CTBA | Center for Tax and Budget Accountability

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Illinois Budget and Fair Tax

THURSDAY, AUGUST 20, 2020; FAIR TAX DEBATE

Presented by:
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and Arthur Rubloff Endowed Professor of Public Policy at Roosevelt University

What Does The State Spend On?

FY2021 General Fund Budget

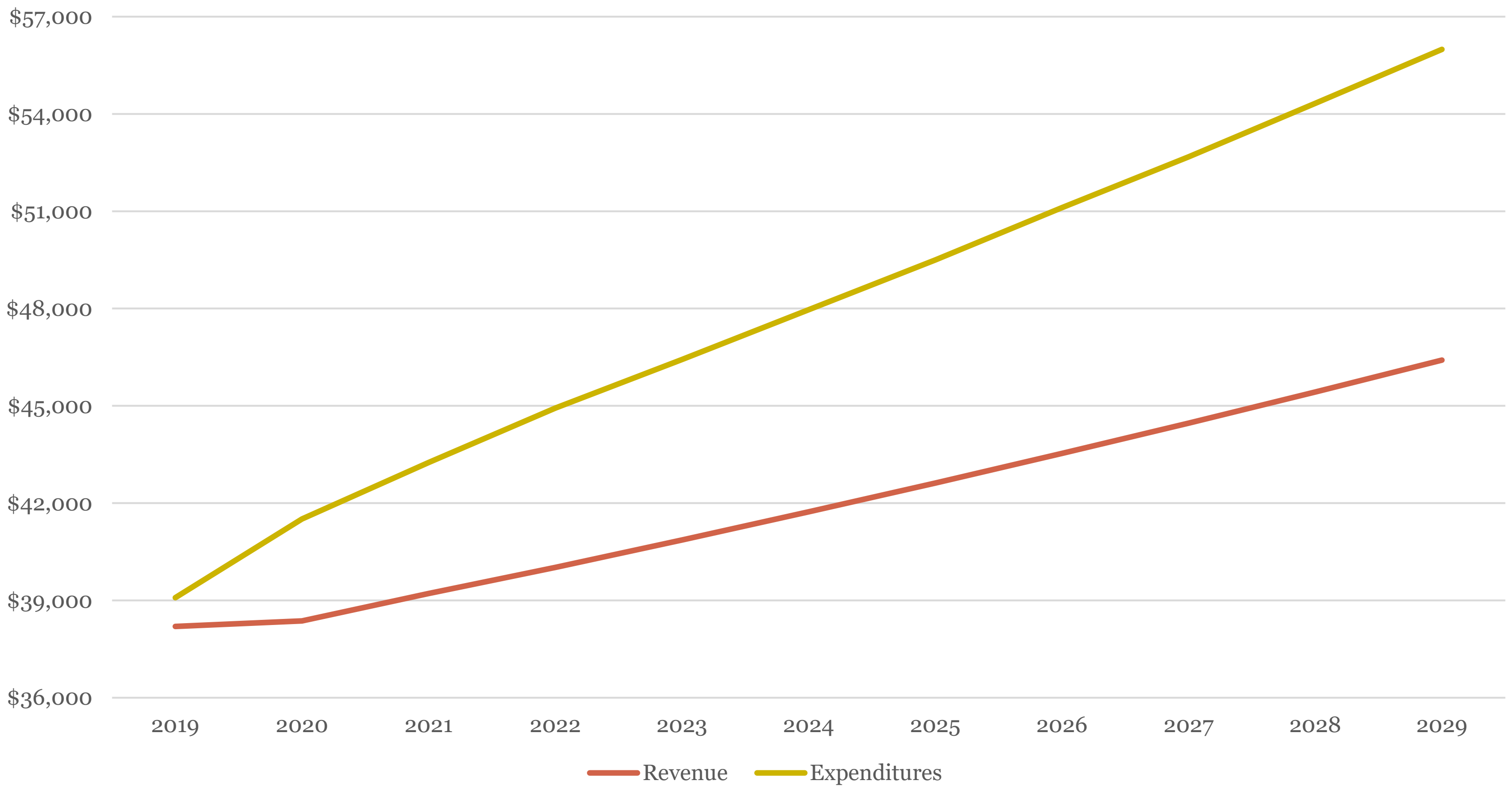
Category	Appropriation (in millions)
1. Net General Fund Appropriations — After Unspent	**$42,934**
2. Total Hard Costs	$14,883
Debt Service (Pension & Capital Bonds)	$1,706
Pension Contributions	$9,039
Other Statutory Transfers Out	$2,166
Group Health Insurance	$1,922
3. General Fund Service Appropriations (Gross)	**$29,163**
Healthcare (including Medicaid)	$8,171
Early Childhood Education	$544
K-12 Education	96% $8,352
Higher Education	$1,943
Human Services	$6,915
Public Safety	$1,909
Other	$1,329
Unspent Appropriations	($1,062)
4. Net General Fund Service Appropriations	**$28,101**

Sources: CTBA analysis of FY 2021 Enacted Budget & GOMB FY 2021 Budget Highlights

How Big Is the Hole Now?
FY2021 Estimated Accumulated Deficit

Step	Item	($ in millions)	
Starting Balance	**FY2021 Revenue**		**$42,995**
Step 1: Subtract	FY2021 Hard Costs	($14,883)	
equals	Revenue After Hard Costs		$28,162
Step 2: Subtract	Accumulated Deficit Carry Forward from FY2020	($8,456)	
equals	Projected Net FY2021 General Fund Revenue Available for Services		$19,706
Step 3: Subtract	Projected Net General Fund Service Appropriations after Unspent Appropriations	($28,101)	
Ending Balance	Surplus/Deficit Remaining after General Fund Service Spending		**($8,395)**
	One-time borrowing to cover spending in FY2021		**($5,000)**
Projected Accumulated FY2021 General Fund Deficit			**($13,395)**
Projected Deficit as a Percentage of Net General Fund Service Appropriations			**-47.7%**

The Problem: Illinois has a Structural Deficit (Full Funding of EBF)



Source: CTBA analysis of COGFA figures. Assumes expenditures keep pace with inflation and funding of the Evidence Based Formula as required under P.A. 100-0465, a total increase of $7.4 billion (on a fully inflation-adjusted basis in FY2018 dollars) by FY2029 (which totals $9.17 billion in FY2029); assumes revenues grow at historic rates, and assumes no change in law.

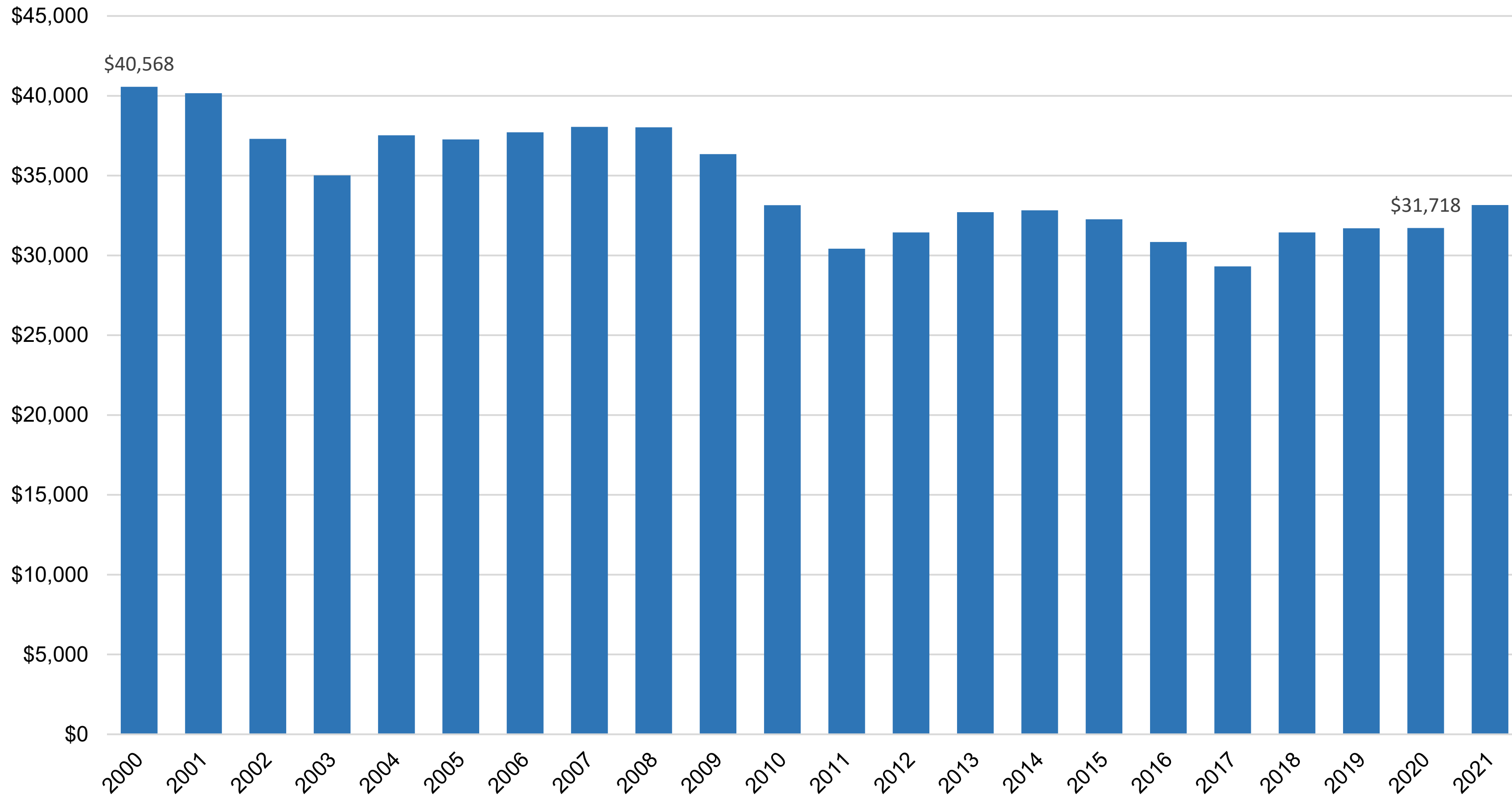
Did Spending Cause the Problem?

General Fund Spending on Current Services, FY2000 Compared to FY2021 ($ Millions)

Category	FY2000 Enacted General Fund Budget (Nominal)	FY2000 Enacted General Fund Budget (Adj for Inflation & Population)	FY2021 Enacted General Fund Budget	$ Difference (ECI and Pop Growth Adjusted)	% Change
K-12 Education	$4,674	$8,238	$8,352	$115	1.39%
Early Childhood Education	$170	$300	$544	$244	81.48%
Higher Education	$2,152	$3,793	$1,943	($1,850)	-48.77%
Healthcare	$5,022	$10,000	$8,171	($1,829)	-18.29%
Human Services	$4,599	$8,105	$6,915	($1,190)	-14.68%
Public Safety	$1,350	$2,379	$1,909	($471)	-19.78%
Net General Fund Service Appropriations	$20,064	$35,362	$28,101	($7,260)	-20.53%

Source: CTBA Analysis of FY2020 enacted budget and SB264

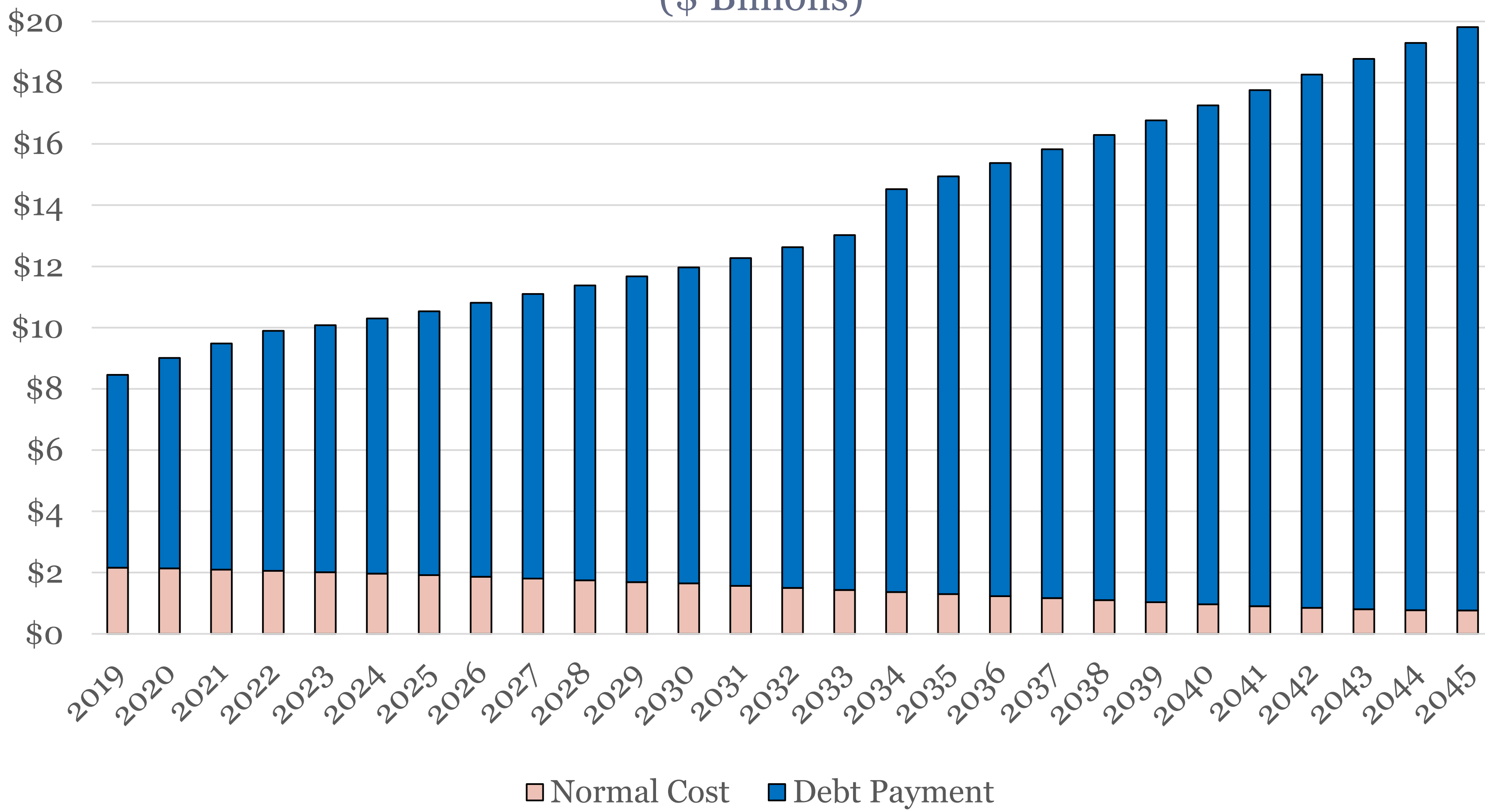
Total General Fund Revenue FY 2000 – FY 2021 ($ millions), Inflation-adjusted Using 2020 Dollars— With Income Tax Rates Held Constant to FY 2000 Levels



Source: : CTBA Analysis using historical revenue data from Commission on Government Forecasting & Accountability and Governor's Office of Budget & Management.

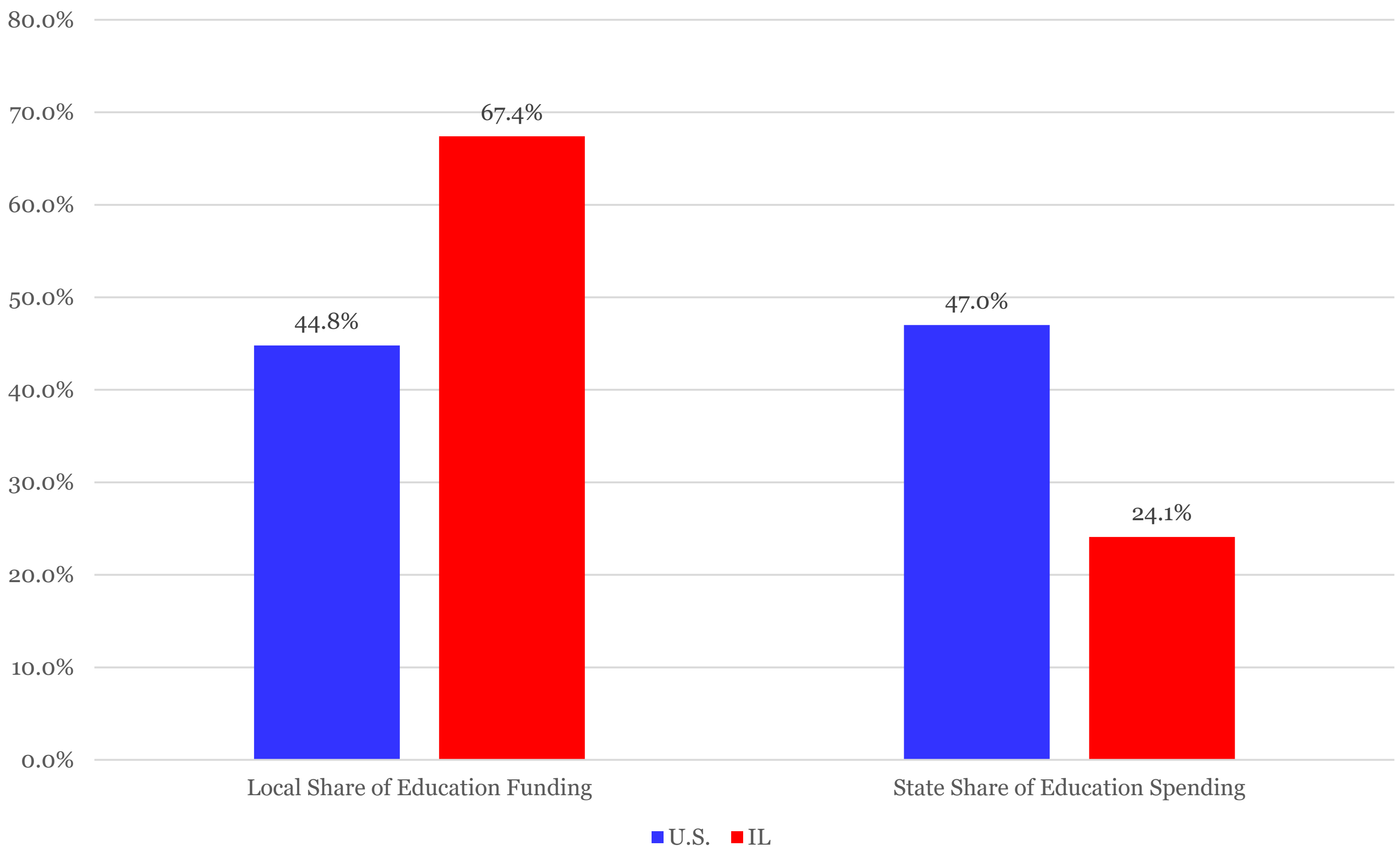
The Pension Ramp – Which Is a Debt Structure Problem: Normal Cost of Benefits Not the Driver

($ Billions)



Source: State pension funds actuarial valuations

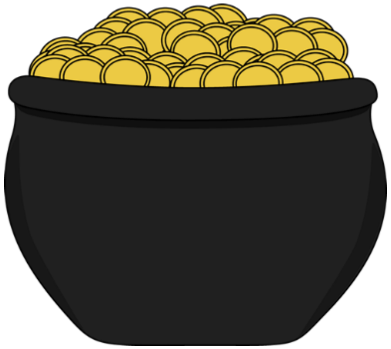
Local and State Share of Education Funding Spending, FY2016



BY FY2019, the Local Share of Education Funding in Illinois decreased to just 66%. Last updated National Data is for FY2016.

Source: NCES Digest of Education Statistics, Table 235. 20; Illinois Report Card Trend Data

Which Implicates Tax Policy Issue No. 1:



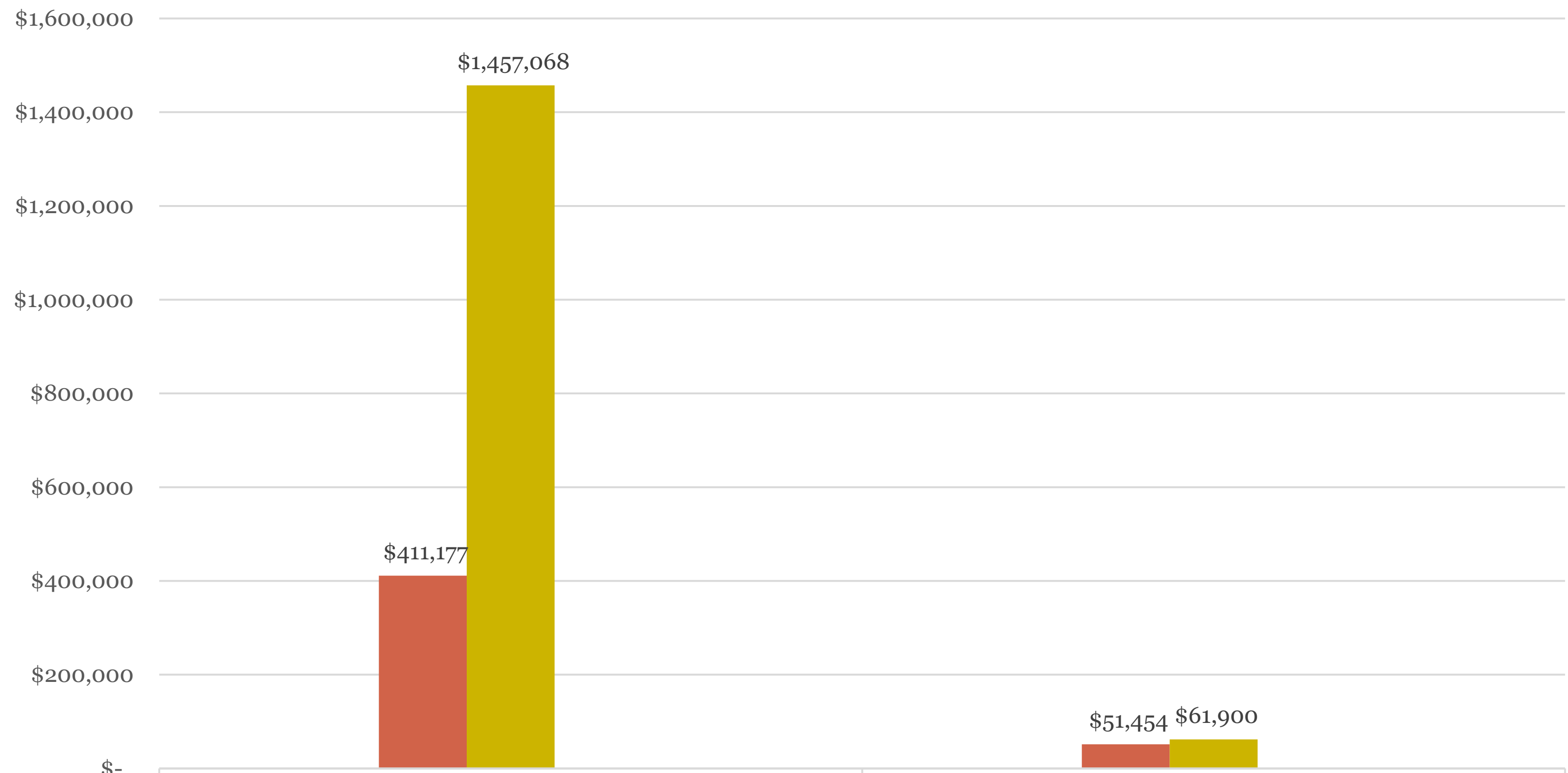
Where needs are greatest
Resources are least

Adam Smith, the father of modern capitalism, contended that for a tax system to be fair it has to be progressive

- **According to Smith:**

"The subjects of every state ought to contribute toward the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state ….[As Henry Home (Lorde Kames) has written, a goal of taxation should be to] 'remedy inequality of riches as much as possible, by relieving the poor and burdening the rich.'"

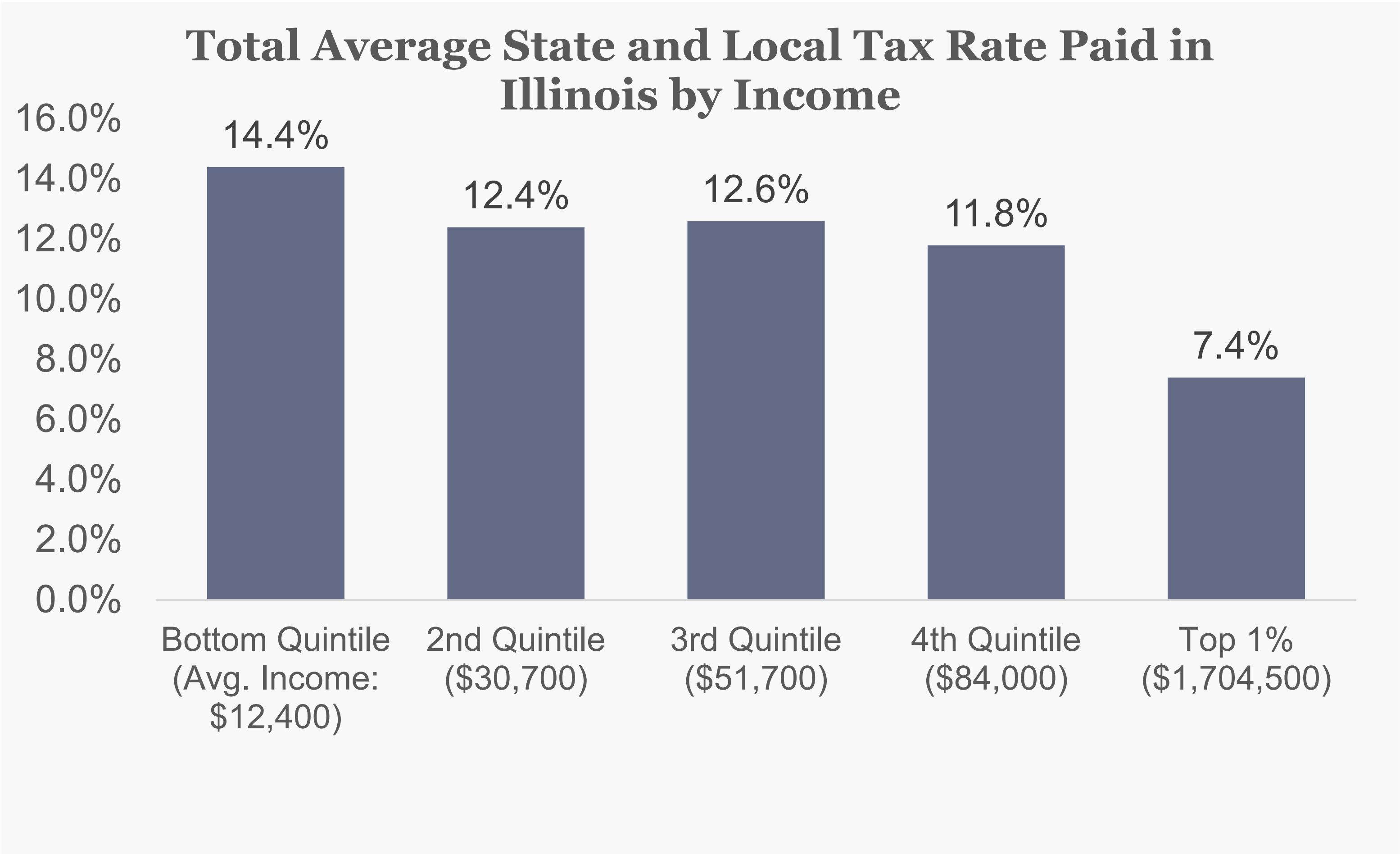
Incomes of Top 1% and Bottom 99% in Illinois, in 2017 Dollars, 1979 to 2017



	Top 1%	Bottom 99%
1979	$411,177	$51,454
2017	$1,457,068	$61,900
% Growth	254%	20%

Source: CTBA Analysis of IRS Table 2. Individual Income and Tax Data, by State and Size of Adjusted Gross Income, Tax Year 2017.& 1979 IRS SOI Report

The Illinois Tax System is Currently the Opposite Of Progressive



Source: ITEP, "Who Pays?" 6th edition, 2018.

Fair Tax Graduated Rate Structure

Marginal Rate	Income Bracket (Single)	Income Bracket (Joint)	Percent of Taxpayers
4.75%	$0-$10,000	$0-$10,000	27.2%
4.90%	$10,001 - $100,000	$10,001- $100,000	58.9%
4.95%	$100,001 - $250,000	$100,001- $250,000	11.1%
7.75%	$250,001 - $350,000	$250,001- $500,000	1.9%
7.85%	$350,000- $750,000	$500,001- $1,000,000	0.6%
7.99% *	$750,001+	$1,000,001+	0.3%

**Earned Income over $750K (single)/$1M (joint) is not subject to marginal rate and will be taxed at flat rate of 7.99% on all income*

Source: CTBA analysis of P.A. 101-0008 and IDOR Individual Income Tax Data

The "Fair Tax" Generates Needed Revenue, Shifts Tax Burden to the Top and has Rates within Midwest Range

- The Fair Tax Proposal:
  - Cuts taxes for 97 percent of taxpayers—only the top 3 percent see an increase
  - Raises $3.6 billion—pre COVID-19
  - Has a top rate of 7.99%—compared to
    - Minnesota —9.85% @ $163,890
    - Iowa — 8.53% @ $71,910
    - Wisconsin — 7.65% @ $258,950

Raising the Income Tax Won't Harm the Economy

- A rigorous 2012 study commissioned by the U.S. Small Business Administration (SBA) found:
  - " No evidence of an economically significant effect of state tax portfolios on entrepreneurial activity."

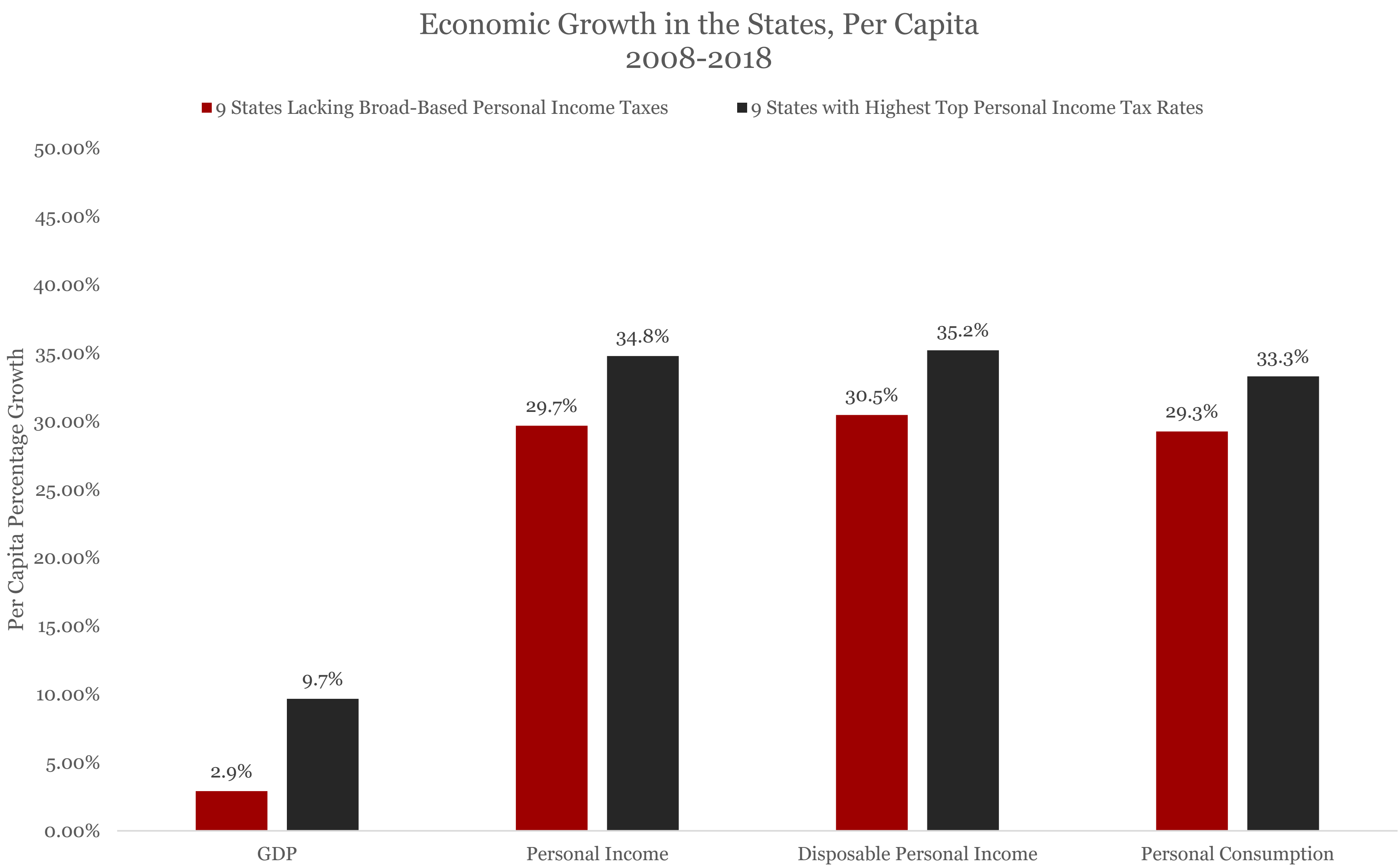
    Can State Tax Policy be Used to Promote Entrepreneurial Activity, Small Business Economics, 2012.
  - The Harry S. Truman Institute @ University of Missouri found that when benefit of a tax break is measured against the economic loss generated by spending cuts—there is always a NET ECONOMIC LOSS.
  - The CBO found no correlation between tax policy & job creation. . . . Private sector demand is what counts.

Two Recent Examples:

- Kansas
  - Cut top personal income tax rate from 6% to 4.5% in 2012
  - Projected to reduce revenue by $920 million in FY2017
  - Income tax as share of state revenue fell from 50% to 40%

- Minnesota
  - Mark Dayton inherited a
    - $6.2 billion deficit
    - 7% unemployment
    - Only 4,000 new jobs prior 7 years
  - So he raised top income tax rate from 7.85% to 9.85%, and 4 years later
    - 172,000 new jobs
    - 3.9% unemployment
    - $1.2 B surplus

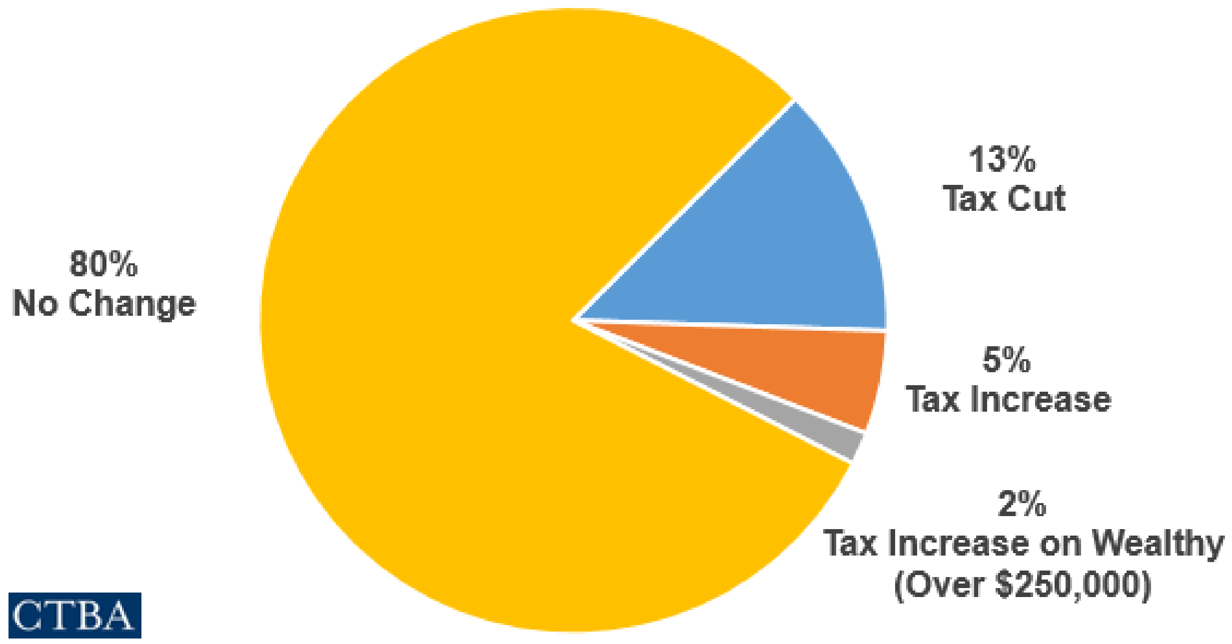
Graduated Income Taxes and the Economy



Source: CTBA Analysis of Bureau of Economic Analysis data

States with Graduated Rate Income Tax Structures are Less Likely to Increase Taxes on the Middle Class

Since 2003, states with GRIT had a roughly 13 percent likelihood of cutting taxes — versus just a five percent likelihood of increasing them on the middle class.



Source: CTBA analysis of Tax Foundation data

Oh, & When Illinois Raises Taxes

- People won't run screaming out of the state:
  - Since 1925, IL has had net outmigration every year except one
  - Illinois' outmigration rate actually declined in 2011, the first year of the temporary tax increase
  - A greater % of the populations of IN and WI moved into IL since the temporary tax increase, than vice-versa

For More Information

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