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Center for Tax and Budget Accountability and Taxpayers' Federation Release Joint Report Calling for Illinois to Expand the Sales Tax Base to Include Consumer Services

SPRINGFIELD – Today, the Center for Tax and Budget Accountability (CTBA) and the Taxpayers' Federation of Illinois (TFI) jointly released a new report, *Expanding the Base of Illinois' Sales Tax to Consumer Services Will Both Modernize State Tax Policy and Help Stabilize Revenue*. The report identifies why expanding the base of the state sales tax to include consumer services—like pet grooming, haircuts, country club membership, health clubs, and lawn care—would simultaneously help to stabilize revenue generation for the state's fiscal system, while reforming tax policy to comport with the modern economy.

"For a sales tax to play its role of generating stable revenue for the fiscal system, it has to apply broadly to most transactions that occur in the consumer economy," said Ralph Martire, Executive Director of CTBA. "Today, consumer spending is the largest segment of both the nation's and Illinois' respective economies, accounting for nearly 70 percent of all economic activity. Also, consumer spending usually does not decline substantially—even during major economic downturns. If a sales tax base broadly applies to most transactions in the consumer economy, that sales tax will have the capacity to provide some stability to a state's fiscal system, even when other more volatile revenues are declining rapidly."

As detailed in the report, Illinois is one of 45 states that impose a general sales tax. And while the state-only sales tax rate of 5 percent is below the national average state-only sales tax rate of 5.5 percent, Illinois' sales tax rate is applied, in large part to the sale of goods (like clothing and furniture) and not services (like pet grooming, health clubs, lawn care, and haircuts). Illinois' sales tax applies to few services. In fact, of the 45 states with a general sales tax, the average number of service industries taxed is 51; Illinois is an outlier, taxing only five consumer service industries. And that is why the state's sales tax policy fails to jibe with the modern economy. Indeed, over 72 percent of the Illinois' economy is derived from the sale of services, while just 17 percent stems from the sales of goods.

“The focus on consumer services in the report is intentional,” said Carol Portman, President of TFI. “There are a number of service industries which should not be included in the state’s sales tax base. For instance, both of our organizations recognize that business-to-business transactions should not be taxed, because doing so creates economic distortions and inefficiencies that often result in ‘tax pyramiding’.”

According to the report, tax pyramiding occurs when essentially one economic transaction is taxed multiple times during production and distribution. This artificially increases the cost of a product or service as it flows through the state’s economy, which is highly undesirable.

Expanding the Base of Illinois’ Sales Tax to Consumer Services Will Both Modernize State Tax Policy and Help Stabilize Revenue, estimates that $2.105 billion in additional revenue could be generated if Illinois’ sales tax base was expanded to include primarily consumer service industries, while excluding business-to-business transactions and professional services. This could go a long way toward addressing the state’s fiscal difficulties. The report also notes that by broadening the state’s sales tax base, Illinois may also be able to reduce the state’s sales tax rate if policy makers so choose.

There may currently be some political will to consider expanding the state’s sales tax base. Increasing state tax revenue by expanding the sales tax base to include services would be timely, because the temporary state income tax rate increases enacted in 2011 began phasing down on January 1, 2015. In FY2016, the rate reductions are estimated to create a year-to-year loss of $3.4 billion in recurring General Fund revenue from FY2015 levels.

“We need a tax code designed to work in the modern economy, but our current policy on the sales tax—with its narrow base focused on the sale of goods—is better suited to 1915 than 2015,” said Senator Toi Hutchinson (D-Olympia Fields), Chair of the Senate Revenue Committee. “Expanding the Illinois sales tax base to include services is not a silver bullet that will solve all the fiscal problems facing the state, but it is a needed and crucial step forward.”

-- 30 --

The Center for Tax and Budget Accountability, established in 2000, is a bi-partisan 501(c)(3) research and advocacy think tank that promotes fair, efficient and progressive tax, spending and economic policies.

The Taxpayers’ Federation of Illinois, formed in 1940, is a nonpartisan state and local tax and fiscal policy organization focused on research, education, and advocacy for a responsible tax structure that encourages economic growth and supports efficient delivery of government services.