

## **Understanding the Tax Fairness Plan**

### **Why is the current income tax (CIT) system unfair to small businesses and individuals?**

- Many large corporations benefit from amenities provided by the state – such as an educated workforce, state roads, emergency services, airports, police protection, etc. – but do not contribute their fair share of the costs associated with those amenities.
- On average from 1997 through 2004 nearly half of all corporations that made \$50 million or more annually in Illinois sales paid ZERO income taxes. This demonstrates that the CIT is flawed and open to manipulation.

### **Why is a Gross Receipts Tax (GRT) the fairest and simplest tax system for Illinois businesses?**

- Economists since Adam Smith have agreed that, all else being equal, taxes with a broad base and a low rate are better – i.e., disrupt the economy less – than a tax with a narrow base and a high rate.
- GRT has a broad base and captures all businesses within the state's economy. This will help make the tax system more equitable by ensuring that all businesses – not just some – will have to contribute their fair share to support public services and amenities, such as education and health care.
- The GRT taxes businesses at lower rates than other taxes and with fewer rate differentials. This creates predictability for businesses because they always know what their tax rate will be and can better plan for their annual cost of doing business.

### **What are the advantages of a GRT?**

- The tax has a broad base and affects all parties within a single industry equally. Due to its broad base, a low rate can be applied, meaning companies can more easily assume the tax as a cost of doing business.
- The GRT will allow the state to capture taxes from large corporations that currently escape paying Illinois taxes but enjoy services and amenities provided by the state; in 2004, nearly 600 corporations with Illinois sales of more than \$50 million paid no income tax. Another 12,521 of the biggest corporations with sales of over \$263 billion in Illinois, on average, paid \$151 in corporate income taxes.
- GRT can generate significant additional revenue. Illinois' GRT, with rates set appropriately low for traditional Illinois businesses such as manufacturers and

retailers, and at an evenly applied low rate for service industries is expected to capture several billion dollars in new revenue (net of credits against corporate income taxes).

### **What protections are built in to the GRT?**

- Small businesses with under \$1 million in revenues will be exempt from the revised tax structure. This means that more than 75 percent of all businesses in Illinois will see no change in their taxes.
- Steps have been taken to mitigate “pyramiding” – where component parts of a finished product are taxed multiple times throughout the production cycle. Manufacturing, agricultural products, wholesale and retail trade will be taxed at an appropriately lower rate, and transactions with affiliated companies will not be subject to the GRT. The governor’s plan also excludes Illinois exports, which minimizes price pressure for goods that are sold regionally or globally.
- Some industry sectors will be exempt to help mitigate any negative fiscal consequences:
  - Insurance will be exempt from the GRT on the sale of insurance products.
  - Retail food and drug sales will not be subject to the GRT.
  - The standard tax will apply to gaming.
  - Medicaid payments to doctors and hospitals will not be subject to the GRT.

### **How does the GRT treat companies that don't make a profit?**

- The GRT, which is predictable and can easily be planned for, is treated as a cost of doing business much like any other expense that a business must account for in its operations – the water bill, the light bill, the CEO's salary and so on. There are many taxes in place that businesses are already used to planning for – property, unemployment, Social Security, utility, telephone, gas – each of these expenses are met regardless of “profit.”
- As evidence proves, taxing profits is an invitation to tax avoidance because the number can be manipulated many ways.

### **What other states have a GRT?**

- In recent years, Ohio and Texas have adopted forms of the GRT, joining Delaware, Hawaii and Washington. Similar to Illinois, the distribution of taxes on business in some of these states was becoming increasingly unfair – the tax burden relied more and more on “old” economy companies, with little consideration to businesses providing services in the new economy. According to a study performed by Ernst and Young, the 2005 imposition of a GRT in Ohio is anticipated to increase gross state product by \$5.6 billion and create 78,500 new jobs.

### **Other states have experienced favorable economic performance under the GRT:**

- **Ohio:** A state experiencing a steady decline of jobs and a struggling economy has experienced economic expansion since the GRT took effect in July 2005. One year later, Ohio's job growth rate was 12 percent higher than it was before the new tax. During this same period, the national job growth rate declined 3 percent.
- **Washington:** Washington (GRT since 1935) outperformed the U.S. economy from 1980-2000 and is a larger exporter than Illinois at half its size. The 2006 job growth rate in Washington State was sixth in the nation and double the national average.

### **Will this hurt the competitiveness of Illinois goods in the global economy?**

- No. The GRT only applies to goods sold in Illinois – exports are excluded.

### **This will take \$6 billion out of the economy. Where is the money going?**

- This money will be invested right back into Illinois. The state will invest in health care to reduce the burden on employers and families and invest in

education to ensure we have a skilled, high-quality workforce and invest in infrastructure.

**Will consumers see increased costs due to the GRT?**

- Exempting sales of retail food and retail drugs and charging lower rates for commodity sensitive economic sectors such as manufacturing, is intended to provide protection to consumers. This stands in direct contrast to an increase in sales and income taxes, which offer little or no protection for consumers.

**Won't the GRT cost jobs?**

- The experience in other states that currently use the GRT is that trends in employment levels are consistent with larger factors in the macro-economy or at the national level.