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The Case Against the Graduated Income Tax

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The Current Constitution

- A tax on or measured by income shall be at a non-graduated rate. At any one time there may be no more than one such tax imposed by the State for State purposes on individuals and one such tax so imposed on corporations. In any such tax imposed on corporations the rate shall not exceed the rate imposed on individuals by more than a ratio of 8 to 5. (Article IX, Section 3a of the Illinois Constitution)

The Drafters of the 1970 Constitution Were Wise

- The drafters of the 1970 Illinois Constitution and the Illinois voters who ratified the constitution determined wisely that Illinois should impose a flat rate income tax
- The debate over whether Illinois should maintain its flat rate tax is the most important current tax policy discussion in Illinois

The Illinois Flat Rate Income Tax

- The flat rate tax ensures all citizens pay their fair share to fund state government
- The flat rate income tax provides a necessary brake on tax rate increases on individuals - everyone at all income levels shares the pain of a tax rate increase

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The Illinois Flat Rate Income Tax

- The Illinois flat tax is not outside of the mainstream
- The current Illinois income tax structure uses exemptions and the earned income tax credit to treat the poorest Illinois citizens better than in many of the surrounding states

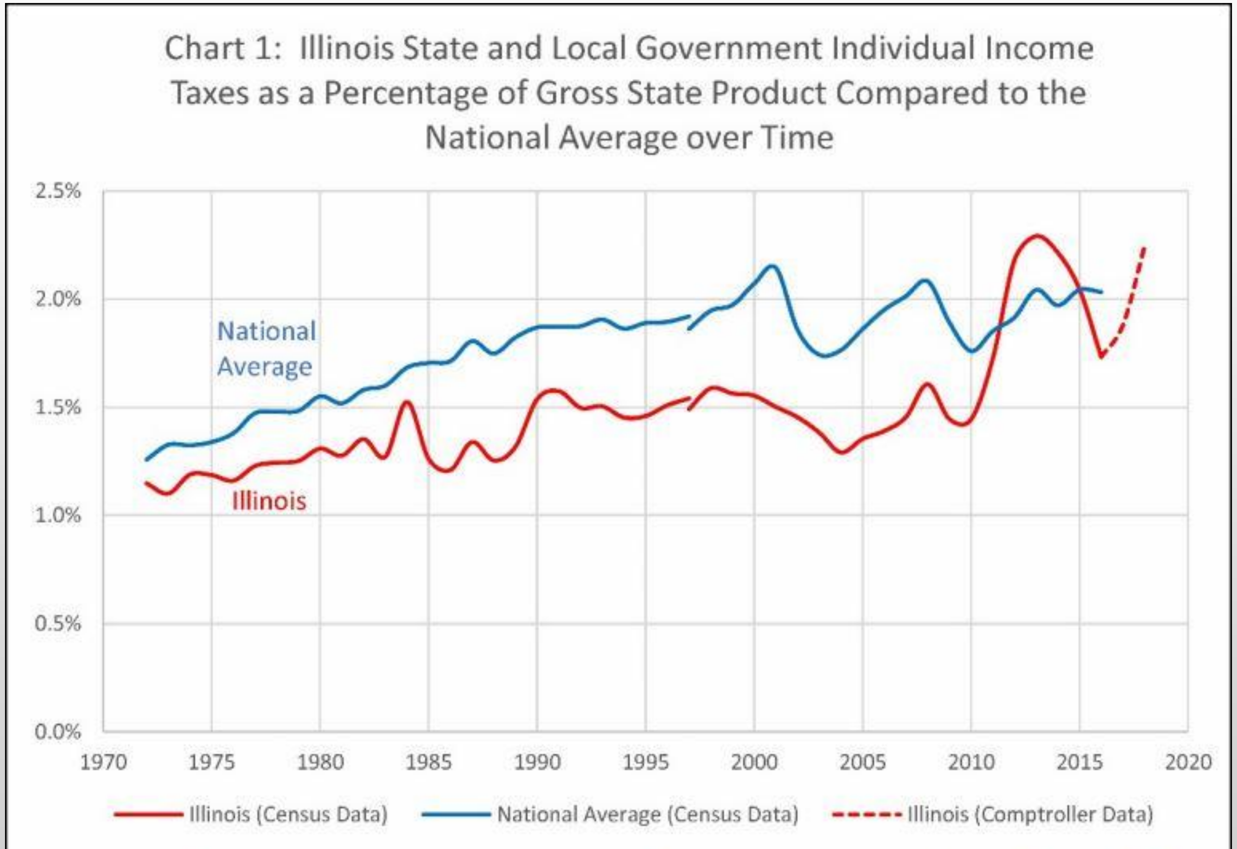
The Illinois Flat Income Tax

- The Illinois flat rate tax is one of the best economic advantages Illinois possesses over neighboring states
- The flat rate tax and the "one tax" requirement prevents Illinois lawmakers from singling out particular classes of taxpayers or particular types of income for discriminatory treatment

A Graduated Income Tax is Not a “Fair” Tax

- A graduated income tax is not a “fair” tax
- A graduated income tax punishes the successful by taxing a greater percentage of their income
- A “progressive” tax is another euphemism for a tax that punishes success

The Illinois Income Tax As a Percentage of Gross State Product



Source: Census Bureau, *State and Local Government Finances*; Bureau of Economic Analysis, Regional Economic Analysis; and Illinois Comptroller

Tax Payers Federation of Illinois. (2019). Tax Facts: Comparing Governor Pritzker's Proposed Graduated Income Tax to Other States

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Myth #1: The current Illinois income tax is outside of the mainstream

- The facts:
  - 43 states have individual income taxes – 41 tax wage and salary income
  - 7 states do not have a personal income tax
  - 9 states have a single rate

Myth #1: The current Illinois income tax is outside of the mainstream

- The Facts:
  - 33 states have a supposed “graduated” rate structure
  - But, 10 states with graduated rates begin their top brackets at under $25,000 in taxable income
  - 2 states begin their top brackets at $30,000 in taxable income
  - A minority of the states have a truly “graduated” rate structure
  - The current Illinois flat tax is consistent with the majority of states

Myth #1: The current Illinois income tax is outside of the mainstream

- The Facts:
  - The constitutional amendment authorizes a graduated income tax on corporations
  - Only 13 states impose a graduated income tax on corporations
  - A graduated income tax on corporations is outside the mainstream - the Illinois flat rate tax is in the mainstream
  - It is inevitable that if there is authority for a graduated rate on corporations, there will be legislation to impose a graduated tax

Myth #1: The current Illinois income tax is outside of the mainstream

- The facts:
  - The constitutional amendment and SB 687 will give Illinois “parity” with the minority of states which have a graduated rate structure that punishes the successful
  - A graduated income tax will not give Illinois “parity” with the majority of the states

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Myth #2: Illinois overtaxes low and middle income families compared to surrounding states

Table 1: Effective Tax Rates in Illinois and Selected States

Income	Illinois Current	Illinois Proposed	Wisconsin	Iowa	Indiana	Missouri	Minnesota	New York	New Jersey	California
$17,160	-2.97%	-4.25%	-6.56%	-2.78%	0.50%	0.00%	-11.00%	-10.49%	-10.58%	-1.09%
$61,000	3.94%	3.50%	2.88%	4.10%	4.43%	2.85%	2.76%	4.61%	1.42%	1.75%
$125,000	4.49%	4.39%	5.21%	4.90%	4.96%	3.94%	4.91%	7.74%	2.93%	4.21%
$250,000	4.70%	4.64%	5.76%	5.67%	5.16%	4.92%	6.28%	9.69%	4.50%	6.77%
$500,000	4.70%	6.01%	6.44%	5.87%	5.15%	5.41%	7.54%	10.28%	5.31%	8.03%
$5,000,000	4.95%	7.95%	7.53%	5.69%	5.24%	5.85%	9.63%	12.65%	8.60%	11.69%

Tax Payers Federation of Illinois. (2019). Tax Facts: Comparing Governor Pritzker's Proposed Graduated Income Tax to Other States

Myth #3 – The current tax system collects inadequate revenue because of "corporate loopholes"

- The facts:
  - Tax base erosion via exemptions, credits, and deductions is overwhelmingly from exemptions, credits, and deductions provided to individual taxpayers — not to corporations
  - 66.2% ($3.82 billion) of the total goes to individuals, 5% to charities, 19.8% to business and 9% to "other" (Source: Comptroller's FY 18 "Tax Expenditure Report")

Myth #3 – The current tax system collects inadequate revenue because of "corporate loopholes"

- The facts:
  - Two exemptions are responsible for most of the erosion of the Illinois tax base
    1. The $2.235 billion exemption for federally taxed retirement income
    2. The $1.865 billion state sales tax exemption for food and drugs
  - The largest reductions to the corporate income tax are:
    1. The Economic Development for a Growing Economy (EDGE) Tax Credit at $82 million
    2. The Research and Development Tax Credit at $34.7 million respectively.

Source: Comptroller's FY 2018 "Tax Expenditure Report"

Constitutional Amendment – Graduated Income Tax – SJRCA 0001

- On the ballot in November 2020
- Removes provisions that provide:
  - A tax on income shall be measured at a non-graduated rate, and
  - The limitation that there may be only one tax on individuals and corporations
- Provides that the General Assembly shall provide by law for the rate or rates of any tax on or measured by income imposed by the State
- Provides that the highest rate imposed on corporations may not exceed the highest rate imposed on individuals by more than a ratio of 8 to 5

Constitutional Amendment – Graduated Income Tax – SJRCA 0001

- Article XIV of the Illinois Constitution provides in pertinent part "[a] proposed amendment shall become effective as the amendment provides if approved by either three-fifths of those voting on the question or a majority of those voting in the election"

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

- Imposes graduated income tax rates on individuals, effective January 2021, if the constitutional amendment authorizing graduated rates is approved by the voters
- Corporations will be taxed at a nongraduated rate of 7.99% (10.49% w/ PPRT – 3rd highest in the nation)
- SB 687 does not establish graduated income tax rates on corporations, but if the amendment is adopted the General Assembly will have authority to impose graduated rates on corporations

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

Tax Rates for Single Filers	
Income	**Tax Rate**
$0 – $10,000	4.75
$10,001 – $100,000	4.90
$100,001 – $250,000	4.95
$250,001 – $350,000	7.75
$350,001 – $750,000	7.85
$750,000+	7.99 (on the entire net income)

Keep in mind: Personal Property Replacement Tax of 2.5% for traditional corporations and 1.5% for pass through entities is added to the total rates for employers

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

Tax Rates for Joint Filers	
Income	**Tax Rate**
$0 – $10,000	4.75
$10,001 – $100,000	4.90
$100,001 – $250,000	4.95
$250,001 – $350,000	7.75
$350,001 – $750,000	7.85
$1 million +	7.99 (on the entire net income)

Keep in mind: Personal Property Replacement Tax of 2.5% for traditional corporations and 1.5% for pass through entities is added to the total rates for employers

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

- Summary of legislation:
  - Marginal tax rate higher than current rate at above $250,000
  - Single Taxpayers with income over $750,000 pay the top rate – 7.99% - on all income
  - Joint filers with income over $1M pay the top rate – 7.99% - on all income
  - Corporate rate increased to 7.99%
  - New child tax credit – income-based phase out

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

- No indexing of the tax brackets – for inflation
- Every year there will be a "stealth" tax increase based on inflation
- Business owners who operate as partnerships and Subchapter S corporations will continue to pay tax at the entity level – the replacement tax, and be subject to higher rates on their income at the individual level

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

- Taxes are increased on approximately 57,000 taxpayers, plus corporations
- Other taxpayers receive a modest tax cut totaling $693 million
- Taxes on individuals increase $3.761 billion
- Corporation taxes increase $332 million
- Designed to raise net new revenues of $3.4 billion

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A Graduated Income Tax Will Make it Easier to Raise Taxes

- Governors, of both parties, and Illinois legislators find it impossible to refrain from adopting new tax credits and exemptions
- Even in the face of the state's budget crisis, the General Assembly enacted additional individual tax credits, including the Invest in Kids Scholarship Tax Credit Program ($75 million), a new Natural Disaster Income Tax Credit (enacted in 2018 and expanded in 2019), a new tax credit allowing teachers to claim up to $250 in deductions for supplies, and an increase to the Education Expense Credit.

Graduated Income Tax Legislation – SB 687 – P.A. 101-0008

- The corporate tax rate will be 3^{rd} highest in the country – only below Iowa and New Jersey and Iowa's rate is scheduled to decline
- Pass-through income will be taxed at the 4^{th} highest rate after – California (13.3%), Oregon (9.9%) and Minnesota (9.85%)

Source: Tax Foundation – "Twelve Things to Know about the 'Fair Tax for Illinois'"

A Graduated Income Tax Will Make it Easier to Raise Taxes

- If the constitution is amended when the Governor and the General Assembly want more revenues to fund additional spending, where will they go for that additional revenue?
- They can continue to go after the "rich"
- How many times and to what extent the state can raise the income taxes on those taxpayers and corporations?

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A Graduated Income Tax Will Make it Easier to Raise Taxes

- The unavoidable truth: There aren't enough "rich" people and corporations to pay for everything. The facts:
  - According to the Governor's numbers, there are around 57,000 income tax returns out of a total of 6.225 million returns with net income over $500,000.
  - That group of 57,000 taxpayers would pay $3.35 billion of the $3.76 billion in new revenues under the Governor's plan.
  - That amount is generated by an increase in the top rate and requiring filers at the top rate to pay tax at the top rate on all income – a flat rate tax on those filers.

A Graduated Income Tax Will Make it Easier to Raise Taxes

- The graduated income tax proponents are taking the easy way out
- It is easier to propose amending the constitution to authorize a graduated income tax to tax a small minority of the successful, than to conduct a detailed review of the current tax system and evaluate the efficacy of some of the items that have contributed to base erosion – under the income tax, the sales tax and the property tax.
- Such an effort is more politically difficult for the proponents than taxing the "rich"

Illinois Looks to… *Connecticut*?

- Connecticut (1996) – the last state to adopt a graduated income tax
- Since its enactment, income tax rates have increased, outmigration continues, proposals to implement new bracket, a tax on capital gains, and more!
- Meanwhile, Colorado recently rejected a graduated income tax in 2018 election (Amnd. 73)
- Texas will ask voters in 2020 election if there should be a BAN on income taxes (Prop. 4)
- Kentucky recently switched from a graduated income tax to a flat tax in 2018
- North Carolina made the switch in 2013
- Utah also made the switch in 2008
- Neighboring states of Indiana, Iowa, Kentucky, and Missouri have all cut income taxes in recent years

The Trust Factor

- 2016 Safe Roads Amendment (aka Lock Box Amendment): 79% Approved (67% of those approving in election)
- Crux of the argument in favor of Lock Box? Lack of trust from Illinois politicians
- Crux of the argument in favor for graduated income tax? Trust us!

The Rates Keep Going Up

- Two income tax increases in one decade
  - 2011: 66% Income Tax Increase
  - 2017: 32% Income Tax Increase
- Gradated income tax rates already on the rise – initial top rate on individuals was 7.95 but was increased to 7.99 in a matter of weeks
- Forget the proposed rates, what will the rates be 5, 10, 15 years from now?

Next Steps

- Visit our **Graduated Income Tax Resource Center** at www.ILChamber.org/graduated-income-tax for more information
- **Sign our petition** in opposition to the graduated income tax and receive updates
- **Communicate with others** on the many pitfalls
- And most importantly, **VOTE NO**

Questions?

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