

NEBRASKA INCOME TAX

History of the Individual Income Tax

- Where have we been
- Why did we change
- Where are we now

Impact of Federal Decisions and State Decisions on the Base

NEBRASKA INDIVIDUAL INCOME TAX

Implemented in 1968

➤ Nebraska Income Tax Liability

= % of Federal Liability before credits

➤ 19% last effective year (1986)

➤ Major Change – 1987 LB773

➤ “Decoupled” from % of Federal Liability

➤ Impetus for change - Federal Tax Reform Act
of 1986

NEBRASKA INDIVIDUAL INCOME TAX

- Federal changes would have resulted in significant revenue loss or significant increase in rate
- “Coupled” to Federal Adjusted Gross Income (AGI)
 - Gives the state control over “Below-the-line” adjustments
 - “Above-the-line” adjustments still a federal decision
- Nebraska one of 30 states and D.C. that use AGI as starting point

FEDERAL DEFINITION OF INCOME

What's Included:

- Wages, salaries, tips, etc.
- Taxable Interest
- Ordinary Dividends
- Taxable refunds, credits, or offsets of state and local income taxes
- Alimony received
- Business income (or loss)

FEDERAL DEFINITION OF INCOME

- Capital gain (or loss)
- Other gains (or losses)
- Taxable IRA distributions
- Taxable Pensions and annuities
- Rental real estate, royalties, partnerships, S corporations, trusts, etc.
- Farm income (or loss)

FEDERAL DEFINITION OF INCOME

- Unemployment compensation
- Taxable social security income
- Other income

= FEDERAL GROSS INCOME

- Exclusions – Items that never go into the base
- Deductions – Reduce taxable income
- Credits – Offset tax liability

FEDERAL DEFINITION OF INCOME

What is **excluded** from federal gross income?

➤ Employer-sponsored health insurance \$248B*

*Single largest federal individual income tax expenditure = 1.5% of federal GDP

➤ Net pension contributions and earnings \$137B

➤ Capital gains assets transferred at death \$43B

➤ % of Social Security and RR Retirement \$33B

Total \$461B

(Source: CBO 2013 estimates)

“ABOVE THE LINE” REDUCTIONS

➤ REDUCTIONS OF GROSS INCOME

- Educator expenses

- Certain business expenses

- Health savings account deductions

 - 2013 Expenditure Estimate \$1.88B

- Moving expenses

- Deductible portion of self-employment tax

“ABOVE THE LINE” REDUCTIONS

- Self-employed SEP, SIMPLE, qualified plans
 - 2013 Expenditure Estimate \$15.03B
- Self-employed health insurance deduction
- Penalty on early withdrawal of savings
- Alimony paid
- IRA deduction
 - 2013 Expenditure Estimate \$12.84B

“ABOVE THE LINE” REDUCTIONS

- Student loan interest deductions

 - 2013 Expenditure Estimate \$1.4B

- Tuition and fees

- Domestic production activities deduction

= FEDERAL ADJUSTED GROSS INCOME

NEBRASKA INDIVIDUAL INCOME TAX

Who must file?

- Nebraska resident who:
 - Is required to file a federal return reporting a federal liability; or
 - Has \$5,000 or more of Nebraska adjustments to federal AGI including non-Nebraska state or local bond interest exempt from federal tax.

NEBRASKA INDIVIDUAL INCOME TAX

- Nonresident who:
 - Has income derived from or connected with Nebraska sources

Resident – Individual who is domiciled in Nebraska or who maintained a permanent place of abode and resided in Nebraska for six month or more during the calendar year.

NEBRASKA INDIVIDUAL INCOME TAX

Nonresident – An individual who is domiciled for the entire year in a state other than Nebraska and did not reside in Nebraska for more than six months during the calendar year.

Partial-Year Resident – An individual who either begins or ends domicile in Nebraska during the year or who resides in Nebraska for more than six months during the year.

“BELOW-THE-LINE” Adjustments

Line 5 Nebraska Return – Federal AGI

Minus Nebraska Standard Deduction

OR

Minus Line 7 – Federal Itemized Deductions

Plus State And Local Taxes Deducted On
Federal Return

Line 10 – Minus Greater Of The Two Calculations

=NEBRASKA INCOME BEFORE ADJUSTMENTS

“BELOW-THE-LINE” Adjustments

Nebraska Adjustments INCREASING AGI

- Interest Income From All State And Local
- Obligations Exempt From Federal Tax
- Financial Institution Tax Credit Claimed
- Long-term Care Savings Plan Recapture
- Nebraska College Savings Recapture
- Other Adjustments

“BELOW-THE-LINE” Adjustments

Nebraska Adjustments DECREASING AGI

- State Income Tax Refund Deduction
- Exempt U.S. Government Obligations
- Federally Taxable Tier I And Tier II Railroad Retirement Benefits
- Special Capital Gains Exclusion
- Nebraska College Savings Contributions

“BELOW-THE-LINE” Adjustments

Nebraska Adjustments **DECREASING** AGI (Cont.)

- Nebraska Long-term Care Savings Contributions
- Other Adjustments

= NEBRASKA TAXABLE INCOME BEFORE CREDITS

Two types of credits: Nonrefundable-may reduce liability to zero, but not below.

Refundable-May reduce liability to zero and excess is refunded

“BELOW-THE-LINE” Adjustments

NON-REFUNDABLE CREDITS

- Credit For Elderly And Disabled
- Credit For Child/dependent Care
- Credit For Tax Paid To Another State
- Community Development Credit
- Financial Institution Credit
- Nebraska Personal Exemption Credit

“BELOW-THE-LINE” Adjustments

NON-REFUNDABLE CREDITS (CONT.)

- Biodiesel Facility Investment Credit
- Nebraska Incentive Programs

REFUNDABLE CREDITS

- Nebraska Incentive Programs
- Credit For Child/dependent Care
- Beginning Farmer Credit

“BELOW-THE-LINE” Adjustments

REFUNDABLE CREDITS (Cont.)

- Earned Income Tax Credit (“EITC”)
- Angel Investment Credit

=NEBRASKA INCOME TAX LIABILITY/REFUND

NEBRASKA INCOME TAX

Largest Nebraska Tax Expenditures

Itemized Deductions	\$252,000,000
Standard Deduction	\$187,700,000
Personal Exemption Credit	\$171,000,000
Interest/dividends U.S. Obligations	\$45,300,000
Both individual and corporate	
Non-Nebraska S Corp Income/Loss	\$45,000,000
Foreign Income Above Fed Max	\$39,100,000
Corporate only	

Nebraska Income Tax

Largest Nebraska Tax Expenditures (Cont.)

Credit for Tax Paid to Another State	\$39,000,000
Earned Income Credit	\$29,000,000
Net Operating Losses	\$27,100,000
Special Capital Gains Exclusion	\$26,000,000
<u>Total</u>	<u>\$861,200,000</u>

(Source: Nebraska Department of Revenue 2012 Tax Expenditure Report)

SINGLE TAXPAYERS

If taxable income

is over – But not over – The Nebraska tax is:
tax is:

\$ 0	\$ 2,400	2.56% taxable income
2,400	17,500	\$ 61.44 + 3.57% of the excess over \$2,400
17,500	27,000	\$ 600.51 + 5.12% of the excess over \$17,500
27,000	—	\$ 1,086.91 + 6.84% of the excess over \$27,000

MARRIED FILING JOINT

If taxable income

is over – But not over – The Nebraska

\$ 0	\$ 4,800	2.56% taxable income
4,800	35,000	\$122.88 + 3.57% of the excess over \$4,800
35,000	54,000	1,201.02 + 5.12% of the excess over \$35,000
54,000	—	\$ 2,173.82 + 6.84% of the excess over \$54,000

MARRIED FILING SEPARATE

If taxable income

is over – But not over – The Nebraska tax is:
tax is:

\$ 0	\$ 2,400	2.56% taxable income
2,400	17,500	\$ 61.44 + 3.57% of the excess over \$2,400
17,500	27,000	\$ 600.51 + 5.12% of the excess over \$17,500
27,000	—	\$ 1,086.91 + 6.84% of the excess over \$27,000

HEAD OF HOUSEHOLD

If taxable income

is over – But not over – The Nebraska

\$ 0	\$ 4,500	2.56% taxable income
4,500	28,000	\$115.20 + 3.57% of the excess over \$4,500
28,000	40,000	\$954.15 + 5.12% of the excess over \$28,000
40,000	—	\$ 1,568.55 + 6.84% of the excess over \$40,000

NEBRASKA INDIVIDUAL INCOME TAX

If taxpayer AGI is more than \$173,650; or
\$86,825 for married filing separate:

- Nebraska “recaptures” the preferential tax rates of the four brackets.
- Recapture phase out AGI of \$713,650 for married filing joint
- Recapture phase out AGI of \$443,650 for single filers.

NEBRASKA CORPORATE INCOME TAX

Nebraska Form 1120N

Use Federal Taxable Income as starting point

- Only C Corporations file
- S Corporations file informational return as do other types of Pass-Through or Flow-Through entities
- Schedule K-1: Income/Loss flow-through to shareholders, partners or members proportionately and are reported on individual income tax return

FEDERAL DEFINITION OF INCOME

What's Included:

- Gross receipts or sales, minus returns, allowances and cost of goods sold
- Dividends
- Interest
- Gross Rents and Royalties
- Capital gain/loss
- Other Income

FEDERAL DEFINITION OF INCOME

What's Excluded:

➤ Officer Compensation	\$1.389B
➤ Salaries and Wages	\$13.834B
➤ Repairs and Maintenance	\$1.536B
➤ Bad Debts	\$0.619B
➤ Rents	
➤ Taxes and Licenses	\$2.706B

FEDERAL DEFINITION OF INCOME

What's Excluded (Cont.)

➤ Interest	\$4.365B
➤ Charitable Contributions	\$0.114B
➤ Depreciation	\$3.599B
➤ Depletion	\$0.217B
➤ Advertising	
➤ Pension, Profit-Sharing and other Plans	\$0.777B

FEDERAL DEFINITION OF INCOME

➤ Employee Benefit Plans	\$1.953B
➤ Domestic Production Deduction	
➤ Other Deductions	\$31.527B
➤ Net Operating Loss	\$0.635B
➤ Special Deductions	\$0.496B
= <u>Federal Taxable Income</u>	

2005 Nebraska Total \$63.068B

NEBRASKA CORPORATE INCOME TAX

Nebraska starts with FTI

- Federal net operating losses, federal capital carryover losses and other adjustments are added back
- Other Adjustments
 - State and local government interest and dividend income
 - Qualified federal interest deduction
 - Foreign dividends, gross-up or special foreign tax credit

NEBRASKA CORPORATE INCOME TAX

- Income not subject to apportionment
 - Expenses, including interest, related to above must be deducted out
 - Nebraska College Savings Plan
 - Other Adjustments
- = Adjusted Federal Taxable Income
- Nebraska net operating losses and capital loss carryovers are then deducted
- = Net Nebraska Taxable Income x Rate
- = Nebraska Tax Before Credits

NEBRASKA CORPORATE INCOME TAX

Credits:

- Insurance Premiums Tax Credit
- CDAA Credit
- Non-refundable Nebraska Incentive Credits
- Refundable Nebraska Incentive Credits
- Beginning Farmer Credit

= Net Nebraska Tax

First \$100,000 taxed at 5.58%, excess at 7.81%

NEBRASKA CORPORATE INCOME TAX

Multistate Apportionment

- Corporations subject to tax within and without Nebraska are required to apportion their income using the single-factor sales formula unless the Tax Commissioner has previously approved an alternative method.
- Corporation subject to tax solely in Nebraska may not apportion their income.

NEBRASKA CORPORATE INCOME TAX

Multistate Apportionment (Cont.)

Three general apportionment formulas:

- Traditional 3-factor
 - Property, Payroll and Sales – 10 states
- Double or triple weighted Sales – 17 states
- Single factor Sales – 20 states including Nebraska
- States with no tax – Nevada, South Dakota, Washington and Wyoming

NEBRASKA CORPORATE INCOME TAX

Nebraska Apportionment

EVERYWHERE	NEBRASKA
Net receipts	Net Receipts
	Deliveries from outside state
	Deliveries within the state
	Deliveries to US Gov't.
Interest, dividends, royalties	Interest, dividends, royalties
Gross rents	Gross rents
Net gain on sales of real, intangible/tangible property	Net gain on sales of real, intangible/tangible property
Other income	Other income
Total Receipts	Total Receipts

NEBRASKA CORPORATE INCOME TAX

Nebraska Apportionment (Cont.)

Total Nebraska Receipts

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Total Everywhere Receipts

= Nebraska Apportionment Factor

x Nebraska Taxable Income

= Net Taxable Income

X Rate = Tax Due/Refund Due

NEBRASKA CORPORATE INCOME TAX

Combined v. Separate Reporting

- Unitary or “Combined” Reporting
 - Generally means all corporations included in the federal consolidated return combine their income or losses on one return
- Separate Reporting
 - Means each corporation files its own return with its own income and losses
 - Generally more susceptible to manipulation

NEBRASKA CORPORATE INCOME TAX

- 26 states including Nebraska now use some form of combined or “consolidated” reporting
- 19 states still utilize separate reporting
- 12 states proposed legislation in 2010-2012 to adopt combined/consolidated reporting
 - Including Arkansas, Indiana, Iowa, Missouri, Michigan, and Oklahoma