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Synopsis of Testimony of Robert M. Coen
Professor Emeritus of Economics
Northwestern University

I have spent most of my career as an academic economist studying economic growth and tax policy. I have learned that there are strong technological, demographic, and political forces at work in growth processes that are difficult to foresee or even to understand fully after they have occurred. I applaud your efforts to find ways to promote growth in Illinois, but rather than my giving attention to specific policies or current proposals, I would like to take a broad look at the recent growth of Illinois in comparison to other states and areas to see what we can learn about the general forces at work. Lessons from the big picture can often be more useful in making good policy decisions than enumerations of special programs or incentives that worked here or did not work there.

Comparative Economic Performance of Illinois

Illinois is lagging the nation in growth of output and employment. National output grew 36.3% from 1997 to 2012, while Illinois's output increased only 21.8% (see Table 1). National employment grew 16.2%, while Illinois's employment grew less than half as fast (see Table 2). The Illinois experience partly reflects the mediocre performance of the Great Lakes area. Within the Great Lakes area, output growth in Indiana and Wisconsin surpassed that in Illinois, but Illinois fared far better than either Michigan or Ohio.

The sectors that contributed most significantly to national output growth were information, insurance, and business services (78.9% growth), health care (45.9%), finance, insurance, and real estate (45.5%), trade (45%), and manufacturing (42.6). States and regions that succeeded in these sectors led the nation and will probably continue to do so. Indiana dominated Illinois due mainly to greater expansion in manufacturing, information and related services, and health care. Wisconsin experienced about the same anemic growth of manufacturing as Illinois, but it had much stronger growth of information and related services. Still, the relative success of Indiana and Wisconsin within the Great Lakes region was far overshadowed by the rapid growth of younger, less-developed states of the Southwest, Rocky Mountains, and Far West, where the percentage gain in overall output was over 10 times that in the Great Lakes. For example, while manufacturing expanded by 48% in Indiana, it grew by 146% in the Far West; information services expanded respectably by 58% in Indiana and 75% in Wisconsin, but these numbers significantly trailed the 134% growth recorded in the Rocky Maintain region.

Growing output does not necessarily translate into growing employment. While the nation's manufacturing output rose 42.6% from 1997-2012, manufacturing employment actually <u>declined</u> 29.7%! The reason is the extraordinary rate of productivity increase resulting mainly from substitution of machines for laborers. Large increases in manufacturing output are required just to maintain the existing level of manufacturing employment. Job creation is more closely correlated with growth of the labor intensive service sectors -- trade, information, finance, management, education, and health care. Because Indiana's growth was more concentrated in the increasingly-automated manufacturing sector, the state failed to generate as much employment growth as Wisconsin and Illinois (Table 2).

Overall Tax Burdens and Economic Performance

Illinois's overall tax burden, as measured by the ratio of state and local tax collections to state income, was relatively low in the late 1990's, averaging around 9.4%, ranking only 35th highest among the states. By 2010, the rate had risen to 10.2%, and the state's rank rose to 11th.

It may be tempting to attribute Illinois's weak performance over the past 15 years to the state's rising tax burden, but there is no simple relation between the two. Output growth and tax burdens are compared in Table 3 for a set of what I call "benchmark states," that is, states geographically and historically close to Illinois and likely to be used as reference points for judging our performance. Indiana may have benefited by keeping a low overall rate of about 9.6%, placing it in the middle range of the 50 states. On the other hand, Wisconsin, which performed almost as well as Indiana in output growth and better in employment growth, has had a much higher tax burden of about 11%, ranking it among the five highest in the country during the period considered here.

Another measure of overall burden is the amount of state and local taxes collected per capita. Illinois has a relatively high burden by this measure, too, $4,512 in 2010, ranking 9th highest in the nation. Wisconsin, which has a higher overall ratio of tax revenue to state income, collects less per capita, $4,379, because it has a lower state income per capita. In 2011, Wisconsin's income per capita was $39,575, 27th in the nation, while Illinois's was $43,721, 16th in the nation. Even with its somewhat disappointing economic performance lately, Illinois continues to be one the nation's most prosperous states.

The strongest growth among these benchmark states was recorded by Minnesota, a relatively high-tax state by either measure. Nebraska, also with comparatively high tax burdens, had the second best growth performance.

The conclusion to be drawn is that high tax burdens do not necessarily deter growth , just as low tax burdens do not guarantee high growth. This should not be surprising for two reasons. First, the amount of revenue collected by a tax is not a good measure of its impact on economic efficiency. For example, a tax on an addictive activity that is difficult to give up will have little impact on economic behavior and the efficient use of resources, compared to a equal-yield tax on a good or activity for which there are readily available, satisfying substitutes Second, there are many factors other than tax levels that impact economic growth, including the extent to which tax revenue is used to foster growth by improving infrastructure, by aiding job training and education, and by creating attractive communities.

While Illinois now has a relatively high tax burden by either measure, there is still a need to increase revenue to meet already outstanding obligations and provide for public services that can aid in fostering future growth. Minnesota, one of Illinois's faster growing neighbors, has a tax burden that is over $200 higher per capita. Taxes can be higher without impinging on growth, provided they are raised in ways that minimize their effects on economic incentives, and provided that revenues are spent in ways that aid growth.

Sources of Tax Revenue and Economic Performance

Since equal-yield taxes are not necessarily the same with regard to their impacts on economic efficiency, differences in the structure of taxation might reveal some relationship to growth. Table 4 shows the distribution of taxes by major type for the benchmark states compared. Once again, systematic relationships to economic growth do not stand out. The tax categories are very broad, and the information is a snapshot for just one year, but even with more detailed data, relationships would be hard to identify.

We do see that Illinois has made comparatively light use of individual income taxation and general sales taxation and heavier use of property taxation compared to the benchmark states, but recent increases in income tax rates will bring Illinois more into line (the data cited here are for 2010). We can

Table 1. Percentage Growth of Real State Product, 1997-2012

	US	Great Lakes	IL	IN	MI	OH	WI
All sectors	36.3	15.8	**21.8**	28.8	1.7	9.6	25.4
Agriculture & mining	1.2	10.5	**5.1**	11.7	28.7	-12.9	37.6
Transport & Utilities	28.4	17.2	**19.0**	24.3	9.1	12.6	27.5
Construction	-20.5	-40.4	**-37.5**	-30.6	-54.0	-39.8	-35.6
Manufacturing	42.6	12.7	**17.3**	48.5	2.0	-7.2	18.0
Trade	45.0	29.3	**38.2**	32.0	17.9	23.6	37.0
Info, business & tech services	78.9	39.4	**41.1**	58.5	14.8	44.2	74.7
Finance, insurance, real estate	45.5	20.1	**27.2**	26.4	0.9	14.6	38.3
Management & administration	37.3	22.5	**34.5**	37.4	-15.9	40.2	37.1
Education	18.6	16.1	**22.8**	19.3	11.3	5.4	18.3
Health care	45.9	35.3	**33.1**	46.3	28.3	34.0	44.2
Arts & leisure	36.1	26.2	**33.4**	24.3	24.1	17.9	29.6
Government	11.7	-1.5	**7.8**	3.1	-12.8	-4.6	0.8

Source data: U.S. Bureau of Economic Analysis, Regional Economic Accounts, Gross Domestic Product by State

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Table 2. Percentage Growth of Employment, 1997-2012

	US	Great Lakes	IL	IN	MI	OH	WI
All sectors	16.2	4.0	**7.3**	5.3	-1.6	1.8	8.7
Agriculture & mining	-0.4	-10.2	**-15.8**	-13.2	-3.7	-6.7	-11.2
Transport & Utilities	12.5	9.2	**11.8**	8.9	5.1	9.4	7.5
Construction	4.1	-10.5	**-9.8**	-7.5	-17.3	-10.7	-3.4
Manufacturing	-29.7	-31.5	**-33.9**	-25.1	-36.8	-35.3	-20.3
Trade	3.1	-8.9	-5.5	-9.5	-13.1	-11.7	-2.5
Info, business & tech services	27.3	10.2	**9.1**	18.8	5.8	7.9	20.4
Finance, insurance, real estate	46.8	24.2	**25.7**	17.9	21.1	22.4	35.3
Management & administration	32.4	26.8	**30.5**	43.9	11.9	24.6	38.2
Education	68.3	65.9	**72.8**	70.2	71.2	56.9	54.9
Health care	43.2	33.5	**33.0**	34.9	29.0	36.8	33.6
Arts & leisure	30.3	18.4	**24.8**	20.1	13.5	13.1	21.7
Government	10.0	1.5	**2.2**	8.7	-5.6	-0.3	7.6

Source data: U.S. Bureau of Economic Analysis, Regional Economic Accounts, Annual State Personal Income and Employment, total full-time and part-time employment by industry

Table 3. Growth of Real State Product and State-Local Tax Burdens, "Benchmark" States

State	Growth 1997-2012 Percent	Growth 1997-2012 Rank	State-local Tax Burden, 2010 $ per capita	State-local Tax Burden, 2010 Rank	State-local Tax Burden, 2010 % of state inc	State-local Tax Burden, 2010 Rank
MN	40.5	18	4,727	7	10.8	7
NE	38.0	22	3,853	17	9.7	21
IA	34.1	25	3,660	26	9.6	24
KS	33.6	27	3,802	19	9.7	22
IN	28.8	32	3,294	32	9.6	23
WI	25.4	37	4,379	11	11.1	5
PA	22.7	39	4,183	14	10.2	10
IL	**21.8**	**41**	**4,512**	**9**	**10.2**	**11**
OH	9.6	49	3,563	27	9.7	20
MI	1.7	50	3,503	29	9.8	18

Sources: U.S. Bureau of Economic Analysis, Regional Economic Accounts, Gross Domestic Product by State; Tax Foundation

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Table 4. Growth of Real State Product and Composition of State-Local Taxes, "Benchmark" States

			-------------------- Percentage of Total Taxes from ------------------				
State	Growth 1997-2012 Percent	Growth 1997-2012 Rank	Property	General sales	Individual income	Corporate income	Other taxes(a)
MN	40.5	18	30.7	18.6	26.5	3.0	21.2
NE	38.0	22	36.8	21.7	20.6	2.1	18.9
IA	34.1	25	34.8	22.9	23.0	1.6	17.7
KS	33.6	27	34.4	25.4	23.6	3.1	13.5
IN	28.8	32	32.8	25.5	23.3	2.6	15.9
WI	25.4	37	39.5	17.4	23.7	3.5	15.9
PA	22.7	39	30.4	16.3	25.4	3.7	24.3
IL	**21.8**	**41**	**43.6**	**15.9**	**15.8**	**2.5**	**22.1**
OH	9.6	49	30.0	20.5	27.7	0.6	21.1
MI	1.7	50	40.3	25.9	16.4	1.9	15.4

(a) "Other taxes" include excise taxes (such as those on alcohol, tobacco, motor vehicles, utilities, and licenses), severance taxes, stock transfer taxes, and estate and gift taxes

Sources: U.S. Bureau of Economic Analysis, Regional Economic Accounts, Gross Domestic Product by State; Tax Foundation