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Debunking the Myth that Tax Policy Causes Out-Migration

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Debunking the Myth that Tax Policy Causes Out-Migration **Research Team**

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1. INTRODUCTION

Building fairness into a state tax system is difficult, because every tax and fee which is available to fund public services provided at the state or local level is regressive—that is, imposes a greater tax burden on low- and middle-income earners than on affluent individuals, when tax burden is measured as a percentage of income except for one: the income tax.[1] The income tax is the only tax that can actually be designed to comport with ability to pay and hence create some tax fairness, because it is the only tax that can be designed to assess higher tax rates on higher levels of income, and lower rates on lower levels of income.

Illinois, however, cannot use its state income tax to create tax fairness by offsetting the regressivity of all other state and local taxes and fees. That is because Article IX, Section 3 of the Illinois Constitution mandates that the state income tax be imposed at one flat rate across all levels of income.[2] Not surprisingly then, Illinois currently is, and has historically been, one of the most unfair taxing states in the nation.[3] Indeed as things stand today, an Illinois worker in the bottom quintile of earnings has an average state and local tax burden which is almost double that of an individual in the wealthiest one percent.[4]

In addition to making the state's tax system unfair, the constitutional mandate that Illinois has to impose its income tax at one, flat rate across all levels of income, prevents the income tax from generating adequate revenue over time, and thereby plays a major role in driving the ongoing deficits in the state's General Fund.[5] That's because it makes it impossible for the state to design its income tax to respond to the significant growth in income inequality that has occurred in Illinois over the last four decades.

Consider that, after adjusting for inflation, the average annual income of the wealthiest one percent in Illinois grew from $411,117 in 1979, to over $1.4 million by 2107, an increase of 254 percent.[6] During that same time period, the inflation-adjusted average annual income for the bottom 99 percent of workers in Illinois grew from just over $51,000 to just over $61,000.[7] Illinois' inability to utilize a graduated rate structure for its income tax means revenue generation cannot grow with the economy over time, because it cannot respond to how income growth is actually distributed in the modern economy.

On November 3, 2020, voters will have the chance to ratify an amendment to the Illinois Constitution which would allow the state to use a graduated rate structure for its income tax.[8] Ratification of this amendment would permit implementation of Public Act 101-0008 ("**P.A. 101-0008**") which was signed into law on June 5, 2019. If implemented, this legislation which is frequently referred to as the "**Fair Tax**" by proponents, would replace the state's current flat rate income tax with a graduated rate structure that: is tied to ability to pay; in normal economic times would raise around $3.5 billion in new revenue annually; and would effectively help eliminate some of the long-term structural flaws that have consistently made Illinois' overall tax system one of the most unfair and poorly performing in the nation.[9]

Many of those opposed to the Fair Tax have tried to mislead Illinoisans into voting against ratifying the proposed amendment to the state's constitution this November, by relying on arguments that have emotional appeal but are not supported by either evidence or the vast body of research. One such specious argument consistently made against the proposed Fair Tax is that the change to a graduated rate income tax structure will cause a mass exodus of middle-income households and millionaires from Illinois.

This claim, however, is exposed for the baseless canard it is when evaluated against the body of research covering the relationship—or as it turns out lack thereof—between tax policy and migration, as well as the relevant data from the Internal Revenue Service (**"IRS"**), U.S. Census Bureau, and the Illinois Department of Revenue (**"IDOR"**).

2. NO STATISTICALLY MEANINGFUL RELATIONSHIP BETWEEN TAX POLICY AND MIGRATION

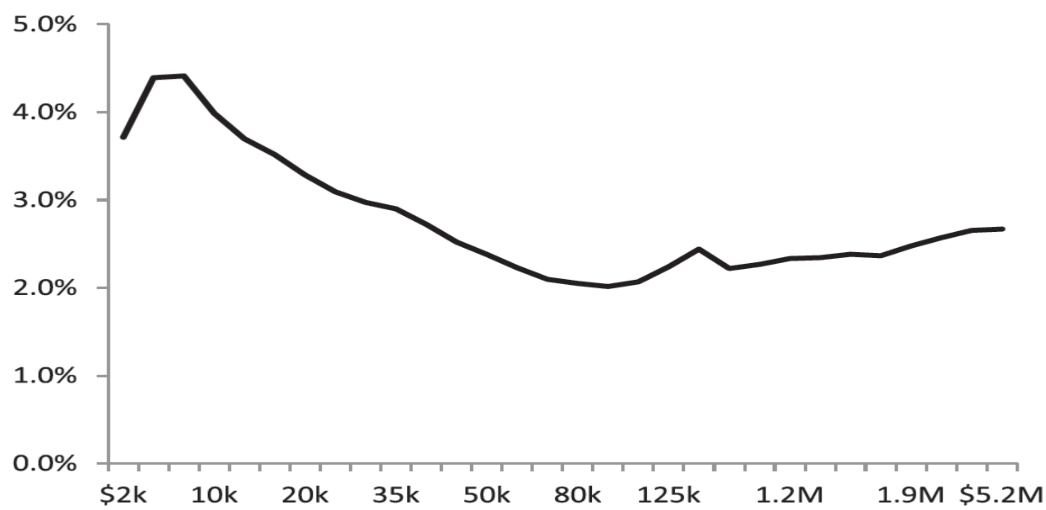
People (including millionaires) move for many complicated, interrelated reasons. The body of research on what motivates people in general, and high income households specifically, to migrate from one state to another, has consistently found no statistically meaningful correlation between a state's tax policies and the propensity for a family in that state to migrate.[10] Other factors, like proximity to family or a job, housing prices, education and even weather are what have a statistically meaningful influence on the decision to move.[11] In fact, a study done by Jeffrey Thompson of the Political and Economic Research Institute at University of Massachusetts Amherst, found that "nearly 9 in 10 working age adults relocate for jobs, housing, and family-related reasons."[12]

The data consistently show that even after taxes are increased, people generally do not leave their home states.[13] According to the PEW Research Center, which surveyed American households, family ties are a major reason people do not leave their hometowns, irrespective of changes in tax or other policies.[14] Other top reasons cited by Americans for staying in their home states were a sense of belonging, connection to friends, and having a good place to raise children.[15]

The aforesaid factors that either influence people to move or motivate them to stay in their home states were confirmed by Stanford Professor, Cristobal Young, who spent the last decade studying migration trends. In his book, *The Myth of Millionaire Tax Flight,* Young found only 2.4 percent of all millionaires in the nation migrated during the period between 1999 and 2011.[16] Of those millionaires who did migrate, 0.3 percent—or 20,000—did so for tax reasons, which he found demonstrates that the number of millionaires who do in fact relocate for reasons related to taxes is insignificant.[17]

Young also found that, as shown in Figure 1, the highest migration rates are realized at lower income levels, which primarily reflects individuals who are migrating in an attempt to better their lives.

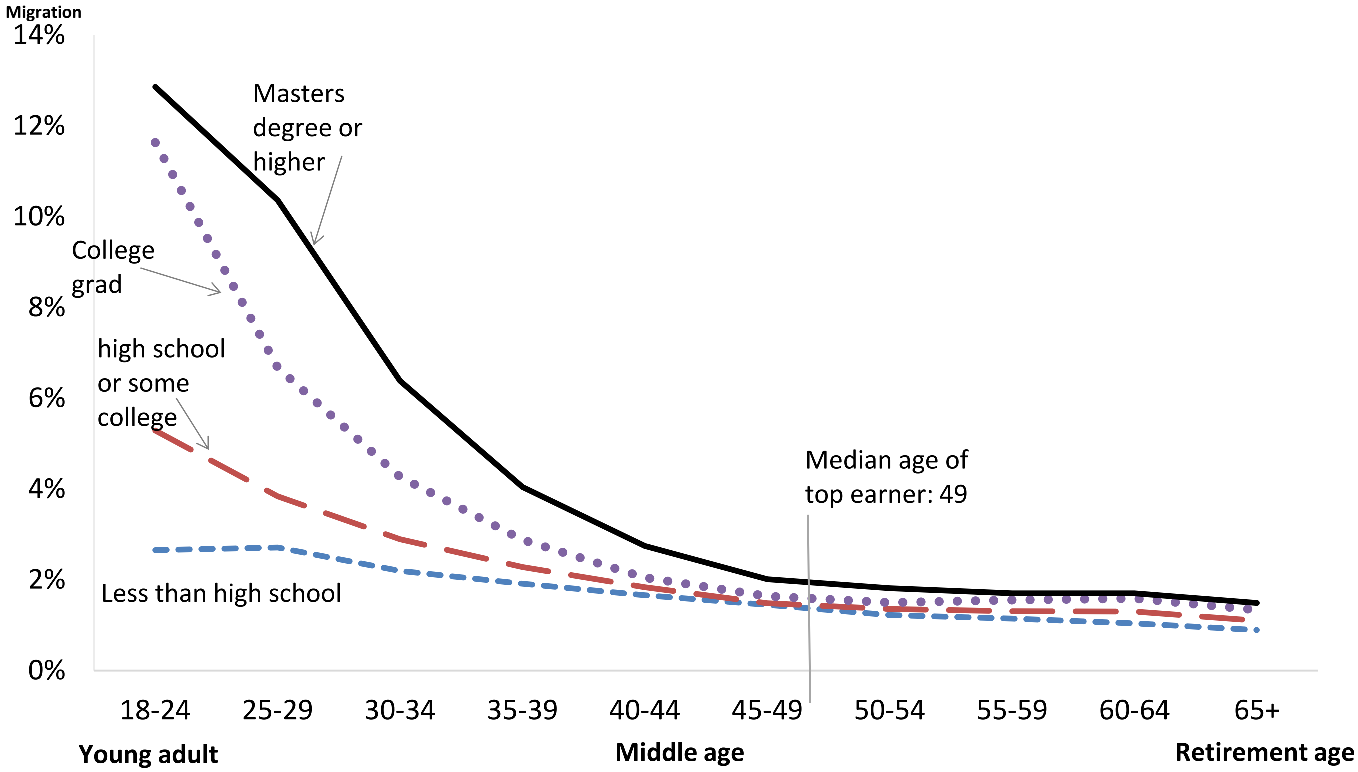
Figure 1
Migration Rates by Income, 1991-2011



Source: Cristobal Young, The Myth of Millionaire Tax Flight, 2017

Young's research also demonstrated that migration rates actually decrease with age and education, while those with a master's degree or higher between the ages of 18-29 have the highest rates of mobility. Young found that by middle-age, all groups of education attainment see an alignment of migration at around 2 percent, about a decade before peak income level, as shown in Figure 2.[18]

Figure 2
Migration Rates by Age, for different education groups, 2005-2014



Source: Cristobal Young, The Myth of Millionaire Tax Flight, 2017.

3. THE NEW JERSEY EXPERIENCE

Forty-one states in America have an individual income tax.[19] Thirty-two of those 41 states, including New Jersey, have a graduated rate structure, while nine have flat rates.[20] In 2004, New Jersey increased its top income tax rate from 6.37 percent to 8.97 percent.[21] This new top rate only applied to taxable income above $500,000, and was dubbed a "millionaire's tax."[22] Given that New Jersey is located close to other states like New York and Connecticut, and to large municipalities like Philadelphia, migration out of state by affluent individuals desiring to avoid the New Jersey "millionaires tax" was more feasible than it would be in many other states, because the individuals moving would be able to retain their jobs and stay close to their families.

For these reasons, two leading researchers, Cristobal Young of Stanford University and Charles Varner of Princeton University, decided to analyze whether implementation of the so-called "millionaire's tax" in New Jersey did in fact encourage millionaires to leave the state. According to their study, which was released in 2011 (the **"Migration Study"**), both before and after implementation of the "millionaire's tax," New Jersey experienced net out-migration of millionaires in every year from 2000–2007.[23]

That said, after implementation of the millionaire's tax in 2004, there was no statistically meaningful increase in the rate of out-migration by millionaires, which remained relatively constant at around 1.2 percent per year.[24] Indeed, the aggregate number of in-state millionaires continued to grow after the state's "millionaire's tax" passed.[25] That is because New Jersey produces millionaires, it is not an importer of millionaires.[26]

What the report did find, however, was that changes in the housing market rather than tax policy, are what really influenced migration rates. This was particularly so when the market was on an upswing, because housing booms made it easier for people to sell their houses.[27] In fact, when the housing market was thriving in New

Jersey from 2003 through 2007, increased housing prices encouraged people of all income levels to try to sell their homes, while simultaneously discouraging people from moving into New Jersey from other states.

The bottom line conclusions reached by the authors of the Migration Study were that people of all income levels, whether millionaires or of more modest means, generally do not migrate in response to a tax increase, and that any migration that does occur as a response to marginal tax policy changes is so small as to be statistically insignificant.[28]

4. NUMBER OF MILLIONARES PER CAPITA IS NOT CORRELATED WITH TAX POLICY

Research on the number of millionaires per capita in a state reveals no statistically meaningful correlation between state income taxes and millionaire location. For instance, a study conducted in 2017 by Phoenix Marketing International, a wealth research firm, ranked U.S. states by millionaires per capita. The firm defined millionaire households as those with $1 million or more in investable assets.[29] What Phoenix Marketing determined was being ranked at the top of the millionaire-ratio list appears to be as much a function of geography as policy.[30] As shown in Figure 3, the top five states in number of millionaires per capita include a no income tax state (Alaska) as well as four states that have graduated rate income tax structures, three of which also have some version of a "millionaire's" tax (Hawaii, Maryland, and New Jersey).[31]

Figure 3
Millionaire Households Per Capita, 2017

Rank	State	Total Households	$1M+ in Investable Assets	Ratio Millionaires to Total Households
1	Maryland	2,263,021	178,003	7.87%
2	New Jersey	3,294,365	258,988	7.86%
3	Connecticut	1,379,979	106,892	7.75%
4	Hawaii	487,708	36,903	7.57%
5	Alaska	272,496	20,444	7.50%

Source: Phoenix Marketing International, Ranking of U.S. States by Millionaires per Capita, Year-End 2017 Cycle

5. SOCIAL CAPITAL, EDUCATION, AND INCOME ARE WHAT MATTER IN CHOOSING A RESIDENCE—NOT TAX POLICY

The body of research also shows that the vast majority of individuals are drawn to live in states that have strong public services, which of course are paid for by tax dollars.[32] One study in particular, released by the Center on Budget and Policy Priorities ("**CBPP")**, found that "amenities such as cultural facilities, recreational opportunities and well-managed public services" attract potential new residents.[33] Well-funded public education matters as well.[34] This suggests, of course, that simply having a graduated rate income tax like the Fair Tax, which imposes higher tax rates on higher levels of income and lower rates on lower levels of income, will not drive people to migrate out of Illinois.

CBPP fairly and accurately summarized what the evidence has to say about the myths of tax flight, when it concluded that **"it would not be credible to argue that no one ever moves to a new state because of the desire to live someplace where taxes are lower. But neither is it credible to say that taxes are a primary motivation, nor that migration has a large influence on the revenue impact of tax measures."**[35]

CBPP determined that six out of seven peer-reviewed studies found that taxes do not drive interstate migration.[36] More so, out of eight additional studies on the impact of state taxes on migration, six of the eight found either that state income taxes had no effect on migration, or that the effect was small or inconsistent.[37] In fact, much like the Migration Study of the millionaire's tax in New Jersey, CBPP found that housing prices are more likely to have an impact on migration than income taxes.[38]

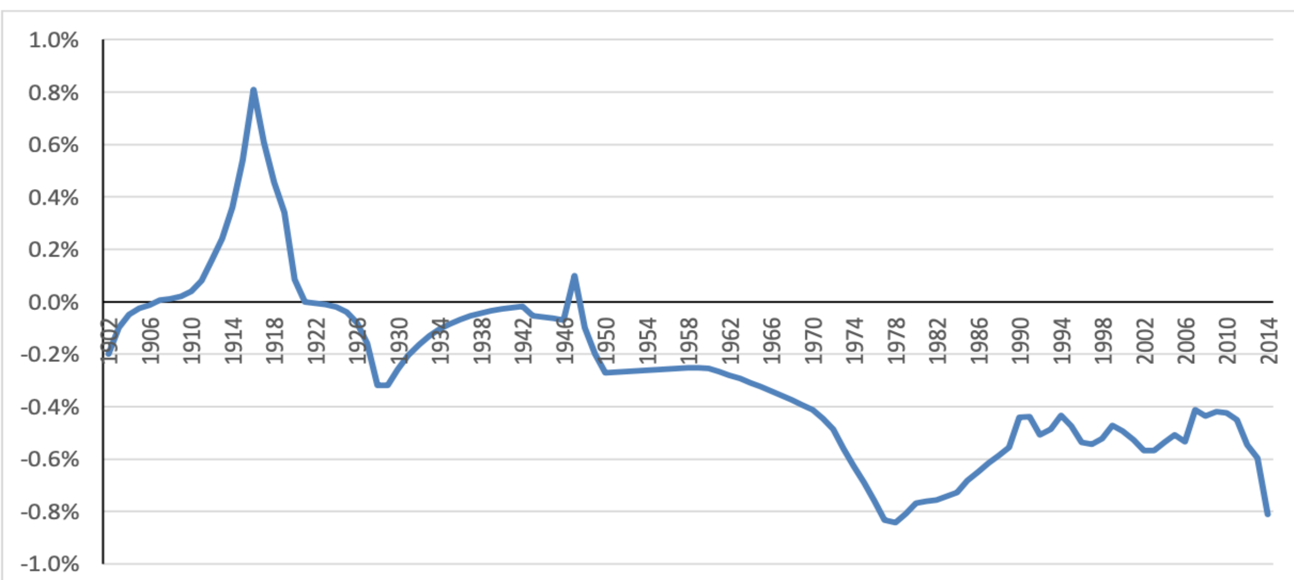
6. MIGRATION PATTERNS IN ILLINOIS

Many of the migration arguments raised against the Fair Tax lack credibility for two reasons. First, contrary to both the body of research in the area and what the actual data show, they claim there is a causal relationship between increasing income taxes on a progressive basis, and out-migration of population, when in fact no such causal relationship exists.

Second, they try to overstate the issue of migration by focusing solely on the number of individuals who leave the state—that is out-migration—without offsetting that population loss against the number of people who migrate into Illinois annually from other states and indeed nations. However, to gain an accurate understanding of overall population migration, out-migration has to be offset by in-migration, to determine the actual "**net migration"** based change to state-level population.

A report published by economist Natalie Davila and tax policy expert Mike Klemens of KDM Consulting, both formally of IDOR, found that Illinois has had negative net migration every year since 1920, with the exception of one year, 1947, as shown in Figure 4.[39]

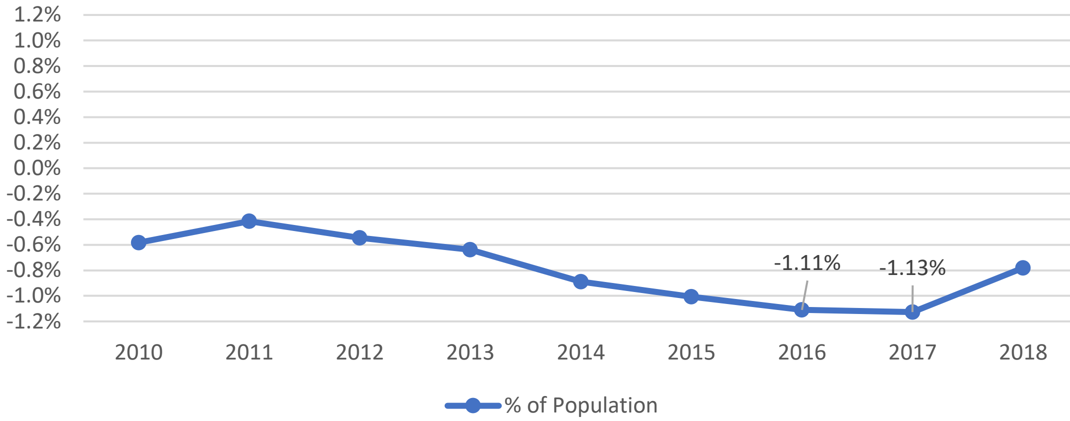
Figure 4
Net Migration in Illinois as a Percent of Population, 1910 to 2014



Source: KDM, "Who is leaving Illinois and why?", 2016.

The KDM report was published in 2016, and therefore data was only available through 2014. So CTBA updated the annual net migration computation for Illinois to include the most recent data available. As shown in Figure 5, **negative net migration peaked in 2016-2017, when Illinois was in the midst of a budget impasse.** Interestingly, over that same two year period, the state's personal income tax rate had been decreased from the 5% level it was in 2015, to 3.75% during the first two years of Governor Rauner's administration.[40]

Figure 5
Net Migration in Illinois as a Percent of Population, 2010-2018



Source: U.S. Census Geographic Mobility Data

Of even greater interest, **net out-migration from Illinois actually decreased from 2017 to 2018—which is after the state raised its personal income tax rate in 2017 to its current level of 4.95 percent, from the 3.75 percent rate that pertained in 2016.**[41]

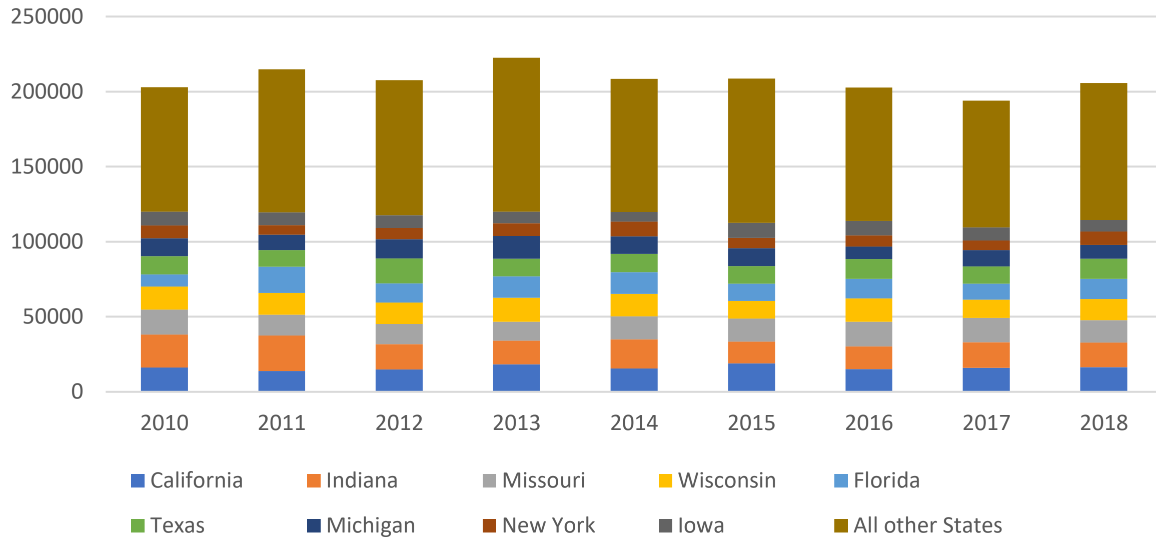
The fact that negative net migration peaked in Illinois when the state's income tax rates were cut, and then lessened in the year those tax rates were increased, certainly indicates that income tax rates do not drive people to move. On the contrary, it may suggest that the uncertainty surrounding a lack of budget and potential disinvestment in core services (education, healthcare, human services, and public safety) had a greater impact on migration decisions, which aligns well with the literature review done, and conclusions reached by CBPP, that are referenced in Section 5 of this Report.

At the end of the day, and despite the charged rhetoric from the anti-Fair Tax crowd, Illinois does not actually have an unusually high out-migration rate. In fact, Illinois had the 33rd highest out-migration rate among all 50 states and D.C in 2018.[42] While it's of course worth trying to keep people from leaving the state, Illinois is better off focusing on what the evidence indicates has a statistically meaningful relationship to attracting people to move to a different state: quality education, job opportunities, and housing prices.

7. THE DATA ABOUT MIGRATION BETWEEN AND AMONG ILLINOIS AND THE OTHER 50 STATES SHOWS NO MEANINGFUL CORRELATION TO TAX POLICY

According to U.S. Census data, in 2018, while 305,000 people moved out of Illinois into other states, 206,000 people from other states moved into Illinois.[43] People moving from other states into Illinois is nothing new. So where do most of the individuals who move into Illinois from other states come from? Since 2010, people from nine states—California; Florida; Indiana; Iowa; Missouri; Michigan; New York; Texas; and Wisconsin—have accounted for over 50 percent of the total gross in-migration for Illinois, as shown in Figure 6.[44]

Figure 6
Top States for Gross Migration Into Illinois: 2010 through 2018.

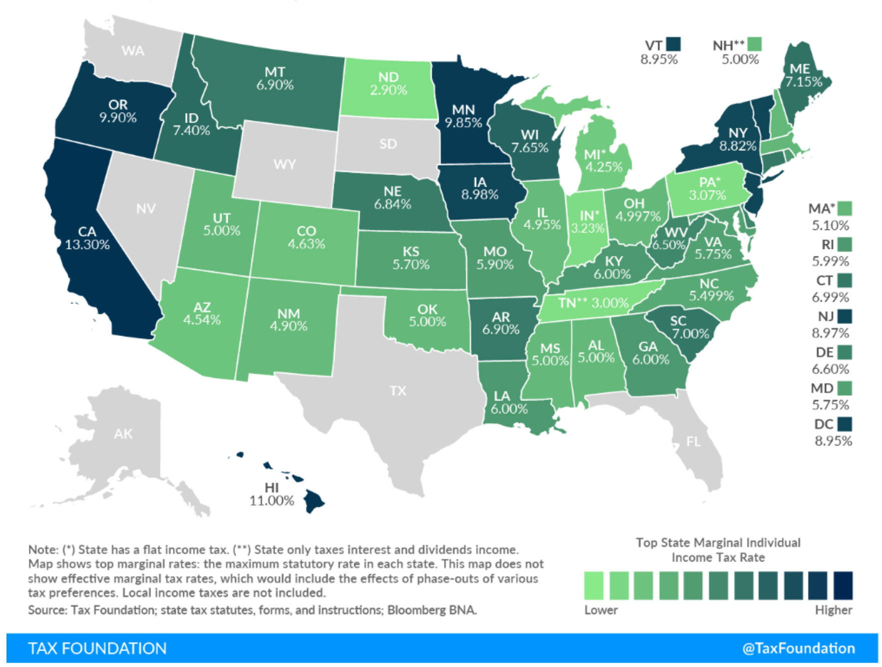


Source: U.S. Census Geographic Mobility Data, Illinois

If the argument that tax policy generally, and increased income tax rates specifically, actually caused people to relocate from one state to another was credible, then one would expect to see the data confirm that in fact people moving into Illinois are doing so to leave higher income tax states.

But that is not what the data show. For instance, of the nine states which account for most of the individuals who moved into Illinois over the last decade, it is true that five of them—California, Iowa, Missouri, New York, and Wisconsin—all have graduated rate income tax structures with a top marginal rate that is higher than Illinois' flat rate, as shown in Figure 7.[45]

Figure 7
Top State Marginal Individual Income Tax Rates, 2018

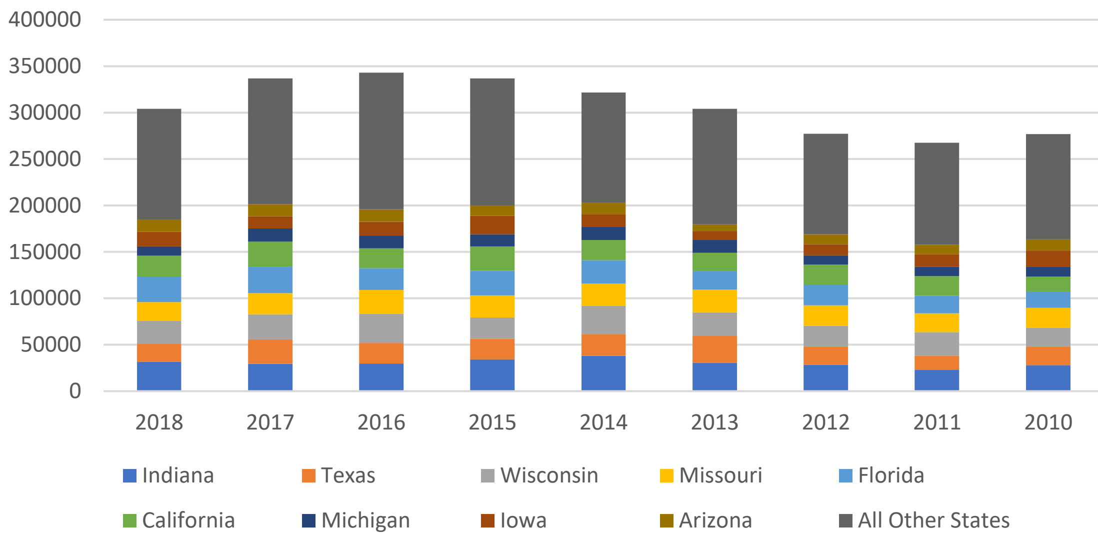


Source: Tax Foundation, "State Individual Income Tax Rates and Brackets for 2018", March 5, 2018.

However, of the remaining four states that account for most of the migration into Illinois, Indiana and Michigan both have a lower flat rate income tax than Illinois, while Florida and Texas have no income tax.[46] This runs expressly counter to the argument that people migrate to avoid higher income taxes, because if that were truly the case, then there would be very little to no migration into Illinois from Indiana, Michigan, Florida, and Texas. Instead, these four states are among the nine states which account for the greatest number of people moving into our state.

On the flip side, into which states do the people who move out of Illinois choose to relocate? Similar to the in-migration trends, nine states—Arizona; California; Florida; Indiana; Iowa; Missouri; Michigan; Texas; and Wisconsin—accounted for over 50 percent of the total gross out-migration from Illinois, as shown in Figure 8.

Figure 8
Top States for Out-Migration from Illinois: 2010 through 2018

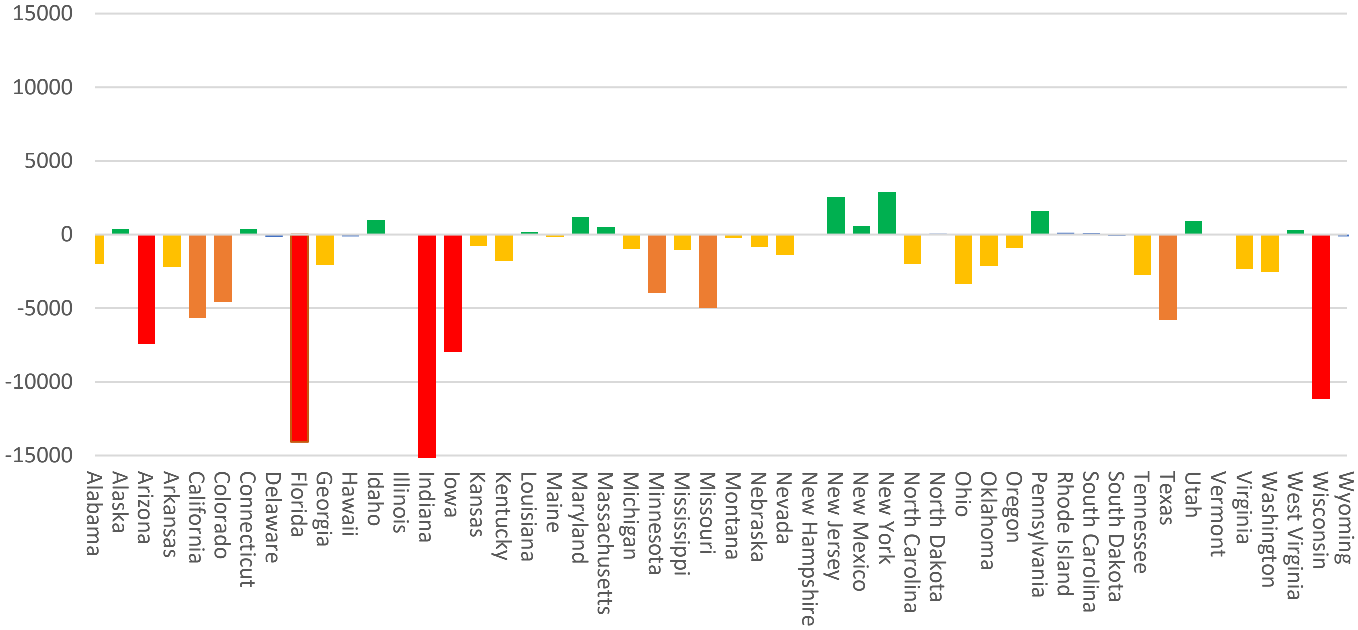


Source: U.S. Census Geographic Mobility Data, Illinois

Again, if the argument claiming a causal relationship between tax policy and migration were credible, then Illinois residents should be leaving the state to move to states with lower income tax rates, or no income tax at all. However, from 2010 through 2018 just the opposite occurred. **Significantly more former Illinois residents—1.6 million—moved into states such as California, Missouri, Wisconsin, and Iowa, where the top marginal income tax rates are higher than the flat rate in Illinois, than the 1.2 million former Illinois residents who moved into states like Indiana, Texas or Florida, which either have lower income tax rates than Illinois, or no income tax whatsoever.[47]** This aligns with the body of research on migration which consistently finds no statistically meaningful relationship between tax policy and migration.

This trend continued in 2018, the most recent year for which there is data. As shown in Figure 9, **more former Illinois residents—170,527—moved into states that had higher top income tax rates than the 4.95 percent flat rate that pertains in Illinois, than the 134,506 former Illinois residents who moved into states with lower top income tax.[48]**

Figure 9
Illinois Net Migration, 2018



Source: U.S. Census Geographic Mobility Data, Illinois

The bottom line is again clear: the actual trends concerning migration into and out of Illinois, as well as the body of research, show there is no statistically meaningful relationship between state income tax policy and migration.

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[43] CTBA analysis of U.S. Census Bureau, “Table 1. State-to-State Migration Flows: 2018.”
[44] CTBA analysis of U.S. Census Bureau, “Table 1. State-to-State Migration Flows: 2018.”
[45] While 2018 is represented due to most recent available data, the statement remains true for 2020.
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