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SENATOR BURLING: We'll go ahead and start. There may be some more come after we start, but that will be fine if they would. I thank each of you for coming. It's only two weeks since our last meeting. Come on in, Doug. She's got your name tag up here. Sit down in one of those, and she'll get you the right name there. And so our facilitator has been working hard to get ready for this meeting and has some reports for us. And we'll review a little bit of what we did two weeks ago, and continue discussion on other areas of taxation. So I think the first thing we'll do is I'll call the meeting to order. And we'll ask Amanda to take roll call. []

AMANDA JOHNSON: John Anderson. []

JOHN ANDERSON: Present. []

AMANDA JOHNSON: Richard Baier. Senator Burling. []

SENATOR BURLING: Yes. []

AMANDA JOHNSON: Doug Ewald. []

DOUG EWALD: Here. []

AMANDA JOHNSON: Senator Fisher. []

SENATOR FISCHER: Here. []

AMANDA JOHNSON: Don Freeman. []

DON FREEMAN: Present. []

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AMANDA JOHNSON: Mike Hybl. Matt Jedlicka. []

MATT JEDLICKA: Present. []

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

SENATOR PAHLS: Yes. []

AMANDA JOHNSON: Senator Raikes. Senator Stuthman. []

SENATOR BURLING: Okay. Thank you. As always, the commission complies with the Open Meetings Act, and there is a notice posted there next to the door. And the meeting was published in the public meetings calendar. The last few meetings we're having here, we've chosen to transcribe these meetings so our facilitator or anyone can go back over the discussion and prepare a final report. And so when it's transcribed, Amanda does not keep minutes. So there are not any minutes to approve, but any time any of us want to, we can go back and review the transcription. So, hopefully, that's okay with everyone. And there will be no minutes to approve today. Come on in, Richard. You're able to be with us, thank you. []

RICHARD BAIER: Yeah, I'm here. []

SENATOR BURLING: After a long time away from us, you're home. []

RICHARD BAIER: I'm here. []

SENATOR BURLING: Good, good, good. I just told the group that these meetings that are transcribed, we have no minutes. We don't keep minutes when we transcribe, so

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there are no minutes to approve. And so any of us can look at the transcription any time we want to, to go back and review something. So last time we made some discussion regarding corporate income tax and tax administration. And we'll review those today. And then our facilitator, Mr. McManus wants to lead us through some discussion on some of the other areas of taxation. We're starting to wind this down and get ready for our final report. So each meeting we have now we'll be doing a little more decision making and get ready for that November report. So did you have anything that you'd like to say at this time? []

_____: No, sir. []

SENATOR BURLING: Just hello, huh? []

_____: (Inaudible), I'm good. []

SENATOR BURLING: Okay. Bob, take over. []

ROBERT McMANUS: Thank you, Senator. I'm going to go over again some of what I think is the critical things that I went over last time. But I'm going to wait and see if Milo and Mike show up before I do that review. So I think the first thing we'll look at will be sales tax. At our last meeting, we spoke about the possibility of using a broader sales tax to raise revenues which might offset another tax. And Don and I have looked at a number of things. And, Don, you might walk through this, the one page. []

DON FREEMAN: Okay, Bob. You have a handout that shows the sales tax exemptions. And we're just trying to crunch some numbers to see what different exemptions or nonexemptions to generate new sales tax. And quite frankly, I'm always surprised at the minimum number of dollars generated by adding in exemptions that are now in place. We went through and picked out some we felt that were...or I felt that were logical, and came up with a total tax...sales tax income of \$118 million, which is marginal. If you

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recall, we talked last time about probably need to generate at least \$1 billion in sales tax revenue in order to reduce some way the property tax burden at the local level. So this falls far short of that, wouldn't even cover the exemption of corporate income tax, if that indeed were put in place. So it's just really...we have to go back to, I think, looking at the entire tax base exemption plan and possibly eliminating most of it, maybe except for medicine and medical. Now, Bob recalled this LB397, which was introduced back in March of '03. And at that time, it was going to be revenue-neutral, apparently, by (inaudible) the base, exempting (inaudible) exemptions and lowering the base rate to 2.8 percent. Now then, if that same bill were put in place, but leaving the tax at 5.5 percent, I made an error in my assumption that only double what the income might be. It's actually going to be about 850... []

ROBERT McMANUS: \$850 million. []

DON FREEMAN: Yeah, \$850 million, close to a billion dollars. If indeed... []

ROBERT McMANUS: And, George, if I...this bill was...basically, you were instructed to just keep only food and medicine exempt. All services and all sales would be taxable. And if you left the rate the same, it generates a lot of revenue. It gets you what you need, but it's draconian. []

DON FREEMAN: Yeah, it is draconian, yes, indeed. So, you know, that's where we're at. And we also talked about a sales tax on fuel that I think Bob will get into. But it just seems that unless we take a way most exemptions, leave the base...sales tax base where it is now, we aren't going to raise very much money. We talked about an export tax, you know, maybe on ethanol; I talked a while about the underground mining we have in limestone, sand, and gravel. Is that logical? I don't know. But it just seems that unless we can convince people that by broadening the base, keeping the tax where it is, in the long run, it may reduce their overall tax burden. I think it would be very difficult to prove that, of course. If we get into sales tax on seed and fertilizer and that type of

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thing, to me that's the same as manufacturing, you're buying raw materials to manufacture. So they should be exempt. So that's a Catch-22. And, of course, you would take that away, then you reduce your sales tax income substantially. So we're at a point now where, I guess, it gets back to local spending districts to control costs, the state to control costs, in order to reduce the tax burden, because I don't think we're going to be able to convince people to broaden their sales tax...or broaden the exemption base, narrow that down to allow us to collect more money. I think it would be very difficult. So those are some of the things we've come up with and discussed. But it was disappointing to find out that, even though you try to reduce exemptions, you don't generate a lot of money. You know, (inaudible) \$118 million is a lot of money, but still we're talking of trying to get \$1 billion or something quite close to that for tax relief. And I think we also discussed the problems of seeing how that money could be channeled back into the local school districts, that would be a problem also, and it would be a control problem, I think, once that...if that were to be done. So there's a lot of complications on that. I guess, we're back to square one, almost, on sales tax. []

SENATOR BURLING: So \$118 million would be equivalent to about one-half percent on the current base? []

ROBERT McMANUS: Yes. []

DON FREEMAN: Yes. Right. So it's not []

SENATOR BURLING: So if you need to raise the sales tax rate to 6 percent, you could look at these and leave it where it's at []

DON FREEMAN: Yeah, but that wouldn't raise very much money. []

SENATOR BURLING: Other comments? []

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SENATOR PAHLS: Well, and to me unless you take a look at the list of exemptions, all of them, don't be selective. []

SENATOR BURLING: Well, we got that somewhere. []

DON FREEMAN: That's what LB... []

SENATOR PAHLS: Right. But if you would take away all of the exemptions, basically, it's not going to generate that much money? []

ROBERT McMANUS: No, it does. What we're saying is in that bill it didn't because the way... []

SENATOR PAHLS: Oh, okay. I misunderstood that. []

ROBERT McMANUS: No. If you eliminate all the exemptions and you keep the rate, maintain the rate as it is, you generate about another \$850 million. []

DON FREEMAN: That's taxing everything but food and medicine... []

GEORGE KILPATRICK: Medical. []

DON FREEMAN: ...medical. []

GEORGE KILPATRICK: Medical issues, medical care. []

DON FREEMAN: Everything else is taxed. []

ROBERT McMANUS: And there are states that do that. There are...South Dakota, very broad sales tax and... []

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JOHN ANDERSON: Yeah, that's because they don't have income tax. []

ROBERT McMANUS: Right, but that's...I mean they don't have an income tax,... []

JOHN ANDERSON: That's what you have to do. []

_____ : But their sales taxes generates enough money that they don't need an income tax. But they just...Hawaii is the same way; Hawaii has an excise tax on everything, very high, but that's how they generate their revenue. []

RICHARD BAIER: They export the tourists. []

SENATOR PAHLS: Which is the most unfair of the taxes? If we just not even talk about whose pocket it is, is it the property tax, sales tax, or income tax? Which one of those is probably the most unfair? []

JOHN ANDERSON: The one you ask me to pay. (Laughter) []

SENATOR PAHLS: I agree with you, I agree with you. But I mean, overall, I mean just... []

SENATOR FISCHER: Unfair to who? []

SENATOR PAHLS: Well, to just the purpose of taxing, I mean. []

SENATOR BURLING: Well, I think what you're asking is, what type of tax meets the criteria for equitable, fair, easy administration and all of those things that we look at. Try to get it away from ourselves and look at... []

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DOUG EWALD: Well, I know they say that the sales tax is the most regressive because it hits the people that can least afford it with the basic necessities in life. Now, the flip side of that is, well okay, those people aren't buying the high-end vehicles and the other things like that, that when you start looking at that, it's...on the top-end stuff it's fairly progressive because people have made conscious decisions that that's what they're going to have. []

JOHN ANDERSON: The lottery tax is maybe five times more regressive than the sales tax, according to most estimates. It's very highly regressive, if that's your measure of what's fair. But people seem not too unhappy about it. I mean, the notion is that it's voluntary. I don't think it's any more voluntary than the excise tax on gasoline, or cigarettes, or anything else. But it's, by measure of regressivity, it's far more regressive than the sales tax, in general. []

GEORGE KILPATRICK: Tax policy, we talk about more than just equity. After all, there's efficiency arguments and economic competitive arguments, what I call adequacy, which is sort of is it enough, and does it...is it stable, and does it grow the ability of the tax to be...to fund government services without a lot of increases over periods of time? So all of those are tax policy considerations. And which you think is more fair or least fair, or most consistent with that tax policy and least consistent with that tax policy is going to depend upon which of those you think is the most important. If what you're after is stability and growth, you're going to love the property tax. But that's what it does. If you're most concerned about (inaudible) equity relative to poor people, then you're going to hate the sales tax because that's what it does the worst. If you're concerned about your economic competitiveness with other states, you're probably going to pay some attention to income tax. So it's...tax policy guidelines are nice things to have because they (inaudible). But how you come down on that is going to depend on what you think us most important. []

SENATOR PAHLS: Okay. Now, just let me give you...you told me that the income tax

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does what now? []

GEORGE KILPATRICK: The income tax, from the standpoint of tax policy, the individual income tax is a great tax in most respects. It reflects ability to pay, it's piggybacked onto the federal, so it's more efficient to collect than a lot of them, we do a lot of (inaudible) withholding so there is less evasion. So it does well. []

ROBERT McMANUS: It's the least predictable. []

GEORGE KILPATRICK: It's also the least stable, so it's harder to rely on it in that case. And as you hear from your business groups, you'll find that it represents the most promise with regard to competitiveness with other states, two of which don't have it, of course, nearby. []

SENATOR PAHLS: Right. So you're telling me if we take a look at that tax, that should help bring more people to the state of Nebraska or not? If it's economically...would that draw people? []

GEORGE KILPATRICK: Well, what your business lobbyists will tell you is that it drives people away from the state of Nebraska, the fact that we have it, and that it's fairly broad (inaudible). []

SENATOR PAHLS: Right. So if we would lower it, chances are more people would come into the state? Is that their argument? []

GEORGE KILPATRICK: Well, you listened to it last spring. (Laugh) What did they tell you? []

SENATOR PAHLS: Well, I'm just curious. []

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GEORGE KILPATRICK: You know, that's the politics of the income tax. The politics of the income tax is that people don't like it, (inaudible) don't like it. []

ROBERT McMANUS: If you listen to the Tax Foundation, which is the business policy think tank in Washington, their view would be they're not opposed to the personal income tax, but... []

GEORGE KILPATRICK: Oh, yes they are. (Laughter) []

ROBERT McMANUS: Well, what they believe primarily is that a broad-based sales tax, as broad as possible, the broader the base the better. And then on the income tax they would say that it should also be very broad-based (inaudible). What the commentator's I've been reading say about sales taxes is that the broader the base, the less regressive it gets, because the very poor are paying on basically 100 percent of their income already. And the broader the base, then he less...they're not saying it's not regressive tax, but (inaudible). And we're going to get into a discussion, in a minute...in a little bit about the progressivity of Nebraska's personal income tax, which will cause us to come back to this discussion. []

SENATOR PAHLS: I'm just trying to see it. How can we get people to want to stay and move to Nebraska? You know, because we say our population hasn't done anything. So the bigger picture is, the more people here, the better off we will be. []

GEORGE KILPATRICK: Increase wage levels. (Laugh) []

SENATOR PAHLS: Okay. So increase...okay, increase the wages. Okay, what do I need to bring that business to the state that would give those type of salaries? []

GEORGE KILPATRICK: Well, I don't know. []

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MILO MUMGAARD: And it may or may not be tax policy that does that. []

JOHN ANDERSON: Well, from an economic point of view, jobs are labor, right? And it takes labor and capital together, capital in the form of buildings, equipment, machinery, and so on, to produce outputs, goods, and generate employment and income and so on. So you want to people. But you also want the capital as well. It takes both. Roughly, you know, payrolls make maybe three-quarters of total costs for most industries. So labor is the most important input in producing goods and services. So you want to keep an eye on your tax policy so that it not only attracts people or retains people, but also attracts or retains capital as well in the state. And you don't want tax policy that encourages capital to flee. Mobile capital can go elsewhere easily. Machinery and equipment is easily movable to other jurisdictions on the basis of how it's taxed. And financial capital is increasingly mobile around the globe. We're finding it's very highly mobile these days. So you've got to very careful as you think about tax policy on financial capital and how it will move in response to a change in your tax policy. []

MILO MUMGAARD: []

_____ : And also, income can move around creative so that...to avoid income tax and so on. []

ROBERT McMANUS: Well, since we've got everybody here, I'd like to go back to some things that came up at the last meeting, because I think it's the fundamental issue that I see. They identified the 1988 study and it continues today, and it really relates to property tax, which as you go through the property tax paper, by any measure the property tax is high. But having gone through all these lists now, I've come to the conclusion that the fundamental problem here is a structural problem in the side of local government that's very historical, coupled with being one of the very lowest, if not the lowest, state in state aid to local government. And I want to just walk through again and point out what I went through last time for those who missed the last meeting. But

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what...when you take a look at the demographics paper and put all these papers together, what emerges is a situation where early statehood created the structure that we have today of local government. And in the 1880s you had a decade that was the wettest decade in recorded history for Nebraska. So at the time that they were giving free land to people to come in, in the 1880s, there was a view that Nebraska, even western Nebraska, was a very fertile place to be. And because of the...free land was given out in relatively small acerages that people had to gather together. Well, towns started forming on an ad hoc basis, all across the state as people got together. And counties, towns, school districts were created with no (inaudible) plan at all. And local government, at the time, was being funded by land sales. And schools were being created by land sales. And there was a surplus of money. And by the turn of the century, you had a population of over 1 million, which was widely scattered across the entire state, and they created over 7,000 school districts, which is an enormous amount of schools, 7,000 school districts. And at that...in our reading about it, they said, that there were more administrative people than teachers back at the turn of the century. So you've got this structure that was put in place that I think Nebraska has never recovered from. What's happened over the course of the twentieth century was there was a pronounced and continuous rural population decline and you had the Depression. And there was consolidation of things by just pure economics. The towns were drying up. But by 1992, you still have Nebraska ranking third highest in local government employment per capita. And in the 1988 Syracuse study, that study said...concluded, Nebraska has an exceptionally large number of local governments, with six times the number of local authorities per 1,000 population of the average state. The task faced by the Legislature is a challenging one. The property tax rates are high, and property tax owners deserve some relief. But in deliberating how to provide such relief, the state's legislators need to recognize that the root of the problem is structural and not a matter of local units getting out of control with respect to their spending levels. And so today you still have a structure where you have 93 counties, you have an extensive road system that's far more expensive than the normal state's, and Nebraska is at or near the bottom in terms of state aid to local governments, but that is our most...a necessity

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because the local government...it's almost like giving money to local government is rewarding bad behavior, because the local governments are so, so bloated. And so when I look at what...that clearly, clearly the (inaudible) tax is high and clearly people are clamoring for relief. But the structure is simply unsound. And to me this is the core dilemma that Nebraska tax structure faces. []

MIKE HYBL: Bob, I have a question. Is there anything out there, just in terms of the history, states from Ohio, Indiana, west that were settled from the 1820s on were, I assuming, the model of development, probably wasn't much different than ours in terms of how the states were settled, where a state did come in and do a fundamental restructuring of local government? Why is it we're different than other states? And what have other states done that we may not have done? Or is it a model that's common across the mid-plains and central states? []

ROBERT McMANUS: From what I've read, I think we're unique in this sense, that Nebraska originally thought of itself as a Midwestern state, similar to Illinois and Iowa. And now it's more like a Rocky Mountain state, with two large population centers and a very rural base. But what makes Nebraska unique is they had a population of over 1 million people at the turn of the century, I mean Nebraska did. And the population decline really is pronounced compared to Illinois, Iowa, those other states. And to a large extent the people just thought that Nebraska was going to be more fertile than it really was. []

SENATOR BURLING: Well, I think Kansas would probably be an example of a state that was settled about like Nebraska was. But when you've got twice as many people down there as they have in Nebraska to divide the cost of local government with, then you don't...it don't look so big. But we have this structural local governments and very sparsely populated, few people to share in that cost is what makes it look overwhelming. So I don't know, you know, some states maybe have done a better job of planning than Nebraska. But also if we had twice as many people, we may not be

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having this discussion. I don't know. []

SENATOR PAHLS: I can interject a little bit, because I left Kansas in '68, and that's when they had school reorganization, totally. You did not have...I mean total, three or four towns together. See, that was in '68. So you can see we're having that issue right now. And that was (inaudible). Some of those decisions automatically cut down a lot of government. []

RICHARD BAIER: Mike, the other thing from my perspective that's unique, having grown up in Kansas, is that because of our Unicameral. I think there are a lot more deals cut in other states to force consolidation. It became a bargaining chip between the House and the Senate. That's the one factor I can find that separates us from the other states that they have already been through this, 30 years ago, is we never had to have that conference cutting of the middle that probably forced some of that discussion, which kind of flies in the face of Nebraska history and politics. It's the one unique feature that we have. []

GEORGE KILPATRICK: Well, it's not like there hasn't been consolidation here. (Laugh)
[]

_____: Well, I understand that. []

ROBERT McMANUS: No, it's not...I mean, 7,000 school districts is not 560 or something. []

GEORGE KILPATRICK: No, it's actually 253. []

_____: Trying to get larger. []

_____: (Inaudible) the entire state of Florida has less than 100. []

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GEORGE KILPATRICK: Texas still has 900 and some. []

JOHN ANDERSON: And they are still litigating, too. []

ROBERT McMANUS: No, that is a problem that it's very difficult. There's been a lot of sweat and blood over the years in consolidating things. And certainly, rural Nebraska has consolidated a lot of things since there are 7,000 school districts. But it's almost as if there are all of these quantitative changes that have occurred over time, the little steps we've taken to consolidate. But there's never been a qualitative change in the fundamental structure of the states organization, the local (inaudible). Milo. []

MILO MUMGAARD: But at the same time, wouldn't you say, and George, wouldn't you agree, that there's been a curve, really an arch over history, the last 25 years I would say in particular, where state aid to local government is, of course, greatly, greatly increased. But yet it has at the same time...I guess, what you're saying is it has at the same time addressed that structural problem of how we organize the taxes, and we organize (inaudible). []

ROBERT McMANUS: Right, and you (inaudible). []

GEORGE KILPATRICK: If I can disagree, what...the history of LB806, for example, is that we're going to treat all school districts and fund them all per student. Meaning that if you are too small, you are going to starve to death, unless your base was large enough to sustain it without state aid. And that's when the number of school districts went from 800 to 500 over the course of about a dozen years, because we simply would not allow them to exist financially. And all of that was voluntary and agreed to, or taken over, or whatever in local area. But to say that there hasn't been consolidation, even forgetting Class I's for the moment, would not be correct with history. And it was done through the financing mechanism, and it was quite effective. []

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ROBERT McMANUS: And there is no doubt that we're giving over \$1 billion a year from the state to local government. But notwithstanding that, (inaudible) the bottom three, in terms of how much state aid is getting to local government (inaudible). So it's not a significant amount, but it's less than other states. []

RICHARD BAIER: Is that actual dollars or per capita? []

ROBERT McMANUS: That's per capita. []

ROBERT MUMGAARD: And, I don't know, it seems to me that it's explainable by the fact that the structure is not set up to facilitate giving to local government. And, you know, there's all these threats that (inaudible). But the sales tax, you have a situation where a sales tax, local government can tax an additional local amount. And that does real well for York, and it does real well for Omaha and Lincoln, and the four counties where there is population. But that money is not distributed up to rural counties. And so, you know, one of the options you could consider would be to take that, you know, piece of that local and move it to a more general aid to local government. But as long as the structures are in place, you're going to get a lot of resistance to that. (Inaudible). []

SENATOR FISCHER: You said that Nebraska is one of just a handful of state that...where revenue is not sent from the state to the local governments. What are the other ones? []

ROBERT McMANUS: Well, Nebraska in the last data that we looked at in that paper was dead last, it was dead last. In terms of the size of local government per 100,000 people or 10,000 people, Nebraska is third to the last, and the two below it are Alaska and Wyoming, which... []

SENATOR FISCHER: I'm just curious if there is any connection between states that

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have what's considered a high property tax? If those states, you know, do they send more money, or less money to local governments? Was there any correlation between that? []

ROBERT McMANUS: I don't know the answer to that, Senator. []

MILO MUMGAARD: Well, haven't there been, I mean, again we've had a (inaudible) to look at. But I certainly remember some of the tax debates over the years that there have been folks who have said, what if we were to eliminate entirely the property tax and that certain amount of money that's raised at the local level, and shift that tax elsewhere? There have been...I'm not sure the Syracuse study or anything like that has actually done that. But there's really been costing-out kinds of approaches that have been done. In other words, when that kind of information is laid out there, I mean it does show the magnitude of the challenge that you've articulated here. You know, if we wanted to increase the state aid to local government and figure out a way to do it and a way that, of course, it doesn't increase people's tax burden, and how would we do that in a way that, you know, makes some sense? And there, of course, have been folks, in all of this property tax debate, have said, well, just eliminate the property tax, and therefore you have to shift that to the other burdens and broaden the base, as we say, so on and so forth. But I'm just throwing out that in the conversation about the very issue you're talking there have been folks talking about, well, what if we just eliminated the tax altogether? What would be the impacts? And I don't think we've talked about it in the meeting I've been at here. But I mean, that certainly is...so that if you were to really go at it and change the tax structure and did the following, what would that mean? I'm going to just throw that on the table. []

SENATOR BURLING: Well, your property taxes are very stable, you know, regardless of what the economy is doing. Just like a few years ago when we had the economic downturn, property taxes picked it up. I mean, sure, they are too high. But where do you go? You know, if the sales aren't there, if the personal income is down, where do you go

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for revenue? Local governmental subdivisions love property tax because of the stability of it. So that answers one of your...that's one item. []

MILO MUMGAARD: Well, at the same time, I'm venturing that you, as a senator, you hear more about the property tax. I mean we've talked about this also. But you hear more about the property tax than any other tax. So, you know, from the public's eye, from (inaudible), the issue of what is the Legislature doing about the property tax is more important in sort of a personalized level, than what is the tax policy or the tax structure? And so it becomes difficult because that becomes then the response, well, it's a very reliable and stable source of funding, and at times regressive, and at times it's a burden on folks who shouldn't have the burden. But it's pretty predictable. I'm mostly just sort of reiterating what we already all know to be true. So when addressing the question you raised, well, ultimately how would you address that, without becoming somewhat radical in your approach to the tax policy. []

ROBERT McMANUS: Right, and if you look at the data, the reliance on property tax has decreased over the years. And since the Syracuse study, I think it's now about 36 percent of the tax generated in the state comes from property tax, whereas back then it was 44 percent. So reliance on property tax has gone down, but what's really happened is not that property taxes have gone down, it's that the other taxes have increased and more money has been coming from sales tax and personal income tax. There are...only one state funds its schools entirely out of this. The state of Hawaii has one school district, the entire state is one school district, funded by the state and not by local property taxes; every other state it's property taxes. And the problem, Milo, would be that if you just decide you're going to eliminate the property tax, then you get that 36 percent of your tax base that you've got to then absorb through the sales tax and the income tax. []

MILO MUMGAARD: Yeah. And I'm not certainly suggesting that that would be a recommendation. I'm saying intellectually, sort of logically thinking through your

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question, a starting point would be, well the troublesome tax, one that is certainly tied to the troublesome governmental structure is the property tax. And therefore, if you're starting to intellectually think about what to do, that would be where you start, if that's presumably where the public and others would be most interested in where you'd be at. And one approach would be, well, why not just get rid of it all and move it elsewhere? And that's been talked about, thought about, it's not going to happen. But intellectually that would be one approach. []

JOHN ANDERSON: And that is consistent with what has actually happened when, you know, there have been attempts through lids to control the amount of local property tax, and through the state aid formula, to provide incentives for districts to combine, in one way or another, if not outright consolidation, then some kind of affiliation or other relationship. So that's been, on the margin, the attempt to slow the rate of growth or reduce on the margin the importance of the property tax by constraining levies or providing financial incentives for school districts to affiliate. []

SENATOR PAHLS: But here's an example, since I got really involved in this (inaudible), is the Omaha area, you have the Omaha school system, then you have their own ESU, which they are, and Lincoln is the same way. They make an interlocal agreement themselves, so there is \$30 million at least that's outside the lid. So all these interlocal agreements, which I understand why we did those, sort of set a lot of things outside the lid. I know that they need those. But I mean, it's amazing, if you start taking a look through all the counties and cities that do things. That's their way of getting around the lid. []

MILO MUMGAARD: And to what degree are those entities accountable for that? To what degree are they accountable for that? I mean, how can they be made accountable for that, if they're outside of a lid, if a lid is what is politically needs to be in place? []

SENATOR PAHLS: Well, we allowed that though through those agreements, to be

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outside the lid. See, that's one of those compromises. That's like when... []

_____ : So it has to be...so accountability is one of those things through the (inaudible). []

SENATOR PAHLS: Well, that's like when I'm looking at all these people exempted, you know over the years it's been a political decision. I'm not saying it's wrong, it's just life. But that's how they did it, some of those school districts. I mean, here's an example, one time Millard and Omaha had an interlocal agreement dealing with busing. See (inaudible), and even sometimes how they hired teachers through the ESU. Because they all are struggling. It's not like somebody is putting money in their pocket, they're finding ways. They're good businessmen and women, they're looking for the way of making it work. []

GEORGE KILPATRICK: By way of defense, I suppose, the reason that the interlocal agreement exemption was put in, in the first place, is to deal with the problem that Bob was talking about. There's a lot of local governments, it was an effort to say, that we can be more efficient if local governments would work together to provide services, so we're going to create an incentive by allowing this to be outside the lid. []

SENATOR PAHLS: Which does (inaudible) well. []

GEORGE KILPATRICK: Well, and there have been instances where it's created some things that were very positive, and there are instances like this where it's a trick with their own ESU to set aside a cost. And, yeah, we kind of live with the outcomes, I suppose. []

DON FREEMAN: George, you mentioned LB806. There was a...what was that tool? []

GEORGE KILPATRICK: LB806 was the school aid formula change that accommodated

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levy limits. And what it did is under the old system the schools were divided into tiers, and there were six of them, or there were seven of them, whatever there were. And the tiers were based on size. And then they were "costed" and equalized within their tier. So small schools had a tier, then the ones a little larger had a tier, and then so on out. Omaha was its own tier. And they were...and we essentially equalized funding relative within a tier. What LB1114, which was the year before, said was that all of your schools are going to be at \$1.10, and then three years later \$1, and you're going to get there somehow. And what the Legislature did at that time, in passing LB806, was say, everybody is in the same tier, unless you are sparse or very sparse, which of course is important to Senator Fischer's district and others, I might add. But within that tier, all the way from Omaha, to York, to Syracuse, what we are going to fund is the same number of dollars per weighted formula student it's called, but essentially per body. And you get 10 cents less than the levy limit, plus our state aid, and that's what you're going...that's how you're going to fund your school is on those two things. And that was LB806. And again, there are any number of small schools who are too close to other schools, to be considered sparse or very sparse, that simply could not make it under that formula without an override vote. And if the voters wouldn't allow the override, then they're gone. I mean, I don't know if it was 200 districts or not, but there was a significant,... []

SENATOR FISCHER: At least (inaudible). []

GEORGE KILPATRICK: ...a significant amount of consolidation that occurred between 1996 and,... []

SENATOR FISCHER: 2000. []

GEORGE KILPATRICK: ...you know, prior to LB126. And those essentially, were K-12 districts, small K-12 districts. []

MILO MUMGAARD: Another question I had for is, as you were talking, is in my

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experience I don't hear people or sense that there is animus toward state aid to local government. In other words, there's nothing wrong with that, I guess is the point. That's what I hear. I mean, when you talk about how do you fund education, or how do you fund social services, or how do you...you know, it's what makes the most sense. Taxpayers are taxpayers kind of thing. What do you folks here, senators though, I mean that that, at times, becomes a dilemma for policymakers is that, well you know, folks may not like this. And I wonder, to what degree the don't like that? Why wouldn't they like that? They clearly like the fact that the state is willing to help with the school districts. So just on that question you're raising about the low state aid, is there a political reason for that, other than, I don't know, Nebraska history, over time, whatever? []

SENATOR BURLING: I think people, in general, like state aid to education. But I think we also have to keep in mind to connect the purse strings with the local decision-makers. Is state aid too high? Then you have local boards out in the country making decisions that somebody else is paying for, rather than the local people sitting there, looking at, you know, looking at them, at the school board meeting or county board meeting or whatever. So somewhere in there I think people generally like state aid. But local decision-makers also need to be help accountable for expenses. So there's...like somebody...where do you land? Somewhere in there. []

GEORGE KILPATRICK: There is a bit of a rural/urban split, as well. []

MILO MUMGAARD: Well, I hear that. Then I say, but the elected official, the county commissioner, or school board member, city council person is going to still be accountable for how the taxpayer dollars are spent. Whether it comes from the pocket of the corporate income tax, or a very small local property tax. And the decision is made locally. There is no...unless there are unusual strings attached to that. There is still going to be decisions about how to spend that money. That would be my response to that, but it may or may not be enough for folks, I don't know. []

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SENATOR BURLING: Well, it's interesting how the philosophy of that works. I was on the community college bill to fund that totally with state aid and no property taxes at all. My goodness sakes, they just came out of the woodwork and said, funding community colleges with property taxes gives us a sense of ownership. This is our college, we pay for it with our property taxes; we want to keep that. Well,... []

SENATOR FISCHER: It depends on where you live, Senator. (Laughter) []

SENATOR BURLING: Well, that's what I heard. []

SENATOR FISCHER: My district wants community colleges off property taxes completely. I introduced that bill. []

SENATOR BURLING: So...but I mean, this is part of that discussion. []

SENATOR FISCHER: And the people I visit with, they view state aid, whether it's to schools, cities, or counties, or whatever, as a return of their sales and income tax back to them. It's not the state just giving them money, it's their sales and income tax coming back to help with property tax relief. []

MILO MUMGAARD: And it was the notion that it's their own money coming back to them. []

SENATOR FISCHER: It is our own money. []

MILO MUMGAARD: Other than "our" money, as in a state's...the population of the state's money. So we share in that bounty and this is what we're doing with it here. In other words, it's our money coming back to us. Is that... []

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SENATOR FISCHER: It's the taxpayers' money, it's the citizens' money. And a third of the money that the state collects does go back to local governments, local political subdivisions in the form of aid,... []

SENATOR BURLING: That's why I use the word psychological. []

SENATOR FISCHER: ...which is in the form of property tax relief. []

SENATOR BURLING: It's kind of up here, you know. Property taxes is ours, state aid is somebody else's. []

SENATOR FISCHER: See, I don't hear that (inaudible). []

SENATOR BURLING: I hear that a lot. []

SENATOR FISCHER: No. []

MILO MUMGAARD: So you think that's an important issue (inaudible) tax policy in the future is, you know, how does a taxpayer view the tax code and what they pay as taxes? Is it theirs and ours, as in a local government; or is it ours, as in the state assuming responsibilities for things within the state? And we've certainly seen that modified, that viewpoint modified with respect to the education issue over time. Because you know, obviously, taxpayers in Omaha are helping to fund education in Hershey, or you know it's happening. And that's viewed over time as a perfectly appropriate thing to do. It's the state of Nebraska taking care of the kids in the state of Nebraska. I'm just saying that that may be... []

SENATOR FISCHER: I don't think taxpayers view that as a perfectly appropriate thing to do. []

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MILO MUMGAARD: Well, I'm saying that that mandate (inaudible). []

SENATOR FISCHER: George was talking...no. When George was talking about a rural/urban split, that's part of it right there. []

MILO MUMGAARD: That's what I'm saying, though. I'm not disagreeing that there is that viewpoint. I'm saying that that is a viewpoint that as tax policy, looking into the future group, is that something to think about? And I think that's a very legitimate thing to think about. I mean, why should the Omaha taxpayer be bothered by the educational opportunities of a fellow Nebraskan being provided by (inaudible) somewhere else? Is there something the state could do to reinforce the feeling that the belief on the part of that taxpayer that that money is well spent? []

SENATOR FISCHER: You're going to see that in the future with the learning community bill now and the state resources that are going to be earmarked for that learning community. But the rest of the state is going to look and say, that's not our problem. []

MATT JEDLICKA: Milo, along those lines, and the answer...I mean, I don't know if I truly believe in this 100 percent, but I've heard it from a university professor, not John by the way, that where are those people ending up that are educated in rural areas? Eighty percent of them are maybe ending up in Omaha and Lincoln. So they're being educated out west, and then moving east. Who should pay for their education (inaudible)? Who's benefitting then? And Milo brings up a good point with this, what do people want, lower taxes or local control of governments? And this where we ended up our meeting, kind of, last time. And I guess, not putting guys on the spot, Senator Fischer and Senator Burling, I mean, what do you think? You guys are both in rural districts, essentially. What do your people want? Do they want local control, or lower property taxes, or does it depend if you have kids in school or not? []

SENATOR FISCHER: Both. []

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MATT JEDLICKA: They want it all. []

SENATOR FISCHER: And it, yeah... []

MATT JEDLICKA: And that may be a problem and (inaudible). []

SENATOR FISCHER: We should have them both. []

MATT JEDLICKA: I've ranted enough to this commission. But, I guess, I want lower property taxes. I look at these other states with more efficient school districts. And I don't know if they are that much more efficient, by some of that 2005 data we saw on per pupil costs. But, I guess, I'm in the camp I want lower property taxes. And I suppose that's a big decision for rural areas. That's the decision for rural areas, I guess. []

SENATOR BURLING: Well, my response to your question, Matt, would be my people want local control, number one. And there's evidence that they want to pay for it. But they want their property taxes lowered by more state aid. But that local control is important. And it goes right back to the history we came from, and we haven't got that out of our blood yet. []

SENATOR FISCHER: My district is a little different because we're so sparse in my 17,000 square miles. (Laughter) And, yes, local control, the idea of local control, the principle of it is very, very important. Basically, we can't consolidate anymore. And so that's why I say, you know, we want both. We can have local control, and half of the counties or more in my legislative district already have one school district per county. What else do you want us to do? You know, we just don't have the kids. So in my district its more the property taxes, I would say. You know, people...you know, I have counties looking and thinking, what are we going to do here? Are we going to start, you know, having Springview and Bassett go together, two different counties, and form a

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school district? We just can't afford to educate the children we have. But if you don't have a school, where's your economic development? You know, the whole thing ties together, which is important with LB806, I feel, that there was a cost-grouping of sparse and very sparse districts on it. You can't force those schools to close because there is no place else to go. So we're a little different, even though we're both rural. []

MATT JEDLICKA: And the state...I think the state has done a great job of recognizing. I mean, family hardships, when you start talking about sending those kids off to school at a young age. I mean, I went to college with a couple guys who basically lived an hour outside of where they went to high school. And they rented a home for them throughout the year so they could stay there, by themselves. And you hate to see too much of that. []

DON FREEMAN: I guess the other point about that, local control is local efficiency. I never hear many citizens talk about how efficient is our school system? All they ask for is more state aid. So I think that's a very important part the point that we probably don't look at enough is how efficient is that system. []

SENATOR FISCHER: But how are we going to measure efficiency? []

DON FREEMAN: I don't know. []

SENATOR FISCHER: I have ideas. (Laugh) But your measurements are different, again, depending on where in the state you live. In my opinion, you can't look at cost per pupil, you really can't. My cost per pupil is going to be much higher than other places in the state. []

DON FREEMAN: Sure it will be, transportation costs and so on. []

SENATOR FISCHER: Well, and just the offerings that our students receive are very,

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very limited compared to what more urban areas can offer their students. So cost per pupil, to me, means nothing. Levies in Nebraska to me mean nothing, because you have to tie it in with valuations, for heavens' sake. So when somebody says, won't your levy go up? Well, no. You should be asking, did your property tax request go up? That's what you should ask at a budget hearing. But, yeah, I think a lot of this when you talk about efficiencies, okay, what does that mean? []

DON FREEMAN: Well, I guess you can look at, you know, the teacher per student ratio, number two; the output of the student, are they learning well; what achievements do they have; how many services are not paid for...sports, outside activities, all those things? There are a lot of different things that can be looked at in the school system that probably aren't or are overlooked. It's just...I still think there's a way to become more efficient. I know in business, of course, in any business we look at the bottom line every day, and in ag, try to see what can we do different to cut costs? So I don't know. It's a very difficult question. But maybe a lower lid, would that force efficiency? (Inaudible). Unless the population votes for it, it's .9. What do I do to get down to .9? Where can I become more efficient? []

SENATOR BURLING: Raise the valuation. []

MILO MUMGAARD: No, no. I just...it's a dilemma. And I don't see any easy way out of it. And I think consolidation is okay, but it would be a very tough pill to get done. You talk about...at the hearings in North Platte, I hear all the time, well it's out-of-state versus Omaha and Lincoln. It's a state within a state. That's the mindset that you hear a lot beyond Lincoln or beyond York, it's a state within a state. And it's very difficult to overcome. []

MIKE HYBL: Do you feel though that there is a...ultimately is there a difference of opinion as to what kind of adequate, fair, equitable, etcetera tax policy do we need to have, as between someone who lives in North Platte and someone who lives in

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Omaha? And I would venture there probably (inaudible) no difference, ultimately, in their viewpoints about what would that look like, you know, if you were able to articulate that. They would probably articulate about the same. Thinking about my own situation as a taxpayer, what do I pay? What's fair in the community? What are the services that government should be doing, fulfilling? They're generally going to be about the same ballpark. So in terms of, you know, thinking about how we could deal with that (inaudible) or you know, I'm a taxpayer here first, not there, etcetera, my money shouldn't go there, vice versa. You know, maybe there are things that could be done in the context of looking at tax (inaudible) into the future that goes to the whole question of, how do we...how does everybody really understand this tax structure? They understand it about the same way, and they all understand they are Nebraskans. So more or less, we're all on the same page. So start from there. I mean, that may sound a little Pollyanish, of course, but nonetheless, it does seem to me in the work I've done over the years, particularly with things like social services, and health care, and things like that, folks are very, very happy that the state has picked up the tab for those things. And we'd not want to see their local community go without those things. And they need more, and they need better of them, things of that nature. So therefore, they're open to ideas about adequacy and, you know, fairness, and equitable ideas. But they're not thinking about it any different than somebody in Omaha (inaudible) sitting there on, you know, quite a taxpaying situation. So maybe that is something to think about as we think about our recommendations is this sort of...and I've talked a lot in these meetings about public perception of the tax code and tax structure. I think that is a meaningful thing to throw out there to the public is, how do you...you know, how...even how should you view the tax code and the tax structure? And by the way, this is probably how you do view the tax code and the tax structure. And you do it the same way Omaha and North Platte does it. And it's the Nebraska tax code that has tried to meet the needs of Nebraskans kind of thing. []

_____ : I think it's probably a pretty easy exercise to go from Omaha to
Scottsbluff and get a consensus across the state what a fair tax structure is that

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everyone can agree to. The trick is, does it generate the revenue to provide the services everyone...and the governmental structure that everyone from Omaha to Scottsbluff wants? I think you could get agreement on what it ought to look like. But then at the end of day, what can you do with it? What's it going to give us for revenue? []

DON FREEMAN: Getting back to Senator Pahls's question about, how do we grow? That's got to be a long-range program. This definitely won't happen...we lower the income tax, personal income tax, nothing will happen right away. It's got to be something that's got to be structured into maybe a ten-year plan. And in the meantime, people are going to be paying, you know, more taxes to support that, to get more people in. And that, to me, that's the base question, we need to get more taxpayers, we need to grow the state. Needing to grow the state means we got to make it more attractive. How do you make it more attractive? Well, we've got the incentives, and the different visions and so on, but the basic program is, how do we lower the personal income tax, or the corporate tax, and the property tax to make it more attractive? That's a dilemma. []

MILO MUMGAARD: I would agree it's a dilemma. But at the same time, there are the additional issues of, how do you pay for it then and provide the services that make it so that it's possible to have quality business with quality employees and so on? And, of course, we all know that. The answer to that is education and infrastructure and so on. Well, somebody has to pay for that. And so therefore, it seems to me that that would outweigh the issue of to what degree is the cost of relatively low state and local taxes? It's more are there...do we have access to an educated workforce, and a workforce that has etcetera, etcetera? So I mean, this is a political debate, a political discussion. But certainly it's not just the tax policy, it is other things as well. So when we think about how do we make sure we have more taxpayers, it is tax policy plus. []

GEORGE KILPATRICK: There is no correlation between tax burden and population growth or shrinkage, none whatsoever. []

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DON FREEMAN: There is no correlation? []

GEORGE KILPATRICK: No. For example, the two states that are by us that have no income tax, Wyoming and South Dakota, are both losing population faster than we are. []

SENATOR PAHLS: Well, they don't provide any services. []

GEORGE KILPATRICK: They don't provide any services. []

SENATOR PAHLS: So why would you stay? []

GEORGE KILPATRICK: Meanwhile, the biggest grower in our area is probably Minnesota, and they have very high income taxes. You know, there is no correlation like that. []

SENATOR PAHLS: But the thing about Minnesota is, because I have some background, over the years it's been known as a state that appreciated education. And so I think it has a different philosophy. See I think part of the problem here is...why we're hearing more and more about property taxes, as I look around this table, just think, how many of you have children in school? If you have children in the public schools, then you are willing to pay for it. If you don't have children in school, most of us are saying, hey, you know, I did my thing. You realize that the tax dollars that we spend per child today...to educate your children for 12 years is around \$100,000, if you look at how much it costs every year for 12 years to educate your kid, at least...close to it anyway. So once your child is out, and I think we're getting more people getting grey hair in the state; they care less about, you know, maybe the education system. I've never had anybody come to me and say about property tax, when I was a school administrator, they said, we want good education. Nobody talked about property tax. But those were

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people who had children in school. And I think that's why we hear more and more rumbling, because we have more people that do not have any. You talk about efficiencies, I agree. There are efficiencies, because when I looked at the...my biggest argument against OPS is the efficiency factor. But even...let's say you take some of the major issues out. If you look at the school in your own hometown, do you really see what you call a lot of waste? So let's say there's an extra teacher there. Well, that would be \$30,000 to \$35,000, I know it's every year, or \$40,000. But I mean, I don't see just tons of them sitting out there. And I taught at Atkinson, Nebraska, and we were always trying to find things happen...you know, to make things happen. Even if you'd get rid of, let's say in the Omaha area, 20 administrators, I know that would run up there, but it still wouldn't be a significant dent. I think if people...to me, what I'm finding interesting right now, because we see education coming to the...you know, educators coming to the trough, wanting more money. And that's going to happen. But look at the two states: Iowa and Wyoming, they have given additional money in their education of the children. Iowa has just this last year, above what's now...they've fallen to like 25th in the nation. I mean they've come up to being about 25th. But they're adding more money. And if Wyoming is doing it, and we're sitting here, not being able to do it, but I'm not saying we need to, but some of these states are finding the additional monies above and beyond, you know, the typical state aid, they're throwing you big chunks, which literally surprised me. You go across the river from Council Bluffs, you know, teach in those area schools you get a significant increase this next year, sort of like a bonus. []

JOHN ANDERSON: The Wyoming revenue stream is highly cyclical and varies quite a bit. And it's only recently that they've had a lot of extra revenue. []

SENATOR PAHLS: I understand. (Inaudible). And here's another thing, too, most teachers are not what I'd say unbelievably overpaid. I mean, I don't believe that. And the biggest part of your budget. I mean, you know, the class sizes, you may have to shrink those, you know. I think if a local community wants to do that, but again there are too many people with my color hair, although I do have a kid in high school, so don't let the

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grey hair fool you. (Laughter) []

MATT JEDLICKA: Well, you are saying Iowa (inaudible) that much more money, that is state aid. []

SENATOR PAHLS: Yeah, state aid, state aid that's coming back, above what typically...I mean, it was in the paper. I don't have the exact information (inaudible). []

MATT JEDLICKA: I think one thing that's maybe starting to bother people is just their valuation is going up so much. And I just know with ag land, if it's on a, correct me if I'm wrong, a three year average, what we've seen ag land prices do, I mean, these schools are seeing 10 percent valuation increases each year. Well, where is that money going? Are their budgets going up 10 percent? My levy hasn't gone down. I think that's starting to irritate a lot of people as well. []

SENATOR PAHLS: But in your local community then you ought to really be eyeballing those school boards. []

SENATOR FISCHER: Well, but the problem is in my area, my local board, they would like the levy lowered... []

DON FREEMAN: Okay (inaudible). []

SENATOR FISCHER: ...because of the problem of valuation increases, you know. We have so much land, and that's where we get all the wealth from, so we have all the resources. And in order to receive that state aid, you're going to have to keep at that levy. But yet you're not giving your taxpayers the break they deserve. So I have...the majority of my school districts would like the state to lower that levy. You won't hear that from other school districts. []

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JOHN ANDERSON: They don't want to do it themselves? []

SENATOR FISCHER: Well, we lose the state aid then. []

MATT JEDLICKA: You're talking about 96 cents. If they drop below that, they start losing...yeah, and I've heard that, too, from our superintendent in our district. []

SENATOR FISCHER: When you see valuation increases, double digits, I mean, that...and what you end up doing then, even if you lower your levy, you're going to be having to ask for a higher property tax request. So you just shoot yourself in the foot. []

JOHN ANDERSON: Yeah, but the problem is not to alter the valuation method on the land. I mean, this is an ad valorem system, we tax on the basis of the value of the land. Commodity prices are high, federal payments are...transfer payments are at an all-time high. It's all being capitalized into the higher land values. []

SENATOR FISCHER: Well, I'm in a ranching district, I'm not a farming district. (Laugh. []

JOHN ANDERSON: Okay, all right, all right. So... []

SENATOR FISCHER: There's a difference there. []

JOHN ANDERSON: So the land values are going up for very predictable reasons. There's no particular problem with that. And where the problem is, is that the rates that are applied to the values then are not being scaled back proportionately. []

SENATOR FISCHER: Right. But I hear property tax concerns, not just in my district. I grew up in Lincoln and have family and friends here that I see a lot and have conversations with. And no matter how old they are the thing that upsets them the most is property tax. And the thing in Lincoln, Nebraska that upsets them the most is property

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tax. So it doesn't matter where you live, and if you have kids in school or not, I hear it from my district to Lincoln, I have family in Omaha... []

SENATOR PAHLS: See, I'm not talking about (inaudible). []

SENATOR FISCHER: But I have family in Omaha and that's what they talk to me about is their property tax on their home in Omaha. []

SENATOR PAHLS: Right. But I'm just saying they don't talk to me about property...they didn't talk to me about...they talked about schools. They didn't, at that time,... []

SENATOR FISCHER: Yeah, but that's what I hear. Do you hear now property tax? []

SENATOR PAHLS: Yeah. Well, right, but that's I haven't (inaudible). []

SENATOR FISCHER: But I also think if people...you view your local school district as being efficient as being a good district. Now, the neighbor district, that's not quite as good. (Laugh) And then you know, we look at Lincoln and Omaha, ooo, they have some problems. Then you get out-of-state, and oh my heavens, you know. It's close to home, it's just like they love their local senator, close to home it's great. (Laugh) Then as the circle widens, then there is...that's where the problems are. []

SENATOR PAHLS: But let me ask you this, because you probably, since you can see your schools really easier than some of us in the metropolitan areas, but do you see that like in Valentine or some of these other schools that they are just adding on staff? []

SENATOR FISCHER: I have very small districts, too. I have districts that have less than 80 students, K-12. []

SENATOR PAHLS: But you don't see them adding on staff, do you? []

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SENATOR FISCHER: No. And they have, you know, you talking about pupil-student (sic, teacher) ratio. I have six kids in a classroom in some of my districts. I was in Tryon this week, I was in Thedford, small schools... []

SENATOR PAHLS: See that's why I'm surprised how in some of the areas how your property tax can continue to go so much, if you're not adding additional teachers. []

DOUG EWALD: Right. Where is it going? []

SENATOR PAHLS: I mean, it's...and you're not giving them these unbelievable rates or giving them raises. So that's why I've always been confused about some of the areas that it's easier to take a look at. []

SENATOR FISCHER: Because you have to have so many staff members just to meet, you know, state requirements. And distance learning, a lot of those really small districts do distance learning. And just to get that set up, you know, it seems like there's changes in that every year, and the schools have to revamp their district...distance learning room. Vans, now the State Board said you can't have vans. Well, when you're hauling seven kids, Tryon, Nebraska has, I don't know, three vans or something. Now they're going to have to get buses. []

DON FREEMAN: Or Suburbans. []

SENATOR FISCHER: I mean, I have a problem with that (inaudible). But just costs like that... []

DON FREEMAN: I think one thing about property tax is that people don't read the whole tax statement to know what other subdivisions are. []

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SENATOR FISCHER: Oh, schools are the big one now. []

DON FREEMAN: The schools are a big one, but... []

SENATOR FISCHER: That's 70 to...I have a district where 89 percent. I mean, you know, that's the big one. []

DON FREEMAN: But you look at county government and all the districts, the natural resource districts, and they all are really starting to become a fairly good recipient of tax dollars. []

MILO MUMGAARD: I wanted to ask you as an administrator, past administrator, the Lincoln paper the other day ran a very good cover article on where do your property tax dollars go and front page. So Lincoln taxpayers looked at this. And there was 62 percent to the school district, and 17 percent for the county, etcetera, etcetera. And I have two seventh graders that go to school in Lincoln. And I used that as a, okay kids, let's sit down and let's do a math problem here. This is how much we pay in property taxes every year, and 62 percent of that goes to your education and other kids education. So figure that out for me. So they quickly figured it out. And I said, isn't that a heck of a deal? And they said, wow, that's all you paid? That's all you paid, you know, for my education and other kids education? I said, that's exactly right. So, I mean, it just strikes me as...I know (inaudible) school districts have done now, they say, what a great deal you're getting for your tax dollar. But it seems abundantly clear that it's a fantastic deal, you know, that everybody gets. And why it's viewed as a burden is a good question, is a messaging and political messaging question. Because otherwise it's fairly obvious, if you're spending \$1,500...in my case, \$1,500 a kid, plus others, that's a pretty darn good full-time education for those kids. []

SENATOR PAHLS: And see that's why I'm saying Minnesota has always had the (inaudible) of education being really significant, and we've been known as a state that

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doesn't put education up as high. []

SENATOR FISCHER: Oh, I disagree with you, I disagree with you on that. I think we have... []

SENATOR PAHLS: Well, I've lived around educators almost 40 years. []

SENATOR FISCHER: My mother was a teacher. (Inaudible). []

SENATOR PAHLS: Well, I don't want to argue about that. []

SENATOR FISCHER: We'll argue some other time. (Laugh) []

ROBERT McMANUS: Well, let me come back to reality (laughter). (Inaudible) goes back to something we were talking about (inaudible) that there is no silver bullet here. That when we went into looking at the whole structure, what do you find? You find that property taxes are high by any measure, sales taxes are not the highest around, but they're high, personal income tax is stout, corporate income tax is not that high, but still in the middle of the pack. And so there is no lever to pull to automatically reduce property tax without (inaudible). But two red flags stuck up in '88 and they're still there today. And those red flags are that on property tax that local government, employees per capita, is strikingly, it was six times higher than (inaudible) back then. Part of it because Nebraska is a low population state, and then take into account that the electric utility are state employee...or local employees. But I worked that into the numbers, it didn't make much difference. Say you have that red flag that local government is...the structure is high. And the second is that aid to state...state aid to local government is very low. So those are two... []

SENATOR FISCHER: How do we rank, if you look at state employees per capita, in Nebraska how do we rank? []

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ROBERT McMANUS: It didn't seem to be on the (inaudible). State employees per capita was not on the (inaudible). I mean it was (inaudible), it was (inaudible). []

SENATOR PAHLS: Except in the Transportation Department. (Laugh) []

_____: State and local we rank seventh. []

RICHARD BAIER: Senator, one of the things... []

SENATOR FISCHER: State and local? []

_____: Yeah. []

SENATOR FISCHER: Did they break it down (inaudible)? []

_____: No, they don't. []

ROBERT McMANUS: But I did look at some data that it was, the local, that was... []

RICHARD BAIER: Senator Fischer, I'm wondering (inaudible) if we should be looking at? I think Deb and I maybe have had this conversation. We could both live with a cost of living increase every year. Because one of the things that happens in my budget, and I don't know about some of the others, but we continue to pick up programs year after year and year. And they...some of them aren't really very darn good, to be honest with you. And I'm looking, right now, at (inaudible) all communities. []

SENATOR FISCHER: We love that. []

RICHARD BAIER: We can't get rid of the money. We've (inaudible) to get rid of it. We

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have programs like that. We have a surety bond program in Omaha we can't get rid of. (Inaudible), some of you may be (inaudible). A bill was introduced two years ago to get rid of it, Governor didn't put it in the budget, he eliminated funding. It came out the other end of Appropriations a double. []

SENATOR FISCHER: What happens to the money? If you don't use, you can just... []

RICHARD BAIER: It comes back. We won't spend it. I refuse to spend it. []

SENATOR FISCHER: It just sits there? []

RICHARD BAIER: Well, it will go back to the General Fund at the end of the biennium, because I refuse to fund that project because I don't like to do that. []

SENATOR PAHLS: Appreciate that. []

RICHARD BAIER: Well, but it's a fact of life. I mean, we're having to go ahead and try and get people to spend state money. So in terms of looking at how do you deal with this... []

SENATOR FISCHER: Don't say that too loudly. []

RICHARD BAIER: That's fine, I don't have a problem with that. []

SENATOR PAHLS: No, I (inaudible). []

RICHARD BAIER: That's part of my job is to provide some leadership in those areas. I'll (inaudible) the same thing. Doug's doing his reorganization. He's able to cut some cost, considerable amounts of cost. (Inaudible), but I appreciate the fact that he's taking a beating in the newspaper for (inaudible) the rest of us. (Laughter) But, you know, I think

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there's some opportunity there, even on the state side, if you wanted to limit annual increases to cost of living, that would be great. Because what you've seen is it's been (inaudible) cost of living. The other thing that sticks out in Don Freeman's book, which he's...I don't know if Don got to that one or not, is higher education per capita cost. We're really high in higher education per capita and per student, both. []

SENATOR FISCHER: And that's without the community colleges. []

RICHARD BAIER: Yep. So there are some other areas that... []

GEORGE KILPATRICK: (Inaudible) in there. I'm not real sure, but they might actually be in there, because it is higher than that. []

_____: Sorry, John. (Laugh) []

JOHN ANDERSON: It's the denominator that's the problem, not the (inaudible). []

RICHARD BAIER: Yeah, there you go, there you go. []

RICHARD BAIER: So there are some other issues like that. And so in terms of, you know, following what Bob just said about it, you know, there isn't a magic bullet. Some of these need to be long-term recommendations from us to hold state spending at the cost of living. We could all live with that. It will force us to make some tough choices. But it's not any different...sooner or later, I think, the voting public is going to give us 412 and 413, if we don't find a way to do it ourselves. And then it will be under primers (inaudible) from a policy perspective. []

SENATOR FISCHER: Whatever the one was last year. []

RICHARD BAIER: Yeah, 413, right? They all went to get their... []

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_____ : 423. []

RICHARD BAIER: 423, thank you; they all run together. []

ROBERT McMANUS: And one of the things the commission might recommend would be to let the Legislature look at these two anomalies and understand why is this local structure so much out of line with other states, and why spending...state aid to local government is so low compared to other states, even though it's substantial. []

SENATOR FISCHER: Do other states have it in their constitution that there are so many counties in the state as Nebraska does? I mean, the Legislature can't just consolidate counties as it does school districts. []

ROBERT McMANUS: I don't have the answer. George? []

GEORGE KILPATRICK: I don't know the answer to that. But there are states with more counties, a number of more counties, actually, than Nebraska. []

SENATOR FISCHER: And I asked that earlier. In Iowa it's comparable, they have twice as many people. []

GEORGE KILPATRICK: It isn't...it's a combination of things. But there's a number of layers... []

SENATOR FISCHER: I just don't know that... []

GEORGE KILPATRICK: ...(inaudible) we invent things like... []

SENATOR FISCHER: ...I necessarily agree with your premise on that, that the number

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of local governments maybe increases cost. Because, as George said, we've seen school district numbers go down tremendously, I think tremendously in this state and costs for education continue to go up for K-12 education, and higher ed. []

ROBERT McMANUS: Actually, I think it merits investigation, because... []

SENATOR FISCHER: Yeah. I don't know if I would agree with that. []

ROBERT McMANUS: ...the data says (inaudible). []

SENATOR FISCHER: Oh, we can all interpret that the way we want. (Laugh) []

GEORGE KILPATRICK: Well, what are those local governments after all? There's about 600 fire districts (inaudible). []

SENATOR FISCHER: Exactly, fire districts, NRDs,... []

GEORGE KILPATRICK: Well, there is only nine NRDs, anyway. I mean, that's not... []

SENATOR FISCHER: I'm trying to think on our tax forms everything we have. Historical societies... []

GEORGE KILPATRICK: Yeah. But we invent things, but we invent things like ag societies, historical societies, building commissions, railroad transportation safety districts. It's hard to even remember all of them. But they don't levy much and they don't spend much, for the most part. But we added all of them up,... []

SENATOR FISCHER: It's the school districts that spend... []

GEORGE KILPATRICK: ...some years ago, as a combined total, everything that was

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lower that...I mean the big...the multicounty things we can't (inaudible). (Inaudible) school districts, and NRDs, and all that other stuff, and everybody else, townships, townships of all things levied somewhere in the order of \$50 million at that time. This was a number of years ago. And a bunch of those are SIDs. It depends on how you want to count SIDs and those taxes, because it's significant with their developer taxes and people, for the most part, aren't paying them. So the numbers are the numbers. I understand numbers, because (inaudible) inside there. Which of those do you think you don't want (inaudible). []

SENATOR FISCHER: Yeah. []

GEORGE KILPATRICK: Partly, it's because the rest of the model of organizing government is that you don't have the city do everything. When you need a new task, you invent this other board to take care of it. And (inaudible) city people. Why do you have an airport authority board that's appointed by the city council to run a city airport, as opposed to simply having the city run the airport? Because that's how we do it here. But does it add cost? Not really. []

MILO MUMGAARD: Well, Bob, you've put those as anomalies. But you're also saying there are structural (inaudible) term, normalities or normal things, such as that we have gone to great lengths over the years to create a tax code that has a broad distribution among property tax, sales tax, try to evenly distribute that. We've gone to great lengths to think about how the base can be broadened, even though obviously it could be broader and it could be (inaudible). We spent a lot of work on (inaudible), thinking about who's paying taxes and who shouldn't pay that. Like in the income tax context, people below poverty do not pay income tax. I mean that's a policy decision, that sort of thing. So there are...but that's pretty normal. The food...food not being sales taxed, that's pretty normal. So there are things that Nebraska has done to create a fairly normal, modern tax code. But yet there are still some anomalies that exist. []

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ROBERT McMANUS: Right. And there is no question if you look at the way that, particularly with property tax, the way that the reliance on property tax has come down over the years and other taxes have taken their place. This is putting Nebraska much more closely in line with your typical state (inaudible) in the paper. But I recollect that the average state is somewhere about 33, 34 percent reliant on property tax, and Nebraska is about 36 or 37 percent; but Nebraska used to be quite a bit higher. And so over time, it's...you know, every number has seemed to be pulling now in the right proportion. But those two factors are, or those red flags were there in the '88 study. And when you look at the data, just raw data, they're still there today. And so it just seems to me that they could use some analysis on, you know, the Senator said, is this really that Nebraska is out of step, or is it all explainable? []

MILO MUMGAARD: And the anomalies go toward the question of the political issues of, are we funding things adequately? Are we able to do the things the government needs to do in the way it needs to do it? []

ROBERT McMANUS: Right. And I even wonder whether you could conclude that the reason there's not more state aid to local government is because the Legislature, in its wisdom over the years, has seen that that may not be the best way to...because of the structure of local government, the best way to...for Nebraska to operate. Tuition may be closely tied, but it's just, I think, something that needs some study. []

SENATOR PAHLS: But just by listening, it sounds like a lot of those positions out there really don't cost anything anyway in local government. []

GEORGE KILPATRICK: The total fire district levy is, you know, \$10 million, \$12 million, statewide, I suppose. []

SENATOR PAHLS: And how many fire districts do you think there are? []

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GEORGE KILPATRICK: Well, there's about 600 of them. []

SENATOR PAHLS: See, that's what I'm saying is if they're not really...so that...the information from that study may be a little bit skewed, because we have a lot of these groups and they really don't cost anything? I mean,... []

GEORGE KILPATRICK: Well, I mean just stating that there is a lot of local government, I mean I disagree with that. Of course, there is a lot of local government. There's a lot of units of local government, there's a lot of people that operate these things. But part of it is the populace tradition because quite often we...you know, our history, our state has solved new problems with new governments as opposed to saying that the city and the county should do this. And that doesn't necessarily mean that it's more expensive to do it that way, but there's an additional tax levy. []

SENATOR FISCHER: We have volunteer fire departments in my area that can levy. You don't pay anybody for staff. You're not hiring a fire chief, you're not... []

GEORGE KILPATRICK: All it is, is a sinking fund and equipment, that's what they're levying. []

SENATOR PAHLS: But if you have this number of people,... []

SENATOR FISCHER: You know, so is it efficient? Is it efficient, or is it not efficient? []

SENATOR PAHLS: But I'm just saying, that shows you we have not only another layer of government, but there really...it's not a very thick layer. []

GEORGE KILPATRICK: Look at SIDs, for example. There are probably 800 SIDs in the state of Nebraska. What they are is they are governments. And the reason they're governments is because their interest becomes federal tax exempt when you do it that

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way. But it's the sort of debt that the developer quite often buys himself or sells to his friends in order to create a development that, hopefully, will be successful. And if it's successful the amount of property tax levied to support the debt, which they may not even pay, incidentally, for a number of years, and just accumulate as delinquent. Hopefully, the base grows enough and is successful enough that the rates come down to some place and then it's annexed. Folks in Sarpy and Douglas County think this is a great way to develop. It doesn't involve a lot of public tax dollars on the part of the city. They sort of rise or fall on their success, depending on how successful they are. If they are successful, they can be annexed without opposition, because that's the goal, after all, (inaudible). But what that is is about \$50 million property taxes at 800 governments that other states don't have, because they finance them privately as opposed to through an SID. So how do you factor that in to your consideration of how high property taxes are and how many local governments you have? []

SENATOR BURLING: Well, along that same line, you have townships, rural fire board members, they don't have levy authority, they don't get paid for what they do. The things that they do would have to be paid for, if they didn't have townships, the county board does it. That wouldn't reduce the cost to do away with the townships, even though I think they ought to be done away with. You wouldn't really save anything. Fire district boards don't cost a lot of money. That equipment would have to be bought and paid for by taxpayers somewhere along the line anyway. So, you know, I think you made a point that you have a lot of people involved in local government, but a lot of them are volunteers. []

_____ : It's only the employees that show up in Bob's numbers, right? I mean, Bob's numbers count employees, not volunteers. Correct, Bob? []

ROBERT McMANUS: Yes. It just merits investigation. What I propose to do is to (inaudible) issue (inaudible), which I really haven't, and look at it, at the next meeting and... []

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SENATOR BURLING: Okay. Where do you want to go from here? []

ROBERT McMANUS: Well, let's...if we can return to sales tax. What I did...I wanted to talk about the issue that Doug brought up last time, which was the severance taxes. And []

DOUG EWALD: Before you move there, this sales tax exemption sheet we were talking about here earlier, these dollars up in here are tax dollars already. If...you don't take that times 5.5 percent to get a tax...tax dollars. []

DON FREEMAN: Can't be. []

DOUG EWALD: Well, I just made a call, back to Revenue, that's why I left, because there was something there that didn't seem right to me. And that's straight from our...that is straight from the Sales Tax Expenditure Report. []

RICHARD BAIER: Those are actual sales tax collections? []

DOUG EWALD: Those are dollars, that would be dollars associated with that. That's not base, that's dollars. []

RICHARD BAIER: Dollars (inaudible) \$2 billion as opposed to... []

DOUG EWALD: Yeah, correct, exactly. Those items would add \$2.75 billion in tax. []

_____ : If we tax those services at 5.5 percent. []

DOUG EWALD: Correct. []

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DON FREEMAN: That's \$2.5 million? []

DOUG EWALD: Right. So that's tax dollars, that's not base. []

DON FREEMAN: Okay. We solved that problem. (Laughter) []

DOUG EWALD: Yeah. []

ROBERT McMANUS: Well, that certainly changes the (inaudible) on what you could get. []

DOUG EWALD: Oh yeah, I mean, you get a lot more bang for...you know, in a few categories. []

SENATOR PAHLS: And if you'd add more, you'd get more. I'm telling you, I think we ought to take a look at the exemptions and if it does hit a certain industry, then we earmark, maybe, on property tax relief. I would be very irritated if I had one of these, let's say if I were a florist and I found out I'm going to get hit, then all of a sudden somebody else sitting over here says, oh gee, he or she has more lobbyists working for me, then I'll get...I think... []

DOUG EWALD: Right, sure. There will be a parade in your office. (Laugh) []

RICHARD BAIER: Senator, I would look at it from an exploitable cost issue, because one of the things I'm looking at, for example, florists, is simply a matter of moving money around. Not that I'm going to make a case for these guys. Fuel aircraft, for the most part, that's being paid by out-of-state people coming into Nebraska. I mean, I think we have to differentiate somehow between those two. []

SENATOR PAHLS: Right, right. []

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_____: So, Doug, just to be clear, these are the tax expenditure numbers out of the report? []

DOUG EWALD: Correct. []

_____: These are estimates of the current revenue losses that come... []

DOUG EWALD: The value of that particular exemption from just an absolute dollar standpoint. []

_____: Right, assuming the current rate would apply. []

DOUG EWALD: Correct. []

MIKE HYBL: And only to the state, not to cities that don't have local option. []

DOUG EWALD: Yes. []

_____: There's no local option sales in here? []

DOUG EWALD: Yeah, I don't think there is. I'd have to look it up. Yeah, I think that's right. []

SENATOR PAHLS: I bet the newspapers would be willing to write us up. (Laughter) []

DOUG EWALD: That's get more depressed. []

SENATOR PAHLS: (Inaudible) would get that in. I'm just having... []

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_____: (Inaudible) Revenue Committee advanced that twice. []

SENATOR PAHLS: No, I was just having fun now. []

SENATOR FISCHER: Really? []

GEORGE KILPATRICK: It took somebody else to go get it and put it in, because nobody introduced such a bill. []

SENATOR FISCHER: You realize last year there was a (inaudible) during floor debate to lower the sales tax? []

DOUG EWALD: Yes. []

JOHN ANDERSON: And do what with the revenue lost? []

SENATOR FISCHER: Oh, to lower it a half cent. []

_____: Just...and to take the revenue hit. []

GEORGE KILPATRICK: Well, as opposed to some of the other (inaudible) that were (inaudible). []

SENATOR FISCHER: That did not pass, by the way. []

SENATOR PAHLS: Add the exemptions, lower the tax. That's what we're about. I think we got to look at this small (inaudible). I think we have to be fair about it, personally. []

SENATOR FISCHER: (Inaudible) bang for your buck you lose the exemptions and keep the tax. []

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_____: Yeah, give me a description on that sales and property, the third line down. []

SENATOR FISCHER: Broaden the tax base formula (inaudible). []

_____: What number is that? []

_____: Oh, off of this sheet, the third one down, sales and property. []

_____: Is there an item number, line item number? []

_____: I've got several of them for you. []

_____: It's in this schedule here. []

_____: You see, all exemptions are numbered. []

_____: Oh, okay. []

_____: So what number was it? []

MATT JEDLICKA: Well, it's 77-2701. Is that what you're looking for? []

DON FREEMAN: Yeah. []

ROBERT McMANUS: It's either sales of real estate, or it's sales for resale, one or the other. []

DOUG EWALD: Yeah, I don't know which one it is. Do you have the expenditure report

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with you? Oh, you do. []

DON FREEMAN: You know, there was something wrong with those figures then because this LB397 should generate a lot more income than just \$800,000 []

_____: But I think if that is sales for resale... []

DON FREEMAN: No, I mean just all this...this LB. You know, they say he went from... []

SENATOR FISCHER: To reduce it (inaudible)? []

DON FREEMAN: Yeah, it only generated \$144 million at 2.8 percent, and they broadened the base substantially. []

SENATOR FISCHER: But they lowered the percentage. []

DON FREEMAN: Yeah, I know, but if you (inaudible) take it up to 5.5, it would go back up to about \$8.2 million...I mean \$820 million. []

_____: George, in your bill did you do sales (inaudible)? []

GEORGE KILPATRICK: No. I think that may be...I think it's sales for resale, which was not included. []

ROBERT McMANUS: The third item \$1.5 billion, and that wasn't included. []

_____: Right. []

GEORGE KILPATRICK: Inventory. []

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_____: Okay, okay. []

DOUG EWALD: Exactly. Yes, that wasn't included in the bill, in LB397. []

ROBERT McMANUS: And that's a huge number. Take that (inaudible). []

DOUG EWALD: Yeah, right. []

GEORGE KILPATRICK: I'm not finding it, so I don't know what it is. Oh wait a minute, here it is. Here's the number. Yeah, it says for resale is what it is. []

DON FREEMAN: All right. []

GEORGE KILPATRICK: So it's inventory purchases, and that was not included in LB397. []

ROBERT McMANUS: So I will rework these numbers, but that...if you take that (inaudible) then (inaudible). []

GEORGE KILPATRICK: Now, when LB397 was done, the state rate was 5 percent. []

DON FREEMAN: Right. []

GEORGE KILPATRICK: So the reduction in rate was not half, like it is not. It was something less than half, if that... []

MATT JEDLICKA: And are these biennial, like the budget, or are these annual? []

GEORGE KILPATRICK: Those are annual. []

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SENATOR PAHLS: Deb, there's something here, the trade-in value of motor vehicle, that would help with your gas tax. I'm just trying to help. []

SENATOR FISCHER: Did you read the fiscal on this one, though? (Laughter) []

GEORGE KILPATRICK: What you should read is the committee statement. It's a pretty lengthy list of (inaudible). []

SENATOR PAHLS: Oh really. (Laughter) It would be interesting, it would stir the mud. (Laughter) But sometimes some of these things need to be revisited. I see coming out holding the schools accountable; I agree with that, and a marriage of...taking a look at the exemptions. I think we'd come out pretty darn good, because they are the ones that come to the table owing money. []

DON FREEMAN: What's the total amount of these exemptions? You ever have that added up? []

GEORGE KILPATRICK: The report sums it (inaudible). The report itself sums it at the bottom. Or you mean the LB397 one specifically? []

DON FREEMAN: I don't see that on here. []

ROBERT McMANUS: Well, clearly, the sales tax, broadening the base is the most easy way to generate substantial revenues within (inaudible). []

GEORGE KILPATRICK: Because you've never tried to do it. (Laughter) []

SENATOR PAHLS: Give the people of setting a lid, like they did in California, or doing some of this, they'd probably start waking up. []

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ROBERT McMANUS: The other thing in the sales tax paper, and I probably would move this, but at the end of our last meeting we had a brief discussion about severance taxes. And I included in the revised sales tax paper a portion on severance taxes, which in the final paper I may pull out. It is an excise tax like a sales tax. But I'll probably pull it into a separate section of other excise taxes. And, Doug, you had started to talk about that last time. You might just talk again about the concept that (inaudible). []

DOUG EWALD: Sure. The concept is, and you get this from looking at the states around us that have the best tax environment, or the least tax burden to their residents. And you look at the best example, obviously, is the state of Wyoming. And why? They're blessed with coal, oil, gas, and they have a severance tax. And that's why Dr. Anderson here talked about well, the ebb and flow is with the price of those commodities, but it's been very high here. You know, Wyoming has a significant surplus to run their government for the next two or three years, and that's after they've already plowed an extra \$600 billion, \$700 billion into education. Well, that severance tax, it's a severance tax, but it's passed on to the ultimate consumer. And where are those ultimate consumers? They are outside, for the most part, outside the state of Wyoming. So for all practical purposes, they have exported their whole tax base to people outside the state of Wyoming. What a great luxury to have. So you look at what do we have? What is our natural resource or resources? We know we don't have enough water. But we have some uranium, and there is currently the first \$5 million of uranium is exempt from the excise tax on uranium. And that...I understand there may be an additional mine being under construction right now out there. But in the past, that manufacturer would start paying the severance tax or the excise tax on uranium in August. The price of uranium has gone from \$2 or \$3 a pound to \$100 a pound. So now they've run through that; they're starting another (inaudible) starting this last February. So they actually called me and said, well, what do you think about us going into, instead of a spot market price, an actual what we're...we're only earning \$35 or \$40 a pound, not the \$100 spot market price. I said, well, okay, who do you see it to? Well, we're selling it to our parent company in Canada. So I said, let me get this straight here, so you don't have an

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arms-length transaction between a subsidiary and the parent, and you have no apportionment factor in the state of Nebraska for income tax because it's a sale outside the state? They said, exactly. I said, so what's your problem? (Laugh) I said, what you have to worry about here is that, okay, we're looking to broaden the base or do some different things here. You're at risk. You said you're on the borderline of getting greedy here because you're at risk of losing your \$5 million exemption, along with the possibility if the per pound price going up. So they asked us to enter into a different arrangement. I denied that just because, I said, no, that's up to the Legislature to decide what we want to do, it's not...I don't have the authority to do that with respect to how...whether it's a price that they...a contract price, or market price. So there is an option there with a natural resource. The other, obviously our biggest natural resource is corn, which we turn into ethanol. And 90 percent of our ethanol is exported to California. So what can we do? The possibility there exists of doing a 2- to 3-cent a gallon production tax on ethanol, which will be passed onto consumers in California. You hold the consumers in Nebraska harmless. You lower the excise tax to pump the 2- or 3-cents to Nebraskans on ethanol, so it's a wash here. But for all practical purposes, at 2 billion gallons at maximum capacity, 3-cents a gallon production tax, all of a sudden you've raised \$60 million, which has been paid for by people in California. And you use that for roads, whatever anyway, something along those lines. We have, obviously, the federal funding for roads is down. But I mean, that goes into the mix, I guess, from that standpoint of how do we export that tax base to people outside the state of Nebraska? So that's the concept behind that. []

ROBERT McMANUS: I've thought about that. And it seems, and John you may help me here, but it seems to me that what you were saying is there's about a 7-cent... []

DOUG EWALD: Yes, that's a good point. Let's finish that. There's about an 8-cent a gallon difference when you look at the rail freight rates of getting a gallon of ethanol from Nebraska to the west coast, versus Iowa to the west coast. So we're 8-cents a gallon cheaper in Nebraska just because of where our physical location is. So you don't

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want to price yourself out from being...not being competitive with Iowa, who's I think the nation's largest producer of ethanol. Is that right, Richard? So you can do 3 cents, still have to be a nickel cheaper than the ethanol coming from Iowa, but export that base. So 3 cents, something there, you don't want to get...you know, I don't know where you draw that line at, I guess. But 3 cents is...you know, you still have that nickel comparative advantage just from a transportation standpoint. []

ROBERT McMANUS: The way I'd say it is you...it's a commodity, which Nebraska adding a tax, they can't recover in the market, because the market is going to be set by whatever other commodity from ethanol is, it's just like crude oil. But so long as your tax is less than that transportation differential, the producers or the manufacturers would not have any incentive to move from Nebraska to Iowa, because it still...so they're going to have to bear additional cost that they probably can't recover in the market. But it's still...Nebraska does have an advantage here that is kind of a unique niche. []

MIKE HYBL: But it's a product in those markets they really can't move away from and not use. They pretty much have to use the ethanol to oxygenate their fuels in California. []

DOUG EWALD: That's right. []

MIKE HYBL: So they've got to buy it. []

DOUG EWALD: That's (inaudible) gone away from that MTBE. []

JOHN ANDERSON: As long as there is a federal mandate. They could change it (inaudible). []

DOUG EWALD: Yeah, right. Oh yeah, they could. The federal mandate...they could mandate more ethanol. []

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GEORGE KILPATRICK: How many gallons were you... []

DOUG EWALD: Two billion a year at full capacity. []

GEORGE KILPATRICK: At full capacity; right now we're what, a fourth of that? []

DOUG EWALD: Oh, more than that. []

_____: We're well over a million. []

DOUG EWALD: Yeah, we're a billion at least. And you look at the mechanism for how you collect that. The checkoff is already in place. So the plant that collects the checkoff, not only do the production tax, there's a mechanism in place. We're not adding an additional layer of complexity at that standpoint. []

JOHN ANDERSON: So we both subsidize and tax the same commodity, federal subsidies, of course. []

SENATOR RAIKES: I think we still have state subsidies on ethanol. []

DOUG EWALD: Sure. On the plants, you bet. []

SENATOR FISCHER: Not on the new plants, not on the recent plants, though. They don't receive the (inaudible). []

RICHARD BAIER: No, (inaudible) June 30, 2004. []

ROBERT McMANUS: So there's no one would argue that it's kind of breach of contract to prove? []

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GEORGE KILPATRICK: Well, they will argue it. []

_____: Oh yeah. []

DOUG EWALD: But there are still those that qualified for the various tax incentives to offset the income they earn. Those are still in place, that's a contract with the state. []

SENATOR FISCHER: But about half of the plants online now do not qualify. Did they, Richard? []

RICHARD BAIER: No, but I think it's probably close to that. I haven't gone back and looked. But there have been a lot of them placed in service since June 30 of '04. There have been three in the last couple of months. []

SENATOR FISCHER: Yeah. []

RICHARD BAIER: In the last two and a half (inaudible) we put three new ones online, most of them are that 100 million, between... []

GEORGE KILPATRICK: They do not qualify? []

RICHARD BAIER: They do not qualify for the '04, correct. []

GEORGE KILPATRICK: And there are old ones, too, after all, under old programs that we're not paying for anymore. []

RICHARD BAIER: Right. []

GEORGE KILPATRICK: The checkoff you mentioned, however, was the corn check.

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You said there was a mechanism in place. (Inaudible) corn checkoff. []

DOUG EWALD: Right. []

GEORGE KILPATRICK: I don't know that we have a mechanism for a checkoff on ethanol. []

DOUG EWALD: Well, who collects the corn checkoff part? []

GEORGE KILPATRICK: Department of Ag. []

DOUG EWALD: At the elevator? I mean, where are we... []

GEORGE KILPATRICK: The first purchaser are typically in an elevator, but sometimes it a feedlot, for example. []

DOUG EWALD: Well, in this case though, the ethanol plant would be the first purchaser. []

GEORGE KILPATRICK: Right. But are you collecting the tax on the gallons of ethanol, or bushels of corn? Because I thought you were collecting it on barrels of ethanol going out. []

DOUG EWALD: Well, it would be a production...it would have to be on all production. That's why you would give the credit at the pump to offset what was going out state. []

GEORGE KILPATRICK: And that is what I mean. There is not...to my knowledge, there is not an actual mechanism in place to tax it going out of the plant. It's corn going in we tax, not ethanol going out. Now there's only a dozen...it's not that hard to find them. There's a dozen of them. I don't necessarily view as a huge problem for your

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department. But it is a new program to that extent. []

DOUG EWALD: Right, sure. I guess, what I'm saying is if the ethanol plant is the first user, they are already collecting the checkoff, so now they're going to send the checkoff in, and now all of a sudden they're going to send the production in. []

GEORGE KILPATRICK: That's true. They are (inaudible) to a checkoff. []

DOUG EWALD: So it's not...they're already a collector as well. []

MILO MUMGAARD: On the sales tax front, I have a suggestion about a recommendation that goes to what you were saying earlier about, (inaudible) to go through all the tax expenditures and the exemptions. And it's always occurred to me that they've called it the Tax Expenditure Report for a reason, which means that it's actually money out of the budget. So a simple enough idea, whether it's politically possible or not is to require that the tax expenditures, the sales tax exemptions, for example, are actually in the budget, whether they're an item that is...somehow or the other is produced side-by-side, as you go along with your appropriations or actually right there for the...in some fashion there for the policymakers to know about. Another step beyond that would be, of course, that every so often a particular exemption would have to reestablish that it's appropriate. You know, if you've got a \$200 million a year expenditure, presumably, that should be...there should be some policy discussion whether that's a good thing or not, as opposed to... []

JOHN ANDERSON: You suggesting automatic sunsets on all exemptions? []

MILO MUMGAARD: I'm just, of course, brainstorming here to some degree. But it just strikes me that in the sales tax exemption area there is a lot of concern about there is a lot of stuff that's exempt from tax, above and beyond the services and everything else that we are worried about. A recommendation, perhaps, from the commission could be,

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well, that should be thought of as a tax expenditure, it's called that, and let's put it into the budget in some fashion so that the policymakers are aware that this is where this is going. It then obviously would open up the opportunity for certain policymakers, state senators to say, hey, I (inaudible) about that. But it may be that nobody else (inaudible). But yet it's information that is side-by-side with the budgeting process, not a separate report that may or may not be integrated with that whole stuff. So anyway, it strikes me that that would be one approach to the exemptions issue that is short of what's going on. What did you say, Bob, what was the easiest one to go after? But anyway... []

SENATOR BURLING: Low fruit? (Laugh) []

MILO MUMGAARD: That's right. So I think the tax expenditure report has a bigger role in the...could have a bigger role in the budget (inaudible). []

SENATOR PAHLS: Well, it would be more transparent. You know, somebody is arguing about something, you say, well gee, looks like something is coming out of here. []

JOHN ANDERSON: At the federal level, if you want the tax expenditure reports, you have to go to the budget document. It's in the federal budget document where you find the tax expenditure report; it's an appendix at the end. It doesn't get the attention it deserves in terms of equal billing with the direct expenditures. But my guess is a lot of states that alter their budget laws to require tax expenditure reports in the 1970s and 1980s, probably did that through the legislation that controls the budget process. I don't happen to know the statute here in Nebraska. Is there a budgetary statute that provides for the tax expenditure? []

GEORGE KILPATRICK: Yes, it is. []

MILO MUMGAARD: Was that Senator Warner's initiative? []

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GEORGE KILPATRICK: Yes. []

MILO MUMGAARD: Because I mean you did...I can kind of remember him talking about these things. []

GEORGE KILPATRICK: It was actually before my time. So it's been there a long time, but that is (inaudible). []

MILO MUMGAARD: And I think, ultimately, that was his goal, is that this stuff should be incorporated into the broader budget decision-making. []

JOHN ANDERSON: That's the main idea. But politically, it's never gotten the same kind of traction as direct expenditures. Although, conceptually, there are expenditures in every (inaudible) the same way as direct expenditures are. []

ROBERT McMANUS: What would be missing there with the services that it...the way the law works, all property, tangible property is taxable, unless it's exempted, but all services are exempt, unless they are taxed, specifically taxed. And so you need to figure out and you need to try to get the services (inaudible) Legislature. []

SENATOR PAHLS: And that gives me something to talk to me about. She cleans houses, she has a company, and she's being taxed. She just said, well, I don't have a lobbyist, that was her answer. So why...and apparently she's gotten...she's a pretty smart woman. She's gotten to this and said, some people would get it, but I don't. So I think...I'm just thinking we ought to be holding everybody accountable. But as you said earlier, if there are schools that need to have their act together, let's get it together. []

MILO MUMGAARD: I used to be on the legislative committee for the bar, and every year I'd vote in favor of the sales tax exemption for the lawyers to be taken away. And I was the one, sole vote on that committee. (Laugh) It was an uphill battle. []

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DOUG EWALD: You had one term, right? (Laughter) []

JOHN ANDERSON: Just as long as he was the sole vote, he wasn't very threatening.
(Laughter) []

ROBERT McMANUS: Well, I'm wondering whether a couple of motions might be appropriate. But first of all, with respect to severance tax on ethanol, Doug, you want to make a motion that... []

DOUG EWALD: I guess, I would...see if I can bring it together here. I would motion that the committee make a recommendation that a severance tax on ethanol be explored as an alternative revenue source for the state to be spent as it sees fit. []

SENATOR FISCHER: I just second that. []

SENATOR BURLING: Is there a second to the motion? []

_____: Senator Fischer. []

SENATOR BURLING: Oh, excuse me. Okay. There should probably be some more discussion before we vote. But this can also be revisited again. What we do...what happens with these motions gives Bob some guidelines on where to go with his next group of papers to hand out. And just like today, we had some conclusions on a couple areas. And he would prepare, if this motion were to carry, he would prepare something on the severance tax and bring it back to us at our next meeting to look at again. And so this is not really final. But it sure would give us an idea of where you want to go with the severance tax issue. Anymore discussion before we vote? There hasn't been a lot. Is there questions? []

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MATT JEDLICKA: I guess, I have a question. Bob, did you say something...if other states are doing this with ethanol, or do we know that at all? []

GEORGE KILPATRICK: I'm not aware of it. []

ROBERT McMANUS: I'm not aware of it either. []

MATT JEDLICKA: Even if they're not though, we seem to have the leeway. And I was just curious. []

ROBERT McMANUS: We do know that in the last legislative session the Governor of Iowa was bristling a bit about oil severance taxes and suggesting that they put a severance tax on all quart. So the topic of putting severance taxes on renewable resources is being discussed. And at least two states, Arkansas and West Virginia do tax...impose severance taxes on crops. And a lot of taxes impose severance taxes on timber, which is a renewable resource. []

SENATOR FISCHER: There's Wyoming on coal. []

ROBERT McMANUS: Yeah, (inaudible) and Montana on coal. []

SENATOR FISCHER: That's how they live. []

SENATOR RAIKES: To change this here a little bit, you would have ethanol plants complaining about this idea, because, in effect, you're cutting their margin. They're going to argue that it's going to reduce the profitability of our plants, or it's going to increase the amount we have to charge for the by-products. Well, it seems to me we're going to get a lot of the same arguments that you get when you try to expand the sales tax base. []

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GEORGE KILPATRICK: Well, what would...I don't know of anybody that really likes to be taxed. []

_____: Right. (Laugh) []

SENATOR RAIKES: Um-hum. And the distinguishing characteristic of this is that the consumers are out-of-state. Whereas, if you expand the sales tax base, almost by definition they're instate. []

DOUG EWALD: That's right. And we have a competitive advantage from a transportation standpoint with the cost of getting the product to California. So they... []

JOHN ANDERSON: There is a spacial dimension to this that makes it a different kind of (inaudible). []

DOUG EWALD: Yeah, exactly. That's a very unique dimension of it that...but for that, I don't know if you could go there? It would be a really, really tough sell. []

SENATOR RAIKES: Well, but obviously... []

JOHN ANDERSON: But this changes the market area... []

DOUG EWALD: Oh sure. []

JOHN ANDERSON: ...over which our ethanol producers could effectively compete, but... []

MIKE HYBL: It would be touch in the least. []

JOHN ANDERSON: Right, right. So I mean, we would have to think about, you know,

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what happens to the market area here, taking transportation costs into consideration. But if most of the product is being sold in southern California or California, I'm thinking southern California in particular, we ought to nail them. (Laughter) I mean, it's an interesting economic problem to think about. Whether it's a good policy or not, plus the competitive nature of the industry right now. How competitive is this? []

DOUG EWALD: Yeah, I mean obviously, Wyoming has a lock on the low sulfur coal. []

JOHN ANDERSON: Right, right. And you're in a different position when you're a monopoly supplier. []

SENATOR RAIKES: Well, your motion was to study it. []

DOUG EWALD: Study it and (inaudible). []

SENATOR BURLING: Are you ready to vote? Anymore discussion? Well, call the roll, Amanda, we'll see what we get. []

COMMITTEE CLERK: John Anderson. []

JOHN ANDERSON: Aye. []

COMMITTEE CLERK: Richard Baier. []

RICHARD BAIER: Yes. []

COMMITTEE CLERK: Senator Burling. []

SENATOR BURLING: Aye. []

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COMMITTEE CLERK: Doug Ewald. []

DOUG EWALD: Aye. []

COMMITTEE CLERK: Senator Fischer. []

SENATOR FISCHER: Yes. []

COMMITTEE CLERK: Don Freeman. []

DON FREEMAN: Yes. []

COMMITTEE CLERK: Mike Hybl. []

MIKE HYBL: Yes. []

COMMITTEE CLERK: Matt Jedlicka. []

MATT JEDLICKA: Yes. []

COMMITTEE CLERK: Senator Kopplin. Senator Louden. Senator McDonald. Milo Mumgaard. []

MILO MUMGAARD: Yes. []

COMMITTEE CLERK: Mark Munger. Senator Pahls. []

SENATOR PAHLS: Yes. []

COMMITTEE CLERK: Senator Raikes. []

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SENATOR RAIKES: Yes. []

COMMITTEE CLERK: Senator Stuthman. []

SENATOR STUTHMAN: Yes. []

COMMITTEE CLERK: 12-8. []

SENATOR BURLING: Okay. Thank you very much. []

ROBERT McMANUS: Okay. And then the second issue that was just discussed, and I don't know whether this one is right for a vote yet, but Milo was talking about the concept of putting the exemptions on budget and perhaps sunseting them so that they would need to specifically be looked at again by the Legislature. []

MILO MUMGAARD: I think a pretty mild recommendation would be to simply recommend that there be a side-by-side presentation or publication of the tax expenditures and sales tax...well, in this context sales tax exemptions, and this is what we're talking about is sales taxes. []

GEORGE KILPATRICK: Well, the expense report contains all taxes. []

MILO MUMGAARD: Um-hum. So when...side-by-side presentation with the annual appropriations process. So to figure out a mechanism or process by which the expenditure report is part of the actual appropriations process. Now, it's not like it's a lost document, or lost report that everybody is looking at, but rather it's simply that that is an affirmative action that takes place. The report is published. It's incorporated into the Appropriation Committee's process, etcetera. I just think that an affirmative action to make it or something specifically that would put those two... []

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DOUG EWALD: If it's published formally today,... []

GEORGE KILPATRICK: Every other year in October. []

DOUG EWALD: Every other year, exactly. So what you're asking for is that this should be made a part of the budget process or the appropriations process? []

MILO MUMGAARD: Yes, exactly, so that there is a side-by-side presentation or discussion or assessment going on. []

MIKE HYBL: Is it published concurrently with the year the budget is done? Or is it done on the off budget year? []

GEORGE KILPATRICK: It's done in even years, even-numbered years. So it would be prior to the full body of the budget... []

MILO MUMGAARD: The reason it's a mild recommendation is it's obviously a report that exists, and it's obviously in a position...it is a fairly contemporaneous report, when the budget process begins. So having there be a next step to make sure that it's incorporated into the budgeting process would seem to be a fairly mild step. That's my motion (inaudible). []

SENATOR BURLING: Comments, questions? []

SENATOR PAHLS: Well, I see it as just being more transparent so people...those of us taking a look at it, will see it, remind us. If I'm pushing a particular issue, I may look at that and say, hmmm, I need to think before I say something. []

GEORGE KILPATRICK: Would you...Bob mentioned a couple of issues with the way

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the tax expenditure is constructed, report is constructed currently, which is that there has to be, there is hereby exempted somewhere in there. And specifically, sales for resale are in the tax expenditure report, the lack of taxation...of (inaudible) services is not, as an example, just in the way that it is constructed. []

MILO MUMGAARD: Then maybe a second recommendation how to improve... []

GEORGE KILPATRICK: I mean, is there some different concept that you have in mind that would vary from that a little bit? []

MILO MUMGAARD: Well, I think that that would be an additional helpful thing, to have it be more descriptive of what is being exempted and how it's being exempted and so on. What I'm really focused on here, in terms of this whole transparency thing, and when you're making decisions about things that you're aware that standards and others are not only theoretically aware of it, but also have it right in front of them that there is a \$200 million exemption right here, while you're simultaneously voting on whether you should or shouldn't have a given program. That is a relevant factor. []

SENATOR RAIKES: Those discussions in the committee process take place in different committees. A lot of program stuff is in Appropriations, the tax policy stuff is in Revenue. I don't know that...when you say make it available in the budget process, I'm not sure how that actually works? []

MILO MUMGAARD: Well, what I'm thinking about is not so much it's the Revenue Committee's problem, it's the Appropriation Committee's issue; it's more the question of, what is being produced as a part of the budgeting process for the public to also be aware of and be looking at? Because, for example, when the Appropriations Committee creates its basic budget, it is of course producing, here's what we're going to spend in a given area, and then in turn hearings are held, and so on and so forth, the whole process plays out. What I'm thinking in terms of is there should also be an element in

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that that has this tax expenditures incorporated. These tax expenditures need to be incorporated into the decision making process, even a simple matter as side-by-side presentation with what's going on with the proposed budget. And therefore that allows for the transparency we're talking about. The public is certainly going to know far better what's going on and so on and so forth. To treat them as different things is not correct, in my opinion. To create...to treat an appropriation...to treat an expenditure on say a given public program as an appropriation, but not to create...to treat an expenditure on a tax exemption as an appropriation is, of course, kind of disconnective. They are both expenditures. So therefore in some fashion we need to be thinking about them in the same kind of ballpark. At the moment they're not really thought of in the same ballpark. As you say, while the Revenue Committee is talking about it in one place, the Appropriations Committee are talking about it in another place. So this is just an idea that goes to the question of bringing it together and then also allowing for the public to be aware of it as well. []

SENATOR FISCHER: I don't think mine will know, though, that the Appropriations Committee, my understanding of the process, they wouldn't need to look at that. Because, although all senators need to be aware of it, the Appropriations Committee need to take that into consideration when they're forming their budget of expenditures. You know, the Revenue Committee looks at taxes and rates and things. I don't think I understand what you're...I don't think that's the proper place for it, in Appropriations. []

GEORGE KILPATRICK: Well, here is a scenario that might be possible. Suppose the Appropriations Committee decides they want to fund, gee, let's say the Department of Roads at a higher level. Okay. And the way they're going to do that is we're going to eliminate the trade-in allowance. Okay? And that's so many hundreds of millions of dollars. I suppose the net result of such a decision would be that if a bill pops up for hearing for Revenue, which there were...we had two, or three, or four of those, four years ago, when we were looking at increasing taxes and also in a variety of way. And Appropriations Committee had introduced had introduced, at their request, a number of

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these sort of substantive bills in other committees. So I suppose it could result in that kind of process. []

MILO MUMGAARD: But it wouldn't be...this would not be something that would be asking for the Appropriations Committee to take action, it would be...in other words, the Appropriations Committee would not have the say so, wouldn't have jurisdiction over, obviously, whether a particular sales tax exemption was or was not going to continue, that would be a Revenue Committee jurisdiction. Yet it would be in the context of a governmental decision-making process about how much we're spending and how much we're spending on what. This is directly on point. This is the same stuff, it's just that there is no jurisdiction (inaudible) that committee would not have jurisdiction over that particular item. Would that be...is that relevant? Sure, because you're looking at a picture of the state of Nebraska that has a \$3 billion budget, but also has a \$1 billion tax expenditure budget, something to that effect. Other places have tax expenditure budgets that are out there. And I'm not sure exactly how they incorporate it into their process. But if there's a way in which we can incorporate this into our process, legislative process, so that the committees are more fully informed about the side-by-side implications of this, as well as the public is more informed. But I think that's all that's all to the good. Whether or not they will be able...have jurisdiction to take action on the sales tax exemption, except in the context that George described, that's a legislative process thing, not necessarily what I'm going towards here, which is more of an informational, what body of knowledge needs to be on the table kind of situation. []

SENATOR RAIKES: Well, at the margin, here's new business tax incentive program X that's been introduced, there's a fiscal note and there's a revenue loss that fits together. So we already got that. And when that comes to the floor, we know how much that's going to cut state revenues as compared to what they'd be without that program. It's kind of...so what you're asking for is some sort of a cumulative number, like let's look at not only this business tax incentive program, but all the ones we've done from day one up to now and what...how much they all reduce revenue? []

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MILO MUMGAARD: Well, according to the tax expenditure report, what kind of revenue are we not seeing because of that particular type of exemption? []

SENATOR RAIKES: And again, on the margin... []

MILO MUMGAARD: (Inaudible) sales tax is the (inaudible). That would be...yes, it would be a cumulative report. It already is a cumulative report. It's simply that it would be installed or put into the...be presented as part of a budget process so that there is full recognition up front of the dimensions of what's going on with respect to these tax expenditures. Whether any of those tax expenditures are addressed, changed or anything, that's a whole other question. But it certainly would give people information about where are we going, in the big picture? Revenue would otherwise be able to address and meet our (inaudible). []

SENATOR RAIKES: So I want to draw a parallel with zero-based budgeting, if you're talking about expenditures programs, rather than saying we got...pick on the Department of Roads, we got the Department of Roads; we're adding \$10 million to the Department of Roads. So the discussion is about the \$10 million, it's not about the \$300 million that we're adding it to. So with zero-based budgeting, what little I know about it is okay, everybody goes back to zero every year, and you add it up. Well, you want to do that same thing on the revenue side. []

MILO MUMGAARD: No, I'm saying that that theory could happen. I mentioned that earlier that, you know, why isn't it logically okay to say that a \$200 million exemption has to at least occasionally come back and be justified? But I'm just saying, you know, actually that's something that could be defensible. I'm not saying that actually would be what I'm recommending. I'm not recommending it now. I'm simply saying that that \$200 million exemption should be at least considered, and the folks who are making these decisions should be seeing those side-by-side to their actual appropriations decisions.

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And more important, the public is going to be putting two and two together. This is a tied together, or pulled together the dots kind of thing for the public more than it will be... []

SENATOR FISCHER: We have a yearly summary on the green sheet, and it's daily. But it's just dealing with the bills that we're faced with that year. So I mean...and we get that updated every day. []

MILO MUMGAARD: Well, when you get a green sheet, what you're saying is that you get updated every day as to what are our decisions as to Appropriations, what are our decisions as to this, and what's the...is it all fitting together? []

SENATOR FISCHER: Um-hum. So you see (inaudible). []

MILO MUMGAARD: But that's a different matter. That's an ongoing legislative process decision. That's not...the backdrop to this is we do not tax X, rather we give an exemption to X, we give an exemption to Y, X, Y, and Z, which is information that is useful at the start of the process, and may or may not be (inaudible). The green sheet is how does it play out and how does it fit. []

SENATOR FISCHER: Right, and the report, as I understand it now, comes out...it will come out this next year, in 2008, correct? So then that report will be used as we go into the budgeting process for the beginning of the school year in 2009. So, you know, you need it ahead of time, so you can have it when you go into the beginning of your two-year cycle, too, on the budget. []

MILO MUMGAARD: I presume that's probably why it's in there (inaudible). []

SENATOR FISCHER: Right. []

MILO MUMGAARD: (Inaudible) some logic, Senator Warner (inaudible), that made

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sense. []

SENATOR STUTHMAN: What you're trying to look at, what I'm understanding from the short time I'm here, but you would like to see a list of all of the exemptions and have that made available so that you can pick out two or three of them that maybe are not worthy of being exempted anymore, and they'll raise \$200 million and go off of that, and then utilize that in the Appropriations? []

MILO MUMGAARD: That's pretty much right. I mean, the reality is that the tax exempt expenditure report is a nice public document that reflects our willingness to be transparent with this information, to a certain point. And that's great. And we (inaudible). The next step is, okay, how do we...is there anything that we should do affirmatively to ensure that that is being incorporated as backdrop to further Appropriations decisions, and obviously for the Revenue decisions, above and beyond be in a report that we have sitting there on our shelf? And that's what I'm suggesting is that that does get incorporated into the front end of the discussion in some fashion. Not that it's going to lead to anything specific. It may and it may very well be, as Senator (inaudible) says, you know, I really do think that the way to fund the new highway X is to go after this tax exemption (inaudible). So be it. They may have figured that...and they probably (inaudible) figure it out anyway, before they come in. But this is tying the information basis together so that we have (one) probably more informed state senators, and (two) we certainly have more potential with the public. It's a good government idea is how I'm crafting this in my head. []

ROBERT McMANUS: Well, let me suggest this, perhaps I could draft a couple of (inaudible) incorporate that. Then I might also draft one which takes that further step and says, let's sunset all of these provision, and force the Legislature to readdress them, force the Legislature to relook at every exemption. (Laughter) []

SENATOR FISCHER: Yeah, whatever. []

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SENATOR BURLING: So you'll bring us back something next month? []

ROBERT McMANUS: Right, and I then I'm going to also try to...the piece that's missing, once again, is services, because they're not taxable unless you specifically tax them. I find it very difficult, very difficult to find out how much a particular service, for instance lawyers, and doctors, and accountants, what's the foregone revenue? I had to really dig, I mean that's not published every year. []

JOHN ANDERSON: It's my experience with both state and federal tax expenditure reports that by their very nature some of these are incredibly difficult to estimate. Doug's people have a hard time calculating the foregoing revenue when we don't tax it, we don't know the size of the base, so we don't know what the rate would raise. And quite frankly, oftentimes, tax expenditure estimates are pretty casual, sort of back of the envelope calculations, because there is no specific data out there. We haven't been collecting tax on that activity, that service, those goods. And so we really don't know the size of the base very well, so we estimate. And even at the federal level, some of the tax expenditure estimates are pretty soft estimates. And then the other problem, just thinking ahead, I'm supportive in principle of the idea that Milo puts out there. But what sometimes is done then is you try to take the foregone revenues and you try to allocate them, like you would in any budget, to expenditure categories, like roads, or like other categories. And it's difficult to take the foregone revenues and decide how those should be allocated to lines of expenditure in a budget to try to get the full picture. Because then you have to make some arbitrary decisions about what those foregone revenues, you know, should be matched up to in terms of categories of expenditure in a budget. That part is very difficult to do for some foregone revenues should be matched up to in terms of categories of expenditure in a budget. That part is very difficult to do for some foregone revenues, in a case of an exemption on an excise tax on gasoline it might be easy. But in the case of a broader exemption, on a whole class of services, it becomes very difficult to know. How would I put this into a budget that's organized by expenditure

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categories? But the idea of sort of raising the prominence of the tax expenditure report and using those numbers more fully in budget debates, I think, is a good one. []

SENATOR BURLING: Mike, did you have a comment? []

MIKE HYBL: No. []

SENATOR BURLING: Okay. Other comments? Questions? How would it be if we had Bob work on this, do a little research, and bring us...bring something back to us next month? Does that... []

MILO MUMGAARD: And I will be happy to help you, Bob, draft up some language and (inaudible) and stuff. []

SENATOR BURLING: Okay. We won't do a motion on that. We'll just ask him to bring us some information next month. Who's next? []

ROBERT McMANUS: Before we leave sales tax, one of the handouts is a colored chart This data is not...I think it's 2003, but it's an issue we talked about briefly last time, and that is with respect to motor fuels. Nebraska taxes motor fuels only for the amount necessary to fund (inaudible). And other states, in addition to funding roads, put a sales tax on gasoline, and that sales tax then goes to general revenues. The 1988 Syracuse study (inaudible) what Nebraska does because they said, really, gasoline doesn't...without that, it doesn't contribute to the overall sales tax that every other tangible, personal property...taxable property does. So I just...there's a...the states use a variety of methods. Some states do put a sales tax on it. Unfortunately, Nebraska's motor fuel tax, because of the road system and everything is high to begin with. And so some states fund...they can put the sales tax and additional motor fuel tax, and they're still (inaudible). Then the other unique thing about Nebraska's method is that, in times of rising oil prices, the cents per gallon tax actually starts getting reduced because there's

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a reduction in consumption of gasoline. And so while oil is \$70 a barrel, and those states which have a sales tax or a percentage-based tax are experiencing a rise in revenues, states which have a cents per gallon tax are actually experiencing a decline in revenues because consumers react to the high price of gasoline. []

MIKE HYBL: Bob, those states that also apply a sales tax to motor fuels, do they recognize the distinction between on-road use and off-road use, or is it just a gallon sold is taxed? []

ROBERT McMANUS: I would say that they generally would be consistent with...I would think it's...they would recognize off-road use, because there would be sales tax (inaudible), agricultural, we don't put a sales tax on other agricultural inputs. []

SENATOR RAIKES: So you wouldn't sales tax diesel fuel on a truck that's hauling input parts from one place to another, but you would put a sales tax on gasoline that's being used by the final consumer? []

ROBERT McMANUS: No. I said most states don't do that. A lot of states do, except off-road use. But all vehicles on the road would be subject to (inaudible). []

SENATOR RAIKES: But there are a lot of production inputs that get transported over the roads. So wouldn't you kind of be violating the principle of only taxing the final product? I suppose you could argue that unless fuel is actually a part of the final product, we retax... []

_____: (Inaudible) component part (inaudible). []

SENATOR RAIKES: Yeah. []

MIKE HYBL: And I'm sure on-road, off-road, the difference between a commercial load

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on a train versus a commercial load on a truck is...I don't know how you'd approach that. I'd just be curious as to how states handle... []

GEORGE KILPATRICK: Yeah. There is a separate exemption for train fuel anyway (inaudible) like construction machinery, for example, would be off-road, but it would not be agricultural and presumably would be subject to a sales tax, even if ag was exempt. []

ROBERT McMANUS: Well, I'll bring this up again next meeting. But let's just kind of hang it up there (inaudible) study (inaudible). How would you (inaudible), Senator? []

SENATOR BURLING: Well, there's a little while yet, okay. []

ROBERT McMANUS: Okay. I think we'll switch to the personal income tax, which we haven't talked about, which we did talk about at the last meeting. I've worked with John on gathering the data here. And, John, I might...I think that we came to the conclusion there were two primary areas that the commission might want to look at, one being the brackets, the second being the (inaudible). []

JOHN ANDERSON: Yeah. We thought that there were two areas that might be worth recommending some consideration be made regarding...the first is the indexing of the brackets, the income tax brackets, so that as inflation pushes up income over time, we would do as the federal income tax does and make the brackets move with the rate of inflation, so that inflation doesn't push people into higher income tax brackets. There is a revenue cost to that. It can be expensive. That's a consequence. But nonetheless, it would be worth looking at carefully, ways in which we could index the Nebraska personal income tax, especially the brackets, so that they just move right with inflation and we don't have to make periodic ad hoc adjustments to them. The other has to do with the degree of progressivity of the personal income tax. There is really a couple of ways to think about progressivity, of course. One is the increase in the nominal rate as

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you move up through those brackets. The other is to take into account, not only that progressivity in the nominal rate structure, but also the effect of exemptions and credits and other things, and look at the effective tax rate. If you want to look at that handout that Bob has given us, you look at the graph, he's plotted by percentile, that is by percent of the income distribution on the horizontal axis the effective tax rate. And we've got it for single filers and for joint filers, right? And you'll see at the bottom end, the bottom...well, for joint filers, the heavier dashed line, you'll notice that the effective tax rate is negative, until we're up to around, what is it, \$7,000 or \$8,000 of taxable income. I suppose this is taxable income (inaudible) another measure of income. That, of course, has to do with the fact that the low end, a family may not have any tax liability, but may benefit from credits that give them a refund. But once you cross that threshold and you're above the zero line, your effective tax rate turns positive. And you'll see that it rises, and it rises at a fairly steady rate, until we get toward the end, when we're up above the 85th percentile or so it starts to rise at a relatively fast rate. So the degree of progressivity is not constant, it's rising at a fairly steady rate, and then takes off toward the end. Bob calls this a hockey stick effect. If you look at the numbers, if you flip over and look at what's labeled as Table G1, on the back of your sheet, look at the lower panel of this table, you've got effective tax rates from 1995 through 2005. If you just look down at the bottom row, 2005, these are estimates of the effective tax rates. You'll see that for the first seven deciles of the income distribution, that is the lower 70 percent of the income distribution, the effective tax rate being paid is 1.94 percent. Now, the nominal rate may be above that, right? But we've got exemptions, and deductions, and credits that make the effective rate lower. But if you look across that row, you see what happens is you go up from the bottom deciles to the eighth decile, to the ninth decile, to the tenth decile. The tenth decile, of course, is the upper 10 percent. You'll notice that what happens is we go from an effective tax rate of 1.94 percent up to 4.78 percent. So what happens is as you move up the income distribution, the effective rate of taxation more than doubles, it's two and a half times, roughly, if you go 1.94 percent up to 4.78 percent. So the degree of progressivity here, in my view, is breathtaking. It's a very substantial degree of progressivity. And so I think there's justification in thinking about

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the degree of progressivity that we've got built into our system, not just the rates as they go up in the nominal structure, but the effective tax rates rise quite substantially. And I know that the degree of progressivity is in the eye of the beholder here, there's a subjective element to this. I'm cautious about this because I realize that we're in a more global economy all the time and that financial capital is increasingly mobile, and we've got to be careful about highly progressive personal income tax structure in terms of discouraging financial capital from staying here in Nebraska for fleeing to other areas where the effective tax rate may not be quite so high. So I'm sensitive to the mobility of capital, potential problem that we have here. And I'm not suggesting a mere simple tax cut that affects those at the highest level. I'm suggesting we need to look at the overall degree of progressivity that you find in the effective tax rates, up and down the income distribution. And think about just how progressive we think it's appropriate to make that. But the current degree of progressivity is very substantial and deserves some consideration. []

SENATOR BURLING: How does that degree compare with other states? Do you know?
[]

JOHN ANDERSON: Well, I mean, we would have to get effective tax rates to compare. I mean, there are a number of Midwestern states that have so called flat rate taxes; it appears to be a flat rate tax. Illinois, for example, has a flat rate tax; Michigan has a flat rate tax. But, of course, when you bring into account the exemptions, deductions, and credits, especially those that have a circuit breaker property tax relief, they can have a much higher degree of progressivity as a result. So we would have to collect effective tax rates to see. But my impression is that this degree of progressivity is rather high in relation to especially those that have flat rate taxes, or rate structures with perhaps three rates that are not so highly progressive with the deductions and exemptions as well. But when you're moving from the bottom 70 percent up to the top, and you've got effectively two and a half times multiplication in the effective tax rate, you've got a very high degree of progressivity. []

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SENATOR BURLING: Remind me or help me remember, do we index AMT, Alternative Minimum Tax? Is that indexed? []

JOHN ANDERSON: Well,... []

DOUG EWALD: No. []

SENATOR BURLING: No? []

JOHN ANDERSON: The feds are changing at an ad hoc basis each year. []

DOUG EWALD: Right. In Nebraska the AMT is flat 29.6 percent of the federal AMT we pay. []

JOHN ANDERSON: Yeah. And the federal AMT is not indexed, but it is effectively being changed year to year on an ad hoc basis. []

SENATOR BURLING: Did your subcommittee or anybody talk about AMT and it's... []

JOHN ANDERSON: We didn't talk much about the AMT in the subcommittee, no, no. I think, my own view is that there's likely to be some change in the federal AMT within the next couple years. Exactly what, we could speculate on. But I don't think the current law, with regard to the AMT, at the federal level is sustainable. []

DOUG EWALD: You are right, it's never been indexed, it's up and down year to year. []

JOHN ANDERSON: Yeah, but the number of taxpayers subject to the federal AMT will rise exponentially over the next few years. And, politically, that just can't happen. []

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DOUG EWALD: And (inaudible) it's going to bring in about \$10 trillion of revenue over the next, I don't know how many years. And, I guess personally, AMT at the state level is a double whammy, because it's on your state income tax deductions. Your state income property taxes that get you there, that's what forces you into AMT at the federal level. So we're going to turn around and ding you at the state level on top of that for your...what you pay in state taxes. So I guess, I view the AMT, especially at the state level, as highly regressive because we're dinging people on their property taxes, their state income tax they pay to Nebraska. []

JOHN ANDERSON: Yeah. One of the first things you lose with the federal AMT is the deductibility of your state and local taxes. And that's the biggest factor involved for most taxpayers who are first hit by the AMT at the federal level. []

SENATOR BURLING: Well, that's why I asked the question how AMT fit in with your progressivity report, if there was any...if that made it better, or worse, or... []

JOHN ANDERSON: Well, we didn't separate that out and look at it. I mean, these effective tax rate numbers are the (inaudible)... []

ROBERT McMANUS: Yeah, this report is the tax burden study that was just completed by the Department of Revenue, a couple months ago. We could ask them. I haven't come across any comparison with other states on this issue like this. It would be nice to have a graph like this on other states, but I don't know where to find it. []

MILO MUMGAARD: We (inaudible). []

ROBERT McMANUS: Yeah. (Inaudible) other states. []

_____ : (Inaudible) effective tax rates rather than nominal rates. Yeah. []

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MILO MUMGAARD: Right. And there is not many states that have AMT at the state level. []

DOUG EWALD: It would be interesting further to lay that chart on top of the other charts (inaudible) that shows the effective tax rates under all tax, you know, the full tax burden, and to show how that plays out (inaudible) income distribution, because (inaudible). I mean it's one thing to have a curve, like the hockey stick curve that you've got there. Even though the taxpayers in the bottom end (inaudible) or 20 percent, whatever it is, which is (inaudible) certainly under the income tax not paying or if they're paying it's very little because of their roughly amount of taxable income and also they are getting certain refunds, childcare tax credits or (inaudible). They're paying such a high level of their income in sales tax and property tax that the ultimate effect of the tax rate is sort of the reverse of this here. So what you have as taxpayers, you have sort of two different pictures. You have (inaudible) income tax rate, we have a progressive income tax, certainly, and people on the bottom of the scale do not pay as much in (inaudible) tax rate. But as for an overall tax rate they pay certainly much higher rates than people (inaudible). []

_____: And that chart is available, and I can bring that to the next meeting. []

GEORGE KILPATRICK: Citizens for Tax Justice used to do this every once in a while. They have not for a number of years. []

MILO MUMGAARD: It's kind of like their bread and butter. []

GEORGE KILPATRICK: Well, it used to be. []

SENATOR BURLING: Any comments on John's report? []

ROBERT McMANUS: So what I propose, once again, is that I could draft up a

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(inaudible) recommendation, what John just described, for consideration at the next meeting. []

SENATOR BURLING: Okay. []

MATT JEDLICKA: I have a question. John, this one, how do we interpret this to where...I mean, you guys, I don't know if your committee studied this anymore. But it shows us that overall we are in line, other than at the (inaudible). []

JOHN ANDERSON: So this is from the D.C. tax burden study? []

MATT JEDLICKA: Yeah. At this \$50,000 income level we jump up a little bit. But other than that, we are consistent the whole way through. []

JOHN ANDERSON: Well, that takes all state and local taxes and puts them all together. We were looking only at the income tax piece of it. So keep in mind this is all state and local taxes, and it's only for Omaha. The D.C. study only does this for the largest city in each of the 50 states. So it's Omaha specific, and it includes all state and local taxes. And so we didn't look at it in detail... []

MATT JEDLICKA: Yeah. []

JOHN ANDERSON: ...because it didn't pertain precisely to the personal income tax, and it didn't represent the whole state. []

MATT JEDLICKA: That's my (inaudible). I was looking at this income level. I was thinking it was income. (Inaudible), never mind. []

SENATOR BURLING: Okay. []

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JOHN ANDERSON: It's a good study, but it really...you've got to be careful when you look at that study, because it's being done for the largest city in each of the states. And they're not necessarily representative of the entire state. []

ROBERT McMANUS: Okay. The last two things that we had were at the last meeting of the commission, the commission voted to reach conclusions on the tax administration paper and the corporate income tax paper. And (inaudible) those conclusions, they're very brief. So looking at the tax administration paper, once again we concluded that based on the information we received at our commission hearing that Nebraska's existing system is fair, and a generally fair and impartial process. And with some minor modifications we could improve the process to what the committee on state taxation would give an A grade, instead of a B grade. And those three bullets, they have some typos. But I'm just going to read those bullets. Extend the 30-day period for protesting sales and use tax assessment to provide ample time for appeal. They recommended 60 days. We just put in the recommendation just to expand. Change the date for filing state income tax returns to at least 30 days after the date for filing the federal tax return. And finally, take steps to insulate the administration hearing officer from the appearance of influence by the Department of Revenue. This could be accomplished by retaining an independent third party to conduct the administrative hearings, or by moving the hearing officer to a neutral state office which was separate from the Department of Revenue. []

SENATOR BURLING: I asked Bob to review these recommendations that we did last meeting, to refresh the memory of those of us who were there and bring it to the attention of those who weren't there. This was sent to you. This will be in our final report, unless there is suggested changes made today or at our next meeting, next month. But that's what we did last month on that particular issue. Any questions or comments on that? Okay. []

ROBERT McMANUS: Okay, then secondly, on the corporate income tax, we concluded at the last meeting that in going back to the 1988 Syracuse study, they recommended

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(inaudible) into a single factor sales formula for local tax. And in '88 the state was in transition, moving from a (inaudible) formula to a single (inaudible) formula, which was finally put in place in '91. And the Legislature did not follow that recommendation. But in the ensuing 20 years, what we've seen is that fewer and fewer states are using the three factor formula, and more and more states are adopting the single factor formula, and every year more states are considering it, so that it's almost...if a neighboring state has single factor sales formula, you almost economically have to also have it to keep flight of corporations across the border. And so once again, this is brief. But I'll just read the conclusions that we reached. The commission concludes of all the utilization of the single factor sales formula is still subject to the criticisms which contained in the Syracuse study and should be retained due to the significant shift in the use of the (inaudible) factor sales formula among the states in the 20 years since the Syracuse study. In 1988, only Iowa applied the single factor sales formula. Today, more states use the single factor sales formula than the traditional three factor formula. And in recent years, more and more state legislatures are considering adopting it in order to remain competitive with other states. In addition, the commission recommends that the Legislature review the corporate income tax...I'll stop here. The second thing that we did last time was had a presentation on the incentives that the state is employing right now to attract business to the state. And those have been incorporated into the paper (inaudible). And we concluded, in addition the commission recommends that the Legislature review the corporate income tax and its role as a vehicle for delivering tax incentives for business making new investment and creating new jobs in the state at the time the Legislature next reviews the business incentive programs. As part of that review, the Legislature should examine the backstop issue and determine whether there is any way...there are any ways in which the individual income tax could be protected if the corporate income tax were modified or repealed and its role as a backstop was limited. []

SENATOR BURLING: Any questions or corrections on that? I guess not. []

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ROBERT McMANUS: What I plan to do for the next time we meet is to meld all these papers together into a single document for the first time with (inaudible) conclusions that we talked about today. So that at the next meeting we will have a single document to review and, hopefully, to take votes on. []

SENATOR BURLING: Anything else anybody has today? Seems like today is just like the last time. After almost three hours well we kind of start to get kind of like this, and (laugh) when we do that, we just as well quit because we're not going to accomplish very much. I said at 1:30, let's get this over with. Too nice outside to be inside today. But we've had a good meeting. And I think it's encouraging to see us start to kind of finally come down maybe to some recommendations. So appreciate your attendance and your work. And I hope you'll make it a priority to be here October 19th at 9:00 a.m. in the morning, because October is the time when we really have to make some final decisions to enable our facilitator to get a final draft prepared for our November meeting. So next meeting will be very important. []

_____: October 19? []

SENATOR BURLING: October 19 at 9:00 a.m. in the morning. []

COMMITTEE CLERK: It's October 12, yeah, it's the 12th. []

SENATOR BURLING: Oh, I thought it said 19th online, and I didn't look at my calendar. []

COMMITTEE CLERK: Yeah, it's the 12th. []

SENATOR BURLING: Thank you for correcting me. I saw it written here somewhere. Anyway, thank you. October 12 at 9:00 a.m. This commission doesn't sunset until December 31, I think. So I guess, we could meet after that, but our final

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recommendation is due November 15. So our next meeting will be before then. We'll set the November meeting, and we'll e-mail all of you, so you can put it on your calendar. But October 12 at 9:00 a.m. Okay, thank you. Meeting adjourned. []