Principles of a Privilege-Free Tax System, with Applications to the State of Nebraska

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Abstract

Tax codes in US states contain a wide variety of special privileges for specific industries, firms, individuals, and types of economic transactions. This paper outlines the main types of privileges in state sales, property, and income taxes. A detailed analysis of the tax privileges in the state of Nebraska provides information for a state that is in the process of potentially reforming its tax code. In Nebraska the total forgone revenue due to tax privileges amounts to just over $2 billion, compared with roughly $7.2 billion in total revenue collected by the relevant taxes. Eliminating these privileges and simultaneously lowering tax rates could save an average Nebraskan family more than $3,200 dollars if the benefits of tax reform are evenly distributed, with no reduction in government services.

JEL codes: H20, D70, H24, H25, D72

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Special privileges are a pervasive feature of modern governments. Privileges found in the federal and state tax codes in the United States are a prominent example. Particular firms and industries receive myriad benefits from all levels of government, such as lower tax rates (or no tax at all) on the goods they sell. Individuals also receive a wide variety of tax privileges, often based on activities they engage in, such as purchasing a home with a mortgage or paying college tuition. These privileges are so widespread that they require higher tax rates on the remaining economic activity that does not receive these privileges. In addition, these privileges are so common that many Americans will simultaneously lament the growth of "special interests" and "loopholes" while claiming that their own privileges are not really privileges, but sound public policy.

In *The Pathology of Privilege*, Matthew Mitchell identifies nine major types of privileges in the United States today, from monopolies and regulatory privileges to subsidies and bailouts.[1] Mitchell shows how government-granted privilege "misdirects resources, impedes genuine economic progress, breeds corruption, and undermines the legitimacy of both the government and the private sector."[2] The tax code is one area in which such privileges manifest themselves. Individuals and firms engaging in certain activities receive lower tax rates than the general public, an implicit subsidy to the favored group.

Governments do not randomly hand out these privileges. Rather, interested firms, industries, and individual taxpayers (or their representatives) actively lobby for them.

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[1] Matthew Mitchell, *The Pathology of Privilege: The Economic Consequences of Government Favoritism* (Arlington, VA: Mercatus Center at George Mason University, 2012), http://mercatus.org/publication/pathology-privilege-economic-consequences-government-favoritism.

[2] Ibid., 3–4.

Economists often refer to the process of lobbying for special favors as "rent-seeking." However, "rent" in this context is both potentially confusing (are we talking about landlords?) and technically incorrect (entrepreneurship is also the seeking of economic rents). Thus, economist David Henderson has suggested the phrase "privilege-seeking" as a substitute for "rent-seeking."[3] Gordon Tullock, one of the originators of the concept of rent-seeking (though not of the phrase itself), has also used the term "privilege" alongside the standard "rent" in rent-seeking, for example in his monograph *The Economics of Special Privilege and Rent Seeking*.[4]

Throughout this paper, I use the term "privilege" in the same way Mitchell uses it, which Henderson also suggested and which some of Tullock's work implicitly suggested. More precisely, I define a tax privilege as a provision in law that lowers an individual's or corporation's tax burden compared with that of others of the same income level. If a tax burden is lower because of the industry a firm operates in, because of how an individual behaves or spends money, or as a means of attracting firms to a state, I label these benefits as tax privileges.

What would a privilege-free tax code look like? The basic principle of a privilege-free tax system is simple: no individual or business should be treated differently for tax purposes from any other similarly situated individual or business. More specifically, I use the public finance principle of horizontal equity as a means of defining privileges in the tax code. Horizontal equity requires that individuals with a similar ability to pay be taxed the same amount. This principle implies that there should be no exemptions for anyone from any type of tax, whether income, consumption, or property tax. There may be some tax exemptions that make sense from an economic point of view, as I will discuss throughout the paper, but even exemptions that fit

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[3] David Henderson, "Rent Seeking," in *The Concise Encyclopedia of Economics*, ed. David Henderson (Indianapolis: Liberty Fund, 2008).
[4] Gordon Tullock, *The Economics of Special Privilege and Rent Seeking* (Boston: Kluwer Academic Publishers, 1989).

standard public finance theory should still be viewed with caution, as advocates of particular privileges often use the language of economics (e.g., public goods) even when these privileges do not meet the technical economic criteria. Public choice theory adds another layer of caution, as special interests often capture policies that originally had a justified economic purpose.

The first half of this paper discusses in general terms what a privilege-free tax code would look like, with specific emphasis on the major types of tax levied by US states: sales taxes, property taxes, and income taxes (both individual and corporate). Based on available data from various states, I estimate that tax privileges are around $400 billion annually at the state level, or around 40 percent of the roughly $1 trillion in federal tax expenditures. Despite this, these state-level privileges have received much less attention than federal tax privileges. This paper will carefully outline which types of exemptions make sense from a strict economic perspective and which are pure examples of economic privilege despite the justifications often given. A guiding principle when assessing tax exemptions in this paper is, Does this tax exemption benefit a *specific* industry, firm, or type of individual? If so, it is likely to be an example of pure economic privilege. This paper will recommend eliminating these types of privilege and will include "second-best" solutions when complete removal may not be politically feasible.

The second half of this paper applies the principles to Nebraska, focusing on income, sales, and property taxes. In general, Nebraska has a fairly privilege-free tax system, though the tax rates on income are high compared with some regional neighbors (neither South Dakota nor Wyoming have an income tax at all). One general suggestion is that the additional revenues from the removal of tax privileges should be used to lower tax rates in general, making the system less prone to privileges while not raising the overall tax burden, and improving economic growth.

Tax Privileges, More Precisely Defined

Since the term "tax privilege" is uncommon, I will distinguish it from the related term "tax expenditure." However, the use of the term "privilege" to describe government favors is quite common both in the colloquial use of "special privileges" and the academic use by Mitchell, Henderson, and Tullock noted above.

Used in most federal government publications since the 1970s, the term "tax expenditure" is now used in many state-level publications as well. Tax expenditures comprise any credits, deductions, or exemptions that reduce revenues from a defined base. Initially applied primarily to the federal income tax, many states now use the term to describe similar features of all types of taxes. The term "tax expenditure" is intended to convey that tax breaks are essentially equivalent to direct government spending. For example, the government could write homeowners a check each year to subsidize home purchases, or it could give homeowners the opportunity to lower their tax burden for engaging in the same activity. Either way, the taxpayer has a larger disposable income, and the government has fewer funds. This is, in a sense, spending through the tax code. Tax expenditures as currently defined are discussed further below, but in this section I offer a brief discussion of the term itself, and how tax privileges are overlapping yet different.

Several objections have been raised to the idea of tax expenditures, which Joshua Hall well summarized in writing for the Joint Economic Committee.[5] Hall discusses how the current use of the tax expenditure concept treats savings differently from wage income, in that savings can (and should, under a strict definition of tax expenditures) be taxed multiple times. This tax treatment of savings biases spending away from savings and toward consumption, showing an important way in which tax expenditures are different from tax privileges, as I define them here.

[5] Joshua Hall, "Tax Expenditures: A Review and Analysis," Joint Economic Committee, United States Congress, August 1999.

A privilege-free tax code would not treat savings and consumption differently, and thus any apparent tax breaks for savings that are designed to reduce this bias would not be counted as tax privileges, though they are currently counted as tax expenditures. And the inclusion of these tax breaks for savings is no minor matter: at the time Hall wrote his analysis (and still today), fully nine of the 25 largest tax expenditures were "aimed at mitigating or eliminating the multiple taxation of income."[6] Finally, and at a more fundamental level, Hall argues that the term "tax expenditure" itself has a normative implication that all income belongs to the government, and anything it does not tax is therefore a form of spending.

As mentioned above, horizontal equity is the primary determination for whether a particular provision in a tax code constitutes economic privilege. Horizontal equity is a principle of public finance that states that individuals with similar ability to pay should pay the same amount in taxes.[7] It is important to note at the outset several provisions in the tax code that would not count as privileges. Any provisions that establish a "zero bracket," an amount of income that is untaxed, do not constitute privilege since they are available to everyone with that income level. The most common examples of such provisions are standard deductions and personal exemptions in the income tax code. Also, antipoverty provisions built into the tax code, such as the earned income tax credit, would not be examples of privilege since they are available to anyone at that income level (and with that family size), rather than only to those in certain industries or engaged in specific activities. However, once again, they are defined as tax expenditures under current practice, showing the difference between that term and my concept of tax privileges.

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[6] Ibid., 5.
[7] Jean-Yves Duclos, "Horizontal and Vertical Equity," in *The New Palgrave Dictionary of Economics*, 2nd ed., ed. Steven N. Durlauf and Lawrence E. Blume (Basingstoke, UK: Palgrave Macmillan, 2008).

A final difference between tax privileges and tax expenditures is that the term "tax expenditures" does not fit as well to the types of privileges individual states give to various taxes compared with the types of privileges the federal government gives. Specifically, for the largest federal tax expenditures (see table 3, page 27) there is usually a corresponding federal agency that also spends resources on this activity. For example, some of the largest tax expenditures at the federal level are for health insurance, home mortgage interest, and retirement contributions. The federal government has corresponding departments to these types of spending: Health and Human Services, Housing and Urban Development, and Social Security. But some of the most common exemptions to state sales taxes (see table 2, page 18) are radio and TV advertising, travel agents, dentists, and veterinarians. Neither the federal government nor many states have departments that spend money on these services (though they do often regulate them). A cursory Internet search suggests that no state has a Department of Laundry, though many states exempt self-service laundry from the sales tax.

1. Principles of a Privilege-Free Tax System

Part 1 of this paper uses the ideas of economic privilege and horizontal equity to examine the three primary sources of revenue for US state governments: sales taxes, property taxes, and income taxes. I list and discuss some of the common types of tax privileges granted by US states through these three taxes. I also discuss common rationales for these exemptions, and I note where certain privileges may be justified by economic theory. For those not justified by economic theory, I also offer some "second-best" policy alternatives to fully eliminating the privileges if there are noneconomic reasons for keeping the privileges that have public support.

From the perspective of the favored group, tax privileges have several main advantages over other forms of privilege. Once put in place, they are unlikely to be repealed, especially when the tax code is as complex as the United States'. The public in general is typically ignorant of particular tax privileges since each is such a small part of the code. And even if people knew about particular privileges, it is typically not in their interest to fight for the repeal of these privileges because of the logic of concentrated benefits and dispersed costs. Industries that benefit from the privileges each stand to lose millions of dollars, while a typical taxpayer only pays a few dollars more in taxes for minor tax privileges. Unlike naked grants of power such as monopoly, regulation, or other policies that restrict competition and may be more obvious to consumers, the tax code often works in ways that are imperceptible to even careful observers.

Using the consequences Mitchell identifies, tax privileges impede economic progress, encourage rent-seeking and cronyism, and can undermine the legitimacy of the economic system when citizens view these privileges as unfair or unjust. While tax privileges have all the indirect effects that Mitchell identifies for government privileges, they also have a more direct consequence: in order to maintain government revenue, for every dollar lost through individual privileges, a dollar must be raised by higher taxes on the general public.[8] For this reason alone, tax privileges should be completely removed from any tax code unless there are sound public-policy purposes for the lower tax rates (e.g., encouraging activities with clear and large positive externalities). It is important to define "sound public-policy purposes" carefully, since most tax privileges have eloquent defenders. By sound public policy, I mean a reason that is clearly within the traditional public finance definition of the role of the state. Moreover, it is important to be mindful of public choice concerns when analyzing tax policy. Even if there is a sound public-

[8] An exception may be if the privilege encourages a business to locate within a particular state, thus increasing economic activity above what it otherwise would have been. This possibility will be discussed later, but it is worth noting here that this competition between states is essentially a zero-sum game.

policy purpose for a given privilege, rent-seeking behavior may push policy away from the ideal public finance functions.

At least 44 states plus Washington, DC, produce some sort of report with information on tax privileges.[9] While the methods used and the frequency of publication varies widely across states,[10] this information gives a sense of the magnitude of these tax privileges and their nature (e.g., which taxes are involved). A relevant number for comparison is the federal "tax expenditures," as they are frequently called in official government documents. The latest estimates from the Office of Management and Budget are that total federal tax expenditures for the individual and corporate income tax have exceeded $1 trillion in recent years: $1.08 trillion in fiscal year (FY) 2012, $1.13 trillion in FY 2013, and a projected $1.18 trillion in FY 2014.[11] For a rough comparison, Appendix 1 provides comparable estimates for 40 states that produce similar reports.[12] These 40 states represent roughly 90 percent of US GDP.[13] I identify $389.3 billion in tax privileges for these 40 states, or roughly $432.5 billion if the other 10 percent of GDP is similar to that of these states.[14] This sum of $432.5 billion is about 40 percent of the total of federal tax expenditures for FY 2012, my preferred year when looking at state data as it is the most recent year available in many state reports. Even if this 40 percent figure is not exact, it is clear that state tax expenditures are a major component of

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[9] For a list and links to many of the reports, see Institute on Taxation and Economic Policy, "Tax Expenditure Reports," http://www.itep.org/other_resources/state_tereport.php.
[10] Michael Leachman, Dylan Grundman, and Nicholas Johnson, "Promoting State Budget Accountability through Tax Expenditure Reporting," Center on Budget and Policy Priorities, Washington, DC, May 2011.
[11] Office of Management and Budget, "Analytical Perspectives: Budget of the United States Government, Fiscal Year 2014," table 16-1: "Estimates of Total Income Tax Expenditures for Fiscal Years 2012–2018."
[12] For four states there are no reports on tax expenditures that I am aware of. For another six states, estimates are available but not in a summary form that is easily accessible at this time.
[13] Author's calculations using Bureau of Economic Analysis data on state GDP for 2012.
[14] Although summing these figures is problematic for several reasons, including differences in data estimation methods, incomplete reporting of some taxes, and differing time periods, it may be useful in giving a very rough estimate. The aggregate figure also makes no adjustment for whether these privileges are justified, other than a balancing adjustment for states that give credits for taxes paid in other states or foreign countries.

tax privileges in the United States today, even though they receive much less attention than federal tax expenditures.

Neither the federal reports nor many state tax expenditure reports incorporate dynamic estimates of the magnitude of tax expenditures. By dynamic estimates, I mean the potential changes in economic activity when increasing or decreasing taxes (either rates or particular tax privileges). All the discussion of specific dollar amounts in this paper simply takes the figures in the tax expenditure reports as accurate. And while they probably are accurate in a static (short-term) sense, they are likely to be inaccurate over a longer time period. Specifically, if a tax privilege is removed without some offsetting change in policy (e.g., lowering income tax rates, as discussed below) this removal represents an increase in taxes on the affected parties. Thus, over time, economic activity may decrease if there is no corresponding policy to offset the removed privilege. I discuss one possibility, lower income tax rates, in a brief subsection below.

Lowering Marginal Income Tax Rates as the Best Solution

A general suggestion throughout the paper is that whenever particular exemptions are removed, some corresponding tax rate can and should be lowered to offset the increased overall tax burden. One assumption in most of the paper is that policymakers are interested in financing a given level of government spending with as minimal an economic burden as possible, rather than trying to maximize government tax revenues. More specifically, lowering income tax rates is generally the best candidate when closing a loophole or eliminating an exemption. A recent series of studies by the Organisation for Economic Co-operation and Development found that shifting taxes from income taxes (both personal and corporate) to consumption or property taxes increased GDP growth. Specifically, a shift of 1 percent of tax revenues away from income taxes increased GDP by between 0.25 percent and 1 percent.[15] While this paper is concerned primarily with economic privilege rather than economic efficiency, if tax rates are going to be lowered, it only makes sense to do so in a way that benefits society the most.

This point on the relationship between income tax rates and economic growth deserves some explanation, as popular and policy discussions treat the relationship as unknown or even the reverse (e.g., claims that the US economy did very well in the 1950s with top marginal tax rates greater than 90 percent). William McBride of the Tax Foundation surveys the recent literature on the relationship between income tax rates and growth, and he finds that the vast majority of peer-reviewed studies find a negative relationship (e.g., higher tax rates reduce growth).[16] Only three of the 26 papers McBride surveys find no statistically significant relationship, while none finds a positive relationship. The papers surveyed are published in the top economics journals, such as the *American Economic Review* and the *Quarterly Journal of Economics*. The papers cover tax rates in a wide variety of jurisdictions, including the US federal government, countries that are members of the Organisation for Economic Co-operation and Development, developing countries, and, most relevant to this paper, US state governments.[17]

McBride's paper has been criticized on several grounds by Chye-Ching Huang and Nathaniel Frentz of the Center on Budget and Policy Priorities, but the criticism most relevant to

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[15] Jens Matthias Arnold et al., "Tax Policy for Economic Recovery and Growth," *Economic Journal* 121 (2011): F59–F80.

[16] William McBride, "What Is the Evidence on Taxes and Growth?" Tax Foundation Special Report No. 207, Washington, DC, 2012.

[17] The papers on tax rates in US states surveyed by McBride all find a negative relationship. See Robert Reed, "The Robust Relationship between Taxes and U.S. State Income Growth," *National Tax Journal* 61 (2008): 57–80; N. Bania, J. A. Gray, and J. A. Stone, "Growth, Taxes, and Government Expenditures: Growth Hills for U.S. States," *National Tax Journal* 60 (2007): 193–204; Marc Tomljanovich, "The Role of State Fiscal Policy in State Economic Growth," *Contemporary Economic Policy* 22 (2004): 318–30; Howard Chernick, "Tax Progressivity and State Economic Performance," *Economic Development Quarterly* 11 (1997): 249–67; John Mullen and Martin Williams, "Marginal Tax Rates and State Economic Growth," *Regional Science and Urban Economics* 24 (1994): 687–705; and Jay Helms, "The Effect of State and Local Taxes on Economic Growth: A Time Series-Cross Section Approach," *Review of Economics and Statistics* 67 (1985): 574–82.

my paper relates to government spending.[18] Huang and Frentz point out that several of the papers in McBride's survey also suggest that the impact of taxes on growth depends on how the government spends the potential tax revenue. If the government spends the money on the programs that have positive externalities and a very high social return (e.g., education), higher taxes have the potential to increase growth in some simulations. While this theory may potentially be true, for public choice reasons I discuss below, governments are unlikely to always spend the resources on high-return investments. Instead, they may spend the additional tax revenue on other economic privileges, compounding the problem. If, on average, governments spend the marginal tax dollars on private goods rather than pure public goods, this part of Huang and Frentz's criticism breaks down.

Lowering tax rates may not always be a politically possible response to removing privileges, and thus throughout the paper I also present "second-best" policy solutions when lowering tax rates may not be optimal or politically feasible. But, in general, lowering tax rates is a simple, nonprivileged way of using the revenue gains from closing loopholes and eliminating exemptions, provided that the tax rate cuts do not disproportionately benefit a specific industry or group of individuals. While distributing the benefits of a tax cut perfectly equally to all citizens of a state is practically impossible (particularly when high-income earners already pay a majority of taxes), across-the-board cuts in tax rates are, in general, an efficient, nonprivileged reform.

Most of what follows in this paper is not dependent on lower income tax rates as the corollary to removing privileges. One could agree with my entire argument but believe that the

[18] Chye-Ching Huang and Nathaniel Frentz, "What *Really* Is the Evidence on Taxes and Growth? A Reply to the Tax Foundation," Center on Budget and Policy Priorities, Washington, DC, February 2014. McBride has also responded in a blog post titled "Empirical Evidence on Taxes and Growth: A Response to CBPP," *Tax Policy Blog*, Tax Foundation, February 21, 2014, http://taxfoundation.org/blog/empirical-evidence-taxes-and-growth-response-cbpp.

additional tax revenue should be used for other public-policy purposes. Other purposes could include lowering other tax rates, such as sales or property tax rates. Or they could include spending the revenue on other public goods, if the government has not yet fulfilled all its basic functions. I would urge caution to policymakers considering this last possibility, however. Most US states are already close to fully funding all the goods that economics defines as pure public goods (e.g., courts and police), plus partially funding many impure public goods (e.g., education) and even some private goods (e.g., roads). Thus, if the additional revenue is left to sit in the public treasury and allocated through the political process, there is the distinct possibility that it will be spent on some other form of privilege, such as direct subsidies to industries. If this is the result, then policymakers are merely trading one form of privilege for another.

Sales Taxes

Sales taxes are applied to final monetary transactions, typically calculated as a percentage of the value of the transaction. In many states, sales tax revenue is the largest source of tax revenue other than intergovernmental transfers.[19] Only five US states do not levy a general, statewide sales tax.[20] Many localities within states, such as cities and counties, also levy sales taxes. The primary form of economic privilege exercised through the sales tax is exemptions or lower tax rates for certain goods, industries, or transactions.

A completely neutral sales tax would tax all final consumer transactions at the same rate. No US state currently adheres to this practice perfectly, though some come closer than others. All states provide some exemptions to their general sales tax, and some of the exemptions are

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[19] US Census Bureau, *2011 Annual Surveys of State and Local Government Finance* (Washington, DC: US Census Bureau, July 2013).

[20] The states are Alaska, Delaware, Montana, New Hampshire, and Oregon, though Alaska and Montana do allow localities the option of establishing a sales tax.

quite large in terms of revenue forgone and number of transactions exempted. It is also worth noting that some goods are taxed at a higher rate than the general sales tax rate, for several reasons. The two most prominent categories are sin taxes, placed on goods such as tobacco and liquor that are regarded as immoral, and Pigouvian taxes, placed on goods that produce negative externalities (there is an overlap between these two categories as well). Another example is attempts to tax nonresidents at higher rates (e.g., hotel taxes). Such taxes are beyond the scope of this paper, but they are another notable departure from horizontal equity.[21]

Before discussing some of the more common exemptions to the sales tax, a brief discussion of one exemption that makes economic sense is in order. Under an ideal, privilege-free sales tax, only the final-consumer transactions would be taxed. Intermediate sales of goods, such as business-to-business transactions, should not be taxed. There are several sound reasons for not taxing business-to-business transactions, but it is most certainly not because businesses deserve any special treatment or tax favors. However, all states do tax some kinds of intermediate sales, though this practice varies widely across states.

Intermediate transactions should be exempt from taxation because industries have different structures of production in terms of the number of intermediate transactions that occur. Some industries may have only one intermediate level between the producer and the final consumer, where one firm produces the good from scratch and sells it to a retailer. Others may have several levels, such as the extraction of raw materials, refining of those materials, production of the actual goods, wholesalers, and eventually retailers. A tax on intermediate, business-to-business transactions will mean that the industry with more layers in its structure of

[21] For a discussion of sin taxes and their relationship to traditional Pigouvian taxes, see Adam J. Hoffer, William F. Shughart II, and Michael D. Thomas, "Sin Taxes: Size, Growth, and Creation of the Sindustry" (Working Paper No. 13-04, Mercatus Center at George Mason University, Arlington, VA, February 2013), http://mercatus.org/publication/sin-taxes-size-growth-and-creation-sindustry.

production will pay more in taxes. Levying sales taxes only on final-consumer purchases avoids this problem. The existence of taxes on intermediate transactions may encourage firms to vertically integrate beyond the point that is economically efficient. Under a value-added tax, used in many European countries, businesses generally receive a credit against sales taxes they are required to pay, mitigating the incentive for vertical integration. But under a general sales tax, the kind used in most US states, no such credit is available, and thus the possibility of vertical integration due to tax pyramiding is a real danger.

One major area of the economy that is often exempt from sales taxes is services purchased by consumers, in contrast to the purchase of physical goods. There is generally no sound economic reason for treating services differently from goods. Consumers ultimately purchase goods for the services that the good provides them, so the distinction is somewhat arbitrary from an economic perspective. For example, I purchase an ice cream cone because I want the services it provides me (e.g., alleviating hunger, tasting good) rather than because of a desire for the physical good itself. Moreover, as the economy becomes increasingly service-based, state sales tax revenues as a percentage of the economy will tend to decline, requiring higher taxes elsewhere to fund a given level of government spending. In the 1930s when many states began enacting sales taxes, services were just above 40 percent of personal consumption expenditures. Today, services are approaching 70 percent of personal consumption expenditures.[22]

The Federation of Tax Administrators regularly sends a survey to the 50 states and Washington, DC, on services that are exempt from sales taxes in their state, and the most recent data are from 2007. The survey asks states about 168 different categories of services and whether

[22] Author's calculations using US Department of Commerce, Bureau of Economic Analysis data on Personal Consumption Expenditures (account code DPCERC1) and the Services subcategory of PCE (account code DSERRC1).

they are taxed. There is a great deal of variation across states in terms of what services they tax. Hawaii, New Mexico, Washington, and South Dakota tax almost all the 168 services in the survey, while Massachusetts, Nevada, Virginia, Illinois, and Colorado tax fewer than 20 of these services. Tables 1 and 2 list the number of services that are taxed in each state and show selected services that are not taxed in a large number of states.

Table 1. Number of Services Taxed by State (out of 168 services)

State	# services taxed	State	# services taxed	State	# services taxed
Hawaii	160	Tennessee	67	Idaho	29
New Mexico	158	Minnesota	66	Rhode Island	29
Washington	158	Florida	63	Kentucky	28
South Dakota	146	Utah	58	Michigan	26
West Virginia	106	Wyoming	58	Missouri	26
Iowa	94	New York	57	North Dakota	26
Texas	83	Arizona	55	Maine	25
Connecticut	79	Louisiana	55	Indiana	24
Nebraska	77	Pennsylvania	55	California	21
Wisconsin	76	Maryland	39	Massachusetts	18
Kansas	74	Alabama	37	Nevada	18
New Jersey	74	Georgia	36	Virginia	18
Washington, DC	73	South Carolina	35	Illinois	17
Arkansas	72	Oklahoma	32	Colorado	15
Mississippi	72	Vermont	32		
Ohio	68	North Carolina	30		

Source: Federation of Tax Administrators, "Sales Taxation of Services," http://www.taxadmin.org /fta/pub/services/services.html.

Note: The five states without sales taxes are not listed, since they do not tax any services.

Table 2. Selected Untaxed Services, by Number of States Not Taxing

Service	# states not taxing
Radio & television, national advertising	49
Service charges of banking institutions	48
Loan broker fees	48
Travel agent services	47
Dentists	47
Nursing services out-of-hospital	47
Physicians	47
Veterinary services	46
Real estate management fees	46
Accounting and bookkeeping	46
Architects	46
Attorneys	46
Engineers	46
Lobbying and consulting	44
Public relations, management consulting	44
Rental of films and tapes by theaters	43

Source: Federation of Tax Administrators, "Sales Taxation of Services," accessed September 10, 2014, http://www.taxadmin.org/fta/pub/services/services.html.

While most physical goods are subject to a sales tax, many states have exemptions for particular goods and industries. For example, nearly all states with general sales taxes provide some form of special treatment for groceries (i.e., the purchase of food for home consumption). Six states tax groceries at a lower rate than other transactions,[23] and five states provide a rebate or credit to offset the cost of groceries for poor households.[24] Only two states, Alabama and

[23] The six states are Arkansas, Illinois, Missouri, Tennessee, Utah, and Virginia.
[24] The five states are Hawaii, Idaho, Kansas, Oklahoma, and South Dakota. Hawaii offers this credit to all households, not just poor ones.

Mississippi, tax groceries at the full rate and provide no offset for poor households.[25] All the remaining states with general sales taxes provide a complete exemption for the purchase of groceries. The recent trend has been to reduce or eliminate taxes on groceries; before 1996 there were eight more states in the same category as Alabama and Mississippi, taxing groceries at the same rate as other consumer goods.[26]

Because the exemption of groceries is so ubiquitous among US states, it deserves special attention. Not only is this practice extremely common, for many states it is the single largest exemption for a consumer good in terms of lost revenue. There are generally two reasons given for exempting groceries from sales taxes: food is a necessity and it imposes a large burden on poorer households. These two reasons exhibit a general problem with all exemptions to the sales taxes, and with exemptions to other taxes as well. Even if one thinks these are sound reasons for an exemption, exempting all groceries from the sales tax is a very blunt instrument for making food more affordable for poorer households.

Food is, of course, a necessity for living, but not all food is necessary. While the obesity epidemic in the United States may be somewhat overstated, it illustrates a general feature of modern life: food is abundant and cheap, and many Americans consume much more than is necessary to maintain life. And while it may also be true that taxing groceries would impose a larger burden on poorer households, this is a feature of all flat-rate sales taxes, not just taxes on groceries. By their nature, sales taxes are regressive.

Additionally, tax incidence analysis shows that the burden of a tax is not necessarily borne by the individual paying the tax. The demand for basic necessities such as food is likely

[25] Federation of Tax Administrators, "State Sales Tax Rates and Food & Drug Exemptions," January 2014, http://www.taxadmin.org/fta/rate/sales.pdf.
[26] Nicholas Johnson and Iris J. Lav, "Should States Tax Food? Examining the Policy Issues and Options," Center on Budget and Policy Priorities, Washington, DC, 1998. The authors are in favor of exempting groceries from sales taxes.

very inelastic, meaning that the main beneficiary of this privilege will be the consumers. However, money spent on food above and beyond the basic necessities will be much more elastic, and thus the main beneficiary of the tax exemption may actually be the grocery stores and producers of grocery products rather than low-income families, since the implicit subsidy will encourage more grocery spending compared with substitutes.

If one believes these are valid criticisms of taxing groceries, targeted exemptions, rather than a full exemption, would be a second-best solution to the problem. For example, as mentioned above, six states provide a means for poorer households to recover some or all of the taxes paid on groceries. The earned income tax credit (discussed below under income taxes) is another way that assistance can be targeted at needy families. Instituting a rebate program or making the EITC more generous would be a much better means of achieving the goal of assisting poorer households to purchase groceries. Purchases of groceries through the Supplemental Nutrition Assistance Program and the Special Supplemental Nutrition Program for Women, Infants, and Children are exempt from taxation by federal law, already providing some relief for poorer households.[27] To address the concern that groceries are a necessity for all families, not just poor ones, there are second-best solutions as well. For example, for states with an income tax, an allowance for grocery purchases could be built in to the standard deduction.

A less sympathetic example of a privilege in state sales taxes is the exemption given to coin-operated laundries. Of the states that impose sales taxes, only four tax laundries, with the remaining 41 states fully exempting this industry from the sales tax. Some of the arguments made in favor of this exemption are similar to those made for groceries: disproportionate harm to

[27] It should be noted that this, too, is a form of tax privilege. But since this privilege is established by federal law, policymakers in individual states must take it as a given.

poorer families and that clothes laundering is a "necessity."[28] More industry-specific arguments are made as well, such as technological arguments: for example, because most laundry machines only accept quarters, it may be difficult to implement a sales tax. And while the magnitude of the tax revenue lost for this exemption is small compared with that of the grocery exemption, the principles for opposing such a privilege are just as strong.

Property Taxes

Property taxes are levied on the value of property held by individuals, corporations, or other organizations. The two main forms of property that are taxed are real property (land and buildings) and personal property (movable property, e.g., vehicles and boats), though taxes on real property are much more common and states are moving away from taxing tangible personal property.[29] Property taxes are by far the largest source of revenue for local governments in the United States.[30] While the formulas for assessing property values and setting property tax rates vary and can be quite complicated, the basic principle of property taxation is simple. Once the value and rate have been determined, the owners of property pay the government an amount based on the value of their assets. The higher an asset's value, as assessed by the government, the higher the amount the owner pays.

The primary form of economic privilege found in the property tax is the practice of taxing property at different rates (or assessing it differently) based on how the property is used. One example would be property owned by nonprofit organizations, which is not taxed at all in

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[28] Coin Laundry Association, "Stop Laundry Tax," accessed April 27, 2014, http://www.coinlaundry.org/about-us/stop-laundry-tax/.
[29] Joyce Errecart, Ed Gerrish, and Scott Drenkard, "States Moving Away from Taxes on Tangible Personal Property" (Background Paper No. 63, Tax Foundation, Washington, DC, 2012).
[30] US Census Bureau, *2011 Annual Surveys of State and Local Government Finance*, appendix table A-1.

many jurisdictions and can represent a major loss of revenue if there is one large nonprofit in an area (e.g., a university located in a small town). Whether such an exemption is good policy is beyond the scope of this paper, but it is an extreme example of treating one organization differently from others for the purposes of taxing property.

More relevant to the discussion of property tax privileges are the different tax rates often applied to three types of property: personal, business, and agricultural. It is somewhat strange to single out agricultural property as being distinct from business property, given that agricultural land is used to produce business income (save for the small portion of the farm where the owner's residence is located). But it is necessary to single out agricultural property because every one of the 50 US states provides some preferential treatment to agricultural land. The most common means by which agricultural land is given a tax privilege is by assessing the land based on its current use rather than its market value (as most other land is assessed).[31]

A second form of privilege in the property tax is the practice in most states of exempting owner-occupied residential property from some amount of the property tax (typically up to a certain dollar amount). Often referred to as homestead exemptions or credits, these tax preferences are offered in some form in 38 states. In some states the exemptions or credits are available to all owner-occupied properties, though many states only offer them to specific groups. For example, 16 states place income limits on who may claim the exemption and 23 vary the amount of the exemption by age (with 10 states only offering the exemption to elderly homeowners).[32]

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[31] Information from table generated for all 50 states in 2012 using Lincoln Institute of Land Policy and George Washington Institute of Public Policy, "Significant Features of the Property Tax," Tax Treatment of Agricultural Property, accessed March 2, 2014, https://www.lincolninst.edu/subcenters/significant-features-property-tax/Report_Tax_Treatment_of_Agricultural_Property.aspx.

[32] Information from table generated for all 50 states in 2012 using Lincoln Institute of Land Policy and George Washington Institute of Public Policy, "Significant Features of the Property Tax," Residential Property Tax Relief Programs, accessed March 2, 2014, http://www.lincolninst.edu/subcenters/significant-features-property-tax/Report_Residential_Property_Tax_Relief_Programs.aspx.

Supporters use several arguments to justify the reduction in property taxes available to owners of agricultural and personal property. For example, the income limits on the homestead exemption in 16 states may be justified as an attempt to combat the regressive nature of property taxes and because of the related "ability to pay" criterion for tax policy in general. The property tax is, in some sense, a regressive tax, since it is applied at a flat rate, and thus low-income individuals pay a greater proportion of their income in taxes (though wealthier individuals may own more expensive property, thereby offsetting some of the regressive nature). Also, applying the "ability to pay" principle to this tax, the value of a home may not be a good indication of the owner's income and thus ability to pay (however, it is not completely uncorrelated, as one would expect that higher-income individuals tend to have more expensive homes, making the tax less regressive in practice). Whether these exemptions for low-income taxpayers make sense depends on one's views about how public policy should assist low-income individuals. But in general, a policy of exemptions for low-income taxpayers is better than applying the exemption to all individuals, though it may be second-best to a completely privilege-free property tax.

The homestead exemption for elderly homeowners and the current-use exemption for agricultural land rely on similar arguments. Both are an attempt to give preference to the current owners of the land over other potential owners. As the market value of land increases, the tax bill for the current owner increases as well. In extreme cases, the tax bill could become so large that the current owner is forced to sell the property to pay the tax. For example, retired homeowners may have saved enough during their working years to pay property taxes only under the assumption that they will not increase dramatically. Many state legislatures used similar arguments for giving preferential assessment to agricultural land, as rapid urban development following World War II began to increase the property taxes of many farmers located near major urban centers. Maryland was the first state to grant such an exemption in 1957, and, as mentioned above, all 50 states now have some form of exemption for agricultural land.[33]

Rising property values provide a clear market signal: the land is now more valuable for other purposes or if owned by other people. This increased demand can come about for a variety of reasons, such as climate or location-specific amenities, but whatever the reason, it is because potential buyers of the land now value it more. It is, of course, completely within the rights of the current property owner to not sell the property. But if property taxes can be viewed as a user fee paid for local government services, it is quite possible that increased property taxes (resulting from increased property values) will lead to higher levels of local government services. Thus, by giving tax preferences to current owners of property over new owners, the current owners may not be paying their "fair share" of the tax burden under some definitions of that term.

For example, California's Proposition 13, passed in 1978, limited the annual increase in property value assessment to a maximum of 2 percent per year. However, when property ownership is transferred, the property can then be reassessed based on its current market value. Over time, this system has created large discrepancies between what owners of similarly valued properties must pay in taxes based on when the ownership was last transferred. Economists have found that the length of time individuals stay in the same home has increased due to Proposition 13 by as much as two to three years for those with the largest implicit subsidy.[34]

Given the discussion above of the exemptions for agricultural and personal property taxes, it follows that nonagricultural businesses tend to pay higher property taxes than other property owners. While this is generally the case, it is not strictly true in all cases. Many states

[33] Richard W. England, "Preferential Assessment of Rural Land in the United States: A Literature Review and Reform Proposals" (working paper, Lincoln Institute of Land Policy, Cambridge, MA, 2011).
[34] Nada Wasi and Michelle J. White, "Property Tax Limitations and Mobility: Lock-In Effect of California's Proposition 13," *Brookings-Wharton Papers on Urban Affairs* 2005: 59–97.

offer a temporary property tax exemption for new businesses as part of economic development efforts. This exemption is discussed in a separate section of this paper under the heading "Tax Incentives for Economic Development," since property tax incentives are not the only form of tax that businesses may be temporarily exempt from paying.

Income Taxes

In most states, taxes are levied on income earned by both individuals and corporations. Only seven states do not have personal income taxes, and just three have no corporate income tax, though the tax rates and tax base vary widely across states.[35] Economic privilege in the income tax code arises when individuals or corporations are able to lower their tax burden by engaging in certain activities. The primary types of privileges are referred to as exemptions and deductions, which lower taxable income, and credits, which lower taxes due. In my general discussion of the income tax, I will follow standard practice and refer to all such means of lowering one's income tax burden as tax expenditures, though I will discuss specific deductions and credits below.

Most income tax expenditures have, at least on their face, some public-policy justification. Governments offering these exemptions may claim that they encourage taxpayers to act in a socially beneficial way, or perhaps that they stimulate economic activity. These claims may be true, but it depends on the particulars of the case. Even if a tax expenditure does have some benefits for society, the exercise of economic privilege implicit in the exemption should count as a cost in the overall benefit-cost analysis. Economic privilege generally, and tax

[35] Tax Foundation, "State Individual Income Tax Rates, 2000–2013," http://taxfoundation.org/article_ns/state-individual-income-tax-rates-2000-2013, and "State Corporate Income Tax Rates, 2000–2013," http://taxfoundation.org/article/state-corporate-income-tax-rates-2000-2013. New Hampshire and Tennessee have income taxes that only apply to interest and dividend income; thus there are actually nine states that do not tax wage and salary income.

privileges specifically, may encourage more rent-seeking behavior even when some of the privileges may provide some social benefit (e.g., encouraging activities with positive externalities.) Thus, even if public finance economics approves of a particular privilege, public choice economics still labels such practices as economic privilege. And in many cases, the stated public benefits are merely cover for private gain.

US states offer many of their own tax expenditures, though many follow the federal tax code closely. For example, the federal personal income tax offers taxpayers either a standard deduction of a certain dollar amount or the option to "itemize" a wide variety of deductions. If those itemized deductions exceed the standard deduction, the taxpayer's tax bill is lowered. Of the 41 states plus Washington, DC, with a broad-based individual income tax, 32 closely follow the federal itemized deduction schedule.[36] In previous research with Brandon Pizzola, I have examined the economic consequence of the largest individual and corporate tax exemptions, which in total add up to over $1 trillion at the federal level.[37]

Table 3 presents a list of the 10 largest tax expenditures in the federal income tax code for FY 2014.[38] These 10 tax expenditures total over $752 billion, or 63.6 percent of the total estimated tax expenditures for 2014. While this paper is primarily concerned with state taxes, given how closely many states mirror the federal income tax code, this list will provide a general idea of the largest tax privileges in the states. A list of data specific to US states would be ideal, but comparable data are not readily available. The list combines both corporate and individual

[36] Institute on Taxation and Economic Policy, "State Treatment of Itemized Deductions," Policy Brief, September 2011.
[37] Jeremy Horpedahl and Brandon Pizzola, "A Trillion Little Subsidies: The Economic Impact of Tax Expenditures in the Federal Income Tax Code" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, October 24, 2012), http://mercatus.org/publication/trillion-little-subsidies-economic-impact-tax-expenditures-federal-income-tax-code.
[38] Office of Management and Budget, "Analytical Perspectives: Budget of the United States Government, Fiscal Year 2014," table 16-3: "Income Tax Expenditures Ranked by Total Fiscal Years 2014–2018 Projected Revenue Effect."

income tax expenditures, though if they were broken down into these two categories, the individual income tax would dominate, with about 90 percent of the total expenditures.[39]

Table 3. Largest Federal Tax Expenditures, Fiscal Year 2014

	Revenue effect (in millions)
Employer-provided health insurance exemption	$212,820
Home mortgage interest deduction	$101,470
Retirement plans exemptions and credits (defined contribution)	$79,720
Imputed rental income exemption	$75,520
Retirement plans exemptions (defined benefit)	$53,060
State and local taxes deduction	$51,560
Capital gains (lower rates)	$46,690
Capital gains on home sales exemption	$45,870
Charitable contributions deduction	$44,060
Deferral of foreign income	$41,770

Source: Office of Management and Budget, "Analytical Perspectives: Budget of the United States Government, Fiscal Year 2014," table 16-2: Estimates of Tax Expenditures for the Corporate and Individual Income Taxes for Fiscal Years 2012–2018.

One major example of privilege in the federal and many state income tax codes is the home mortgage interest deduction. This is the largest explicit form of tax privilege (i.e., tax deduction) offered to individuals at the federal level. The exclusion of employer-provided health insurance from taxation is much larger at the federal level (about twice as large, or three times as large including payroll taxes and income taxes), but that exemption is an implicit one (i.e., a tax exclusion), rather than one that taxpayers itemize on their annual return.

The home mortgage interest deduction is sold to the public as a means of increasing homeownership and helping out the middle class, but these two claims lack much empirical

[39] Ibid., table 16-2: "Estimates of Tax Expenditures for the Corporate and Individual Income Taxes for Fiscal Years 2012–2018."

support.[40] Only about one-fifth of taxpayers take this deduction in any given year, and the benefit for middle-class families (those with $30,000–$75,000 in annual income) is on average between $500 and $700.[41] Instead, the deduction largely benefits high-income taxpayers with more than $200,000 in annual income, about three-quarters of whom take the deduction and receive more than $5,000 on average. A close analysis of the mortgage interest deduction reveals flaws in both the efficiency (more homeownership) and equity (benefits the middle class) claims.[42] The imputed rental income exclusion, the fourth item listed in table 3, also benefits homeowners, though there is debate among economists over whether this item should be included in the federal list of tax expenditures.

Examining table 3 raises several questions about how tax expenditures are defined. Most important for this paper is whether there is any legitimate public policy purpose for any of these privileges based on economic theory. The clearest candidates for legitimacy are the exemptions for contributions to tax-protected retirement plans and lower tax rates for capital. The two primary justifications for these exclusions are that they make the income tax more closely approximate a consumption tax and that the lower capital gains tax rates serve as a partial correction for the double taxation of corporate income.[43]

The avoidance of double taxation of capital income is the more important reason for allowing or even requiring these tax expenditures. Horizontal equity requires that individuals

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[40] On this issue of homeownership rates, see Edward L. Glaeser and Jesse M. Shapiro, "The Benefits of the Home Mortgage Interest Deduction," *Tax Policy and the Economy* 17 (2003): 37–82.
[41] See table 2 in Dean Stansel and Anthony Randazzo, "Unmasking the Mortgage Interest Deduction: Who Benefits and by How Much? 2013 Update" (Reason Foundation Policy Study 421, December 2013).
[42] Jason Fichtner and Jacob Feldman, "Reforming the Mortgage Interest Deduction" (Working Paper No. 14-17, Mercatus Center at George Mason University, Arlington, VA, June 2014), http://mercatus.org/publication /reforming-mortgage-interest-deduction.
[43] Jeremy Horpedahl and Harrison Searles, "The Tax Exclusion for Retirement and Pension Plans" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, September 2013), http://grad.mercatus.org /publication/tax-exclusion-retirement-and-pension-plans.

with the same income and family size be taxed similarly. However, taxes on dividends and capital gains treat income differently when it first flows through a corporation, given the presence of a corporate income tax. The income is first taxed when the corporation earns it, and it is taxed again as income when it is passed to the shareholders or realized through the sale of stock. If the business were organized differently (e.g., as a sole proprietorship or partnership), the income would be taxed only once. In the absence of a corporate income tax, double taxation becomes less of a problem and may disappear entirely, and these tax expenditures may then be regarded as forms of economic privilege. But under the present tax system, there is a strong rationale for excluding capital income from taxation.

Thus, not all income tax expenditures fall under the category of economic privilege. Some may be justified, even without getting into efficiency criteria, because of the way the tax system is structured, because of how businesses are organized, or because of income earned in multiple jurisdictions. For any US state income tax, it is crucial to examine whether a provision falls under one of these justifiable exclusions according to economic theory. Politicians may attempt to justify some categories of economic privilege on efficiency grounds: that is, by arguing they are a form of economic development (creating more jobs or more economic activity). For these efficiency-based exclusions, policymakers face a difficult tradeoff between increasing economic activity and giving out favors to specific taxpayers. But on close examination the efficiency justification of many provisions turns out to be overstated.

Tax Incentives for Economic Development

In addition to the many general provisions relating to particular taxes discussed above, many state governments offer packages of tax incentives to businesses that agree to relocate to their state. These tax incentives usually consist of the right to pay lower tax rates or completely avoid one or more taxes, typically for a limited time and sometimes contingent on certain outcomes (e.g., the number of jobs created). These tax incentives are usually proposed and offered to promote economic development and job growth in a state.

There are important efficiency questions implicit in the use of tax incentives, which are whether they work and whether they pass a benefit-cost test. I will discuss the answer to these questions briefly below, but before answering them, these types of tax incentives are a clear example of economic privilege. This is true even if they achieve their stated goals. Temporary tax incentives for businesses will often mean that certain other individuals and businesses must pay higher rates to compensate for these incentives. These tax incentives show up in different states for all three major tax categories discussed in this paper.

But do tax incentives for economic development actually achieve the stated efficiency justifications of creating jobs and increasing economic activity? Most recent research suggests that, at least on average, these tax incentives do not produce the stated effects. Alan Peters and Peter Fisher survey the empirical literature on tax incentives and find mixed results, but they suggest that there is little definitive proof that these incentives are justified.[44] More recent research by William Fox and Matthew Murray agrees with Peters and Fisher's survey of past research by examining large firms that changed locations.[45] Christopher Coyne and Lotta Moberg argue that targeted tax benefits lead to the misallocation of resources and encourage rent-seeking.[46]

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[44] Alan Peters and Peter Fisher, "The Failure of Economic Development Incentives," *Journal of the American Planning Association* 70, no. 27 (2004).
[45] William F. Fox and Matthew N. Murray, "Do Economic Effects Justify the Use of Fiscal Incentives?," *Southern Economic Journal* 71, no. 78 (2004).
[46] Christopher J. Coyne and Lotta Moberg, "The Political Economy of State-Provided Targeted Benefits" (Working Paper No. 14-13, Mercatus Center at George Mason University, May 2014), http://mercatus.org/publication/political-economy-state-provided-targeted-benefits.

One problem with all empirical studies is that they look at the net effect across all firms. Perhaps even if there is no effect on average, the movement of some firms across state lines was, on net, beneficial to the new state. While it is almost certainly true that some firms migrate based on tax incentives, the problem is that there is no clear formula for deciding which tax incentives will be successful and which will not. Not only do bureaucrats lack the information to pick the winners, they may also lack the incentive due to the rent-seeking behavior of potential beneficiaries. This rent-seeking behavior, identified by economists working in the public choice tradition, has the potential to dominate any benevolent economic development tax incentives.[47] Thus, states may find it in their interest to "tie their hands" and avoid all such development-based tax incentives in a privilege-free state tax code.[48]

2. Applying the Principles to the State of Nebraska

The second part of this paper applies the principles of a privilege-free tax system to the state of Nebraska. Fundamental tax reform has been under discussion in Nebraska for the past few years, following a bold proposal by the governor in January 2013 to eliminate both the individual and corporate income taxes completely or significantly lower their rates. These reforms would be revenue neutral in the short run, and paid for by eliminating many sales tax exemptions.[49] But many of these exemptions were for business-to-business transactions; in particular, many were for the purchase of inputs in the agricultural sector. Within one month of the initial proposal, the governor had backed off from his proposal after pressure from the impacted industries, and instead

[47] Ibid.
[48] Geoffrey Brennan and James M. Buchanan, *The Power to Tax: Analytical Foundations of a Fiscal Constitution* (Indianapolis, IN: Liberty Fund, 2000 [1980]). See especially chapter 8, "The Domain of Politics."
[49] Communications Office of Governor Dave Heineman, "2013 Tax Reform," January 2013.

set about investigating less dramatic tax reforms.[50] After a year of studying the tax system by a special state committee, several tax reforms were signed into law in April 2014. However, nearly all the reforms added more privileges to the tax code, by exempting some Social Security and military retiree income from taxation and exempting agricultural repair parts from sales taxation. The reforms also indexed income tax brackets to inflation.[51] Nebraska's 2014 legislative session thus did not achieve fundamental tax reform, though it is likely to be discussed in future sessions.

During the state's study of tax reform, several outside groups also produced studies that contained their own recommendations. For example, one prominent study produced jointly by the Tax Foundation (in Washington, DC) and the Platte Institute (in Nebraska) outlines tax reform that will "promote long-term economic growth and boost job creation."[52] The principles presented in my study are primarily about removing economic privilege, regardless of the effect on efficiency. While the goal of the Tax Foundation's study is different from that of the present study, many of the potential tax reforms are similar to those outlined below.

One major difference in approach is that the Tax Foundation study has lower tax rates as the goal of reform, with specific reforms as a means to this goal. Instead, I treat removing economic privilege as the goal of reform, with lower rates being a positive by-product.

Background on Tax Revenue by Source in Nebraska

According to the US Census Bureau's most recent data for Nebraska, in FY 2011, the state and local governments had $21.6 billion in revenue and spent $19.5 billion. Of that $21.6 billion in

[50] Paul Hammel and Martha Stoddard, "Bowing to Critics, Dave Heineman Scraps Tax-Reform Bills," *Omaha World-Herald*, February 16, 2013, http://www.omaha.com/apps/pbcs.dll/article?AID=/20130216/NEWS/130219576.
[51] Martha Stoddard, "Heineman Signs $412 Million in Tax Cuts, Calls for More Relief," *Omaha World-Herald*, April 2, 2014, http://www.omaha.com/article/20140402/NEWS/140409687.
[52] Joseph Henchman and Scott Drenkard, *Building on Success: A Guide to Fair, Simple, Pro-growth Tax Reform for Nebraska* (Washington, DC: Tax Foundation, 2013).

revenue, only \$7.8 billion came from tax revenue, with the other major revenue sources being federal aid, utility revenue, insurance trust revenue, and charges for services such as higher education. Of the \$7.8 billion in tax revenue, \$4.15 billion came from statewide taxes and \$3.65 billion from local taxes. The largest category of tax revenue is property taxes, at almost \$2.9 billion—virtually all of it at the local level. The next largest categories are the general sales tax and the individual income tax, which each raised roughly \$1.7 billion in FY 2011. All the individual income tax revenue was at the state level, as well as about 84 percent (\$1.4 billion) of the general sales tax revenue. Other important sources of tax revenue in Nebraska are the corporate income tax (\$155 million, all at the state level) and several selective sales taxes (\$717 million, about 90 percent at the state level).[53]

Sales Taxes in Nebraska

Nebraska currently has a statewide sales tax of 5.5 percent, with local governments authorized to add an optional tax of up to 2 percent. The major reforms necessary for Nebraska's sales tax are of two kinds. First, some transactions are excluded from the sales tax when they should be included, such as most services and some goods (e.g., groceries). But some transactions are currently taxed when they should not be, such as business-to-business transactions. I discuss the reasons for not taxing business-to-business transactions more completely in part 1 of this paper, but, in brief, taxing these sales may encourage inefficient vertical integration by businesses to avoid tax pyramiding. An ideal, privilege-free tax system would only impose a sales tax on the final purchase and value of consumer goods.

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[53] US Census Bureau, *2011 Annual Surveys of State and Local Government Finances*.

The Nebraska Department of Revenue produces a tax expenditure report every two years. The 2012 report estimates that more than $4 billion in revenue is lost due to exempting various kinds of transactions from the sales tax.[54] However, I calculate that a large part of this lost revenue, roughly $2.8 billion, is from business-to-business transactions in selected industries, and another half billion is from transactions involving nonprofit organizations (including governmental organizations) or required by federal law (e.g., use of Supplemental Nutrition Assistance Program payments).[55] This leaves around $654.8 million in lost tax revenue from privileged goods categories, a smaller but still significant sum: about 27 percent of the $2.4 billion collected in Nebraska from general and selective sales taxes in 2011.[56] The largest items exempted from the sales tax are motor fuels, groceries, medical equipment and medicine, room rentals by certain institutions, and motor vehicle trade-ins, accounting for more than $600 million of the $654.8 million mentioned above. These categories all have their constituencies and rationales, but all are forms of economic privilege. Table 4 shows the major categories for goods that are exempt from the general sales tax.[57]

The Nebraska Department of Revenue report is very useful in identifying goods that are not taxed, but it is of little help when it comes to identifying services exempted from the sales tax. Survey data compiled by the Federation of Tax Administrators is useful to supplement the Nebraska Department of Revenue data, although the federation only lists the categories of services taxed, not estimates of the revenue impact. Overall, Nebraska does well compared with

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[54] For the sales and use tax, see section A of Nebraska Department of Revenue, "State of Nebraska Tax Expenditure Report 2012," October 2012, http://www.revenue.nebraska.gov/tax_exp/2012/contents.html.

[55] Whether or not nonprofit institutions should pay taxes is beyond the scope of this paper, but current law at both the federal and state levels reflects this fact and thus I exclude it as a form of economic privilege.

[56] US Census Bureau, *2011 Annual Surveys of State and Local Government Finances*.

[57] Some of these goods, such as motor fuels, are subject to separate selective sales taxes. But these other taxes have other justifications, such as serving as proxies for user fees or as Pigouvian taxes on negative externalities (the motor fuel tax arguably serves both of these purposes). Their exemption from the general sales tax still deserves to be treated as a form of economic privilege.

other states ("well" meaning exempting few services), with the ninth highest number of services taxed according to the Federation of Tax Administrators at 77 out of 168 service categories. However, even with this high ranking, Nebraska only taxes roughly half as many services as the states with the broadest tax bases (see table 2).[58] Table 5 shows selected services that are exempt from the sales tax in Nebraska and the number of other states that do tax these same services. Table 5 includes two sets of services: those which Nebraska exempts but many other states tax (first 10 services listed), and those which Nebraska exempts and so do most other states (second 10 services listed).

Table 4. Largest Exemptions of Goods from the General Sales Tax in Nebraska

Exempt good	Estimated lost revenue
Motor Fuels	$248,042,000
Food or Food Ingredients	$127,812,000
Certain Medical Equipment and Medicine	$114,346,000
Room Rentals by Certain Institutions	$63,966,000
Motor Vehicle/Motorboat Trade-Ins	$55,527,000
Nebraska Lottery	$15,539,000
Minerals, Oil, and Gas Severed from Real Property	$10,654,000
Aviation Fuel	$8,216,000
Newspapers	$2,274,000
Data Centers	$1,674,000
Meals Sold by Institutions at a Flat Rate	$1,172,000

Source: Nebraska Department of Revenue, "2012 Tax Expenditure Report," State of Nebraska, October 2012, http://www.revenue.nebraska.gov/tax_exp/2012/contents.html, section A.

[58] Federation of Tax Administrators, "Sales Taxation of Services," accessed September 10, 2014, http://www.taxadmin.org/fta/pub/services/services.html.

Table 5. Selected Services Exempt from Sales Tax in Nebraska

Tax-exempt service (in Nebraska)	# states that tax this service
Interstate telephone & telegraph	27
Auto services	25
Laundry and dry cleaning services, non-coin op	22
Landscaping services (including lawn care)	21
Parking lots & garages	21
Labor charges on repairs to motor vehicles	21
Telephone answering services	20
Automotive storage	19
Pinball and other mechanical amusements	19
Movies/digital video, downloaded	18
Accounting and bookkeeping	5
Architects	5
Attorneys	5
Engineers	5
Advertising (sale of time or space)	4
Bail bond fees	4
Dentists	4
Nursing services out-of-hospital	4
Physicians	4
Travel agent services	4

Source: Federation of Tax Administrators, "Sales Taxation of Services," http://www.taxadmin.org/fta/pub/services/services.html.

The Tax Foundation's report on Nebraska gives a rough idea of the dollar value of these untaxed services. In table 29 of the report, the authors estimate that under the current sales tax base, roughly $21 billion of transactions are subject to the sales tax, or about 32 percent of personal consumption spending. Under a scenario where the sales tax base is greatly expanded, the Tax Foundation estimates that $52 billion of transactions would be included in the sales tax base, or roughly 80 percent of personal consumption expenditures. This is approximately a two-and-a-half-fold increase in the size of the sales tax base. The Tax Foundation further estimates that this base expansion could be used to eliminate the corporate income tax (currently the top rate is 7.81 percent), to reduce the top individual income tax rate to 3 percent (from 6.84 percent), and to reduce the sales tax rate to 4 percent (from 5.5 percent).[59]

Property Taxes in Nebraska

Nebraska currently has three main forms of economic privilege in its property tax system. The first is the homestead exemption, which applies to certain elderly homeowners, veterans, and disabled individuals. The second is the Property Tax Relief Credit, which is a more generally available credit for property taxes. And finally, agricultural and horticultural land is assessed at only 75 percent of current value, rather than at full market value.

For FY 2013, the Homestead Exemption was estimated to cost $72.5 million.[60] For the Property Tax Relief Credit, current law appropriates $115 million for the credit, and since FY 2009, more than 98 percent of the appropriated funds have been used.[61] Agricultural land is taxed at an average rate of approximately 1.56 percent, while residential and commercial property is taxed at an average rate of approximately 2.09 percent. In 2012, more than $768 million was collected from agricultural property, plus almost $95 million in agricultural outbuildings, farm site land, and agricultural machinery and equipment.[62] As a very rough estimate, taxing this property at the same rate as residential and commercial property could

[59] Henchman and Drenkard, *Building on Success*.
[60] See table 3C in Nebraska Department of Revenue, Property Assessment Division, *2012 Annual Report*, http://www.revenue.ne.gov/PAD/research/annual_reports/2012/NE_RevenuePAD_annrpt2012_fullbook.pdf.
[61] Ibid.
[62] Ibid., table 19.

generate another $293.1 million in revenue. In total, roughly $475.6 million in property tax revenue is forgone in Nebraska due to the privileged exemptions discussed in this section.

Income Taxes in Nebraska

Nebraska currently has both an individual and a corporate income tax. The individual income tax has four brackets, starting at 2.46 percent and with a top bracket of 6.84 percent. The top bracket applies to single individuals with more than $27,000 in taxable income and married couples with more than $54,000. The corporate income tax has two rates, with the first $100,000 of profits taxed at 5.58 percent and profits above that taxed at 7.81 percent.

Nebraska's *Tax Expenditure Report 2012* provides information on exemptions to the income tax, although it does not distinguish between individual and corporate taxes.[63] Using the data from the report, in 2012, more than $925 million in revenue was forgone in the income tax code due to tax expenditures. However, $84 million of this sum can be removed immediately, as these were credits and exclusions for activity outside Nebraska by corporations and for taxes paid to other states. Since that income was already taxed in another state, excluding it from taxation in Nebraska is not a form of economic privilege, but is, in fact, what the principles of a privilege-free tax code require.[64] Of the remaining $841.5 million, $610 million is from just three items: the personal exemption, the standard deduction, and itemized deductions.

Most tax codes, including the federal tax code, use personal exemptions and standard deductions to establish a minimum income below which a household is not taxed. Whether such a practice is justified relies on equity concerns, though one justification may be that since sales

[63] Ibid., section B.

[64] Some states may tax that activity at a lower rate than Nebraska, but this lower rate is not a privilege offered by the state of Nebraska. Rather, it is simply a feature of a world with corporations operating in multiple jurisdictions with different tax systems and rates.

and property taxes are regressive, low-income families deserve a break on the income tax. However, under the horizontal equity standard, these provisions in the tax code are not forms of economic privilege, since they are available to everyone at that income level.

The third of these items, itemized deductions, is a much clearer candidate for the category of economic privilege. As discussed in part 1 of this paper with regard to the federal income tax, a large number of the itemized deductions are forms of economic privilege, most prominently the home mortgage interest deduction. The Nebraska income tax allows individuals to use the same itemized deductions amount from their federal tax return, less any Nebraska taxes deducted on the federal return. Itemized deductions result in total tax collection being $252 million lower than without this category, though taxpayers would be able to claim the standard deduction in lieu of itemizing if it were removed.

Nebraska also has an earned income tax credit (EITC) equivalent to 10 percent of the federal EITC. According to the report, the refundable portion of the tax costs the state $29 million. It gives no estimate for the nonrefundable portion. The EITC is, in general, a very good "second best" solution for the removal of many of the economic privileges discussed in this report that will adversely affect low-income families. Rather than being simply a handout to anyone below a certain income level, the EITC is designed to encourage individuals to work more, as working increases the size of their credit up to a certain income level. Some changes in the tax code, such as subjecting groceries to the sales tax, may adversely affect low-income households. An offsetting increase in the size of the EITC would be an excellent second-best solution to address this issue if public support remains for providing assistance in the tax code to low-income families.

Tax Incentives for Economic Development in Nebraska

Nebraska offers a variety of tax incentives to businesses in an effort to promote economic development. In fact, these incentives are so generous that according to the Tax Foundation Nebraska has the lowest effective tax rate for new businesses of all the states, despite having only the ninth lowest effective tax rate for mature businesses.[65] The tax incentives are offered under a wide variety of programs. The Nebraska Department of Revenue provides data on the number of credits earned and used in recent years, though only for five of the programs.[66] In 2012, companies earned more than $332 million in credits and used more than $123 million in credits to lower their tax burdens.[67] Companies may earn credits in one year to be saved and used in future years; hence the different figures for earned and used credits.

Also using data from the Nebraska Department of Revenue, the Tax Foundation provides data offering a longer perspective on these tax incentives. It calculates that more than $596 million in credits have been used since 2006. This figure represents 44 percent of the total amount of tax revenue collected through the corporate tax code. The amount of unused credits is currently close to $400 million. Together, the used and unused credits amount to 71 percent of corporate taxes actually collected since 2006.[68]

As with similar tax credits in other states, the primary justification is that these credits promote economic development since Nebraska competes with other states for business. But as discussed in part 1 of this paper, much of the empirical research into this topic indicates that on

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[65] Tax Foundation, *Location Matters: A Comparative Analysis of State Tax Costs on Business* (Washington, DC: Tax Foundation, 2012), http://taxfoundation.org/sites/default/files/docs/location%20matters.pdf.

[66] The credits are the Nebraska Advantage Act, the Nebraska Advantage Rural Development Act, the Nebraska Advantage Microenterprise Act, the Nebraska Advantage Research and Development Act, and the Employment and Investment Growth Act.

[67] Nebraska Department of Revenue, *Nebraska Tax Incentives: 2012 Annual Report to the Nebraska Legislature*, July 15, 2013.

[68] Table 18 in Henchman and Drenkard, *Building on Success*.

average, there is little economic benefit to the state from these credits. Their sheer magnitude and blatant favoritism makes them one of the clearest examples of economic privilege in the Nebraska tax code. A simpler way of competing would be to lower the corporate tax rate for all firms, which would improve economic activity across the state and would not grant any special privileges.

Total Estimates of Economic Privilege in Nebraska

Based on the analysis in the second part of this paper, I can provide some rough estimates for the overall amount of economic privilege in the Nebraska tax code. The total figures for the relevant tax privileges are as follows: for the sales tax, $654.8 million; for the property tax, $475.6 million; for the income tax, $841.5 million; and for tax credits for economic development, $123.3 million. Altogether, these privileges total just over $2 billion in forgone tax revenue for Nebraska in 2012.[69]

To put that figure in perspective, compare it to various categories of tax revenue for Nebraska in 2011.[70] Total revenue in Nebraska, at both the state and local levels, was $21.6 billion; thus the privileges were almost 10 percent of Nebraska's revenue for 2011. However, the $21.6 billion includes revenue from the federal government, revenue from operating public utilities and liquor stores, and insurance trust revenue. Focusing instead on what the Census Bureau calls "own source" revenue (essentially taxes and fees for government services), the relevant figure is $11.6 billion, of which tax privileges are now 18 percent of the total. Narrowing the figure further to tax revenue from the three sources this paper analyzes (sales,

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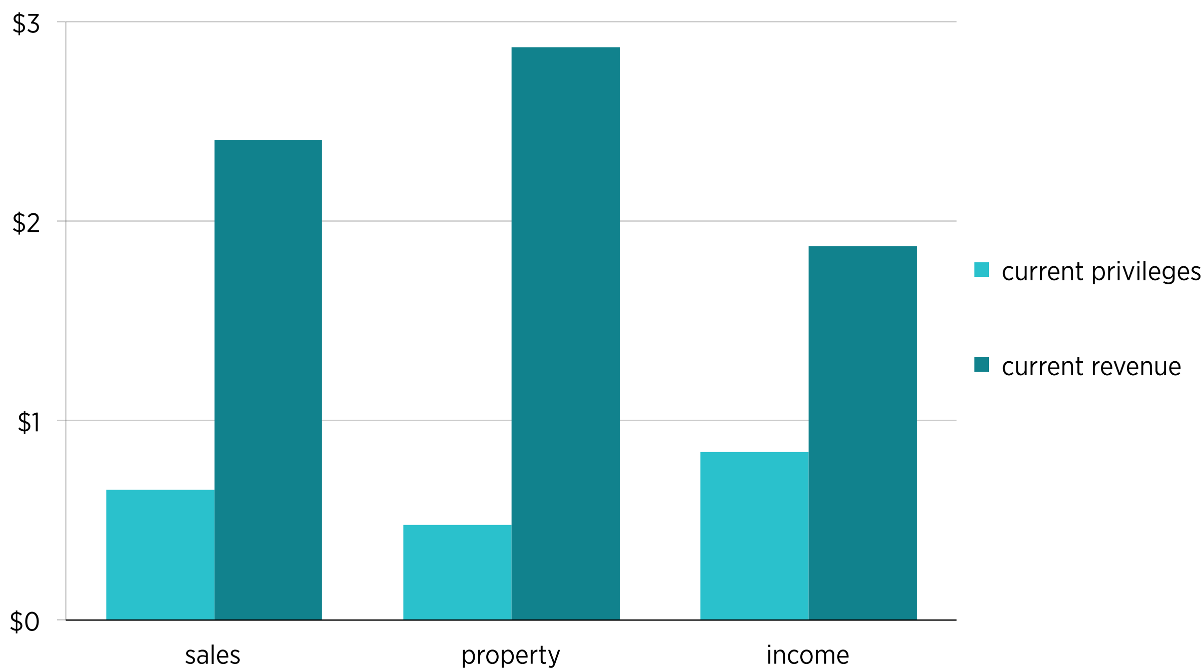
[69] There are some methodological problems with simply adding all these figures together, but my goal here is to provide a rough estimate for comparison. In particular, the tax credits for economic development may not represent forgone tax revenue, as some of the companies may not have relocated to Nebraska without the credits; thus the tax revenue cannot reasonably be called "lost." Nevertheless, the figures give us some notion of the magnitude of economic privilege in the Nebraska tax code.
[70] All data that follow are from US Census Bureau, *2011 Annual Survey of State and Local Government Finance*.

property, and income), the amount of Nebraska revenue shrinks to roughly $7.2 billion. Thus, using the most relevant comparable revenue data, tax privileges in Nebraska are more than 29 percent of total tax collections. Figure 1 shows the comparisons of tax privileges and current tax revenue for each of the three major tax categories in Nebraska.

Figure 1. Nebraska Tax Privileges and Tax Revenue (in billions)



Sources: Author's calculations using US Census Bureau, 2011 Annual Survey of State and Local Government Finance, and Nebraska Department of Revenue, "2012 Tax Expenditure Report," State of Nebraska, October 2012.

Conclusion

Reforming a state's tax code to remove privileges is often quite difficult. Privileges are frequently put into place by rent-seeking interest groups. Even if the original impetus was more broad-based, once the privileges are in place interest groups arise to defend them to the bitter end. Through a combination of lobbying politicians and appealing to the general public, these interest groups defend the privileges because they stand to lose a lot if their privileges are removed. Meanwhile, taxpayers do not stand to gain much by the removal of any specific privilege, though they would benefit greatly if all or many privileges were simultaneously removed (principally in the form of lower tax rates). This familiar logic of collective action often leads to preservation of the status quo, or even to an increasingly privileged tax code.

In this paper I have provided information on the extent of privileges in US state tax codes, with much more detail on the privileges in Nebraska. Nebraska was not chosen because it is representative (though it is not particularly unusual), but rather because comprehensive tax reform has been discussed and analyzed fairly extensively in Nebraska. The bottom-line numbers on privileges in the Nebraska tax code amount to roughly 29 percent of total tax collections, or just over $2 billion, compared with the roughly $7.2 billion in taxes actually collected. The clear implication is that tax rates could be lowered substantially across the board in Nebraska if all $2 billion in privileges were removed.

A reduction of taxes by $2 billion in Nebraska would be a huge boon to a typical family. According to estimates from the Census Bureau, Nebraska's population in 2011 was about 1.84 million.[71] With a mean family size of slightly more than three people,[72] Nebraskan families are paying on average $11,739 in taxes. The savings from moving to a privilege-free tax code would amount to more than $3,200 per year for the average family (assuming the family is not directly benefitting from a privilege being eliminated). For families not currently enjoying the benefits of a tax privilege who are struggling to make ends meet, trying to improve their quality of life, or simply looking to enjoy life to the fullest, this additional income would be most welcome. And importantly, these tax savings require no reduction in government services. The analysis in this paper makes no mention of reducing the spending

[71] US Census Bureau, Population Division, "Annual Estimates of the Population for the United States, Regions, States, and Puerto Rico: April 1, 2010 to July 1, 2013 (NST-EST2013-01)," December 2013.
[72] The precise figure is 3.04 persons per family. See table 4 in US Census Bureau, "Households and Families: 2010," 2010 Census Briefs (April 2012).

side of the state budget. Instead, all that is required is the removal of the privileges in the tax code identified throughout this paper.

The precise means by which the tax rates should be reformed is beyond the scope of this paper. Which taxes (sales, property, or income) should be lowered? Where rates are progressive, such as the income tax, which rates should be lowered and by how much? Should the corporate or personal income tax rates be lowered? The process of reform will, inevitably, involve some rent-seeking activity as well. Dividing up the spoils of tax reform presents its own challenges. But the principles of this paper could potentially be applied to that process as well. The lowering of tax rates could be done in such a way that no specific industry, firm, or class of individuals benefits disproportionately from the average benefit. Some difficulty arises in this process since some industries, firms, or individuals already pay much more of their income in taxes than the averages discussed in the conclusion. But we should not abandon the idea of removing economic privilege from the tax code simply because it would be challenging to fairly (in the eyes of all individuals) distribute the benefits of the reform.

Appendix 1: Tax Privilege Estimates for the 50 States

State	Year	Corporate income	Individual income	Adjustment for "other states'" credits	Property	Sales and use	Development credits	**TOTALS**
Alabama	no known report							
Alaska	2010	$670,000,000						**$670,000,000**
Arizona	2012–13	$114,379,124	$255,280,000	−$82,150,000	$328,874,395			**$616,383,519**
Arkansas	2012	$84,709,323						**$84,709,323**
California	2012–13	$6,310,000,000	$34,058,000,000		$119,000,000	$20,573,000,000		**$61,060,000,000**
Colorado	2011		$666,576,000	−$172,016,000		$1,969,383,000		**$2,463,943,000**
Connecticut	2012	$298,000,000	$398,100,000		$13,409,900,000	$3,565,100,000		**$17,671,100,000**
Delaware	2013	$5,170,000	$120,600,000					**$125,770,000**
Florida	2013–14	$1,371,600,000				$11,541,000,000		**$12,912,600,000**
Georgia	2012	$412,000,000	$6,846,000,000	−$174,000,000		$6,589,000,000		**$13,673,000,000**
Hawaii	2011			−$28,584,000			$277,401,000	**$248,817,000**
Idaho	2012		$330,723,000	−$67,231,000		$1,803,998,000		**$2,067,490,000**
Illinois	2012	$319,000,000	$3,916,000,000			$3,512,000,000		**$7,747,000,000**
Indiana	2009		$934,600,000	−$134,586,950				**$800,013,050**
Iowa	2010	$320,500,000	$4,460,500,000	−$1,778,400,000	$151,200,000	$6,376,227,000		**$9,530,027,000**
Kansas	2012		$1,722,918,792		$37,586,043	$5,701,237,181	$25,420,654	**$7,487,162,670**
Kentucky	2012	$292,300,000	$8,200,000,000		$766,400,000	$2,675,800,000		**$11,934,500,000**
Louisiana	2012–13	$1,685,000,000	$2,069,000,000			$2,663,000,000		**$6,417,000,000**
Maine	summary estimates not currently available							**$0**
Maryland	2014	$1,944,900,000	$221,100,000		$117,000,000	$2,098,300,000		**$4,381,300,000**
Massachusetts	2012	$1,258,500,000	$5,718,000,000			$17,230,200,000		**$24,206,700,000**
Michigan	2012	$2,596,650,000	$8,585,425,000		$7,621,780,000	$14,569,699,000		**$33,373,554,000**
Minnesota	2014	$770,100,000	$5,569,700,000		$1,911,400,000	$5,851,500,000		**$14,102,700,000**
Mississippi	2012	$70,702,000	$1,200,446,000	−$58,300,000		$1,235,270,839	$22,000,000	**$2,470,118,839**
Missouri	summary estimates not currently available							**$0**
Montana	2011		$340,100,000		$12,635,089			**$352,735,089**
Nebraska	2012		$925,491,000	−$84,000,000	$65,927,192	$4,061,561,000	$123,310,820	**$5,092,290,012**

Nevada	no known report							
New Hampshire	2013						$149,571,000	**$149,571,000**
New Jersey	2013	$5,118,300,000	$5,889,900,000			$9,608,200,000		**$20,616,400,000**
New Mexico	summary estimates not currently available							**$0**
New York	2011	$2,122,200,000	$9,874,300,000			$10,487,000,000		**$22,483,500,000**
North Carolina	2012	$395,700,000	$1,866,500,000			$3,011,600,000	$184,200,000	**$5,458,000,000**
North Dakota	2012					$311,158,000		**$311,158,000**
Ohio	2012	$403,100,000	$1,851,600,000			$4,668,200,000		**$6,922,900,000**
Oklahoma	summary estimates not currently available							**$0**
Oregon	2011–13		$5,732,200,000		$21,481,200,000			**$27,213,400,000**
Pennsylvania	summary estimates not currently available							**$0**
Rhode Island	2009	$83,764,786	$530,507,799			$1,032,449,500		**$1,646,722,085**
South Carolina	2012–13					$3,052,364,706		**$3,052,364,706**
South Dakota	no known report							
Tennessee	2012–13	$236,000,000				$3,850,100,000		**$4,086,100,000**
Texas	2013	$1,475,600,000			$6,209,200,000	$35,984,600,000		**$43,669,400,000**
Utah	2013				$29,400,000	$666,217,978		**$695,617,978**
Vermont	2011	$1,971,400	$47,348,360		$282,977,000	$560,100,000		**$890,425,360**
Virginia	2010		$791,600,000		$950,000,000	$377,500,000		**$2,119,100,000**
Washington	2012				$7,769,116	$16,876,932		**$24,646,048**
West Virginia	summary estimates not currently available							**$0**
Wisconsin	2012	$6,065,590,000	$378,494,000	−$287,000,000	$25,134,000	$4,319,171,000		**$10,501,389,000**
Wyoming	no known report							
TOTALS		**$34,425,736,633**	**$113,501,009,951**	**−$2,866,267,950**	**$53,527,382,835**	**$189,961,814,136**	**$781,903,474**	**$389,331,579,079**

Sources: Alaska Department of Revenue, Tax Division, *Revenue Sources Book*, Chapter 3, December 2010; Arizona Department of Revenue, *The Revenue Impact of Arizona's Tax Expenditures FY 2013*, November 2013; Arkansas Department of Finance and Administration, Revenue Division, Office of Excise Tax Administration, *Business Incentives and Tax Credits, Program Costs through December 31, 2012*, September 2013; California Department of Finance, *Tax Expenditure Report 2013–14*; Colorado Department of Revenue, Office of Research and Analysis, *Colorado Tax Profile and Expenditure Report 2012*; Connecticut Office of Fiscal Analysis, *Connecticut Tax Expenditure Report*, January 2012 (revised April 2012); Delaware Department of Finance, Division of Revenue, *Tax Preference Report 2013 Edition*; Florida Revenue Estimating Conference, *Florida Tax Handbook 2014*; Fiscal Research Center of the Andrew Young School of Policy Studies at Georgia State University, *Georgia Tax Expenditure Report for FY2014*, December 2012; Hawaii Department of Taxation, *Tax Credits Claimed by Hawaii Taxpayers 2011*, December 2013; Idaho Division of Financial Management, "Idaho's Tax Structure," in *General Fund Revenue Book Fiscal Year 2015*, January 2014; Illinois State Comptroller, *Tax Expenditure Report, Fiscal Year 2012*, July 2013; Indiana State Budget Agency, Tax and

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