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The war of the 'woulds'

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One of this 159-year-old newspaper's core legacies is its conviction that government should intrude as little as possible on the lives of the citizens it serves. So when government says it needs more money from your pocket, this page sets a high burden of proof.

Today we propose a necessary increase of \$3 billion in state tax revenues for an aggressively reformed system of public education in Illinois. We believe the proof of need is there.

That increase in school funding should be inflexibly contingent on school reform. More money should not simply be ladled atop the system of education most children now experience.

This series argues that we don't devote enough dollars to education--and don't get enough in return for the dollars we devote. Prior installments urged specific steps to increase the accountability of public education here and advocated proven strategies for parlaying new revenues into student achievement.

Policy debates about how fully Illinois should fund education devolved decades ago into an uninspiring war of the "woulds."

Proponents of various rival revenue schemes say their plans would reduce our schools' reliance on much-resented property taxes, or would treat rich and poor districts more equitably, or would relieve state government's rising indebtedness. Opponents of these schemes say a tax increase would cripple many Illinois businesses, would discourage others from creating jobs here and would dump good money after bad.

After parsing these arguments--we could fill a page on each, so count your blessings--we're not sure that this dueling melodrama is justified.

We have, though, become sure of a few things:

Without more revenue, Illinois can't afford a meaningful rise in school funding. A scandalous habit of allocating tomorrow's revenues today has put Illinois on a path toward "financial implosion," as the Civic Committee of the Commercial Club of Chicago warned in December: Because the state owes \$106 billion--a number that's rising, not falling--Illinois can't meet its current obligations, let alone absorb new ones.

The state needs to make progress on its various crises, but fixing education, to improve the prospects of Illinois' economy, comes first.

Increased funding needs to come from a stable and broad-based revenue stream that grows with the state's economy. No one-shot gimmicks.

The governor of Illinois is in his fifth year of pledging to veto an increase in state sales or income taxes. Couldn't legislators override a veto? Not likely. Many of them are too skittish to push that hard for any tax hike--especially against a governor who shows no sign of flinching.

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So what's a reasonable approach to raise more dollars for Illinois schools? That's a question both of economic policy--What's the least harmful way for governments to raise money?--and of re-election politics. It's a question that has gridlocked Springfield for decades.

There are many ways to boost revenue, each with pluses and minuses. We favor one tax scheme, an unorthodox proposal to break the gridlock. But the tax scheme that would most help Illinois schoolchildren is whichever one lawmakers summon the courage to enact--in conjunction with education reform--in 2007.

A sampler of the basic schemes and themes:

- Legislate a so-called "tax swap"

That phrase is workshpeak for reducing property taxes that go to schools, while increasing state income taxes. The property tax cut supposedly would put citizens in the mood for a companion tax increase to help schools. This has been a loser in Springfield, in part because many taxpayers think it's a ruse: They suspect any drop in property tax bills would be short-term. They don't trust a swap. This idea has failed too often, because too many voters see it as misleading.

- Raise the state sales tax

Political Fact No. 1: Democratic lawmakers dislike sales taxes, which consume a big share of low-income families' money. Illinois collects 6.25 percent on most goods and shares one-fifth of that with local governments. Some of those local governments then pile on additional sales taxes. Bottom line: This is a regressive tax that many legislators won't want to raise much if at all. Netting \$3 billion would require hiking the state sales tax by 2 percentage points. Tough sell.

- Tax services

Illinois doesn't apply sales taxes to most services, the fastest growing sector of the economy. J. Thomas Johnson, a former state revenue director who heads the Taxpayers' Federation of Illinois, calculates that broadening the tax base to include services to individuals would raise state sales tax receipts from the current \$9 billion to about \$12 billion a year. (Johnson isn't endorsing that, just running the numbers.) That's defensible, but still regressive. It's also relatively unstable, overly dependent on consumers to keep shelling out for services in hard times. Too risky for this mission.

- Hike the state's personal income tax

Political Fact No. 2: Republican lawmakers dislike raising the income tax because they believe it falls hardest on their constituents. Boosting the income tax to 4 percent from 3 percent would increase revenues by \$3 billion a year. If you're raising taxes, this is a simple and fair way. But it's also easy to demagogue: Expect tax foes to target any legislator who votes for "a 33 percent tax increase!" In the DNA of many Illinois lawmakers you'll find visceral fear of raising this tax. And there's that veto threat.

- Sell or lease the state lottery

This shortsighted proposal would unload an asset capable of producing education money indefinitely. The payoff: big bucks to spend now on popular school programs. But the money would be gone in just a few years, leaving no source of revenue to replace it. This is just a terrible idea, something many Illinois legislators understand.

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Here's the best idea.

Voices as disparate as Cook County Assessor James Houlihan and Glenn "Max" McGee, a former state schools superintendent who now leads a district in Wilmette, have been trying to break the Illinois gridlock with an idea largely novel to this state: Collect a very low tax on the gross receipts of every business.

A 1 percent tax on gross receipts in Illinois--goods, services, the works--would raise more than \$13 billion a year, according to a study for Houlihan's office by Alma, Wis., consulting firm Program Analysis Inc. Illinois then could repeal the 5 percent state portion of the sales tax, which now gives Springfield \$7.5 billion per year, and kill the \$2 billion corporate income tax. The state would have revenue for a \$3 billion education fund, plus about \$500 million that could be directed to other needs or for other tax relief.

The breadth of its base would make the gross receipts tax a stable, growing source of money. Washington, Hawaii, Delaware, Ohio and Texas have extensive gross receipts taxes. Because it's easy to compute and collect, many other states apply such a tax only to utilities or other specific industries. Illinois taxes its casinos on gross receipts minus winnings paid out to gamblers.

The downside: Because it touches every business in a production cycle, a gross receipts tax pyramids as, for example, a forester's walnut tree becomes a sawmill's lumber, which becomes a furniture-maker's table, which becomes a store's retail sale. Imposing a 1 percent tax at each step makes items manufactured in Illinois less competitive elsewhere--and, for that matter, could tempt Illinois manufacturers to buy cheaper components in other states.

That said, zeroing out the state sales tax would instantly make Illinois a more attractive place for consumers to buy their retail goods. Killing the corporate income tax would be another bonus for many (granted, not all) Illinois companies. And while a gross receipts tax appears to fall on businesses, you can argue that it's factored into their prices and thus borne instead by the final purchasers.

So is this it? The solution guaranteed to please everyone? A species that lovely hasn't been seen in captivity. But endless debate over tweaks to sales, income and property taxes hasn't yielded a good way to fund schools. Time and again, we've all failed. So let's discuss something new. A gross receipts tax wears the blemish, and the beauty, of being a relative unknown here.

Johnson of the Taxpayers' Federation says businesses looking to locate or expand dislike unusual tax structures. If so, introducing a gross receipts tax to Illinois also would introduce a competitive disadvantage.

Ah, but now we're back to the war of the "woulds." What Illinois businesses and citizens most want, we suspect, is assurance that any new tax burden will make a genuine difference in the quality of education dispensed in Illinois classrooms. If Illinois lawmakers could deliver accountability and reform, they would find that a new tax is more palatable than they fear.

Sunday: Getting it done

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