



POLICY REPORT

Modernizing Nebraska's Sales Tax Base to Secure Income and Property Tax Relief

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Sales Tax Modernization

Nebraska's sales tax turns 60 next year, and it is beginning to show its age. Services make up a much larger share of today's economy, yet they are under-included in Nebraska's sales tax base. Exemptions adopted over the decades have collectively whittled away still more of the tax base. These policy choices come at a cost, because non-neutral tax policy distorts economic decision-making, favors some taxpayers and activities over others, and shifts tax burdens onto other—often worse—taxes.

As Nebraska competes for workers, entrepreneurs, investment, and new residents, policymakers have rightly made income tax rate reductions a priority. Meanwhile, addressing the state's above-average local property tax burdens is a top priority for taxpayers and lawmakers alike. An eroding sales tax base makes income and property tax relief harder, while responsible sales tax modernization could help enable it.

This policy brief outlines a range of options for broadening the sales tax base, with estimates of the additional revenue that each expansion would generate in FY 2028. Base broadening would generate additional revenue for both state and local governments. A responsible approach would dedicate state revenue to ensuring that Nebraska can afford its final scheduled income tax rate reduction in 2027 and paying for additional reforms. Lawmakers could also adopt provisions ensuring that additional local sales tax revenue offsets property tax rate reductions.

Options are divided into three tiers, though lawmakers could choose any combination of base-broadening options. The first tier consists of a modest expansion to currently untaxed goods and services like lawn care, laundromats, home maintenance, and hair care. The second tier contains motor fuel and groceries, while the third tier includes certain outpatient medical services and personal use of accounting, legal, and other services. Expanding to the first tier would generate about \$200 million in additional state sales tax revenue. Adding everything in the second tier

would yield about \$630 million, and taxing everything in all three tiers would raise an estimated \$1.6 billion in state sales tax revenue.

States with more competitive tax structures are often better positioned to attract business investment, encourage job creation, and retain families looking for opportunity. Nebraska's neighbors are implementing significant tax reforms designed to improve economic growth and attract investment. If Nebraska wants to remain competitive in the years ahead, policymakers should continue pursuing reforms that encourage growth rather than penalize it.

When Iowa, Kentucky, Louisiana, North Carolina, and other states implemented large-scale income tax cuts, they offset part of the cost by broadening the sales tax base. Policymakers in these states understood that income taxes are worse for economic growth than sales taxes, and that sales tax modernization efforts would allow them to cut income tax rates more than they could otherwise. Nebraska policymakers contemplated a similar approach, and the Platte Institute has long championed combining these two reforms, but legislators ultimately chose to cut income tax rates without broadening the sales tax base.^{1 2}

That income tax rate relief represents a historic victory for Nebraska families and is crucial to efforts to grow Nebraska's economy. Preserving the reductions already implemented and phasing in the target rate of 3.99 percent should remain a top priority. Consequently, while it wasn't part of lawmakers' original package, responsible sales tax base broadening deserves to be part of the conversation to lock in a highly competitive income tax rate while balancing the budget.³

Two tax policy axioms are relevant here: (1) whatever you tax, you get less of; and (2) well-designed taxes feature broad bases and low rates.⁴

Taxes on consumption are more economically efficient than taxes on income. Income taxes fall on labor and investment, reducing both — whatever you

tax, you get less of. An income tax, moreover, is a tax on both present and future consumption, since it reduces the savings from which future consumption will draw.

Consumption taxes are less harmful, particularly when limited to final (personal) consumption. Shifting some of the tax burden from income to sales taxes makes a state's tax code more competitive, as economic studies have documented extensively. The best way to raise additional sales tax revenue, moreover, is to broaden the base to include currently untaxed final consumption rather than to raise rates on the goods and services that are already taxed — broad bases, low rates.⁴

Most economists believe that the sales tax base should include all final consumer transactions, involving both goods and services, while excluding intermediate (business-to-business) transactions to ensure that all consumption is taxed once, but no more than once. Exempting some forms of final consumption is inefficient, favoring certain purchases over others and requires higher rates on products that remain in the base (or on income).

Conversely, including intermediate transactions in the sales tax base can lead to tax pyramiding, where the tax is imposed at multiple points in the production process and is embedded several times over in the final price paid by consumers. Taxing these inputs also turns that portion of the sales tax into a production tax, making it more expensive for businesses to operate in the taxing state and encouraging them to shift production to states that tax fewer business inputs.

A major study involving data from 21 OECD countries found that a 1 percent shift of tax revenues from income taxes to consumption taxes would increase gross domestic product by 0.74 percent. In Nebraska context, this means that every \$70 million that the state can shift from income to sales taxes would increase gross state product by \$1 billion.⁵

Most sales taxes, including Nebraska's, are badly out of date. They tax the sale of most tangible goods (with significant exceptions, like groceries) while exempting most services. Existing statutory language is also often insufficient to capture new personally consumed digital products by default.

When Nebraska taxes lawnmowers but not lawn care services, and washing machines but not laundromats, its formalistic distinction between goods and services creates distortions and unnecessarily narrows the tax base. And whereas many states tax repair services broadly, Nebraska imposes sales tax on parts but not labor. Maintenance services, haircuts and other personal care services, dating app subscriptions, event admissions, interior design, mini-storage, moving services, small animal (non-livestock) veterinary and pet grooming services, and other consumer purchases are also outside the tax base, while gasoline is subject to a motor fuel tax to pay for road maintenance, but not to the sales tax to capture driving as consumption.

Modernizing the sales tax is progressive, because most of the categories of consumption currently exempted are consumed in greater quantity by higher-income households. It also promotes economic neutrality, because it involves a broader base with fewer carveouts and resulting economic distortions.

Perhaps surprisingly, even taxing groceries can be progressive if it pays for tax relief elsewhere. Higher earners spend more on groceries, but low earners spend more on groceries as a percentage of their income, meaning that adding groceries to the sales tax base is regressive in isolation. However, federal law prevents states from taxing groceries purchased with SNAP or WIC benefits, meaning that a significant share of lower-income households' grocery purchases are exempt even if groceries are added to the base. If these households benefit from tax relief funded by base broadening, they can come out ahead with grocery taxation.⁶

Sales Tax Base Broadening Options

The following table lists potential base-broadening options, with projected revenue implications as of FY 2028.

Tier 1

Sales Tax Base Broadener	State Revenue	Local Revenue
Motor Vehicle Repair (non-business/agriculture)	\$43,399,825	\$11,267,058
Pet-Related Services	\$31,306,209	\$8,127,426
Home Maintenance, Repair, and Painting	\$30,732,170	\$7,978,399
Lawn Care, Gardening, and Landscaping Services	\$22,828,599	\$5,926,548
Household Moving Services	\$11,181,581	\$2,902,858
Residential Water Services	\$10,700,629	\$2,777,997
Taxi, Limousine, and Other Transportation Services	\$9,511,547	\$2,469,299
Hair Care Services	\$8,686,564	\$2,255,125
Memberships and Admissions	\$7,843,729	\$2,036,316
Newspapers	\$4,581,788	\$1,189,481
Travel Agency Services	\$3,583,868	\$930,410
Laundry and Dry Cleaning Services	\$3,560,511	\$924,347
Miscellaneous Personal Care Services	\$3,156,388	\$819,432
Household Storage Services	\$2,360,433	\$612,794
Feminine Hygiene Products	\$2,023,545	\$525,334
Weight Loss Services	\$1,684,203	\$437,237
Miscellaneous Personal Services*	\$1,415,628	\$367,512
Flower Deliveries	\$1,412,622	\$366,732
Nail Care Services	\$1,322,278	\$343,277
Laundromats	\$772,095	\$200,444
Tour Operator Services	\$179,526	\$46,607
Subtotal	\$202,243,736	\$52,504,633

SALES TAX BASE BROADENING OPTIONS

Tier 2

Sales Tax Base Broadener	State Revenue	Local Revenue
Motor Fuels (non-business/agriculture)	\$325,881,659	\$84,602,358
Groceries (excluding SNAP and WIC purchases)	\$303,630,559	\$78,825,735
Subtotal	\$629,512,218	\$163,428,094

Tier 3

Sales Tax Base Broadener	State Revenue	Local Revenue
Physician Services	\$323,713,962	\$84,039,601
Medical Equipment and Medicine	\$234,789,490	\$60,953,859
Legal Services (non-business)	\$81,603,375	\$21,185,107
Dentistry	\$67,030,750	\$17,401,898
Other Outpatient Services	\$47,889,081	\$12,432,517
Accounting Services (non-business)	\$17,172,425	\$4,458,145
Chiropractor Services	\$12,241,005	\$3,177,896
Investment Advice	\$9,923,791	\$2,576,322
Optometry	\$7,155,547	\$1,857,656
Subtotal	\$801,519,425	\$208,083,001
Total (all tiers)	\$1,633,275,379	\$424,015,729

* Excludes funeral and burial services (retaining the sales tax exemption for these services), which Nebraska otherwise includes in its broader definition of “personal services.”

Sources: Nebraska Department of Revenue data; Nebraska biennial budget; author's calculations.

Securing Tax Relief

State income tax systems are increasingly diverging, and Nebraska's future tax competitiveness relies on Nebraska being among the lower-income-tax states. Sales tax base broadening was considered as a partial pay-for from the start, and it should remain on the table as lawmakers navigate the current budgetary environment and work to ensure that Nebraska can afford the final stage of planned income tax rate reductions.⁷

Lawmakers could also use expenditure limitations or other measures to dedicate additional local sales tax revenue from base broadening to property tax relief.

Nebraska stands at an important crossroads. The state has already taken meaningful steps toward a more competitive tax code through income tax relief, but maintaining that momentum will require policymakers to think long term about how to build a stable, pro-growth tax system.

Modernizing the sales tax base offers one path to preserve planned income tax relief while creating a simpler, broader, and more economically neutral tax structure. At a time when states across the country are competing for workers, entrepreneurs, families, and investment, Nebraska cannot afford to stand still. A more competitive tax code can help create the kind of economic environment that encourages growth, attracts opportunity, and keeps Nebraska competitive for the next generation.

Endnotes

1. https://files.taxfoundation.org/legacy/docs/TF-Platte_Nebraska.pdf
2. <https://platteinstitute.org/nebraskas-sales-tax/>
3. <https://platteinstitute.org/nebraska-must-defend-its-historic-2023-income-tax-cuts/>
4. <https://taxfoundation.org/research/all/state/state-sales-tax-reform-guide/>
5. <https://www.econstor.eu/bitstream/10419/50575/1/619013052.pdf>
6. <https://taxfoundation.org/research/all/state/sales-tax-grocery-tax-exemptions/>
7. <https://taxfoundation.org/blog/state-income-tax-trends/>