Policymakers Can Choose to Avoid Cuts to Essential Services

INTRODUCTION

Illinois is over $6 billion short of what it needs to fund schools, health care, and other services in the coming fiscal year thanks almost entirely to the 25-percent cut to income tax rates that lawmakers allowed to go into effect on January 1, 2015.

Governor Rauner has proposed to close this massive gap through damaging cuts to essential programs and services that strengthen Illinois families, children, communities, and our economy — including child care and early intervention services, K-12 education, afterschool, child protection and welfare, public health, higher education, health care, public transportation, and revenue-sharing with local governments.

Cuts have consequences. If our goal is to create a stronger future for Illinois, the worst thing we can do is weaken the public services a strong economy needs, like education, health care, transportation, and public safety.¹ Relying on cuts to balance the budget jeopardizes both past investments we have made and the foundation for future prosperity.

The good news is that devastating cuts to services are not inevitable: They are a choice.

This report highlights a broad range of available revenue options that policymakers can choose to avoid cutting areas such as services for children with epilepsy and autism, police and fire protection, and in-home services for seniors and people with disabilities that help keep them out of expensive nursing homes.

Choosing to invest in children, families, and communities is the best thing we can do to propel our state toward economic prosperity. That’s why lawmakers and the governor must choose to develop new revenue instead of cutting the services that make Illinois families and communities strong.

CUTS HAVE CONSEQUENCES

The governor’s proposed cuts would be damaging for kids, families, and communities across Illinois, as well as damaging to our economy — undermining the strength of Illinois’ workforce and its local communities; the development of children and youth; and access to cost-effective health and disability care.

The following outlines just a sampling of the harm that would follow the governor’s cuts to Illinois families and communities.

Cuts Undermine Illinois’ Workforce and Local Communities:

- Cuts to public transit agencies will make it more expensive to commute to work due to fare increases and service reductions
- Cuts to local government revenue sharing will lead to reductions in local police, fire, and public works departments across the state
- Working families with young children will lose access to affordable child care as budget cuts increase copayments and limit participation for children over 5 years
- Higher education will become even more cost-prohibitive for many students due to likely tuition increases as public colleges and universities see 30% cuts
- 155,000 households will lose access to state Low Income Home Energy Assistance Program services that help them afford heat for their homes during the winter
- Over 10,000 homeless households will lose access to supports that help them obtain secure, permanent housing

Cuts Undermine the Development of Children and Youth:

- 10,000 fewer infants and toddlers with developmental delays will receive early intervention services, increasing the likelihood they will need costly special education
- 14,000 youth will lose access to afterschool programs in over 57 communities
- Increased risks of infant mortality as thousands of fewer at-risk pregnant woman and new mothers will receive screenings
- 18 to 21 year old DCFS wards will lose access to all counseling, college, and other support services that help them transition successfully to independence

Cuts Undermine Health and Cost-Effective Care:

- Cuts to psychiatry, care coordination, and housing supports for individuals with serious mental illness will lead to expensive hospitalizations and incarcerations
- Cuts to residential and respite services for individuals with disabilities will lead to higher use of more expensive state development centers
- Elimination of 12,000 screenings will result in undetected breast and cervical cancers
- Loss of access to case coordination, case management, and outreach for over 21,000 Illinoisans with epilepsy
- Loss of non-emergency dental care for hundreds of thousands of adults, leading to costly emergency room visits
Without new revenue, actual cuts will be even deeper and more severe, since the governor’s budget relied on over $2 billion in savings from pension cuts that will almost certainly be impossible to realize next fiscal year due to legal challenges.

**Cuts Are A Choice: Choosing Revenue for a Stronger Illinois**

Policymakers can make other choices; they can choose to avoid cuts to education and other services that are key to a strong economy by raising the revenue our state needs to pay its bills and maintain strategic investments in the current and future well-being of Illinois children, families, communities, and the economy.

Rather than lay out a comprehensive tax reform package, this report outlines a menu of revenue options available to policymakers. Revenue options are organized in four areas: personal income tax; business taxes; sales taxes; and alcohol, nicotine, and sugary-beverage taxes.

Because the Illinois Constitution currently prohibits an income tax structure that applies lower rates for lower incomes and higher rates for higher incomes, many of the available revenue options unfortunately do not make Illinois’ tax system fairer. Illinois already has one of the most regressive tax systems in the nation, where low-income households pay a higher share of their income in state and local taxes than wealthy households. To improve tax fairness in a targeted way, policymakers should double the state’s Earned Income Tax Credit (EITC), which would help reduce the gap between the share of income low- and moderate-income working families pay in taxes and what wealthier households pay.

**Table of Contents**

- Table of Revenue Options ................................................................. 4
- Personal Income Tax ................................................................. 5
- Business Taxes ................................................................. 11
- Sales Taxes ................................................................. 21
- Alcohol, Nicotine, and Sugary-Beverage Taxes ............................................. 31
# Options to Avoid Cuts

## Personal Income Tax

<table>
<thead>
<tr>
<th>REFORMS</th>
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<tbody>
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<td>Restore income tax rate</td>
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<tr>
<td>Tax retirement income</td>
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</tr>
<tr>
<td>Cap residential property tax credit</td>
<td>$95 M - $225 M</td>
</tr>
<tr>
<td>Reduce personal exemption at higher incomes</td>
<td>$69 M</td>
</tr>
<tr>
<td>Adopt a multi-tiered income tax structure</td>
<td>Varied</td>
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## Business Taxes

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<tr>
<th>REFORMS</th>
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<td>Limit tax avoidance by capturing income held in offshore tax havens</td>
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<tr>
<td>Capture offshore drilling in corporate taxable income</td>
<td>$75 M</td>
</tr>
<tr>
<td>Close accounting loophole for corporations avoiding state taxes</td>
<td>$25 M</td>
</tr>
<tr>
<td>Limit or eliminate the Illinois Film Services Tax Credit</td>
<td>$13-20 M</td>
</tr>
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</table>

## Sales Taxes

<table>
<thead>
<tr>
<th>REFORMS</th>
<th>CUTS AVOIDED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broaden sales tax by taxing services</td>
<td></td>
</tr>
<tr>
<td>Model Iowa’s taxation of services</td>
<td>$4.6 B</td>
</tr>
<tr>
<td>Bruce Rauner’s proposal</td>
<td>$600 M</td>
</tr>
<tr>
<td>Raise the general sales tax rate</td>
<td>$410 M for every 0.25%</td>
</tr>
<tr>
<td>Suspend, reduce, or cap the retailer’s discount</td>
<td>$125 M</td>
</tr>
<tr>
<td>Close loophole for print news</td>
<td>$32 M</td>
</tr>
<tr>
<td>Suspend, reduce, or cap cost of collection discounts</td>
<td>$29 M</td>
</tr>
<tr>
<td>Extend sales tax to internet downloads</td>
<td>$14 - 18 M</td>
</tr>
<tr>
<td>Close hotel tax loophole for long-term rentals</td>
<td>$12 M</td>
</tr>
<tr>
<td>Tax full retail value of hotels booked online</td>
<td>$6 - 9 M</td>
</tr>
</tbody>
</table>

## Alcohol, Nicotine, and Sugary-Beverage Taxes

<table>
<thead>
<tr>
<th>REFORMS</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Tax sugar-sweetened beverages by 1 cent per ounce</td>
<td>$600 M</td>
</tr>
<tr>
<td>Raise cigarette tax by $0.50 per pack</td>
<td>$175 M</td>
</tr>
<tr>
<td>Tax electronic cigarettes</td>
<td>$800,000 - $38 M</td>
</tr>
<tr>
<td>Raise alcohol tax</td>
<td></td>
</tr>
<tr>
<td>Spirits by $3 per gallon (3.5 cents per drink)</td>
<td>$53 M</td>
</tr>
<tr>
<td>Beer by $0.15 per gallon (1.4 cents per drink)</td>
<td>$40 M</td>
</tr>
<tr>
<td>Wine by $0.30 per gallon (1.2 cents per glass)</td>
<td>$10 M</td>
</tr>
</tbody>
</table>
Avoid Cuts to Essential Services Through Income Tax Reform

Illinois is over $6 billion short of what it needs to fund schools, health care, and other services in the coming fiscal year thanks almost entirely to the 25-percent cut to income tax rates that lawmakers allowed to go into effect on January 1, 2015. Governor Rauner has proposed to close this massive gap through damaging cuts to essential programs and services that strengthen Illinois families, children, communities, and our economy — including child care and early intervention services, K-12 education, afterschool, child protection and welfare, public health, higher education, health care, public transportation, and revenue-sharing with local governments.

Cuts have consequences. The path to prosperity lies in investing in Illinois families and communities, not cutting services that are key to a stronger economy and a brighter future.

Illinois has many choices when it comes to meeting our needs and balancing the budget. Rather than make devastating cuts, policymakers can choose to raise the revenue necessary to pay our bills and keep investing in our future.

Policymakers can make several reforms to Illinois’ individual income tax to avoid cuts to education and other services that are key to a strong economy.

**Figure 1**

Avoid Cuts to Essential Services Through Personal Income Tax Reforms

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<td>Adopt a multi-tiered income tax structure</td>
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RESTORE THE INDIVIDUAL INCOME TAX RATE

**Approximately $1 billion for every 0.25%**

The $6 billion budget shortfall next fiscal year is caused almost entirely by cuts to state income tax rates that took effect on January 1, 2015, shifting the individual income tax rate from 5% to 3.75%.

Approximately $1 billion in cuts to vital services could be avoided for every 0.25% restoration of the personal income tax rate.

Examples:¹

<table>
<thead>
<tr>
<th>Tax Rate</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.25%</td>
<td>$2 billion</td>
</tr>
<tr>
<td>4.75%</td>
<td>$4 billion</td>
</tr>
<tr>
<td>5%</td>
<td>$5 billion</td>
</tr>
</tbody>
</table>

Why restore the individual income tax rate?

- The income tax is one of two major sources of revenue that supports vital services in Illinois, making it difficult to avoid cuts to education and other services that are key to a strong economy without reforming the individual income tax.

- Avoiding cuts through changes to the personal income tax is less regressive than other tax changes (such as increasing general sales or excise taxes).

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¹ Source: Illinois Institute on Taxation and Economic Policy

How Does Illinois Compare?

Illinois has the lowest effective income tax rate in the Midwest. This means Illinoisans spend a smaller percentage of their incomes on non-federal income taxes than taxpayers in neighboring states.
TAX SOME PORTION OF RETIREMENT INCOME

$500 million - $750 million

Illinois is the only state besides Mississippi that provides a blanket exclusion of retirement income from taxation. This cost Illinois over $2 billion in fiscal year 2013.

Millions of dollars in cuts to vital services could be avoided by asking taxpayers to pay their fair share of taxes on non-Social Security and IRA income. Lawmakers can protect seniors living on fixed incomes by allowing taxpayers 65 and over to exclude a set amount of retirement income.

Examples:

<table>
<thead>
<tr>
<th>Exclusion</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100,000 per spouse</td>
<td>$500 million</td>
</tr>
<tr>
<td>$75,000 per spouse</td>
<td>$550 million</td>
</tr>
<tr>
<td>$50,000 per spouse</td>
<td>$600 million</td>
</tr>
<tr>
<td>$25,000 per spouse</td>
<td>$750 million</td>
</tr>
</tbody>
</table>

Why tax some portion of retirement income?

- The exclusion of all retirement income from the individual income tax is the largest tax break in Illinois. With rapid growth of the aging population, the costs will quickly increase.

- Allowing the exemption of retirement income up to a capped amount is a more cost-effective way to provide tax relief to seniors living on fixed incomes.

- The number of senior taxpayers who move out of state is small and stable, which suggests they are unlikely to leave due to changes in tax rates.

How Does Illinois Compare?
Illinois is the only state in the Midwest that doesn’t tax some portion of retirement income.
CAP THE PROPERTY TAX CREDIT AT A FLAT AMOUNT

$95 million - $225 million

Illinois’ property tax credit allows homeowners to reduce the amount of income tax they owe by up to 5% of the property taxes paid on their homes. This is a very expensive and inefficiently targeted attempt at property tax relief.

Illinois can avoid tens of millions of dollars in cuts to essential services by capping the annual value of the property tax credit at a flat amount and indexing it to inflation so that property tax relief only goes to those who need it.

Examples:

<table>
<thead>
<tr>
<th>Cap on Property Tax Credit</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>$300</td>
<td>$95 million</td>
</tr>
<tr>
<td>$150</td>
<td>$225 million</td>
</tr>
</tbody>
</table>

Currently the property tax credit cannot be claimed by renters, even though they pay property taxes in the form of higher rent. If the property tax credit was extended to renters — who would be able to consider 10% of their rent as property tax — and capped at $150 for all taxpayers, Illinois would generate an additional $68 million a year in revenue.

Why cap the property tax credit at a flat amount?

- The property tax credit is the third-largest tax break in Illinois and is a very expensive form of tax relief since it is available to homeowners of all income levels, not just those in need of relief.

- The property tax credit as it is currently designed disproportionately benefits the wealthy since it is not available to renters, who tend to have lower incomes. Renters also typically pay property taxes through higher rents.

- Capping the credit more effectively targets property tax relief to low- and moderate-income households than a percentage credit without a cap.

How Does Illinois Compare?

Illinois is one of seven states and DC that offer both homestead exemptions and property tax credits. Ohio — the only neighboring state with both — has a credit of 2.5% (half the value of Illinois’).
Option #4  Adjust the Personal Exemption Based on Ability to Pay

$69 million

The personal exemption currently costs over $1 billion annually. By adjusting the exemption based on ability to pay, Illinois could avoid millions of dollars in cuts.

Example: $69 million in cuts could be avoided by phasing out the personal exemption according to the following schedule.

<table>
<thead>
<tr>
<th>Adjusted Gross Income</th>
<th>Exemption Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>under $100,000</td>
<td>$2,125</td>
</tr>
<tr>
<td>$100,000 - $200,000</td>
<td>$1,875</td>
</tr>
<tr>
<td>$200,000 - $300,000</td>
<td>$1,625</td>
</tr>
<tr>
<td>over $300,000</td>
<td>$0</td>
</tr>
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</table>

Why adjust the personal exemption based on ability to pay?

- The personal exemption is designed to decrease tax liability based on the fact that, for most families, the ability to pay taxes declines as family size increases. However, as income rises, so does ability to pay, diminishing both the need for and the relative benefit of the exemption.

- By basing the exemption on ability to pay, taxpayers in the top 1% — with average adjusted gross incomes of over $1.9 million — would see their state taxes increase by less than $300.

How Does Illinois Compare?

13 states and the federal government adjust their personal exemptions based on ability to pay — offering higher exemptions at lower-income levels and phasing them out at higher levels.
Illinois’ constitution currently restricts the state income tax to a flat rate, which means all taxpayers are taxed at the same rate despite how much they make. By adopting a multi-tiered income tax structure — with lower rates for lower incomes and higher rates for higher incomes — Illinois could avoid repeated and devastating cuts to education and other vital services while also increasing tax fairness.

**Why adopt a multi-tiered income tax structure?**

- Instead of cutting support for schools, safe communities, and other areas crucial to economic growth, we should make sure the wealthiest pay their fair share.

- Middle- and low-income families bear more responsibility for state taxes as a share of their income than the wealthy. We can partly fix this unfair imbalance through a multi-tiered tax, so that average working people have more opportunities.

- Since the 1970s, incomes of the top 5 percent of Illinoisans have risen 123 percent — six-and-a-half times the rate for middle-income households. A multi-tiered income tax would target where income is growing and those who can most afford to pay taxes, ensuring Illinois has the resources necessary to fund education and other vital services into the future.

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1 Source: 2015 estimates from the Institute on Taxation and Economy Policy.
2 Estimates do not include taxation of Social Security income or IRA distributions, and exclusion amounts apply only to taxpayers 65 and older. Additional revenue would be raised if the personal income tax rate was increased above the current 3.75 percent. Source: 2015 estimates from the Institute on Taxation and Economy Policy.
4 Source: 2015 estimates from the Institute on Taxation and Economy Policy.
Avoid Cuts to Essential Services by Having Businesses Pay Their Fair Share

Reform Business Taxes  For A Stronger Illinois

Illinois is over $6 billion short of what it needs to fund schools, health care, and other services in the coming fiscal year thanks almost entirely to the 25-percent cut to income tax rates that lawmakers allowed to go into effect on January 1, 2015. Governor Rauner has proposed to close this massive gap through damaging cuts to essential programs and services that strengthen Illinois families, children, communities, and our economy — including child care and early intervention services, K-12 education, afterschool, child protection and welfare, public health, higher education, health care, public transportation, and revenue-sharing with local governments.

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Policymakers can make several reforms to Illinois’ business taxes to avoid cuts to education and other services that are key to a strong economy.

Figure 1

Avoid Cuts to Essential Services by Having Businesses Pay Their Fair Share

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The budget shortfall Illinois faces is caused almost entirely by cuts to the income tax rates that went into effect on January 1, 2015. The cut to the corporate income tax rate — from 7% to 5.25% — is costing the state about $800 million.

Approximately $300 million to $800 million in cuts to vital services could be avoided by undoing part or all of the corporate income tax rate cut.

Examples:

<table>
<thead>
<tr>
<th>Tax Rate</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>6%</td>
<td>$330 million</td>
</tr>
<tr>
<td>6.5%</td>
<td>$550 million</td>
</tr>
<tr>
<td>7%</td>
<td>$770 million</td>
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Why restore the corporate income tax rate?

- The decrease in the corporate income tax will account for over 15% of the revenue lost next fiscal year. Rather than cut services like education and health care that help Illinois families and strengthen our economy, corporations should pay their fair share.

- State corporate taxes make up only 0.25 percent of corporate expenses. A small increase to the corporate income tax in order to avoid cuts to critical state services is highly unlikely to alter corporate decision-making. (See Figure 2)

- Businesses rely on healthy, well-educated workers; strong communities; and a safe and efficient transportation system to succeed. Cutting support to educate our children, improve our infrastructure, and implement cost-effective solutions to problems such as homelessness weakens the building blocks of economic prosperity and long-term profitability.
Money from reduced corporate income taxes often flows to shareholders, suppliers, and employees out of state. Had these dollars continued to fund state services, they would have stayed mostly in Illinois. The net result is an outflow of dollars.

Illinois calculates corporate income tax based on sales in the state. Because a corporation’s Illinois income tax liability is not tied to the location of its headquarters, offices, distribution facilities, or factories, cutting corporate income taxes does virtually nothing to encourage job creation in the state.

Option #2

LIMIT OR ELIMINATE ENTERPRISE ZONES AND EDGE TAX CREDITS

Over $100 million

Illinois hands out more than $100 million in corporate tax breaks through EDGE — Economic Development for a Growing Economy — and Enterprise Zone programs. EDGE credits allow corporations to offset their taxes by keeping as a credit a portion of what their workers pay in personal income tax. The Enterprise Zone program encompasses a variety of tax incentives, including sales and utility tax exemptions and corporate and individual income tax credits.

While it is obviously laudable to try to increase economic development, there is little evidence that these tax breaks are effective at achieving this goal. Until Illinois subjects these credits to stringent review, policymakers should consider limiting, or even eliminating, these tax breaks.

Why limit or eliminate Enterprise Zones and EDGE tax credits?

- A recent evaluation of state enterprise zones nationwide concluded, based on a review of the evidence, that they “have generally not been effective at creating jobs.” It also found that, even if they provide some help, “it is hard to make the case that enterprise zones have furthered [ ] goals of reducing poverty in the zones....”

- During last fall’s campaign, then-candidate Bruce Rauner claimed the “EDGE tax credit program is broken.”

- These workers’ personal income tax withholdings — like all other withholdings — should go to supporting economic development tools that we know actually work, such as education and infrastructure. Instead, under the EDGE program, workers effectively pay taxes to their employer.

- Illinois is one of only four states offering EDGE tax credits where 100% of workers’ tax withholdings are diverted to their employers.

How Does Illinois Compare?

Illinois is one of 26 states not meeting any of the Pew Center on the State’s criteria for scope or quality evaluations of tax incentive programs.
States around the country have decided that they should no longer have their taxes automatically tied to a federal corporate tax break known as the “domestic production deduction.” However, Illinois hasn’t “decoupled” from this federal tax break. As a result, Illinois gives a tax break to corporations whenever they make a qualifying investment anywhere in the U.S., even outside Illinois.

At the federal level, this tax break is meant to encourage investment in the U.S. For states, this tax break makes little sense. This is because corporations reduce their taxable income in Illinois if they invest in qualifying activities in Indiana or as far afield as Hawaii.

Illinois’ failure to opt out cost the state about $100 million in fiscal year 2014.6

Why decouple from the domestic production deduction?

- Illinois should not be paying to encourage production in other states. The amount corporations pay in Illinois taxes is reduced even if those corporations’ qualifying “production activities” occur outside of Illinois.

- This deduction only exists because, like other states, Illinois’ income tax is tied to the federal tax code. Our elected officials never signed off on this corporate tax break.

- As the value of the federal deduction has increased, Illinois has continued to lose more money. Corporations are now allowed to deduct up to 9% of qualifying income — up from only 3% in 2004. Illinois has lost more money over time.

- The deduction disproportionately benefits the largest multi-state corporations. In 2009, 0.5% of the largest corporations with assets over $100 million claimed 93% of the deductions nationally.7

- Maintaining this inefficient and costly deduction causes deeper cuts to be made to critical services that strengthen Illinois children, families, and communities.

How Does Illinois Compare?

As of January 2013, 21 other states and the District of Columbia disallowed the domestic production activity deduction. State that have decoupled include CA, TX, IN, WI, SC, and MN.
Corporations pay Illinois income tax on the share of domestic corporate profits attributable to our state. However, to avoid taxes, corporations frequently employ a variety of gimmicks to — on paper — move profits out of the U.S. and onto the books of subsidiaries located in offshore tax havens that have extremely low, or even no, taxes.

Every year, Illinois loses over $100 million due to these tax havens.9

However, Illinois can take steps to reclaim this revenue by treating income held in known corporate tax havens such as the Cayman Islands as domestic income.10

Why treat income held in corporate tax havens as domestic income?

- Corporations are the direct beneficiaries of taxpayer dollars at work: schools and affordable colleges produce a skilled workforce; transportation infrastructure brings their goods to market; and public safety protects their employees and businesses. By taking the easy steps of treating income held in tax havens as domestic, Illinois can make this abusive practice less lucrative for businesses and less costly to Illinois.11

- The reason profits are held in these countries is almost always to avoid taxes, as there is little economic rationale for holding large amounts of corporate income in countries that tend to have small domestic markets and populations.

- Nearly half (46%) of corporate earnings held “offshore” for tax purposes in 2011 were actually invested in U.S. assets, according to a U.S. Senate committee investigation.12 As former U.S. Senator Carl Levin, then chair of the committee, said at the time, “U.S. multinationals are benefiting from the stability and security that U.S. banks, U.S. investments, and U.S. dollars provide without paying their fair share to sustain our economy.”13

- There is strong support for making it harder for corporations to shift income overseas — both from the general public and small businesses that don’t have an army of tax attorneys and accountants. A January 2013 poll found that 73% of Americans surveyed wanted to “close loopholes allowing corporations/wealthy to avoid U.S. taxes by shifting income overseas.”14 Another poll found that 90 percent of small business owners believed their businesses had to pay taxes that large, multinational corporations use loopholes to avoid paying.15
Option #5  CAPTURE OFFSHORE DRILLING IN CORPORATE TAXABLE INCOME

$75 million

Currently, Illinois does not count profit from offshore drilling for natural resources as taxable income for companies with a presence in Illinois when calculating the amount of corporate tax the company owes.

This can be fixed very easily and is an issue that has received support from key policymakers. Former Governor Pat Quinn supported this fix and so has Senate President John Cullerton. Governor Bruce Rauner championed closing this “Big Oil Loophole” during his campaign, writing in his “Bring Back Blueprint: Corporate Welfare Reform”:

*Illinois excludes corporate income generated in the outer continental shelf – effectively treating U.S. property as foreign lands. This loophole allows oil companies with a presence in Illinois to drill offshore and not pay Illinois taxes on that income... Oil companies should pay their fair share of taxes....*

In 2012, the Governor Pat Quinn said this change would raise $75 million.\(^{16}\)

**Why capture offshore drilling in corporate taxable income?**

- There’s little justification for excluding from taxation corporate profits generated from areas under U.S. control but not part of any U.S. state.
- The legislative fix is extremely simple.
- Governor Rauner, Senate President Cullerton, and senior House Republicans\(^ {17}\) have supported closing this loophole.
- Excluding offshore drilling revenue from corporate income causes deeper cuts to be made to critical services that strengthen Illinois children, families, and communities.

Option #6  CLOSE ACCOUNTING LOOPHOLE FOR CORPORATIONS AVOIDING STATE TAXES

$25 million

When filing income taxes, most corporations are required to report the income of both the parent corporation and any subsidiaries in a single, combined tax return. This “combined reporting” requirement makes it harder for corporations to avoid taxes by artificially moving profits to subsidiaries in lower tax jurisdictions.

However, Illinois has a large loophole that exempts financial, transportation, and insurance corporations from this requirement. As a result, Illinois loses millions of dollars every year.
needed to support education and other vital services, while large corporations get away without paying their fair share.

Closing this loophole would have raised about $25 million in fiscal year 2014.\textsuperscript{18}

**Why require combined reporting for financial, transportation, and insurance corporations?**

- Large corporations shouldn’t be able to avoid paying their fair share of taxes that are needed to support education and other services that are key to both their business success and a strong economy.

- Small, in-state corporations are at a disadvantage when the law permits large corporations to set up complicated tax avoidance structures.

- Governor Rauner and former Governor Quinn both have supported closing this loophole.\textsuperscript{19}

- Closing this loophole will not harm economic growth, as there is no evidence that combined-reporting requirements diminish economic activity in states.\textsuperscript{20}

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**How Does Illinois Compare?**

23 of the 45 states with corporate income taxes require combined reporting.  
These states include TX, NY, WI, KS, and CA.

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**Option #7**  
**Limit or Eliminate the Film Production Services Tax Credit**

**Revenue Est.**  
$13 million - $20 million

Illinois offers a tax credit equal to 30% of qualifying expenditures for film, television, and commercials produced in Illinois. Qualifying expenditures include goods and services purchased from Illinois vendors and compensation paid to employees who are Illinois residents.

These tax credits are not a good use of public resources. Numerous studies have shown that these subsidies cost more than the value of any additional economic activity they may create,\textsuperscript{21} depriving the state of resources needed to support education and other vital services that are key to a strong economy.

Since its adoption in 2008, this subsidy has cost Illinois on average $13 million a year. In fiscal year 2013, it cost Illinois approximately $19 million.
Why limit or eliminate the Film Production Services Tax Credit?

- These subsidies don’t pay for themselves, producing revenue gains of only $0.07 to $0.28 for every dollar of tax credit. Every dollar spent on ineffective tax credits is a dollar taken away from cost-effective investments in education, job training, and other vital services that are key to a strong economy.

- Most work created from film and television projects for in-state residents is temporary, part-time, and relatively low paying, which is not the basis for strong, long-term economic development.

- These tax credits reward producers for projects they would have created in Illinois even without the subsidy, depriving the state of needed resources without any return.

- It is not advantageous for Illinois to participate in “bidding wars” with other states for film production. While Illinois may be able to lure production to the state by offering a more generous tax credit, ensuring this advantage requires perpetually “upping the ante” — tying up resources that should be free to invest in education and other more cost-effective development strategies like job training and infrastructure.

- Illinois’ film tax credits are transferable, which means they can be sold to other corporations with tax liability in the state. These tax credits are frequently purchased by financial services firms that have nothing to do with the film industry and who use the credits to get out of paying their fair share.

How Does Illinois Compare?

After a period of rapid popularity, many states have recently pared back their film tax incentives: AZ, ID, IN, IA, KS, MO, and WI have recently ended or not included funding in their budgets; CT ended the subsidy for film; and other states have decreased the overall rebate or credit that can be claimed. Illinois doesn’t cap the amount that can be claimed by producers or for the tax credit program in its entirety.

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1 Source: 2015 estimates from the Institute on Taxation and Economic Policy.
2 Compare labor costs, which are 100 times greater than state corporate income tax costs. Based on analysis of Michael Mazerov of Internal Revenue Service and Bureau of Labor Statistics data. See “Cutting State Corporate Income Taxes is Unlikely to Create Many Jobs” (Center on Budget and Policy Priorities, September 14, 2010).
4 David Neumark and Helen Simpson, “Do Place-Based Policies Matter?,” Federal Reserve Bank of San Francisco Economic Letter (March 2, 2015).
5 Other states include Indiana, Missouri, and Mississippi. Philip Mattera, Kasia Tarczynska, Leigh McIlvaine, Thomas Cafcas, and Greg LeRoy, “Paying Taxes to the Boss: How A Growing Number of States Subsidize Companies with the Withholding Taxes of their Workers” (Good Jobs First, April 2012).
The estimated revenue raised by ending this and other tax breaks depends on the tax rate in place at the time of the estimate. Where the estimate was made when the higher corporate income tax rate was in place, the actual revenue raised would tend to be less given the recent rollback. However, where the underlying economic activity (e.g. corporate profits) have increased since the time of the estimate, that would tend to partially — or perhaps even totally — offset the effect of the lower tax rate.


8 This estimate assumes the combined reporting loophole for financial, transportation, and insurance corporations has been closed.

9 “Closing the Billion Dollar Loophole, How States Are Reclaiming Revenue Lost to Offshore Tax Havens” (U.S. PIRG, Winter 2014).

10 This is accomplished through strengthening the requirements of combined reporting to include subsidiaries of parent corporations that are located in jurisdictions that are known tax havens. For more on combined reporting, see revenue option #6 in this section.

11 See ORS 317.715 for an example legislative fix, passed by Oregon in 2013.


15 “Small Business Owners’ View on Taxes and How to Level the Playing Field with Big Business” (American Sustainable Business Council, Main Street Alliance and Small Business Majority, February 6, 2012), poll conducted by Lake Research.


17 Senate President John Cullerton supported in Senate Amendment 2 to HB 5342 (2012). Representatives Robert Pritchard and David Harris were chief co-sponsors of HB 6289 (2014).


19 Id.


21 Joseph Henchman, “Motion Picture Association Attacks Tax Foundation Critique of Film Tax Subsidies” (June 29, 2011)

22 Robert Tannenwald, "State Film Subsidies: Not Much Bang For Too Many Bucks" (Center on Budget and Policy Priorities, December 9, 2010).
Avoid Cuts to Essential Services Through Sales Tax Reform

Illinois is over $6 billion short of what it needs to fund schools, health care, and other services in the coming fiscal year thanks almost entirely to the 25-percent cut to income tax rates that lawmakers allowed to go into effect on January 1, 2015. Governor Rauner has proposed to close this massive gap through damaging cuts to essential programs and services that strengthen Illinois families, children, communities, and our economy — including child care and early intervention services, K-12 education, afterschool, child protection and welfare, public health, higher education, health care, public transportation, and revenue-sharing with local governments.

Cuts have consequences. The path to prosperity lies in investing in Illinois families and communities, not cutting services that are key to a stronger economy and a brighter future.

Illinois has many choices when it comes to meeting our needs and balancing the budget. Rather than make devastating cuts, policymakers can choose to raise the revenue necessary to pay our bills and keep investing in our future.

Policymakers can make several reforms to Illinois' sales taxes\(^1\) to avoid cuts to education and other services that are key to a strong economy.

**Figure 1**

Avoid Cuts to Essential Services by Reforming Sales Taxes

<table>
<thead>
<tr>
<th>REFORMS</th>
<th>CUTS AVOIDED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broaden sales tax base by taxing services</td>
<td></td>
</tr>
<tr>
<td>Model Iowa’s taxation of services</td>
<td>$4.6 B</td>
</tr>
<tr>
<td>Bruce Rauner’s proposal</td>
<td>$600 M</td>
</tr>
<tr>
<td>Raise the general sales tax rate</td>
<td>$410 M for every 0.25%</td>
</tr>
<tr>
<td>Suspend, reduce, or cap the retailer’s discount</td>
<td>$125 M</td>
</tr>
<tr>
<td>Close loophole for print news</td>
<td>$32 M</td>
</tr>
<tr>
<td>Suspend, reduce, or cap cost of collection discounts</td>
<td>$29 M</td>
</tr>
<tr>
<td>Extend sales tax to internet downloads</td>
<td>$14 - 18 M</td>
</tr>
<tr>
<td>Close hotel tax loophole for long-term rentals</td>
<td>$12 M</td>
</tr>
<tr>
<td>Tax full retail value of hotels booked online</td>
<td>$6 - 9 M</td>
</tr>
</tbody>
</table>
The sales tax is intended to apply broadly to goods and services purchased by consumers. Illinois’ sales tax falls substantially short by failing to include most services — Illinois taxes only 17 services, compared to the national average of 56. As a result, Illinois loses substantial amounts of revenue that could support education and other services crucial to a strong economy; biases certain purchases over others; and increases tax unfairness by taxing similar products differently (for example, purchasing a DVD and watching a movie through an online subscription service).

Illinois has the potential to raise significant amounts of revenue by broadening the sales tax base through taxing services. If taxing a full range of consumer services, Illinois was estimated to be able to raise around $4 billion a year in 2011 — a conservative estimate by the Illinois Commission on Government Forecasting and Accountability (CGFA). This revenue potential has grown along with the professional, finance, insurance, technical and other service sectors in Illinois.

The revenue this option would generate of course depends on the selection of services policymakers choose to tax. If Illinois expanded its sales tax base to include services currently taxed by Iowa (94 services), it would generate around $4.6 billion a year, according to a 2015 estimate from the Institute on Taxation and Economic Policy. The sales tax expansion proposed by Bruce Rauner in his “Bring Back Blueprint: Jobs and Growth Agenda” would generate $600 million a year.
Examples:

<table>
<thead>
<tr>
<th>Tax Proposal</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Iowa’s Taxation of Services</td>
<td>$4.57 billion</td>
</tr>
<tr>
<td>Rauner’s “Bring Back Blueprint”</td>
<td>$600 million</td>
</tr>
</tbody>
</table>

**Why extend the sales tax to include services?**

- By not comprehensively taxing services, Illinois is losing billions of dollars that could support education and other programs that are key to a strong economy.

- There is no sound economic reason for excluding the purchase of services by consumers from the sales tax. The failure to do so is the result of history — the sales tax was enacted in 1932 when most consumer purchases were goods, not services — and organized opposition from service industries that don’t want to lose special treatment.6

- Governor Rauner has supported expanding Illinois’ taxation of services.7

- Taxing services makes the sales tax fairer while reducing distortions in the economy. It doesn’t make sense to tax someone who buys DVDs in a store and not someone who purchases access to the same films through an online subscription service. There is no reason for the state to bias one of these purchases over the other.

- Illinois does not need to exclude virtually all services from the sales tax to reduce the harm of the sales tax on low-income individuals and families. Excluding items that low-income consumers spend most of their incomes on— food, apartment rentals, child care, and health care — while expanding the EITC are more effective and less costly ways to improve tax fairness.

- Including more services will make the sales tax a more reliable and stable source of support for education and other programs crucial to a strong economy. That’s because households have shifted more of their purchases from goods to services and the demand for services doesn’t rise or fall as much as the demand for goods during economic booms and busts.

**How Does Illinois Compare?**

Illinois’ economy is more dependent on services than any of the other Great Lake states due to the growing finance, insurance, professional, technical, and information industries. However, Illinois taxes the fewest services among its neighboring states.
RAISE THE GENERAL SALES TAX RATE

Revenue Est.
Approximately $400 million for every 0.25%

State sales taxes generate almost a quarter of the revenue needed to support key services like education, health care, and human services. Increasing the general state sales tax rate is one way to generate more revenue to avoid cuts to these key services.

Approximately $400 million in cuts to vital services could be avoided for every 0.25% increase to the general sales tax rate.

Examples:

<table>
<thead>
<tr>
<th>General Sales Tax Rate</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.5%</td>
<td>$410 million</td>
</tr>
<tr>
<td>6.75%</td>
<td>$820 million</td>
</tr>
</tbody>
</table>

However, this option has several drawbacks. Illinois already has the 12th highest sales tax rate in the nation and the 10th highest when local tax rates are added. Additionally, the sales tax disproportionately affects low-income families, who pay a larger share of their income in sales taxes than wealthier taxpayers. Increasing the general sales tax rate without an offset for low-income families and individuals would make Illinois’ already unfair tax system even more unfair.

Why raise the general sales tax rate?

- Revenue from an increase in the sales tax rate could help avoid cuts to critical services including education, preschool and early childhood intervention services, health care, and revenue-sharing with local governments.

- Any increase in the sales tax rate should be combined with an increase in the Earned Income Tax Credit (EITC), which allows low-income working families to keep more of their earnings so they can afford things that help them stay employed such as child care and transportation.

How Does Illinois Compare?

Illinois has the 12th highest state sales tax rate and the 10th highest combined state and local tax rate. Raising the state sales tax rate to 6.75 percent would bump Illinois up to the 7th highest state tax rate, behind California’s 7.5 percent.
Option #3  SUSPEND, REDUCE, OR CAP THE RETAILER’S DISCOUNT

Revenue Est.  Up to $125 million

The Retailer’s Discount allows Illinois retailers to keep 1.75% of the sales taxes they collect from consumers, designed to compensate them for costs associated with collecting and reporting the tax. This “discount” dates back to the 1930s when the process for record keeping and transferring the sales tax receipts was much more labor intensive than it is now given technological advances.

Failure to reform the retailer’s discount in light of current technologies cost Illinois $125 million in fiscal year 2013.

Why suspend, reduce, or cap the retailer’s discount?

- By suspending, reducing, or capping the retailer’s discount, Illinois could net millions of sorely needed dollars to support education and other services that are key to a stronger economy.

- It costs less to collect, record, and submit sales tax receipts now than it did when the retailer discount was first enacted. The law should be updated to reflect current costs.

- Illinois loses more money to this loophole than any other state. From 2002 – 2012, Illinois lost over $1 billion.12

- Because Illinois does not cap the amount of tax receipts any one taxpayer can keep, the “discount” disproportionately benefits the largest retailers — those whose compliance costs are actually the lowest. For example, Walmart (the largest retailer in the country) collects over $8 million a year in retailer “discounts” from Illinois alone.13

- Several states — including Nevada, Colorado, and Virginia — have reevaluated their retailer discounts during difficult budget times, resulting in reductions and temporary or permanent suspensions of the discount. Thirteen states cap the discount at a median value of $4,000 to $5,000 a year.14

How Does Illinois Compare?

22 states and DC do not offer retailer discounts. Of the 28 states that do, 16 of them offer lower rates than Illinois’ and 13 of them cap the total amount of the discount any one taxpayer can retain.
**CLOSE THE LOOPHOLE FOR PRINT NEWS**

**Revenue Est.**  
$32 million

Print news — newspapers and magazines — are exempt from Illinois’ sales tax, an exemption that cost Illinois $32 million in fiscal year 2013.

**Why close the loophole for print news?**

- Rather than cut billions of dollars in support for education, health care, revenue-sharing with local governments, and other services that are key to a strong economy, Illinois should close loopholes like the Newsprint and Ink Exemption.

- Governor Rauner has supported closing this loophole.\(^{15}\)

- Newspapers and magazines are goods purchased for consumption just like many other goods subject to the sales tax. There is no compelling reason for the state to bias the purchase of print media by exempting it from the sales tax.

**SUSPEND, REDUCE, OR CAP COST OF COLLECTION DISCOUNTS**

**Revenue Est.**  
Up to $29 million

Like the Retailer’s Discount, retailers that collect certain selective sales taxes,\(^{16}\) such as cigarette taxes, are allowed to keep a percentage of the receipts as reimbursement for expenses for record keeping, billing, filing, and remitting the taxes.

These “discounts” cost Illinois a combined $28.5 million in fiscal year 2013.

**Why suspend, reduce, or cap cost of collection discounts?**

- By suspending, reducing, or capping the cost of collection discounts, Illinois could return millions of sorely needed dollars to support education and other services that build a stronger economy.

- It costs less to collect, record, and submit sales tax receipts now than when these types of discounts were first created. The law should be updated to reflect current costs.
EXTEND THE SALES TAX TO INTERNET DOWNLOADS

$14 million - $18 million

Goods like games, movies, books, off-the-shelf computer software, and music that can be purchased in stores are subject to Illinois’ sales tax. However, if these goods are purchased online, only digital software and games are taxed.

Because of a failure to extend the sales tax to all digital goods and services, Illinois loses an estimated $14 and $18 million dollars a year.17

Why extend the sales tax to Internet downloads?

- Digital goods and services are a growing part of the economy. Continuing to exempt large categories of digital goods will cost Illinois increasingly more money in years to come. Lawmakers should update the sales tax to reflect the Internet age.

- Taxing digital goods and services levels the playing field for retailers by removing the bias in favor of digital goods.

- Extending the sales tax to more digital goods and services will increase tax fairness, since buyers of digital goods and services are disproportionately upper-income families who pay a lower share of their incomes in sales taxes than lower-income families.

CLOSE THE HOTEL TAX LOOPHOLE FOR LONG-TERM RENTALS

$12 million

Illinois hotels pay a selective sales tax on income they receive from renting rooms to guests — a cost that is passed on to consumers through higher room rates. However, guests — individuals or businesses — who rent a room for 30 or more days are considered permanent residents, and rentals to these guests are exempt from the tax.

In fiscal year 2013, this exemption cost Illinois around $12 million.
Why close the hotel tax loophole for long-term rentals?

- The permanent resident exemption primarily benefits for-profit businesses, such as airlines, consulting firms, railroad and trucking companies, and others who keep long-term rentals for traveling workers. Rather than cut education and other services that are key to a strong economy, Illinois should require businesses to pay their fair share.

- Eliminating this loophole would have very little impact on private individuals because they typically make up a very small share of guests who rent hotels for 30 or more days.\(^{18}\)

- In efforts to improve government effectiveness and efficiency, the Texas Legislative Budget Board staff recommended the elimination of that state’s permanent resident exemption in 2011.\(^{19}\)

Option #8  
**TAX THE FULL RETAIL VALUE OF HOTELS BOOKED ONLINE**

*Revenue Est.* $6 million - $9 million

Illinois loses an estimated $6 million to $9 million a year by allowing online travel companies (like Orbitz and Priceline) to pay less in lodging taxes on bookings than the hotels themselves must pay when the same room is booked directly with them or through a travel agent.\(^{20}\)

Why tax the full retail value of hotels booked online?

- Illinois is losing millions of dollars a year because it hasn’t updated its hotel tax to reflect new methods for booking hotels that have emerged during the Internet age.

- The full rental value of hotel rooms is taxed when a room is booked by a travel agent or by the guest herself — online bookings should be treated no differently.

How Does Illinois Compare?

> Along with 44 other states, Illinois loses revenue every year because it fails to tax the full retail value of hotel rooms booked through online travel companies.

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1 Reform proposals discussed in this section refer not only the four Illinois sales and use tax acts (Retailers' Occupation Tax, Service Occupation Tax, Service Use Tax, Use Tax), but also discussion of some selective sales taxes — like the Hotel Operator's Occupancy Tax.

2 "Service Taxes, 2011 Update" (Commission on Government Forecasting and Accountability, April 2011).

3 Id.
4 701 IAC Chapter 26. For list of taxable services, see https://tax.iowa.gov/iowa-sales-and-use-tax-taxable-services-0.
5 "Bring Back Blueprint: Jobs and Growth Agenda" (2014).
6 Table 2.3.5. Personal Consumption Expenditures by Major Type of Product (Bureau of Economic Analysis, April 29, 2015).
7 "Bring Back Blueprint: Jobs and Growth Agenda" (2014).
8 State and Local Government Finances by Level of Government and by State (U.S. Census Bureau, 2012).
9 “State Budget: Fiscal Year 2016” (Governor’s Office of Management and Budget, February 18, 2015).
11 See EITCWorks.org.
12 Thomas Cafcas and Greg LeRoy, “Closing Corporate Loopholes, Bolstering Illinois’ Budget” (Good Jobs First, February 2012).
13 “Skimming the Sales Tax: How Wal-Mart and Other Big Retailers (Legally) Keep a Cut of the Taxes We Pay on Everyday Purchases” (Good Jobs First, November 2008).
14 “Reduce General Revenue Loss from Sales Tax Discounts,” Texas State Government Effectiveness and Efficiency (Legislative Budget Board Staff, January 2011).
16 Cost of collection discounts are offered for the following selective sales/use taxes: Cigarette Tax; Telecommunications Excise Tax; Hotel Operator’s Occupation and Use Tax; Liquor Gallonage Tax; and Gas Use Tax.
18 “Eliminate the Hotel Permanent Resident Exception,” Texas State Government Effectiveness and Efficiency (Legislative Budget Board Staff, January 2011).
19 Id.
20 Michael Mazerov, “State and Local Governments Should Close Online Hotel Tax Loophole and Collect Taxes Owed” (Center on Budget and Policy Priorities, April 12, 2011).
Avoid Cuts to Essential Services by Reforming Alcohol, Nicotine, and Sugary-Beverage Taxes

Illinois is over $6 billion short of what it needs to fund schools, health care, and other services in the coming fiscal year thanks almost entirely to the 25-percent cut to income tax rates that lawmakers allowed to go into effect on January 1, 2015. Governor Rauner has proposed to close this massive gap through damaging cuts to essential programs and services that strengthen Illinois families, children, communities, and our economy — including child care and early intervention services, K-12 education, afterschool, child protection and welfare, public health, higher education, health care, public transportation, and revenue-sharing with local governments.

Cuts have consequences. The path to prosperity lies in investing in Illinois families and communities, not cutting services that are key to a stronger economy and a brighter future.

Illinois has many choices when it comes to meeting our needs and balancing the budget. Rather than make devastating cuts, policymakers can choose to raise the revenue necessary to pay our bills and keep investing in our future.

Policymakers can make several reforms to Illinois’ taxes on cigarettes, alcohol, and a proposed tax on sugary beverages to avoid cuts to education and other services that are key to a strong economy.

**Figure 1**
Avoid Cuts to Essential Services by Reforming Alcohol, Nicotine, and Sugary-Beverage Taxes

<table>
<thead>
<tr>
<th>REFORMS</th>
<th>CUTS AVOIDED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax sugar-sweetened beverages by 1 cent per ounce</td>
<td>$600 M</td>
</tr>
<tr>
<td>Raise cigarette tax by $0.50 per pack</td>
<td>$175 M</td>
</tr>
<tr>
<td>Tax electronic cigarettes</td>
<td>$800,000 - $38 M</td>
</tr>
<tr>
<td>Raise alcohol tax</td>
<td></td>
</tr>
<tr>
<td>Spirits by $3 per gallon (3.5 cents per drink)</td>
<td>$53 M</td>
</tr>
<tr>
<td>Beer by $0.15 per gallon (1.4 cents per drink)</td>
<td>$40 M</td>
</tr>
<tr>
<td>Wine by $0.30 per gallon (1.2 cents per glass)</td>
<td>$10 M</td>
</tr>
</tbody>
</table>
Option #1  
**TAX SUGAR-SWEETENED BEVERAGES BY 1 CENT PER OUNCE**

**Revenue Est.**  
$600 million

The proposed Healthy Eating and Active Living Act would add a one-cent-per-ounce excise tax on sodas, energy drinks, and other beverages with more than 5 grams of sugar per 12 fluid ounces.¹ This new tax is estimated to raise more than $600 million to strengthen wellness in communities and support Medicaid disease prevention services.²

**Why tax sugar-sweetened beverages?**

- Revenue from a small tax on sugary beverages would strengthen communities by supporting health initiatives such as disease prevention services, nutrition education, physical education, and healthier school meals.

- This tax would discourage consumption of sugary beverages by increasing the shelf price of these drinks, which could lead to reductions in obesity, heart disease, diabetes, and some cancers, as well as decreased medical costs for treating these conditions. Obesity-related conditions cost the Illinois Medicaid program over $1 billion a year.³

- Research shows the tax could result in a net increase of 4,500 jobs, due to increased spending on non-beverage goods and services and new public jobs created by the revenue from the tax.⁴

- While a tax on sugary beverages would fall heavier on low-income populations because the flat price of the tax makes up a larger share of their personal income, targeting the health initiatives supported by the tax to those communities may offset this problem.⁵

**How Does Illinois Compare?**

The majority of states tax sugary beverages, typically through a sales tax. Arkansas, Tennessee, Virginia, and West Virginia also levy an additional tax on the distributors of sugary beverages.
RAISE THE CIGARETTE TAX BY 50 CENTS PER PACK

$175 million

The cigarette tax in Illinois is currently $1.98 per pack.

Raising the excise tax on cigarettes by $0.50 per pack would generate an additional $175 million a year, the Institute of Government and Public Affairs at the University of Illinois estimates.⁶

Why raise the cigarette tax?

- Additional revenue from the cigarette tax could help policymakers avoid or restore cuts to critical services including substance abuse treatment and prevention; the tobacco quitline, a telephone hotline that helps smokers who want to quit; and Medicaid dental care.

- Higher cigarette taxes discourage smoking,⁷ which may lead to healthier behavior, decreased second-hand smoke, and decreased medical costs.

How Does Illinois Compare?

Fourteen states have cigarette taxes over $2.00 a pack, including Wisconsin at $2.52, Minnesota at $3.43, and New York at $4.35.
Electronic cigarettes (e-cigarettes) are not subject to Illinois’s cigarette tax, despite their similar nicotine content, appearance, and use. Taxing e-cigarettes could generate as little as $800,000 to as much as $38 million a year depending on the proposed tax rate.

Examples:

<table>
<thead>
<tr>
<th>Tax Rate</th>
<th>New Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0.05 per ml of e-liquid</td>
<td>$800,000</td>
</tr>
<tr>
<td>$0.68 per ml (equivalent rate of tobacco cigarettes)</td>
<td>$11 million</td>
</tr>
<tr>
<td>$1.71 per ml (95% of wholesale price)</td>
<td>$27.4 million</td>
</tr>
<tr>
<td>$2.38 per ml (95% of retail price)</td>
<td>$38 million</td>
</tr>
</tbody>
</table>

**Why tax electronic cigarettes?**

- Revenue from an extension of the cigarette tax could help policymakers avoid or restore cuts to critical services including substance abuse treatment and prevention; the tobacco quitline, a telephone hotline that helps smokers who want to quit; and Medicaid dental care.
- Vapor has been shown to increase the risk of respiratory viral infections and has unknown long-term health effects.\(^{12}\)
- Higher e-cigarette prices are likely to discourage use,\(^ {13}\) which is particularly important for youth, whose use of e-cigarettes has tripled between 2011 and 2014.\(^ {14}\) According to the CDC, nicotine exposure at a young age can cause lasting harm to brain development, promote addiction, and may lead to later tobacco use.\(^ {15}\)
RAISE ALCOHOL TAXES

$53 million from spirits
$40 million from beer
$10 million from wine

Alcohol taxes are levied by the gallon, with spirits taxed at $8.55, wine at $0.30, and beer at $0.23.

Raising spirits by $3 per gallon (3.5 cents per drink), wine by $0.30 per gallon (1.2 cents per glass), and beer by $0.15 per gallon (1.4 cents per beer) would generate over $100 million a year, the Institute of Government and Public Affairs at the University of Illinois estimates.\(^\text{16}\)

Why raise alcohol taxes?

- Additional revenue from alcohol taxes could help avoid cuts to critical services including substance abuse treatment and prevention, mental health, and local police and fire services in municipalities across the state.

- As alcohol prices increase, binge drinking declines\(^\text{17}\) along with alcohol-related deaths (for example, liver cirrhosis), drunk driving accidents, violence, and crime.\(^\text{18}\)

- Because alcohol is taxed by volume and not price, alcohol taxes have to be adjusted regularly in order to keep pace with inflation. The last time Illinois adjusted its alcohol taxes was in 2009.

- Buyers may purchase more alcohol in other states after a tax increase, but the effect is usually small.\(^\text{19}\)

How Does Illinois Compare?

Even with an increase to Illinois’ alcohol taxes, buyers would have to pay more in neighboring Iowa for spirits and wine and would have to pay more for beer and wine in Kentucky.

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1 See Illinois House Bill 5690 and Senate Bill 3524.
2 Frank J. Chaloupka et al., “Estimating the potential impact of sugar-sweetened and other beverage excise taxes in Illinois” (Cook County Department of Public Health, 2011).
5 See EITCWorks.org.

Most studies find that for every 25 percent increase in the cost of a pack of cigarettes, there is an 11 percent decrease in cigarette purchases. Iris J., Lav, "Cigarette Tax Increases: Cautions and Considerations" (Center on Budget and Policy Priorities, July 11, 2002).

North Carolina levies a tax on e-cigarettes at $0.05 per milliliter of e-liquid.

FPC estimate based on analysis by the Arizona Joint Legislative Budget Committee. Assumes an effective cigarette tax rate of 27.3 percent. "Fiscal Impact of E-Cigarettes," Arizona JLBC Staff Report (November 20, 2014).

Minnesota levies a tax on e-cigarettes at 95% of the wholesale price of e-liquid.


