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Governor Blagojevich's Gross Receipts Tax Plan Represents Largest State Tax Increase This Decade

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During his recent State of the State Address, Governor Rod Blagojevich of Illinois proposed the "Illinois Tax Fairness" plan. While the plan would phase out the corporate income tax over four years, it would also institute a new gross receipts tax on businesses which is forecast as a net tax increase of $6 billion.

The new tax would be problematic not only because of the additional tax burden it would impose, but also because of the way in which it would do so. Gross receipts taxes are one of the most economically damaging ways for states to extract revenue, and economists from all ends of the political spectrum are nearly unanimous in their opposition to them.[1]

In addition to the gross receipts tax, Governor Blagojevich proposed a new payroll tax on selected companies,[2] bringing the total cost of the plan to $7.1 billion for Illinois taxpayers.[3] If enacted, the tax increase would consume an average of $550 per person in Illinois and, as illustrated in Table 1, would represent the largest single-year state tax increase this decade.

Table 1. Top Ten State Tax Increases as a Percentage of State GDP, FY 2000-2007

Rank	State	Tax Increase as a Percentage of State GDP[4]	Fiscal Year
N/A	Illinois*	1.227†	2008
1	Indiana	.446	2003
2	Tennessee	.432	2003
3	Idaho	.407	2004
4	New Jersey	.402	2007
5	Massachusetts	.398	2003
6	Connecticut	.354	2004
7	Ohio	.343	2004
8	New Jersey	.314	2003

9	Nevada	.300	2004
10	New Hampshire	.288	2000

*Proposed
† Assumes payroll tax is fully implemented
Source: National Association of State Budget Officials (NASBO), Tax Foundation

If enacted, Governor Blagojevich's tax plan would raise far more than other state tax increase enacted since the year 2000. The $7.1 billion tax increase would consume a full 1.227 percent of the state's economy. This is nearly three times larger than the highest enacted state tax increase of the decade, approved by Indiana lawmakers in that state's FY 2003 budget.

Measuring tax increases as a percentage of economic output is one effective way to compare the magnitude of tax hikes, but it is also important to measure tax increases as a percentage of revenue. This comparison allows us to gauge the impact of the tax increase on the budget as a whole. Table 2 lists the top ten tax increases this decade as a percentage of state general fund (SGF) revenue.

Table 2. Top Ten State Tax Increases as a Percentage of State General Fund Revenue, FY 2000-2006

Rank[5]	**State**	**Tax Increase as a Percentage of SGF Revenue**	**Year**
N/A	Illinois*	26.98	2008
1	Nevada	14.05	2004
2	New Hampshire	13.54	2000
3	Tennessee	11.75	2003
4	Nevada	10.43	2005
5	Indiana	10.08	2003
6	Idaho	8.87	2004
7	New Hampshire	7.52	2001
8	Oregon	7.50	2004
9	New York	6.20	2004
10	Ohio	6.09	2004

*Proposed
Source: National Association of State Budget Officials (NASBO), Tax Foundation

Expressed as a percentage of SGF revenue, the governor's tax increase is still significantly larger than any other state tax increase this decade. If enacted, the Blagojevich tax increase would equal 26.98 percent of state general fund revenues. That's nearly twice the size of the second highest (Nevada in 2004).

This tax increase would certainly add to the cost of living, working and investing in Illinois and would move Illinois' fiscal policy in the wrong direction, especially at a time when many other states have moved in the opposite direction by cutting taxes. Since recovering from the post 9-11 economic downturn, most states have hit a "fiscal sweet spot."[6] In fact, 46 states enjoyed revenue gains that exceeded projections and the remaining four states met projections in fiscal 2006. On average, personal income tax revenue, sales tax revenue and corporate tax revenue have all exceeded expectations. In 2006 alone, corporate income tax collections exceeded expectations by over 20 percent.[7]

This solid revenue growth has allowed many states to avoid major tax increases. Furthermore, it has given many states the opportunity to look at ways to improve the competitiveness of their business tax systems. Illinois has also enjoyed strong revenue growth due to the robust national economy. In fact, the governor's FY 2008 budget shows an increase in state general fund revenue of 4.7 billion since just FY 2006.[8] However, the governor has decided not to take advantage of this extra revenue and this opportunity to increase Illinois' competitiveness by cutting taxes as so many other states have.

If the governor successfully enacts his gross receipts tax plan, it is clear that taxpayers in the Land of Lincoln will be on the hook for the largest state tax increase of the decade.

Notes

1. For more on the negative economic impact of gross receipts taxes, see "Gross Receipts Taxes in State Government Finances: A Review of Their History and Performance" and "Tax Pyramiding: The Economic Consequences of Gross Receipts Taxes," available at http://www.taxfoundation.org/.

2. The payroll tax would be levied on businesses with 10 or more employees, who pay less than 4 percent of their payroll for health care costs.

3. The Illinois State Budget, Fiscal Year 2008, page 2-2. Available at: www.state.il.us/budget

4. Listed tax increases represent the net effect of a state's legislative action during the selected fiscal year.

5. Rankings in Table 1 and Table 2 differ due to the inherent disparity between measuring tax increases as a percentage of SGF revenue verses taxes as a percentage of the state economy. States structure their general funds with wide divergences. While this causes discrepancy between the two rankings, it is important to consider the impact of a tax increase with both measures.

6. National Association of State Budget Officials, The *Fiscal Survey of States*, December 2006. Available at: http://www.nasbo.org/

7. Ibid

8. The Illinois State Budget, Fiscal Year 2008, page 2-15

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