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July 27, 2024

VIA EMAIL
Nebraska Legislature

Re: Tax Changes Should Be Based on Sound Tax Policy and Improve (Not Deteriorate) Nebraska's Tax Structure

Dear Senator:

On behalf of the Council On State Taxation (COST), I am writing in opposition to proposed new taxes on business inputs (*e.g.*, advertising services tax, sales tax base expansion to business inputs, etc.) and provisions that would unnecessarily add more complexity to the State's tax code. Taxes on business inputs increase the cost of doing business in the State, represent poor tax policy due to pyramiding and lack of transparency, and would impair Nebraska's ability to attract and retain business activity (and jobs) in the State. Imposing multiple sales tax rates as proposed in LB 1, the proposed luxury tax in LB 8, and the delivery service taxes and fees in LB 19 and LB 26, would also add unnecessary complexity to the State's tax system and take it out of substantial compliance with the Streamlined Sales and Use Tax Agreement (SSUTA),¹ jeopardizing sales tax revenue streams from out-of-state sellers. As you debate the appropriate mix of revenue derived from income taxes, consumption taxes, and property taxes, we respectfully encourage you, consistent with sound tax policy, to refrain from adopting new taxes on business inputs or increasing the complexity of the State's tax system.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 500 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. Many COST members conduct operations in Nebraska that would be negatively impacted by tax legislation proposed in this extraordinary session.

¹ Section 308.A of the SSUTA states that "No member state shall have multiple state sales and use tax rates on items of personal property or services ...".

COST Opposes Sales Taxes on Business Inputs

The COST Board of Directors has adopted a formal policy position opposing the imposition of sales taxation on business inputs.² That policy position provides:

Imposing sales taxes on business inputs violates several tax policy principles and causes significant economic distortions. Taxing business inputs raises production costs and places businesses within a State at a competitive disadvantage to businesses not burdened by such taxes. Taxes on business inputs, including taxes on services purchased by businesses, must be avoided.

Imposing sales tax on business inputs specifically violates the tax policy principles of neutrality, equity, simplicity, and transparency, and it causes a number of economic distortions. These distortions result primarily from pyramiding, which occurs when a tax is imposed at multiple levels and results in a hidden effective tax rate that exceeds the retail sales tax rate. Pyramiding forces companies to either pass these increased costs to consumers or reduce their economic activity in the State to remain competitive with other producers who do not bear the burden of such increased taxes. Because of these choices, the economic burden of taxes on business inputs inevitably shifts to labor in the State (through lower wages and employment) or consumers (through higher prices).

Sound tax policy dictates that an optimal sales tax system should only tax end-user consumption and exempt business inputs. The following are direct taxes on business inputs that should not be adopted or should allow an exemption for business purchasers:

Advertising Service Tax: Taxing advertising imposes a direct tax on an intermediate business input, and not on final consumption. Although the proposal attempts to mitigate some of the legal issues raised in Maryland by not exclusively taxing digital advertising,³ it will likely incur protracted litigation and questionable revenues. Businesses providing these services are already subject to the State's income taxes, and when advertised taxable products are sold to final consumers, they are subject to the State's sales tax. Thus, the tax on advertising services results in pyramiding, duplicative taxation, and an effective tax rate on final goods that is higher than the statutory rate. COST's attached comments on this tax in LB 388 are still applicable.⁴

Sales Tax Base Expansion: LB 1 would expand the State's sales/use tax base to numerous services that are predominantly business-to-business (B-to-B) transactions. Examples of these services include: (1) storage and moving services, (2) legal services, (3) accounting services, (4) real property maintenance and repair services, (5) seismograph and geophysical services, (6) real estate management services, (7) debt collection services, (8) credit report information, (9) employment agency and temporary help services, (10) lobbying services, (11) marketing and

² See <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/sales-taxation-of-business-inputs.pdf>.

³ See Michael Bologna, "[Apple, Peacock Battle for Top Position in Maryland Ad Tax Fight](#)," Bloomberg Daily Tax Report, February 13, 2024 (discussing the ongoing litigation in state court).

⁴ COST's letter opposing the Advertising Services Tax in LB 388 is also available at:

www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-comments-and-testimony/04162024-cost-testimony-in-opposition-to-ne-ad-tax-proposal-in-lb388-final.pdf.

telemarketing services, (12) public relations services, (13) secretarial and court reporting services, (14) telephone answering services, (15) lab testing services, (16) information services, (17) data processing services, (18) mainframe computer access and processing services, (19) income from parking lots/garages, (20) land surveying services, (21) chartered flights, (22) labor for repair or maintenance of railroad rolling stock and aircraft, and (23) products transferred electronically.

Some of these services are almost exclusively B-to-B transactions, such as information services and data processing services, and should not be included in the State's sales/use tax base. Other services may be a mix of business to consumer (B-to-C) and B-to-B transactions. Those transactions that are B-to-B should be exempt from taxation.⁵ Any new taxable service should have a clear definition that specifies the scope of the tax imposition; such definitions are absent from LB 1. Also, importantly, equipment and services used to provide a taxable service should also be exempt from sales/use taxation, and this is not addressed in LB 1. The best time to exempt B-to-B purchases is at the same time the state expands its sales tax base.⁶ Doing otherwise would harm the State by discouraging increased business activity (investment and jobs). Currently, Nebraska derives approximately 44% of its sales tax revenue from the taxation of business inputs (already above the 42% average for all other states imposing a sales/use tax⁷), and that should not be increased.

New Taxes and Different Rates Increase Complexity

The COST Board of Directors has adopted a formal policy statement urging states to impose fair, efficient, and customer-focused tax administration. COST's policy position is as follows:

Fair, efficient and customer-focused tax administration is critical to the effectiveness of our voluntary system of tax compliance. A burdensome, unfair, or otherwise biased administrative system negatively impacts tax compliance and hinders economic competitiveness.⁸

LB 1 would impose different sales/use tax rates for certain products, which would violate Nebraska's substantial compliance with the SSUTA. Two of the fundamental purposes of the SSUTA are to provide uniformity and reduce complexity, which assist both Nebraska retailers in collecting taxes in other SSUTA states and out-of-state sellers in collecting Nebraska's taxes. Non-compliance with the SSUTA risks current revenue streams from out-of-state sellers. Rather than adding complexity to the administration of the State's sales/use tax, we encourage you to

⁵ A broad exemption could be used to exclude all transactions purchased by businesses or at least cover some purchases made by business. For example, Iowa has a "commercial enterprise" exemption for digital products and services (Iowa Code § 423.3) and that concept could be expanded to apply to other services.

⁶ See Karl A. Frieden and Fredrick J. Nicely, "[Digital Business Input Exemptions: Lessons from Sales Tax History](#)," *Tax Notes State*, January 29, 2024, especially Part 6.

⁷ The COST Sales Tax Scorecard, "The Best and Worst of State Sales Tax Systems" is available at https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/270677_cost_salestaxbk_2022_final.pdf.

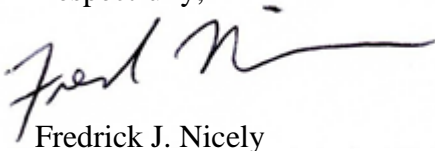
⁸ COST's Fair, Efficient, and Customer-Focused Tax Administration policy is available at: <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/fair-efficient-and-customer-focused-tax-administration.pdf>.

instead simplify the sales/use tax structure.⁹ The proposed luxury tax (LB 8) and delivery service taxes and fees in LB 19 & LB 26 would also increase the complexity of the State's tax system. The addition of multiple sales tax rates and imposition of new taxes cause significant compliance challenges, including expenses for computer system changes and other administrative expenses. Sellers who act as the State's tax collectors should be allowed adequate time to modify systems to comply with a new tax, fee, or other statutory change, and the government should compensate taxpayers for significant compliance costs associated with a new tax or fee (or for changes to an existing tax or fee).

Conclusion

COST respectfully requests you to reject as poor tax policy any new taxes on business inputs (e.g., advertising services tax, sales tax base expansion to business inputs, etc.) and avoid increasing the complexity of the State's tax code. Please contact me with questions and/or if you would like to discuss these comments further.

Respectfully,



Fredrick J. Nicely

cc: COST Board of Directors
Patrick J. Reynolds, COST President & Executive Director

Attachment: COST Opposition to Advertising Services Tax in LB 388.

⁹ The SSUTA does not apply to hemp products, thus Nebraska can impose a separate tax rate on such products. Rather than decreasing the tax rate, which is an SSUTA compliance issue even with the State's current Good Life Districts, partial exemptions could be used to lower the overall tax rate.



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April 16, 2024

VIA EMAIL

Senator John Arch, Speaker
Nebraska Legislature

Re: COST Opposes the Proposed Advertising Services Tax Act in L.B. 388 (Final Reading)

Dear Speaker Arch:

On behalf of the Council On State Taxation (COST), I am writing in opposition to the proposed Advertising Services Tax in L.B. 388 that would be imposed on businesses in Nebraska whose combined gross advertising revenue exceeds \$1 billion at a rate of 7.5 percent. This proposed Advertising Services Tax is a new, controversial, and untested tax and will likely face protracted litigation similar to Maryland's Digital Advertising Tax.¹ It would put Nebraska at a competitive disadvantage with respect to businesses seeking to maintain or expand their operations in the State because the tax is ultimately a gross receipts tax on business inputs,² and the activities are already sufficiently taxed under the State's corporate income tax regime.

About COST

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¹ See Bloomberg Daily Tax Report: State (2/13/24) by Michael Bologna, "Apple, Peacock Battle for Top Position in Maryland Ad Tax Fight," available at: <https://news.bloombergtax.com/daily-tax-report-state/apple-peacock-battle-for-top-position-in-maryland-ad-tax-fight>. Litigation is also pending at the federal court level, Civil No. 21-cv-410 (D. Md., filed February 18, 2021). Unlike Maryland, Nebraska allows declaratory relief (Neb. Rev. Stat. §§ 25-21,149 and 25-21,159) and injunctive relief (Neb. Rev. Stat. §§ 25-1062-1080) to be immediately available to contest the Advertising Services Tax.

² Business inputs constitute intermediate transactions of goods and services that businesses either resell or use to produce other goods or services that are subsequently sold for final consumption by consumers.

COST Opposes Excise Taxes on Business Inputs

The COST Board of Directors has adopted formal policy statements opposing both gross receipts taxes and sales taxes on business inputs. While the position on business inputs primarily concerns the states' sales taxes, its logic also applies to the proposed Advertising Services Tax, which is a gross receipts tax on business inputs. COST's policy positions are as follows:

*Gross receipts taxes are widely acknowledged to violate the tax policy principles of transparency, fairness, economic neutrality and competitiveness; generally, such taxes should not be imposed on business.*³

*Imposing sales taxes on business inputs violates several tax policy principles and causes significant economic distortions. Taxing business inputs raises production costs and places businesses within a State at a competitive disadvantage to businesses not burdened by such taxes. Taxes on business inputs, including taxes on services purchased by businesses, must be avoided.*⁴

The imposition of the Advertising Services Tax is primarily focused on taxing business inputs, not consumer purchases. This disproportionate taxation of business inputs violates several core tenets of sound tax policy—transparency, economic neutrality, effective tax administration, and fairness.

- *Transparency.* A transparent tax, like the sales tax on consumer purchases, is obvious to the taxpayer, and its economic effects are easily understood. The Advertising Services Tax, on the other hand, is a stealth tax that will affect Nebraska businesses and residents in several unseen ways. The tax will impact residents as purchasers, by imposing hidden taxes and thus making the products they purchase more expensive, and as workers, by depressing investment and thus reducing wages and employment opportunities.
- *Economic Neutrality.* An economically neutral tax does not influence business choices (of location, of operational entity, of suppliers, etc.). This tax will force companies to either pass their increased costs on to consumers or reduce their economic activity in the State in order to remain competitive with other companies in other states that do not bear the burden of such taxes.
- *Effective Tax Administration.* Effective tax administration is enabled by taxes that can be easily administered by a state and can facilitate voluntary compliance by all businesses. This entails tax base and sourcing rules that are comprehensible to both tax administrators and taxpayers. The Advertising Services Tax is anything but easy to administer. As an untested and novel tax, companies will be forced to adopt sophisticated accounting and recordkeeping systems to evaluate transactions on a continuous basis. For example, verifying what portion of the national advertising audience was within the State will be extremely difficult using IP addresses. The increased use of virtual private networks (VPNs) and allowing the use of “another reasonable method” to source the revenue is very

³ <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/grossreceiptstaxes.pdf>.

⁴ <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/sales-taxation-of-business-inputs.pdf>.

open ended and unclear. This tax does not conform to or harmonize with any prior national or uniform state model, leading to additional complexity for taxpayers and the Department of Revenue.

- *Fairness.* A fair tax treats similarly situated taxpayers equally. Instead of having a broad base and low tax rate, the Advertising Services Tax is selectively imposed in a punitive manner based on those providers exceeding a \$1 billion threshold.⁵

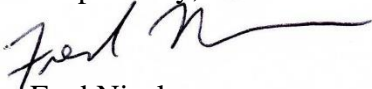
Businesses Subject to the Advertising Services Tax Are Already Subject to the State’s Corporate Income Tax

Businesses subject to the Advertising Services Tax are already subject to the State’s corporate income tax on their net income. The corporate income tax requires mandatory unitary combined reporting and is imposed on the privilege of corporations earning or receiving income in Nebraska. This imposition threshold gives the State expansive jurisdiction to impose the corporate income tax without requiring a physical presence in the State. As a result, the same businesses that would be subject to the Advertising Services Tax are also subject to the State’s corporate income tax. Nebraska also imposes a market-based sourcing regime for receipts from services and apportions such receipts using a single-sales factor formula. Market-based sourcing seeks to tax a receipt based on where the customer receives the benefits from the service rather than the location of the taxpayer. To the extent a business collects advertising revenue from Nebraska customers, that income is already sourced to Nebraska for corporate income tax purposes under the State’s market-based sourcing rules. Under the single-sales factor apportionment formula, the physical location of a corporation’s business now has minimal effect on how receipts are apportioned to the State. As a result, Nebraska’s corporate income tax regime sufficiently taxes the same activities that would be subject to the Advertising Services Tax.

Conclusion

COST remains aligned with the Association of National Advertisers (ANA) and others in our request that the Advertising Services Tax should be rejected. We respectfully oppose the Advertising Services Tax included in L.B. 388 because it is a direct tax on business inputs that violates several key tax policy principles, and would immediately lead to protracted litigation similar to that facing the Maryland tax. Advertising activities are already subject to Nebraska’s corporate income tax, which would result in the proposed Advertising Services Tax serving as a second or “double” tax.

Respectfully,



Fred Nicely

cc: COST Board of Directors
Patrick J. Reynolds, COST President & Executive Director

⁵ This raises issues under the Commerce Clause (*e.g.*, extraterritorial taxation), First Amendment (exemptions for news media providers), and the Internet Tax Freedom Act.