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Civic Committee
COMMERCIAL CLUB OF CHICAGO

CIVIC COMMITTEE OF THE COMMERCIAL CLUB OF CHICAGO

POLICY POSITION OPPOSING THE GRADUATED INCOME TAX REFERENDUM

A comprehensive plan to restore the State's fiscal health will promote job growth and enable the State to provide critical services to all residents on a sustainable basis in the future. The proposed constitutional amendment to permit a graduated income tax is not a comprehensive plan: it does not solve the State's fiscal issues or change the negative narrative about the State.

If the amendment passes without a comprehensive plan, it will ensure that Illinois will continue to have the worst credit rating of any state in the country, suffer additional deterioration in job growth, experience further erosion of the tax base of individuals and businesses to pay for the existing unfunded liabilities, and force long-term cutbacks in critical services provided by the State to all residents.

Therefore, we oppose the graduated income tax amendment.

With its chronic budget deficits, growing pension debt, and backlog of unpaid bills, the State of Illinois has been the poster child for poor fiscal management for decades. Its challenges are well-known: its pension systems have roughly $137 billion in unfunded liabilities, a figure that is projected to continue to grow for almost ten more years. Its bill backlog stands at roughly $7.5 billion. Unlike most every other State, it has no reserve fund to speak of. The State's financial situation has become even more dire in the wake of the COVID-19 pandemic with revenues projected to plummet an additional $4.6 billion this fiscal year. Indeed, the State of Illinois has the worst credit rating of any State in the country.

These are not just abstract numbers. The State's longstanding fiscal mismanagement has real consequences for the people of Illinois. Despite our many competitive advantages – including our diverse economy, broad mix of industries, talented workforce, outstanding educational institutions and research facilities, central location, and diversified transportation network – our job growth is far below our potential and lags our peers.

Since 2000, real spending on core government services such as education, human services, and healthcare has *declined* by more than 23% as the State's financial resources have increasingly been consumed by the costs associated with our ballooning pension obligations. In fiscal 2021, State contributions to our pension system account for 20% of the State's general funds budget and these contributions are scheduled to grow significantly in future years. The State's fiscal situation is not only a chronic disincentive for people and businesses to locate in Illinois, but it also seriously jeopardizes the ability to provide critical services to Illinois residents. Simply put, Illinois' financial situation is unsustainable.

The Civic Committee of the Commercial Club of Chicago has consistently sounded the alarm about the scope of the State's fiscal issues and the need to develop a comprehensive plan to solve the State's financial issues and change the narrative about Illinois. In December 2006, we issued our report, *Facing Facts,* which put a spotlight on the State's growing pension debt, then $45.7 billion. In our 2019 report, *Restore Illinois: A Foundation for Growth*, we estimated that the State would need an additional $8 billion a year in increased revenues and expense reductions to fully address its financial challenges and change the narrative about the State's fiscal situation. We laid out a comprehensive plan through a Financial Framework to keep Illinois on a competitive footing and promote economic growth, and provided a menu of policy options to address the State's financial issues.

Proponents of the amendment seem to think that a graduated income tax will do the trick, and that the projected $3.6 billion in additional revenue is enough to address the State's financial difficulties. It is not.

Proponents emphasize that the ability to increase taxes on only a portion of the population is a feature that would make our tax system less regressive. While we understand the regressivity argument, (Illinois is one of only 9 states with a flat income tax while 32 states have some form of graduated income tax), unless a change of this nature is accompanied by a comprehensive plan to address the State's financial challenges, it will only make it easier for the General Assembly to avoid difficult decisions and refuse to face the State's financial problems head-on.

And, because the tax rate structure can be changed at any point, there is a serious risk that the General Assembly would attempt to increase tax rates on high earners (and potentially others) in the near-term future as financial pressures increase, which could push tax rates for the highest income taxpayers to levels that would make Illinois an extreme outlier and even less competitive as a place to live and work.

The bottom line is that unless the Graduated Income Tax is part of a larger, long-term plan to fully address the state's financial issues and change the narrative about the State's fiscal future, it is a piecemeal approach that will do more harm than good.

We could support a graduated income tax if it were part of a comprehensive plan that incorporates the following elements:

1. Balance the annual operating budget and pay down the excessive bill backlog.
2. Increase annual funding to pensions to get to "tread water" -- the point at which the State's unfunded pension liability stops growing -- sooner. This could result in billions of dollars of savings between now and 2045 and provide greater security on the payment of the existing obligations of the plans.
3. Place the State on a path to achieve an AA credit rating in the near-term future not simply to have a better rating to reduce the State's borrowing costs, but because a credit rating reflects a wide range of objective measurements of a State's fiscal health.
4. Include policies that will not make Illinois an "outlier" or create an anti-competitive environment in Illinois relative to other states.
5. Include defined timeframes to meet key benchmarks of the comprehensive plan.
6. Implement other reforms consistent with the rest of the country to alleviate the fiscal crisis which could include ending the exclusion on taxing retirement income and reducing the number of governmental units in Illinois.

We also believe that the time has come to consider action to modify the state's pension provisions, which currently provide for automatic 3% annual increases, to a new approach that ties annual increases to the actual rate of inflation. The current approach is an outlier compared to virtually every other state. Inflation has been far below 3% for years and is projected to remain there, making the automatic 3% increase a windfall rather than a way to keep up with the cost of living. Given the financial challenges faced by Illinois, we need to move to an approach more consistent with the rest of the country.

We hope that the voters in Illinois recognize that the Graduated Income Tax Amendment does not provide a real solution to the State's financial issues and similarly hope that the State's political leadership will commit to develop a comprehensive plan. If the Amendment passes, we fear that the hard work of seriously addressing the State's fiscal issues will continue to be delayed, at the expense of Illinois' future. We remain confident that there is still time to solve these important challenges and look forward to providing our support to focus on comprehensive solutions in the future.