

Thursday, April 19, 2007

From: Steve Morrill

Subject: GRT - 4/18 Senate Hearing - UPDATE

On Wednesday April 18, the Senate Education Committee and the Senate Revenue Committee held a joint hearing to discuss the Governor's GRT proposal contained within Senate Amendment #1 to SB 1 (Jones, E.). The committee, originally scheduled to begin at 1 pm, did not start until after 2:30 pm and ended just before 9 pm that evening.

The committee hearing was structured in two parts: (a) the Senate Education Committee convened first to discuss the education funding aspect of the GRT proposal; and (b) the Senate Revenue Committee convened thereafter to discuss the tax policy of the GRT proposal. Further, testimony for both committees was structured so that all of the proponents testified at the beginning, while any opposition testimony was delayed until the end of the committee.

The Administration paid for three economists, all from out of state, to testify on behalf of the positive effects of increased funding for education through increasing state taxes. One economist stated that increasing taxes for increased education will be a net benefit by "freeing up" local funds for other purposes. Another economist stated that increasing taxes is beneficial because it will create jobs and economic development. The third economist stated that increased education funding, through increased taxes, results in the biggest investment return for businesses.

The panel of out-of-state economists was greeted with some skepticism because none would be directly impacted by the GRT proposal if it became law in Illinois. Furthermore, many of the statistics cited by the economists were challenged by the committee on the basis that the Governor's GRT proposal is drastically different, in terms of size, scope and structure, when compared to GRT currently imposed by any other state.

Ohio was specifically called into question because the GRT rate in Ohio is substantially lower (.26%) and Ohio eliminated corresponding business taxes to make the fiscal impact of the GRT almost revenue neutral in Ohio. The State of Washington was also singled out because the tax structure is completely different in that there is no state income tax, but instead a state property tax. An observation was made that most states that currently impose a GRT border either an ocean, Canada, or both, so the businesses in those states cannot (unlike Illinois) easily move to a different state to base their operations.

During the Senate Education Committee hearing portion, two issues were acknowledged by all parties: (1) the property tax relief portion of the Governor's GRT proposal is not guaranteed to occur, since it is subject to appropriation; and (2) the vast majority of the revenue raised by the GRT will not go to increase education funding in Illinois.

Sen. Meeks made a pointed question to each of the economists and to the Illinois Department of Revenue: what is the estimate, in hard numbers, of the GRT that will be paid by Illinois businesses with gross revenues between \$2.0 million and \$10.0 million? The Department of

Revenue agreed to work with the Senator and the committee members to provide the answer to that question.

During education portion of the committee hearing, representatives from the Chicago Public Schools identified four criteria that the Mayor of Chicago must have met before he can support a tax increase for education funding. The four criteria are as follows: (1) the tax must provide automatic increases in education funding every year; (2) the proposal must contain reforms in education spending; (3) the proposal must contain a mechanism for property tax relief; and (4) the tax must impose the least possible burden upon working families.

During the Senate Revenue Committee portion of the hearing, the testimony was structured so that proponents would speak first, followed by business owners who wished to testify, and concluding with the business lobby associations.

Economist and former Illinois State Representative Doug Kane, who spoke in favor of the GRT proposal, made three relevant statements: (a) that pyramiding would occur with a GRT, averaging at 2.5 times the actual rate, but stated if the rate is low the pyramiding would not have a significant impact; (b) the GRT is a regressive type of tax, but less regressive than a sales tax; and (c) a GRT is successful if the rate is kept low and has a broad base. Mr. Kane also stated that, in order to raise \$7.6 billion in new revenues, the personal income tax would have to be doubled to 6%.

During the testimony of the Administration-sponsored economists, it became apparent that many Senate Democrats were asking pointed questions in an effort to get the answers they would need to vote in support of the GRT. It became apparent that Senate President Emil Jones has been exerting tremendous pressure on his caucus members to support the GRT.

Testimony from those opposing the GRT proposal included five business owners, the Taxpayer's Federation of Illinois, the Illinois Farm Bureau, the Illinois Manufacturers Association, and the Illinois Retail Merchants Association.

Testimony by the business owners demonstrated to the committee the practical effect the GRT proposal will have upon small businesses with gross receipts of between \$2.0 million and \$10.0 million. In summary, those businesses would either: (a) see all of their profits eliminated; (b) cause them to function with a net operating loss; (c) raise the price of their goods and services charged to consumers to make up the difference; (d) lose any competitive advantage they currently have as a "local business" to out-of-state companies that are not subject to the GRT; or (e) a combination of the above. In support of option (c) above, it was noted that a case originating in Kentucky had found that the State of Kentucky cannot prohibit the pass through of their GRT by a business due to the business' first amendment rights.

The owner of Wiley Furniture, who began the testimony for those opposed to the GRT, during questioning by the Senate President, stated that there are alternatives that should be considered over the enactment of a GRT. First and foremost, to control state spending by passing a budget plan that does not contain any spending increases or new programs until the natural revenue growth of the state is able to cover all of the expenses paid out. Also, to review all of the

“corporate loopholes” currently in state law and close those that may be fiscally necessary to help generate revenue. After those efforts are made, then look at what taxes, and preferably income or sales taxes, can be raised to make up any remainder of funding that is needed to pay for the functions of the state.

Also discussed was whether the GRT could be imposed upon a company based outside of Illinois’ borders. The issue revolved around the point of delivery. If a person bought a product from an out-of-state company, but had the product delivered into Illinois, then that transaction would be subject to the GRT as an imported good. However, in the same example, if the person purchased the product and picked up the product themselves to bring back into the state, then that transaction would not be subject to the GRT. Thus, companies just over the Illinois border will have a substantial competitive advantage over Illinois businesses if the GRT became law.

Finally, in a very brief mention, the Taxpayer’s Federation stated that there are potential constitutional issues with the imposition of a GRT in Illinois, and that the enactment of a GRT would more than likely trigger litigation challenging its validity.

Until the Senate Democrats begin to caucus specifically on a GRT vote, it will be difficult to determine the sentiment in the Senate for the GRT.

Best regards,
Steve

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