dakota being one of them. South Dakota taxes very broadly on all tangible goods and all services. And then kind of (inaudible) here, but one of the interesting things about the taxes, in Nebraska the tax is specifically on tangible personal property. And so, if you want to not tax personal property, such as food, then you have to exempt it. But it does not tax services unless they're specifically enumerated, and so it's....and so you can't look merely at exemptions to figure out tax is foregone because the services never get taxed unless they're put in, so it makes calculating the amount of foregone tax kind of difficult. But in any event, we started looking at all of the items that are exempt and what could we...could we do, and when we looked at services we found that there are states that tax a lot more services, things such as attorneys, accountants, newspapers. But when we looked at the list of services that was put out by the Federation of State Tax Administrators, they listed 160 services...168 services, categories of service, that could be taxed, and Nebraska was taxing about 70 to 80 of those and that was more than most states. So we start off, we tax more on those services. So, Don, I'm going to... []

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DON FREEMAN: Okay. []

ROBERT McMANUS: ...kind of turn to you about (inaudible). []

DON FREEMAN: Thank you. First of all, I want to thank Bob for the work he did on all these reports. I think it's been very good and very complete. Sales tax, we've bounced back and forth on the use of sales tax, exemptions, additions for since we started, and it seemed to me that taking exemptions away that are exempted now would be a very difficult process. I don't know politically how it would ever be done. I think that people do save, of course, and it's been echoed that the sales tax is the least abrasive to pay. It's still a tax, but it's the least abrasive. If you don't use it, you don't pay it. So it seems to me that the only way for us to increase the revenues of the state through sales tax would be to broaden the base and add on add-ons now that are out. I do want to point out that adding on, we talked about all foods, and Bob kind of said how that could be used as an exemption with the debit cards for those of lower incomes; adding on services, i.e., accounting, legal, that type of thing. One of the things I think we've got to be careful of if we do recommend this type of increase, we've got to make sure that the conduit for payment of this increased income is for property tax relief. I don't know how that's going to be done, but I can't see it being put into a General Fund, period. It's got to be earmarked for property tax relief because I think that's one of the things we've tried to do throughout this process, is how can we reduce the, I guess, most abrasive tax--property tax. How do we do that? Well, maybe increasing the...adding on to the sales tax base would work. But I'll just go through, make a couple of...comment on a couple of highlights about the tax. Corporations pay in about, what, \$110 million in use tax. So that is a substantial amount. Private citizens don't pay in, not very many of them do. It's got to be reported. There probably should be a line added on to the tax return for use tax, you might call a guilty tax. []

DOUG EWALD: There you go. []

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DON FREEMAN: But it could be added on to the line and that way the accountants would be aware of it and maybe be able to explain to people filing income taxes that, now you bought a bunch of stuff and...and, by the way, the Senate is going to act in November on Internet sales tax. They have the power right now to exempt it permanently. That will be taking place in November. I guess there are a couple of board of governors, state governors, who's trying to lobby on it, and I would guess that would probably be passed. So that would not be an option for...to look at in the future. Nebraska tax is about half of the possible tax base, and the average is about 40 percent. So we're taxing half of what's possible. We're the 12th highest in the nation for tax per capita, \$1,007. It appears that the use of the debit cards, as I said, would take care of the food costs. The sales tax holiday, Bob mentioned that, I...that doesn't seem to be a major item one way or the other and may be politically tasteful to do it because of the competition from Iowa on a certain day. They talked about a possible sales tax on gasoline or on fuel. That doesn't seem to be very acceptable right now. It could be done, and a lot of states do have it. []

ROBERT McMANUS: It was also one of the recommendations of the '88 commission. []

DON FREEMAN: Right. []

ROBERT McMANUS: Because what you have right now is from their perspective. Gasoline goes totally...escapes sale...(inaudible) motor fuel tax is dedicated, that the gasoline is...that product is not contributing at all to the general sales tax fund. And a number of states do have a sales tax investment. []

JOHN ANDERSON: You could adjust the excise tax and earmark some of the revenues to the General Fund instead. That's another solution. []

ROBERT McMANUS: It would be, except, as I understand it, the amount of tax every

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year on motor fuel is determined by the road needs. []

JOHN ANDERSON: That's right. Yeah. []

DOUG EWALD: Right, and we're looking for more money for roads. []

DON FREEMAN: Right. And as we talked about, a 1 percent sales tax brings in \$250 million, so it's a very lucrative tax. And it appears that we would not take away the exemptions we have now. As I said, we'd add on taxable on, I think, food and legal, accounting fees. That would be...I guess that's somewhat controversial because of the inability or they don't want to be able to find out what is out of state and what's in state. We do that all the time in our businesses, with exemption certificates and so on, and if it's out of state we don't collect the tax. So it just seems to me that we need to get some concrete numbers, which we will have, but adding on the food and services--like we do tax some services right now--by adding on these additional services should generate some substantial, I would call, tax relief on the local level if, indeed, it can be funneled to the local level. []

SENATOR BURLING: Don, you didn't speak about sales tax on goods or services as far as business inputs compared with the ultimate consumer. []

DON FREEMAN: Now what now was that? []

SENATOR BURLING: Sales tax on either goods or services paid by businesses for inputs, versus ultimate consumer. []

DON FREEMAN: Well, you know, that's usually...input is exempt normally. If it's for manufacturing processes, that's not (inaudible) taxable anyway. []

SENATOR BURLING: Well, that's what I'm asking. Is that part of your recommendation,

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or how are you recommending on... []

DON FREEMAN: Well, there would be tax of the corporation using legal, accounting and legal fees would be, and pay a sales tax on it. But I think that would be...it should be offset by a relief in property tax. So corporations would pay that tax. []

SENATOR BURLING: Okay. So then you have small corporations who hire legal services. []

DON FREEMAN: That's right. []

SENATOR BURLING: Large corporations who have theirs in-house. []

DON FREEMAN: Probably knew they wouldn't be paying taxes on that. []

SENATOR BURLING: I see that as a problem. []

DON FREEMAN: Because? []

SENATOR BURLING: Well, it's not a level playing field for... []

DON FREEMAN: Well, that's probably true. []

SENATOR BURLING: I'm just commenting. I'm not... []

DON FREEMAN: Yeah. That might be true. []

ROBERT McMANUS: Yeah, that was one of the two problems identified, was that what happens if you tax those services is the large corporations will move them in-house because you've just...you've just put a 7 percent... []

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DON FREEMAN: Right. []

ROBERT McMANUS: ...increase on it; that they would look at that and could move some in-house. []

DON FREEMAN: Right. []

ROBERT McMANUS: The second problem is the Omaha/Iowa problem that most states wouldn't face; that you'd have...you could have a flight over to Iowa, legal firms or accounting firms, just to save tax. So that Iowa problem is there for every tax. []

DON FREEMAN: Yeah, that's a point well taken. It could be tiered to make it so they really couldn't afford to move in-house at a lower tax rate, which is... []

GEORGE KILPATRICK: Doug, you know...I assume you know about licensing accountants, which I don't know much about... []

DOUG EWALD: Right. []

GEORGE KILPATRICK: With lawyers at least, they have to be licensed in the state, which provides a nexus. []

DOUG EWALD: Right. You know, attorneys, you have Iowa bar, Nebraska bar, you know, they're... []

GEORGE KILPATRICK: They can be a member of the Iowa bar, but they can't appear in a Nebraska court unless they're a member of the Nebraska bar. []

DOUG EWALD: That's correct. []

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GEORGE KILPATRICK: Which could prove to be difficult. I mean a lot of those folks who work in the area are members in both because that's... []

DOUG EWALD: That's right. I mean, it's pretty universal, anybody in a law firm in Omaha has a license to practice in Iowa and Nebraska. []

GEORGE KILPATRICK: Right, and the license provides nexus, which allows the collection of the tax. []

DOUG EWALD: That's right. []

GEORGE KILPATRICK: Now accountants are...CPAs, for example, is a national designation. []

DOUG EWALD: That's right. []

GEORGE KILPATRICK: Probably it doesn't work out quite that same thing. Am I correct? []

DOUG EWALD: That's correct. And you have your license... []

GEORGE KILPATRICK: We do have a local state licensing board. []

DOUG EWALD: Yeah, state licensing board, you can...I know you used to be able to request reciprocity, but that was for when you actually passed the CPA exam. That has nothing to do with actual licensing, so... []

GEORGE KILPATRICK: Okay. []

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DOUG EWALD: ...I don't know the specifics. I think, because it's a national designation, per se, at the CPA level, that means you can practice in any one particular state. It's just a matter of where you're...just you have a license, a CPA license in Nebraska, doesn't mean you can't do that service in Iowa. So... []

GEORGE KILPATRICK: That's what I thought. []

DOUG EWALD: And then the big thing here is these types of firms are fairly portable, you know, from one side of the river to the other side of the river. And would they...you know, all of a sudden everybody would make a move to Iowa and have the services performed there for their Nebraska clients? []

JOHN ANDERSON: But would the use tax apply to services you purchased across the state line? []

DOUG EWALD: Well, it depends on... []

GEORGE KILPATRICK: Assuming the destination source,... []

DOUG EWALD: Right. []

GEORGE KILPATRICK: ...that shouldn't make any difference. []

DOUG EWALD: Right, exactly. If you wrote it correctly (inaudible), that would prohibit that type of movement or enticement, I guess. []

JOHN ANDERSON: Right. []

DOUG EWALD: Yes, Senator. Oh, I'm sorry. []

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DON FREEMAN: Right. That may not be an option then. I don't know. []

SENATOR McDONALD: Getting back to the food issue, just recently we were in Colorado and went to a grocery store. And I know that when we go to a restaurant there are sales tax. []

DON FREEMAN: Sure. []

SENATOR McDONALD: When you go to the grocery store, the food that we purchased there was not taxed, but the food that we bought in the deli was taxed. Is that the way it is in Nebraska? The food that's prepared in a deli... []

DOUG EWALD: It is prepared, prepared. []

DON FREEMAN: Prepared food is taxed. []

SENATOR McDONALD: Even in a grocery store. []

DOUG EWALD: Yes. []

GEORGE KILPATRICK: Yes. []

SENATOR BURLING: Yeah, sometimes. []

DON FREEMAN: Right. Well, depends on how big the store is. []

SENATOR BURLING: It depends on the store. []

SENATOR McDONALD: And I guess, you know, I never thought of that, but when I did pull that out and it was amazing to look at that there was a city sales tax on all the food,

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not state, but city sales tax they were taxing. []

DOUG EWALD: Colorado is one of the unique state, home rule, where the locals can deviate from what the state has done. So I think Arizona might be that way as well and... []

GEORGE KILPATRICK: Well, there's a number of them, particularly in the South. []

DOUG EWALD: There's a number of them that set their own rules with respect to taxability for their items. []

DON FREEMAN: But I think it's up to our committee to make some concrete recommendations with numbers and what it will do to affect the overall tax revenue for the state of Nebraska, but I think we are leaning towards taxing food and maybe some services. []

ROBERT McMANUS: There were two bills that George gave me that were looked at in the past and one of them was to tax the services of engineers, lawyers, and accountants. And, as I recall, the fiscal note on it was only \$55 million, so...and this is kind of (inaudible). No single item really amounts to a lot of money and that's why it's difficult to get them. You know, there will be such a fight against it for a relatively small amount of money. And the second bill we looked at was one that came several years ago where it was a very broad bill to do away with almost all exemptions. (Inaudible) George. []

GEORGE KILPATRICK: What you told me to preserve was medical and essentially (inaudible) component parts and food. That was all that was exempt. But the other, containers and all that other stuff in there, (inaudible). []

DOUG EWALD: Right. Well, I know that one thing we talked about in the subcommittee

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was if we want to earmark this for property tax relief, it needs to be significant. The hundred million dollars that we did in the Legislature this last year and the next year is okay, but if we're talking significant, we need ten times that probably. And how do you get a billion dollars of additional sales/use tax? I mean that's the... []

DON FREEMAN: You tax everything. []

DOUG EWALD: That's the struggle from that standpoint that can you broaden that base enough, and that's new items as well as...mean, you need to look at the exemptions. I know it's tough but, you know, politically is that any tougher than adding on a new service? I don't know, but it deserves consideration. []

SENATOR PAHLS: Well, here's the way I'm thinking, because you really brought this up to my...you say 90 percent of the population lives in four counties, so if you are raising things that will cause 90 percent of the people in four counties, spreading it across the state, see, I wouldn't have any argument with that if you look at the ag exemptions. Do away with those so...because then they would be...that would bring that up so then they could get their property tax relief. Look at the exemptions and say we will help you lower your property tax, but let's take a look at some of these exemptions. There are some significant exemptions here. Do away with those ag exemptions, but we promise you tax, property, relief. Makes sense to me. Because if you keep saying 90 percent of the people in four counties will end up paying more, and then you want relief of property taxes all of the state,... []

DOUG EWALD: Right. []

SENATOR PAHLS: ...I see this... []

DON FREEMAN: Yeah. []

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SENATOR PAHLS: ...as a fair thing of let's start taking a look at some of these exemptions that would help the property owner who also is the ag person. I mean it just...there's a fairness here. And even though you say sometimes some of these taxes are...you don't really make that much, I see it almost as a fairness. If I'm an attorney and I don't have to pay something but somebody else has to, you know, and I like to give some of those attorneys on the floor some bad times anyway. (Laughter) []

SENATOR McDONALD: The only part of that that I see that's difficult to deal with is property taxes stay in your local community and so if you're lowering property taxes then the local community is the one that struggles with it. We're taking away the exemptions and so we're going to pay sales tax, which goes to Lincoln, which goes to General Fund, and then it has to make sure it comes back out. []

SENATOR PAHLS: Well, that's what... []

DOUG EWALD: That's the... []

SENATOR PAHLS: That's what we're saying. []

DON FREEMAN: Yeah, it's got to come back. []

SENATOR PAHLS: This is going to go there. []

DOUG EWALD: Earmarking those funds. []

SENATOR PAHLS: Earmarking. []

SENATOR McDONALD: Because otherwise, if not, then you're going to lose (inaudible).  
[]

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DON FREEMAN: No, no, it's got to be earmarked. []

DOUG EWALD: (Inaudible) exactly (inaudible). []

SENATOR PAHLS: It's got to be earmarked. []

DOUG EWALD: Yes. []

DON FREEMAN: Absolutely. []

SENATOR PAHLS: I mean, and I have no problem with that. I mean that way maybe everybody will look at the bigger picture and just say, gee, I'm really paying these unbelievable taxes but, you know, because I have an issue with 90 percent of four counties picking up the tab. Because 90 percent of the people will be eating most of the food so that tax will come from that area. []

SENATOR McDONALD: Rural people don't eat (inaudible). []

SENATOR PAHLS: I didn't say that. (Laughter) (Inaudible). But, no, I mean I think we ought to look at... []

DON FREEMAN: I understand and you're right, Senator. You're right. []

DOUG EWALD: That's...you need to look at that big...the global picture, what's going on, and it's... []

SENATOR PAHLS: Yeah, and I think maybe afterwhile there will be a fair...a balance will be so that the rancher or the farmer isn't paying his or her unfair share as opposed to that person living in that small town. I don't know. I haven't looked at the numbers, but... []

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JOHN ANDERSON: But there's also the deductibility issue. As long as we've got a state personal income tax, for most people, their property tax is deductible at the federal level and their sales tax is not, right? []

RICHARD BAIER: Correct. []

JOHN ANDERSON: It's only in states that don't have an income tax that their sales tax is deductible. So for all of our itemizers in the state, there's an incentive to prefer the property tax to the sales tax. Now the itemizers are in the minority, probably, with... []

DOUG EWALD: Yes. []

JOHN ANDERSON: (Inaudible) 30 percent (inaudible)... []

DOUG EWALD: Yes, something like that. []

JOHN ANDERSON: ...of filers are itemizers. But they tend to be the high income taxpayers of the state. So there's...the deductibility issue is not one to ignore in this whole process. []

SENATOR PAHLS: Right, I understand, because I've heard, you know,... []

GEORGE KILPATRICK: Well, the more sales tax you do, the more (inaudible) get deducted. I mean, what, 5 percent of the returns I suppose are deducting sales tax to income tax now,... []

DOUG EWALD: Something like that. []

GEORGE KILPATRICK: ...something like that. Dave told me once. []

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JOHN ANDERSON: Yeah, yeah, but the majority probably still be preferring, as long as we've got a personal income tax, they'll do better with deductions on property taxes and mortgage interest, so... []

SENATOR BURLING: Well, I thought it was interesting that even though the statistics show that we are more of a service-oriented society than a goods-oriented society like we used to be, states still really haven't grabbed on to taxing services. And is it because of more difficulty of administration or just what is the reason? Is it what your neighbor is doing or...? []

JOHN ANDERSON: The sales tax was designed from the beginning to tax final goods, not services. The very design of the tax is to tax goods. []

SENATOR PAHLS: And I do need to bring this up, because one of my constituents who does clean houses, I was talking to her yesterday, she says...because she knows I'm serving on this committee, and she says would you at least bring up how unfair it is for me, as a small business owner who cleans homes, that I...you know, the sales tax is an issue with her. And I don't know...at least I brought it up. []

JOHN ANDERSON: Well, the countries that want to tax both goods and services and do it comprehensively have a value-added tax. That's the solution for taxing all of it. []

SENATOR PAHLS: And this same lady, because I've been working with her, this cleaning lady is so unique because she cleans houses for lots of people so she's put me with a 92-year-old woman and an 80-some-year-old woman who could probably sit right around this table because they're that smart, but they were...they're having problems with the property tax, the valuation, so they've gone through the process, and one home was like \$250. They got it down to \$185. It's because of the tenacity of this cleaning woman. Hope she doesn't run against me. (Laughter) But anyway, she said that they

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still want to go up the line, and I'm going to ask somebody because somebody around this table may know, she says, she has been told, for this lady is 92 years old, because she wants to go up the line about the property tax. []

DOUG EWALD: The TERC? []

SENATOR PAHLS: And she says it will be three years. []

GEORGE KILPATRICK: (Inaudible). []

SENATOR PAHLS: Well, that's what she was told by Douglas County Assessor. []

DOUG EWALD: Three years for what? []

GEORGE KILPATRICK: I'm sure. For a TERC decision? []

SENATOR PAHLS: Yes, at the state level. []

DOUG EWALD: No. []

GEORGE KILPATRICK: No way. []

DOUG EWALD: You know, you file your protest with the board of equalization. They give you that. Then you have until like I think this...well, like September 10 to appeal to TERC, which right now the TERC is hearing stuff from a year ago. So it's roughly a year. []

GEORGE KILPATRICK: It's a year. []

SENATOR PAHLS: Okay. Okay. []

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DOUG EWALD: It's probably, roughly, a year after you've paid your last property tax payment for that prior year, you know, from that standpoint. So it's around a year. []

GEORGE KILPATRICK: Yeah, it is a year. []

SENATOR PAHLS: Okay. []

GEORGE KILPATRICK: Now Douglas County isn't negotiating any cases Wickersham tells me, so... []

DOUG EWALD: They're what? []

GEORGE KILPATRICK: They're not negotiating any of their cases, so they're going to dump 20,000 appeals on them and see what happens. []

DOUG EWALD: Well, they're moving some. Let me put it that way. []

GEORGE KILPATRICK: All right. Fair enough. []

SENATOR PAHLS: So I can tell her within a year. []

DOUG EWALD: Yes. []

SENATOR PAHLS: I'm sorry about interjecting it, but it's... []

GEORGE KILPATRICK: Well, it's about a year. I wouldn't say within a year. []

DOUG EWALD: Right. Yeah, about. []

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SENATOR PAHLS: She says she's 92 years old (inaudible) live (inaudible). []

GEORGE KILPATRICK: Well, then what does she care? []

SENATOR PAHLS: Well, (inaudible) three years is too much. She's just as (inaudible).  
[]

DON FREEMAN: (Inaudible) Doug, it's got to be a large amount. I mean, we've got to really show a very solid amount of sales tax/income increase to make it even palatable, I think. Probably a billion dollars, would be my guess. []

SENATOR PAHLS: Well, you can start looking at some of those...it could be those exemptions. []

DON FREEMAN: Well, sure. []

SENATOR PAHLS: Move that up. []

DON FREEMAN: Right. []

SENATOR PAHLS: And earmark it. []

DON FREEMAN: Yeah. It's got to be earmarked. []

DOUG EWALD: You can make a conscience decision in the Legislature here, we're going to earmark that, so... []

GEORGE KILPATRICK: Would you extend the earmark to the \$1.2 billion that we're already spending on it? []

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DOUG EWALD: We can do that. []

MATT JEDLICKA: Senator Pahls, when you talk about ag exemptions, you talking about some of these sales exemptions that Bob outlined in the summary here. []

SENATOR PAHLS: Yeah. Yeah, and I'm not...I'm not against them. I don't know enough about them to be pro or con on them. I just think look at those and, who knows, maybe we'll generate and maybe people will see that, you know, they may need to be moved around. []

SENATOR STUTHMAN: I think, you know, looking at this, and I didn't attend one of those sales tax meetings, but, you know, when you look at some of these exemptions on page 5 there, you know, irrigation farming, energy costs, and animal life, and ag chemicals, with the fact of less and less farmers and a big land base and one person doing a lot, I think if we really look at that, he's going to probably end up paying more in taxes. If he's going to...if these items are taxed also and his property tax won't lower very much, he'll probably end up paying more. Total tax bill will probably be higher than what he's paying right now. I mean I've got neighbors, you know, that... []

SENATOR KOPPLIN: You could say that (inaudible) believe, I mean I don't have any data on this, but let's say you did tax food. The consumer may get a little bit of a break on his property tax but then...I'm not doubting your figures, but I can't imagine people not filing with the exemptions. You're going to lose that on your federal taxes. What do you really gain, I guess? Are you going to pay more in the taxes on food and so on, and lose because of your property tax exemption? I don't know, maybe not that many people file with exemptions (inaudible), but I can't imagine why they wouldn't. []

SENATOR BURLING: Well, one thing about it, everybody eats food. You'll catch everybody. []

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DON FREEMAN: Well, it's a very complex situation. []

SENATOR BURLING: And we've discussed... []

SENATOR KOPPLIN: Then you get in the argument of who do you exempt from paying tax on food? []

SENATOR BURLING: Well, food...federal food stamp people, they don't use food stamps anymore but they use the card, they're already exempt. I mean they would be if we had a sales tax on food. Those people would not pay it. And then I don't know what... []

DOUG EWALD: Right. Well, another way of maybe the approach, instead of, you know, looking at where they're going with the debit card and all, instead of putting another layer of complexity with that is as simple as increasing your earned income tax credit at the state level, focusing on those people. You know, that's a mechanism that's already in place as opposed to something unique and additional that we're adding for food, changing forms, putting this and that in place, who...where do we drop it off at. We have the earned income tax credit today as a percent of the federal. Maybe we just...we could increase that a little bit to handle the same thing. []

SENATOR PAHLS: Yeah. Just proves there are ways to do some of this stuff and, you know, to be honest with you, and we know this, a lot of people in the low income, they eat fast food. Do they not pay taxes there? []

DOUG EWALD: Absolutely. Yeah, that's the thing you talked about. []

SENATOR PAHLS: And that's the sad thing about it, is the culture, you know, is... []

DOUG EWALD: And unfortunately, I think what the studies show is that the people that

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can least afford it eat a higher percentage of food at the fast food so they're paying the sales tax on that anyway,... []

SENATOR KOPPLIN: Right. That's right. []

DOUG EWALD: ...you know? So it's...not that we want to tell people what to do, that's for sure, but they've made a conscious decision there to go through the drive through. []

DON FREEMAN: Yeah, pay the tax. []

SENATOR BURLING: Well, I know we've discussed in the Legislature, you know, taxing some food, like snacks and soft drinks. We've never been able to come up with who to put on or what to put on that list, and so we just, oh well, won't tax anything. []

DOUG EWALD: Yeah, they tried that in California a number of years ago. That thing went down in flames. They couldn't draw that line. []

SENATOR BURLING: Well, almost all states around us tax some... []

DOUG EWALD: Sure. []

SENATOR BURLING: ...tax some snack food, but here we don't because we never could come up with a list. And I've been kind of watching lately when I go to different stores and some stores, some grocery stores, will tax a certain prepared food, and go a block down the street and another grocery store won't tax that same thing. So they're making a decision on what they sell, whether to tax it or not as far as, well, is this prepared. Is a package of cookies a prepared food? I mean, you open it up and eat them. I don't know. []

SENATOR KOPPLIN: Well, if they're doing it right. Their... []

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SENATOR BURLING: What? []

SENATOR KOPPLIN: Their cost of what they're not charging you a tax on, they're paying it to the state, so it's basically this is costing me 98 cents, but I'm charging \$1 for it because I got to pay the tax, but I don't charge you the tax. Isn't that the way it works? []

GEORGE KILPATRICK: Well, no, it's not supposed to. []

DOUG EWALD: I know...yeah, they're supposed to...that's supposed to be...might want to go audit that. []

SENATOR PAHLS: Maybe ought to do some auditing. (Laugh) []

GEORGE KILPATRICK: Well, but then (inaudible) find people who are doing it wrong all the time. []

DOUG EWALD: Right. Oh yes. Absolutely. We're (inaudible) education. []

DON FREEMAN: We'll continue to plod through this and... []

ROBERT McMANUS: Yes. Well, so at the next meeting then what I contemplate is that we will revisit sales tax, we'll revisit property tax, and we'll talk for the first time about personal income tax. I think the next meeting is September 14 and we've scheduled it for 1:30, but I'm hoping that we'll be able to change that to 3:00. []

SENATOR BURLING: Well, we've been here two hours and a half today, of which is probably about long enough. And Bob has asked for the September 14 meeting to be changed from 1:30 to 3:00. Is that acceptable? Now if he can't get here before 3:00, do

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we have a choice? So I, you know, I guess I'm suggesting that we do that and... []

MATT JEDLICKA: Fourteenth, is that a...what day of the week is that? []

SENATOR BURLING: Friday. []

ROBERT McMANUS: Friday. []

MATT JEDLICKA: Friday. (Laugh) []

GEORGE KILPATRICK: Friday afternoon at 3:00, huh? []

SENATOR BURLING: Bite into your weekend? []

MATT JEDLICKA: No. No, I'm probably okay there, but... []

SENATOR STUTHMAN: And the 15th is the OSC game? []

SENATOR BURLING: Yeah. []

DON FREEMAN: You know, Doug brought up one more tax (inaudible) severance tax.  
[]

DOUG EWALD: Yes, one thing we've... []

ROBERT McMANUS: Oh yes. []

DOUG EWALD: ...one thing I think we want to talk about at the next meeting as well is other types of taxation that we can possibly do in Nebraska here, and that was a severance tax that we talked about at our last sales tax subcommittee. []

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DON FREEMAN: Uh-huh. Right. []

DOUG EWALD: When you look at the states around us that have the most favorable tax structure, you look over to Wyoming. They have a severance tax and basically what they've done is they've exported their tax base to consumers, everybody outside the state of Wyoming predominantly, because it's on oil, gas, (inaudible). They tax it and it gets passed on to the consumer in the using state. So if you look at Nebraska, what are our natural resources here? We talked we have a little bit of uranium, but... []

RICHARD BAIER: Tourist traffic. Tourist traffic. []

DOUG EWALD: Well, here's one thought for you we did talk about and we can talk more about later, but it's the...corn is a natural resource and what does corn make? It makes ethanol. And maybe we do a severance tax, 2-3 cents a gallon, on the production of ethanol, because 90 percent of ethanol is exported to California. So all of a sudden they pass that on to consumers in California. The...because where we're located, strategically, it's about 8 cents a gallon cheaper, the rail freight rates are in Nebraska, compared to Iowa. So you could do 2-3 cents, still be more competitive to Iowa. You could lower the ethanol rate at the pump in Nebraska to keep it neutral for Nebraskans, but export that whole base to Californians. []

SENATOR BURLING: Or any western state. []

DOUG EWALD: Yeah. []

SENATOR BURLING: Or any state, really. []

DOUG EWALD: Any state where we export to, and 90 percent of ethanol goes... []

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SENATOR BURLING: West. []

DOUG EWALD: ...goes west, exactly. So... []

SENATOR BURLING: Okay. []

MATT JEDLICKA: I have a couple questions to clarify. Don, did I hear you right in saying that anything that's exempted now your committee is looking at leaving...? []

DON FREEMAN: Well, the inaudible) seems to be very difficult to remove it from an exempt list. Now if it's maybe it's easier than what I feel it is, if that's the case, then we would maybe look at some of the items and remove those. But I've always understood it's very difficult to; once it's there, it's difficult to get removed. So I don't know. []

SENATOR PAHLS: It depends. Unless they see there's...they come out ahead on someplace else is, you know, I'm...I'd go looking at some of these. []

DOUG EWALD: I think...I mean I guess I...mean, we need to talk about it and draw that conclusion, but I think our recommendation probably should be that it needs to be considered at least. []

DON FREEMAN: Right. []

DOUG EWALD: I mean I wouldn't want to close the door and not consider... []

DON FREEMAN: No. Right. []

DOUG EWALD: ...removing an exemption, I guess. []

DON FREEMAN: Right. Right. []

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MATT JEDLICKA: You know, I guess I looked through this and some of these appear to be luxury services that probably could be taxed, I look at them as luxury, I'm sure people would see them other ways, but landscaping services, marina service, maybe travel agent services, swimming pool cleaning and maintenance, dating services, you know, that's just a few that come to mind. []

DON FREEMAN: Right. []

MATT JEDLICKA: I don't know. []

DOUG EWALD: Sure. []

DON FREEMAN: You're right. []

DOUG EWALD: (Inaudible) some lower hanging fruit there than you would think. []

DON FREEMAN: Right. []

MATT JEDLICKA: Just came through this today. []

DON FREEMAN: Not politically dangerous. []

MATT JEDLICKA: You know, and nobody is going to die if they don't have those,... []

DON FREEMAN: Right. []

MATT JEDLICKA: ...in most cases, I assume. []

DON FREEMAN: I do think one of the things that I'm concerned about, if we start

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adding taxes to our ag economy, ripple effect on that is phenomenal. It goes out into every community. And so we've got to be very careful about doing that, I think. Even though you're being more efficient, you're buying bigger equipment and using bigger equipment, and so I...and in my business, of course, I know exactly when business is good for the farmer and when it's not good for the farmer, (inaudible) I'd say 50 percent of the communities, people in these communities outside of Lincoln and Omaha, and even they are affected by ag. []

SENATOR PAHLS: Well, you know, I think...yes, I agree. I think we're all affected. But I started pulling up the subsidies from the federal level too. I mean it's an interesting world out there. And most of my...and most of my relatives are farmers so, you know,... []

DON FREEMAN: Yeah. Well, we have cheap food. []

SENATOR PAHLS: Yeah. []

DON FREEMAN: We have cheap food. []

SENATOR PAHLS: Yeah. []

SENATOR BURLING: Anything else today? Bob? []

ROBERT McMANUS: Senator, back to you. []

SENATOR BURLING: Okay. Any other comments before we close? Okay, two weeks from today at 3:00, come if you can, please, and let us know if you can come or not, same room; October the 12th at 9:00 a.m. in this room. And then Bob and I were talking this morning, we'll probably want another meeting the first part of November. So if you could remember to look at your November calendar before you come to our next

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meeting in two weeks, we'll try to set the November date two weeks from today. Anything else to come before us before we depart? Again, thank you for coming. I think the discussion has been good, give us something to think about and prepare us for some final decisions in the next couple of months. And hope you can keep attending and if you're on a subcommittee, get a hold of your subcommittee chair any time you have an idea, or get a hold of myself or Richard or Bob, and sometimes you have an idea between meetings, why, you know, let it be known. So if there's nothing else, is there a motion to adjourn? []

DON FREEMAN: So move. []

DOUG EWALD: Second. []

SENATOR BURLING: And seconded. All in favor say aye. Thank you very much for coming. []

DON FREEMAN: You bet. []