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The Progressive Income Tax Referendum: What Illinoisans Need to Know

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PROPOSED AMENDMENT TO THE ILLINOIS CONSTITUTION

That will be submitted to the voters
November 3, 2020

This pamphlet includes
EXPLANATION OF THE PROPOSED AMENDMENT;
ARGUMENTS IN FAVOR OF THE AMENDMENT;
ARGUMENTS AGAINST THE AMENDMENT;
FORM OF BALLOT

Published as set forth in compliance with the Illinois Constitutional Amendment Act (5 ILCS 20).

Jesse White • Secretary of State

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To the Electors of the State of Illinois:

The Illinois Constitution establishes a structure for government and laws. There are three ways to initiate change to the Illinois Constitution: (1) a constitutional convention may propose changes to any part; (2) the General Assembly may propose changes to any part; or (3) a petition initiative may propose amendments limited to structural and procedural subjects contained in the Legislative Article. The people of Illinois must approve any changes to the Constitution before they become effective. The purpose of this document is to inform you of proposed changes to the Illinois Constitution and provide you with a brief explanation and a summary of the arguments in favor of and in opposition to the proposed amendment.

Proposed changes in the existing constitutional amendment are indicated by underscoring all new matter and by crossing with a line all matter which is to be deleted.

PROPOSED AMENDMENT
TO SECTION 3 OF ARTICLE IX
OF THE ILLINOIS CONSTITUTION

ARTICLE IX – REVENUE

SECTION 3. LIMITATIONS ON INCOME TAXATION

(a) The General Assembly shall provide by law for the rate or rates of any tax on or measured by income imposed by the State. ~~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 upon corporations the highest rate shall not exceed the highest rate imposed on individuals by more than a ratio of 8 to 5.

(b) Laws imposing taxes on or measured by income may adopt by reference provisions of the laws and regulations of the United States, as they then exist or thereafter may be changed, for the purpose of arriving at the amount of income upon which the tax is imposed.

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Arguments in favor of the proposed amendment (per the Secretary of State)

- This Amendment Would Make Illinois' Tax System Fair.
    - The federal government and most states use the graduated tax system proposed in this amendment, not the unfair system currently used in Illinois.
    - Illinois' current income tax system relies on taxes from middle and lower income earners, while a graduated system would lower that burden and fund critical programs such as education and human services.
    - After the COVID-19 pandemic, we need to do all we can to help the economy and middle-class and working people.

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Arguments against the proposed amendment (per the Secretary of State)

- The Amendment gives the Legislature power to increase taxes on any group of taxpayers with no limits and no accountability and without any requirement to use the additional revenue to fund essential needs such as healthcare, education or public safety.
- Taxes and spending are out of control. The Legislature should not be allowed to keep raising taxes until they get their spending under control.
- In the wake of the COVID-19 pandemic, now is the worst possible time for a massive tax increase.

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Background

- **Senate Bill 687 (2019)**
- Gov. J.B. Pritzker (D) signed Senate Bill 687 (SB 687), which was designed to enact a graduated income tax, on June 5, 2019. SB 687 would not go into effect unless voters approve SJR 1 on November 3, 2020. The Illinois House of Representatives passed the final version of SB 687 on May 30, 2019, in a vote of 67-48. The Illinois State Senate passed the final version of SB 687 on May 31, 2019, in a vote of 37-20.[21]
- SB 687 would change the state's income tax from a flat rate to six graduated rates beginning on January 1, 2021. The following table illustrates the graduated rate under SB 687 for single and joint filers

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Source: Ballotpedia (https://ballotpedia.org/Illinois_Allow_for_Graduated_Income_Tax_Amendment_(2020))

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Legislated personal income tax rates should the constitutional amendment pass

Up until now about $100 million has been pledged for spending for or against the amendment. Almost all of this money has come from either Gov. Pritzker ($56 million, he is in favor) or Ken Griffen ($48 million, he is opposed)

Illinois SB 687 (2019) income tax rates				
Brackets	Single		Joint	
	Income	Rate	Income	Rate
1	Up to $10,000	4.75% marginal rate	Up to $10,000	4.75% marginal rate
2	$10,001—$100,000	4.90% marginal rate	$10,001—$100,000	4.90% marginal rate
3	$100,001—$250,000	4.95% marginal rate	100,001—$250,000	4.95% marginal rate
4	$250,001—$350,000	7.75% marginal rate	$250,001—$500,000	7.75% marginal rate
5	$350,001—$750,000	7.85% marginal rate	$500,001—$1,000,000	7.85% marginal rate
6	Annual income of $750,001 or above	7.99% on net income instead of marginal rates	Annual income of $1,000,000 or above	7.99% on net income instead of marginal rates

Source: Illinois General Assembly, "Senate Bill 687," accessed June 11, 2019

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Positive (as opposed to normative) discussion of graduated versus flat rate income taxes

- Fairness
  - It is hard to talk about “fairness” in a positive way, but we can talk about “progressivity”
  - Note that a flat rate tax can be “progressive”
  - A tax is said to be “progressive” if the share of income paid in tax (i.e. the average tax rate) rises with income.

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Fairness

- Which systems is most fair?
- I have no objective (or scientific) way to determine this.
- Many people believe that taxes are fairer if the amount of tax due:
  - Increases with the ability to pay and
  - Increases with the benefits of government

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Potential objections to a graduated rate system

- High income people might leave the state if we increase their tax rates.
- This would give legislators more flexibility and they might use that to raise tax rates on the middle class.

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Potential objections to a graduated rate system

- Five states (California, Connecticut, Maine, New Jersey, New York) and DC have "millionaires" taxes.
- Also lawmakers in Massachusetts, Maryland, Wisconsin, Hawaii, Oklahoma, Vermont have proposed various forms of tax increases on high earners, according to the National Conference of State Legislatures.
- Studies of NJ, California and nationally suggest little migration as a result of their millionaire taxes.
- One California study suggests somewhat bigger effects.
- Several studies suggest significant migration of professional athletes, star scientists and others due to high regional income taxes.

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Potential objections to a graduated rate system

- This argument is examined in my recent (short) paper. How often do graduated and flat-rate states change their tax rates? By David Merriman October 7, 2020
- https://igpa.uillinois.edu/sites/igpa.uillinois.edu/files/reports/Merriman_TaxRateChanges_100720.pdf
- Bottom line result: Since 2002 (when my data starts) there has been almost no difference in the frequency, amount or direction of tax changes in flat and graduated rate states.

(see next slide)

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Overall

Any Rate Change	Structure		Total
	Flat	Grad-uated	
No	126 82.24	498 84.15	624 83.26
Yes	27 17.76	94 15.85	121 16.24
Total	153 100.00	592 100.00	745 100.00

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Conclusion

The proposed constitutional amendment on November’s ballot would move Illinois from a flat rate to a graduated rate system which is a change unlike any that a U.S. state has made since at least 2002. The full implications of this change for tax-setting behavior are difficult to predict. However, examination of the recent experience of other U.S. states finds little difference in the frequency of tax rate changes in general, and whether tax rate increases occur in particular, in states with graduated and flat rate tax systems.

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Thank You

- **David Merriman**
  James J. Stukel Presidential Professor of Public Administration
  Urban Planning and Public Affairs
  Senior scholar, University of Illinois Institute of Government and Public Affairs
  dmerrim@uic.edu
- **Christopher Mooney, PhD**
  W. Russell Arrington Professor of State Politics
  Liberal Arts and Sciences
  Senior scholar, University of Illinois Institute of Government and Public Affairs
  cmoon1@uic.edu

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Revenue Implications of Alternative Personal Income Tax Structures in Illinois

By David F. Merriman, Kenneth Kriz, Patricia Byrnes, Glen Cassidy

May 7, 2019

Report discusses whether high income people might leave the state if we increase their tax rates (among other topics).

Conclusion: “the elasticity of taxable income (or ETI) is a measure of the relationship between tax rates and taxable income…the best available estimates …[suggest that]the [top] US marginal.. rate is far from the top of the Laffer curve [i.e. the rate at which increases in the rate would cause revenue to fall.] However...[t]here is much evidence to suggest that the ETI is higher for high-income individuals…there is a voluminous, informative and growing literature on the relationship between income tax rates and taxable income. While there is a great deal of uncertainty, the best available current estimates show that, for the US as a whole, increases in tax rates substantially increase tax revenue and, at least in the short run, cause at most only modest declines in the tax base.

However, experts caution that the impact of any particular tax-policy change may vary depending upon the circumstances. We know that past increases in Illinois’ (flat) income tax rate have resulted in substantial increases in revenue but have probably resulted in somewhat diminished economic activity. Research about increases in taxes on very high income households shows that they have little or no impact on the location of those households in general but that they may have more impact on particular types (star scientists or professional athletes) of very high-income individuals.

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Three tax systems

- Flat tax with no standard deduction
  - Tax=tax rate* income for example Tax=0495*income
- Flat tax with standard deduction
  - Tax=tax rate* (income-standard deduction) for example Tax=.060* (income-100,000)
- Progressive (graduated rate) tax
  - Marginal tax rate varies with income. For example
  - **
  - *   Income   Rate
  - *1 Up to $10,000   4.75% marginal rate
  - *2 $10,001—$100,000   4.90% marginal rate
  - *3 $100,001—$250,000   4.95% marginal rate
  - *4 $250,001—$350,000   7.75% marginal rate
  - *5 $350,001—$750,000   7.85% marginal rate
  - *6 Annual income of $750,001 or above   7.99% on net income instead of marginal rates
  - **
  - This system could be combined with standard deduction.

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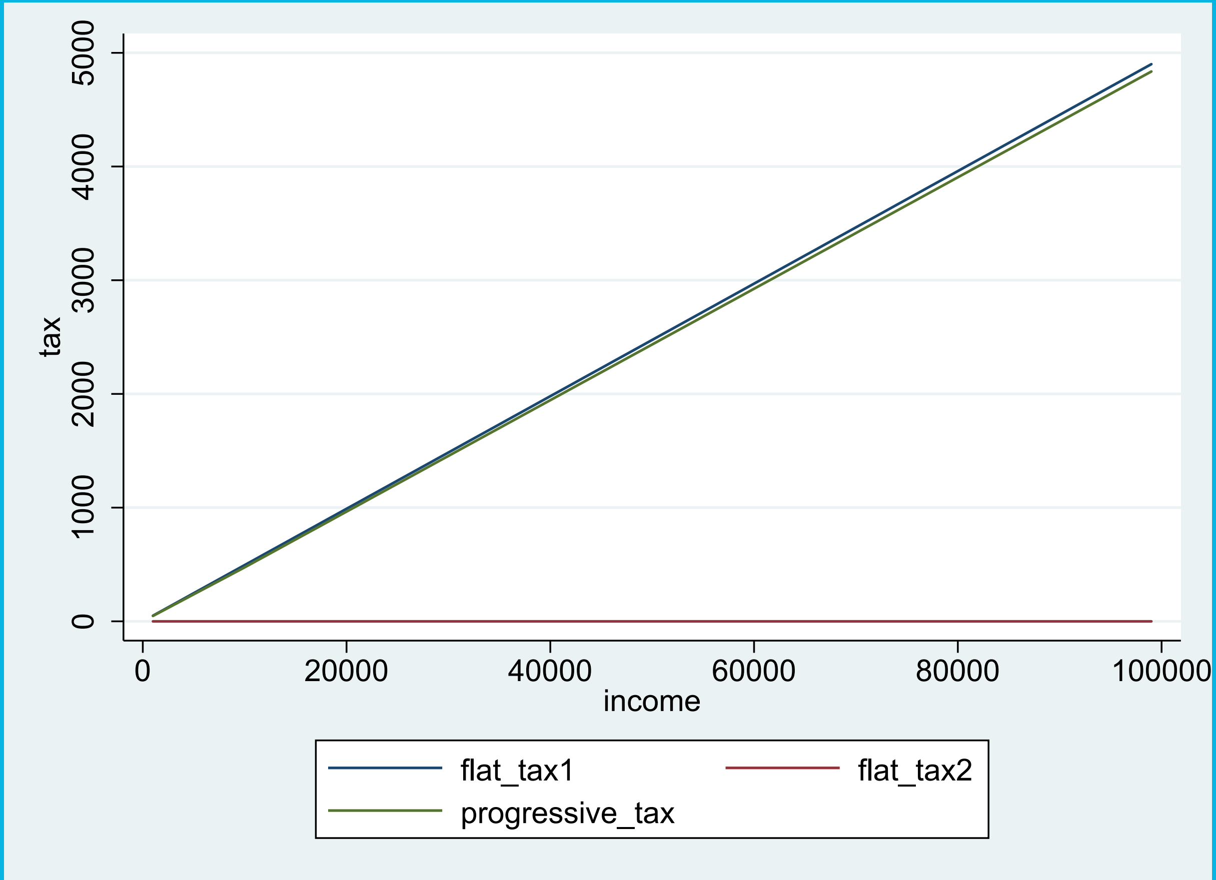
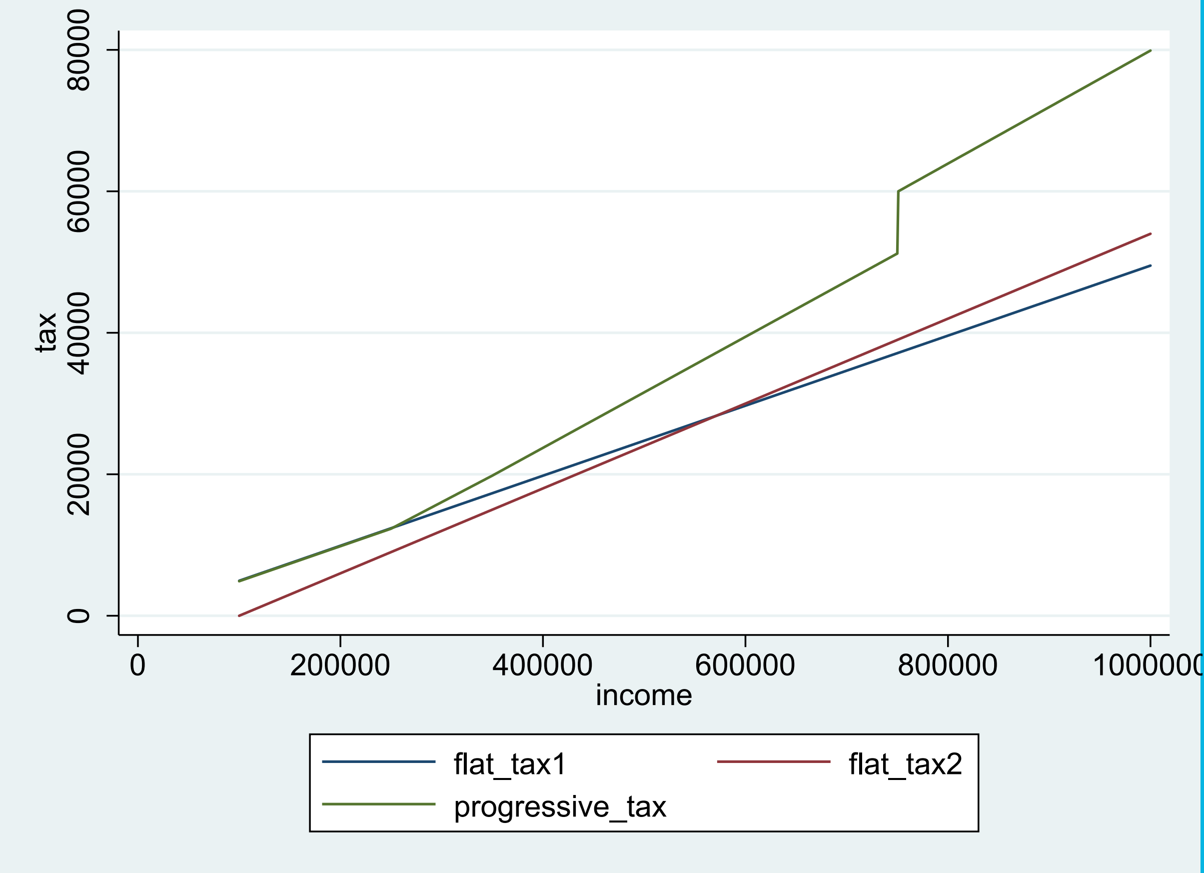
For incomes below $100K
The flat tax system with no standard deduction is very similar to the progressive tax system.

Of course, under the flat tax system with a $100K deduction everyone with incomes of less than $100K would pay not income tax.



For incomes above $100K the tax payments of the flat tax system gradually rise and eventually (at about $600K) are greater than the tax payments with the flat tax system with a lower rate but no standard deduction.

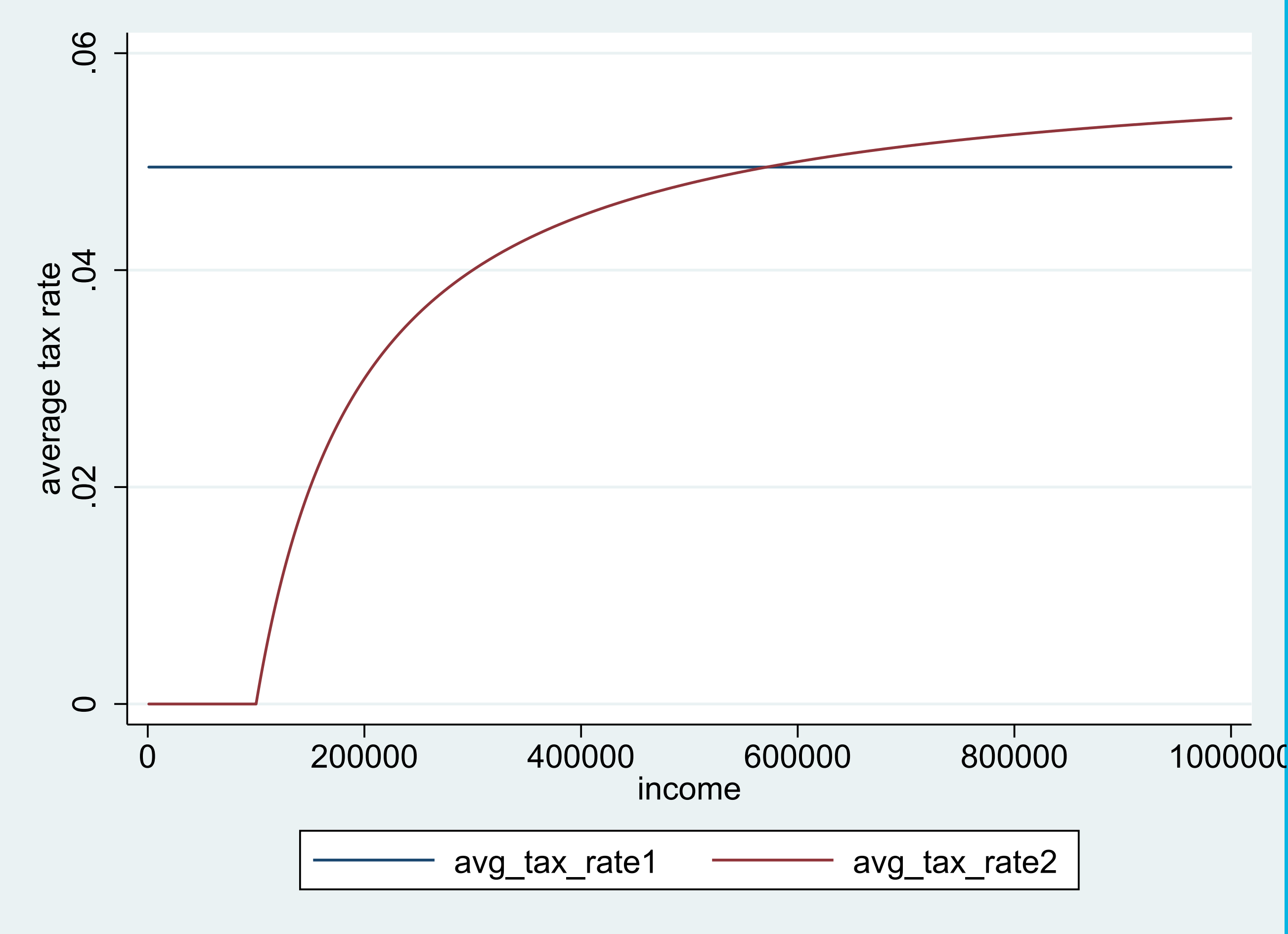
The tax due under the graduated rate system becomes significantly higher than the tax due under the other two systems once income exceeds $300K or so.



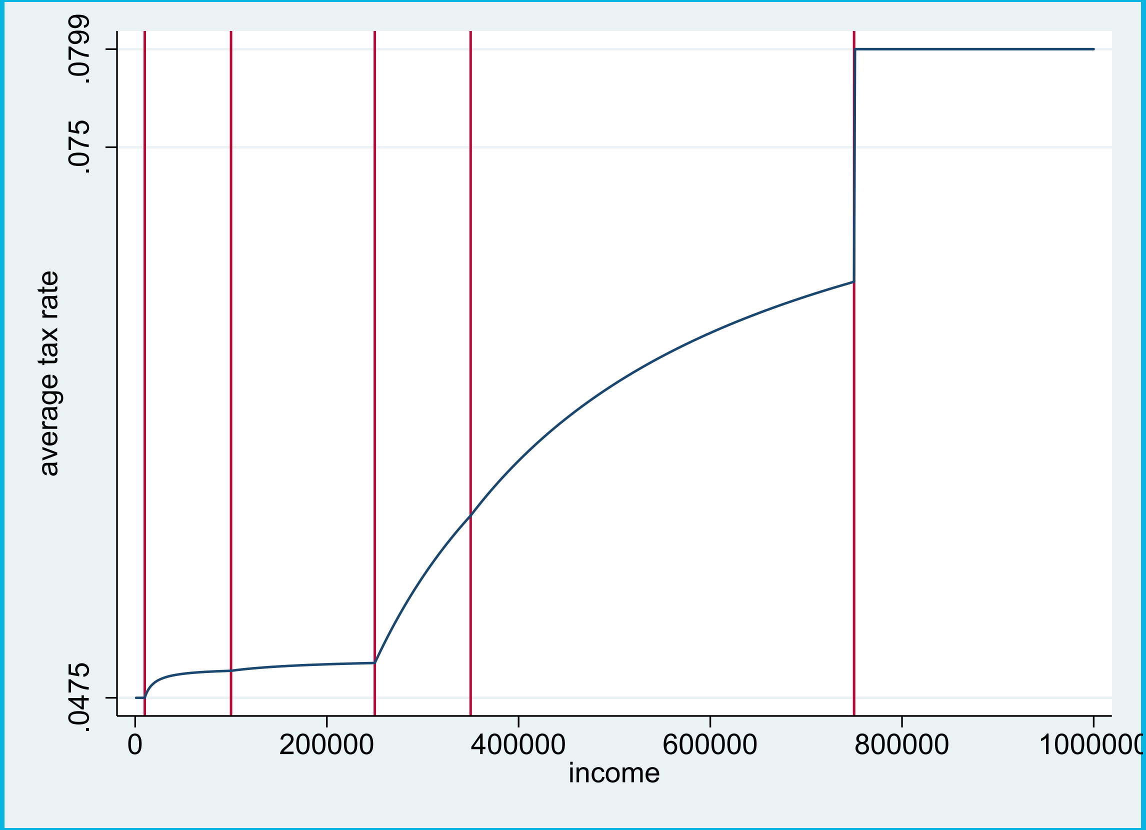
The two flat tax systems have very different patterns of average tax rates.

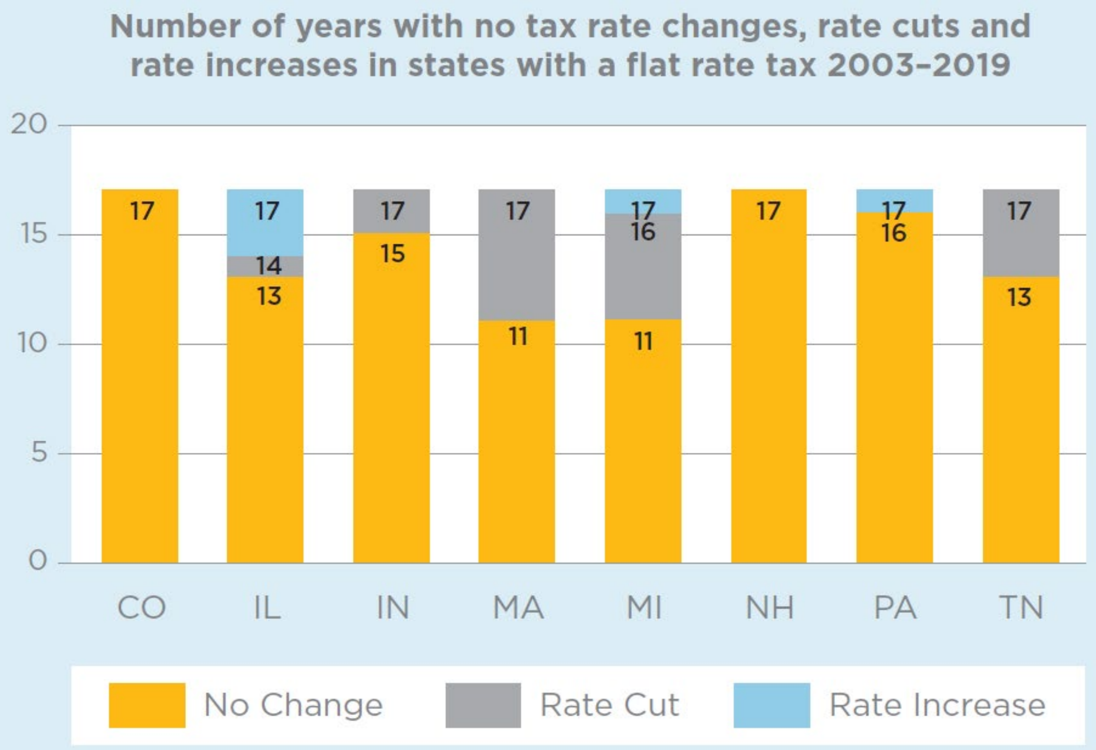
The flat tax system without a standard deduction has a constant average tax rate. The tax is always 4.95% of income.

The average tax rate of the flat tax system with a $100K deduction varies. For incomes below about $500K the average tax rate is less than 4.95%. However, the average tax rate grows with income.



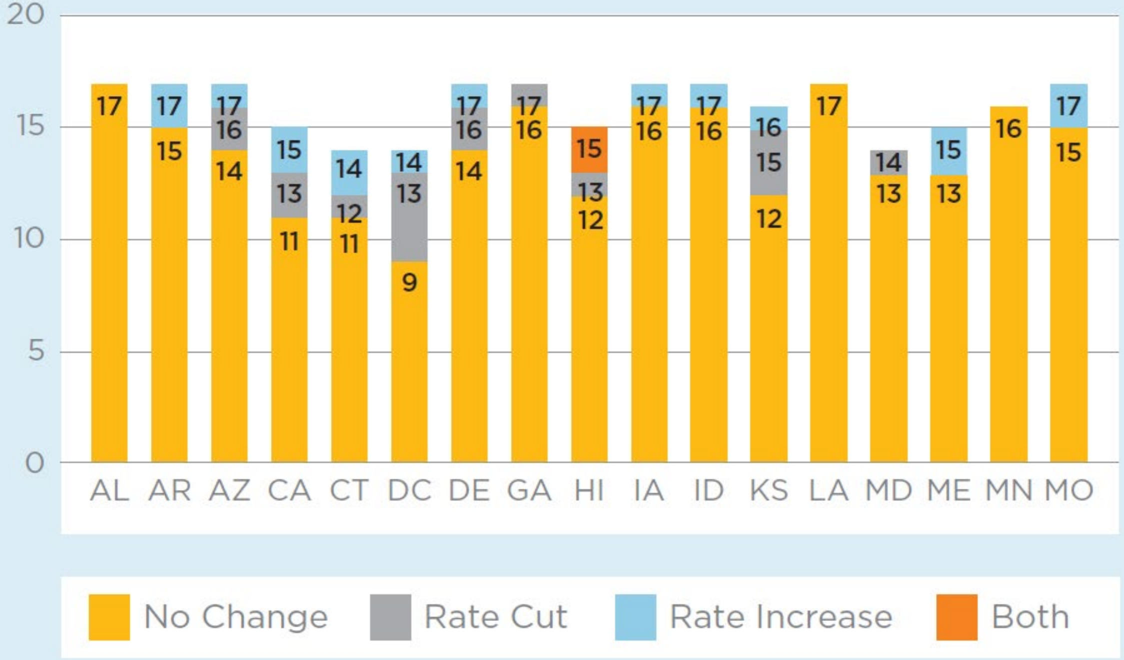
With a graduated (or progressive) rate system the average tax rate changes with income. This graph shows the average tax rate as a function of income under the tax system that will take effect if the proposed amendment to Illinois' constitution passes.





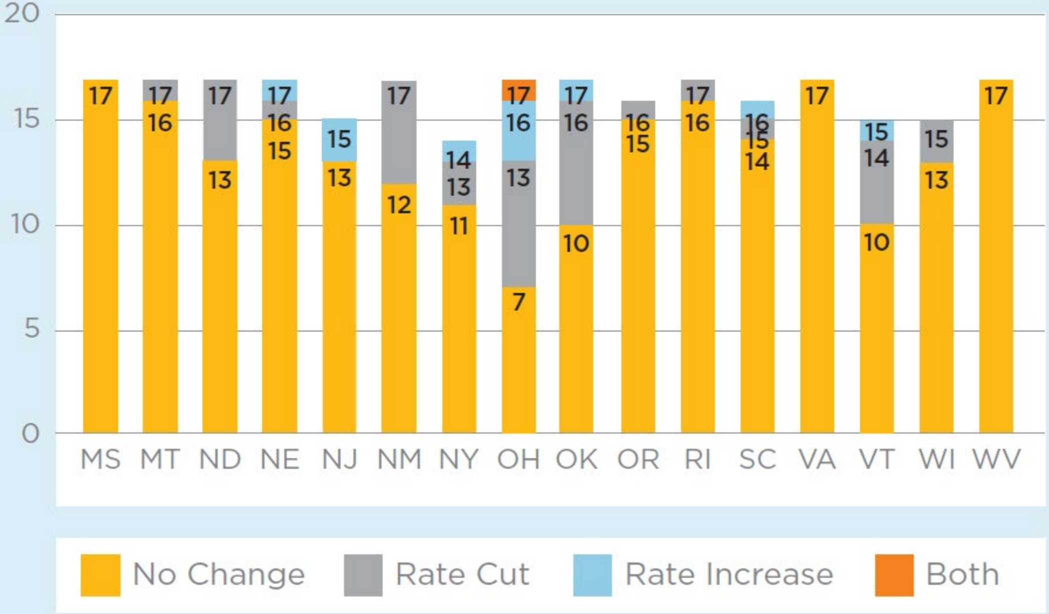
Source: Taxfoundation.org and state websites.
Number in bars indicate cumulative total number of years.

Number of years with no tax rate changes, rate cuts and rate increases in states with a graduated rate tax 2003–2019



Source: Taxfoundation.org and state websites. Numbers in bars indicate cumulative total number of years. State-years when number of tax rates changed are omitted. KY, NC and UT switched from graduated to flat rate systems during these years and are omitted.

Number of years with no tax rate changes, rate cuts, rate increases and both cuts and increases in states with a graduated rate tax 2003–2019



Source: Taxfoundation.org and state websites. Numbers in bars indicate cumulative total number of years. State-years when number of tax rates changed are omitted. KY, NC and UT switched from graduated to flat rate systems during these years and are omitted.