Chicago Metropolitan Agency for Planning

Regional Tax Policy Task Force

Report to the CMAP Board - DRAFT

December 9, 2011

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Letter of Transmittal

December 9, 2011

To the Board of the Chicago Metropolitan Agency for Planning:

We are pleased to submit to you the final report of the Regional Tax Policy Task Force.

Our charge was defined in GO TO 2040, northeastern Illinois' Comprehensive Regional Plan, to advise the Board by:

"…addressing issues central to state and local fiscal policy, viewed through the lens of the regional economy, sustainability, equity, and the connections between tax policy and development decisions."

We appreciate your selection of each of us to serve on the Regional Tax Policy Tax Force, and your confidence that we can provide advice and guidance on how CMAP should exercise its responsibilities with respect to the design and execution of tax policies.

The members of the Task Force bring a wide range of expertise and experience with respect to the issues of tax policy. The observations and recommendations contained in this report reflect the views of the individual members. In no way are they directly or indirectly endorsed or supported by the governments or organizations with each of the members are affiliated.

Finally, it has been an honor to serve on the Task Force. Thank you for the opportunity to serve the region's interests.

The Regional Tax Policy Task Force

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Introduction

The region's comprehensive plan, GO TO 2040, is the central reference point for the Regional Tax Policy Task Force. The plan, which was adopted unanimously by the CMAP Board in October 2010, identifies the critical role that tax policies play in supporting, or inhibiting, the accomplishment of the goals and policies adopted in the plan. GO TO 2040 contains a detailed discussion of the ways that tax policies may influence achievement of its goals and identifies a number of possible changes to tax policy. It recommends the creation of the Regional Tax Policy Task Force as a mechanism to further evaluate the issues and to make more specific recommendations.

GO TO 2040 emphasizes that our tax system has a large impact beyond the public revenue raised for public services. Tax policy directly influences the commercial and residential development of our communities as well as the region's economic productivity. These policies sometimes distort land use decisions rather than allow markets or quality of life factors to guide them. Tax rates are often set high while the tax base is narrow rather than broad. The transparency and accountability of these systems to the taxpayers has room for improvement.

GO TO 2040's vision is for state and local tax policy to encourage local decisions that make effective use of land, generate good jobs, and trigger sustainable economic activity. It should set high standards of transparency and predictability for the taxpayer. It should also not create large inequities across households, businesses, and local governments. By reforming state and local taxation, the region would benefit from new policies that help to advance rather than undermine GO TO 2040's goal for sustained regional economic competitiveness.

GO TO 2040 was built on the premise that the region is both a collection of independent governments, as well as a single economic entity that is competing with other metropolitan areas throughout the world. CMAP is a unit of government, created by state law, with a mandate to make the region successful.

GO TO 2040 recognizes that tax policy is a complex and often controversial topic. Proposals to change taxes are usually met with intense debate among the governments that require revenue to meet the service and infrastructure needs of the public, and the business and individuals who pay the tax bills. The composition of the Task Force was designed to reflect these multiple interests.

Tax policy is essentially the responsibility of state government. The State sets tax policy for itself and defines the conditions under which local governments may raise and spend tax revenue. Typically, a tax proposal will draw the interest of individual governments as well as associations of local governments, counties, townships, schools boards and special taxing districts. In addition, the debate might involve individual businesses as well as entities that represent various taxpayer interest groups.

The CMAP Board, through the publication of GO TO 2040, has determined that because of its charge to make the region successful, it should have a voice in the determination of tax policy. That determination is based on the fact that the CMAP region represents around two-thirds of the State's population, income, tax revenue, and assets. It is further based on the legislation that created CMAP, and the fact that many issues critical to the region's success cannot be addressed simply as the sum of individual government interests.

The character and limits of the CMAP voice are discussed in the Plan. The charge to the Task Force was to provide further guidance and advice to the Board as to how, and under what circumstances, CMAP should exercise its responsibilities with respect to tax policy. The Task Force was free to make specific recommendations with respect to existing or new legislation or to offer more general guiding principles

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or observations. The Task Force exists to advise the CMAP Board and has no statutory or independent authority.

This report contains three major sections:

1. Summary of Tax Policy Issues: This section is a necessarily brief summary of the discussions, debates, and observations that were part of the Task Force deliberations. None of the comments in this section should be viewed as recommendations. They are meant to reflect the range of opinion expressed by individual members of the Task Force.

2. Recommendations: This section represents a consensus view of the Task Force with respect to its assignment to advise the CMAP Board on carrying out its responsibilities to address issues of tax policy.

3. Analysis of Existing State and Local Tax Policy Conditions: This section contains a summary of the detailed background information and data used by the Task Force as it deliberated the policy implications of various tax systems.

Membership

The Regional Tax Policy Task Force was created in spring 2011 by the CMAP Board. The Board ensured a balanced membership, comprised of representatives from state, county, and municipal government, academia, civic organizations, and business. The Board approved the appointment of Frank Beal, Executive Director, Metropolis Strategies, as Chair of the Regional Tax Policy Task Force. The other members are as follows:

- Zahra Ali, Director, Cook County Department of Revenue
- Paul Braun, Mayor, Village of Flossmoor
- Barry Burton, County Administrator, Lake County
- Karen Darch, President, Village of Barrington
- Paul Fisher, President and CEO, CenterPoint Properties Trust
- Larry Hartwig, Mayor, Village of Addison
- Tom Johnson, President, Taxpayers' Federation of Illinois
- Mike Klemens, Manager, Office of Policy and Communications, Illinois Department of Revenue
- Dan Long, Executive Director, Commission on Government Forecasting and Accountability
- Daniel McMillen, Department of Economics and Public Affairs, University of Illinois
- Laurence Msall, President, Civic Federation
- Chris Nash, Assistant Budget Director, Office of Budget and Management, City of Chicago
- Michael Pagano, Dean, College of Urban Planning and Public Affairs, University of Illinois at Chicago
- Donovan Pepper, Senior Manager, Government Relations, Walgreen Co.

Process

The Task Force held ten monthly meetings between April 2011 and January 2012. Policy topics were discussed during the first seven meetings. The last three meetings were dedicated to discussing and crafting final recommendations. The following provides a summary of the first seven meetings.

April 8 meeting. The introductory meeting included staff presentations on GO TO 2040 as well as a general overview of state and local finance issues. The members also discussed the mission and scope of work for the Task Force.

May 13 meeting. During this meeting, Mike Klemens, Illinois Department of Revenue, gave a presentation on the history of state revenue sharing. In addition, the Task Force discussed state sales

tax revenue sharing with local governments and alternatives for modifying the criteria used for disbursing revenues.

June 17 meeting. Michael Pagano, University of Illinois at Chicago, began the meeting with a presentation on the land use implications of taxation, with an emphasis on case studies from other regions. The Task Force was provided with an example formula for changing the criteria for sharing state sales tax revenues with municipalities and members continued discussion of state sales tax revenue sharing.

July 8 meeting. This meeting began with a presentation from Frank Beal, Metropolis Strategies, about the economy of metropolitan Chicago and its growth relative to the rest of the country. Following discussion of the presentation, the members discussed expanding the sales tax base to services. In addition, the Task Force discussed the personal property replacement tax and the criteria used for distributing these revenues to local governments.

August 12 meeting. During this meeting, the Task Force discussed two recommendations already adopted by the CMAP Board: ending the "55/45 split" for Illinois transportation funding and increasing the state motor fuel tax. In addition, the Task Force discussed state motor fuel tax revenue sharing with local governments.

September 9 meeting. The Task Force discussed both expanding the state income tax base to retirement income as well as methods to make the income tax more progressive. After this discussion, the Task Force moved onto property taxes. Lise Valentine of the Civic Federation gave a presentation on property tax issues including property tax rates, assessment, and classification and the members discussed property tax classification in Cook County.

October 14 meeting. The Task Force began the meeting by discussing the Property Tax Extension Limitation Law. In addition, the Task Force discussed guiding principles to use for developing final recommendations.

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1. Summary of Tax Policy Issues

This section is a necessarily brief summary of the discussions, debates, and observations that were part of the Task Force deliberations. **None of the comments in this section should be viewed as recommendations**. They are meant to reflect the range of opinions expressed by individual members of the Task Force.

The Regional Tax Policy Task Force was created by the CMAP Board to address a number of high priority state and local tax policy issues included in GO TO 2040, the regional comprehensive plan for northeastern Illinois. GO TO 2040 specifically recommended the following topics for evaluation by the Task Force:

- Existing state and local revenue sharing criteria with particular emphasis on the sales tax
- Property tax assessment classification and the property tax extension limitation law
- Broadening the tax base and lowering tax rates, including expanding the sales tax to the service sector
- The efficiency and equity of the state income tax
- The existing wide disparities in local tax capacity

State Revenue Sharing with Local Governments

GO TO 2040 recommended that the Task Force evaluate state revenue sharing criteria, including the sales tax, income tax, personal property replacement tax (PPRT), and motor fuel tax (MFT). State statute requires different criteria for disbursing the revenue depending on the tax from which the revenue was generated.

The main policy question for the Task Force was whether this large-scale investment, allocated through various formulas, promotes desired regional outcomes such as economic productivity, sustainable spatial development patterns, and efficiently providing sustainable revenues for state and local governments to provide necessary services and infrastructure investments. In response to GO TO 2040's charge, the Task Force examined the impacts of revenue sharing on the region.

Sales Tax Revenue Sharing

GO TO 2040 charges the Task Force to "place a particular emphasis on the sales tax" because of its direct link to retail development decisions and thus, the overall spatial pattern of the region. The State disburses approximately $1 billion in state sales tax revenue to municipalities, which receive 16 percent of the sales tax collections based on local point of sale.

GO TO 2040's analysis of this disbursement structure found that it can create a fiscal incentive for local governments to emphasize retail land use at the expense of other uses, such as offices or industrial uses. In addition, the sales tax revenue sharing criteria can create incentives for intraregional competition for businesses, leading to shifts between communities that add no new jobs or economic value to the region.

The Task Force examined the current sales tax revenue sharing criteria as well as different methods for changing the criteria. It was generally acknowledged that local governments have planned for their future based on the current revenue sharing policies. Retail development comes with positive attributes, but also negative impacts like noise and traffic that must be mitigated. The revenue benefits from sales taxes must be balanced with the infrastructure, public service and other costs that the community incurs as a result of hosting retail establishments.

Many local governments have struck a balance between residential, commercial, and industrial development. Some members expressed that it is important to ensure that communities that have made planning decisions based on the current criteria do not incur negative consequences from future policy changes.

Other members of the Task Force were concerned that criteria based on the location of sale resulted in residents of neighboring communities paying sales taxes for municipal services above and beyond those required for the businesses that generate the revenue. According to an analysis using CMAP's trip generation model and information from CMAP's recent Travel Tracker survey, approximately 47 percent of daily shopping trips are made to destinations outside of shoppers' home municipalities.[1] These residents shopping outside of their home municipality travel through other municipalities that must provide services or infrastructure associated with that trip.

In addition, some Task Force members were concerned about the varied distribution of the state sales tax revenue across the region. According to 2010 data, municipalities covering 26 percent of the region's population received 50 percent of the municipal disbursements. The municipalities with the remaining 74 percent of the population shared the other half.[2] Many communities with low tax bases are unable to raise the revenue required to provide the public services necessary to attract residents and businesses to their community.

Some members also expressed concern regarding the provision of municipal sales tax rebates. These rebates are an outgrowth of the high tax revenues some retail establishments can generate for local governments. Under these arrangements, taxpayer dollars are paid to private businesses rather than being used for government services. The purpose of these rebates varies, and some of the funds are used for infrastructure projects and other services that contribute to the public good.

The existence or the details of these sales tax rebate agreements is not always disclosed to taxpayers. One recent symptom of the intense intraregional competition over retail business location can be seen in the current litigation regarding how sales taxes are sourced in Illinois. The Regional Transportation Authority (RTA) and several other taxing bodies have filed a lawsuit alleging that the villages of Channahon and Kankakee have used sales tax rebate agreements to encourage companies to set up sales offices outside the RTA service area, resulting in lost sales tax revenue for the RTA.[3] The Task Force agreed that local governments should enhance transparency in the sales tax rebate agreements they make with businesses, while ensuring that the private financial information of private companies is safeguarded.

Personal Property Replacement Tax Revenue Sharing

The Task Force discussed the disbursement of the PPRT. Some members voiced that disbursing this revenue based on the amount of local government personal property tax revenue generated in 1977 has resulted in a system that no longer has a relationship to the needs of the region and its economy.

The local disbursements of the PPRT have not changed in accordance with any shifts in demographics or economic activity, but are still heavily relied upon by many units of government, especially special

[1] See http://www.cmap.illinois.gov/travel-tracker-survey for more information on the Travel Tracker Survey. The analysis assumes that the percent of shopping trips made outside the home municipality shown in the Travel Tracker Survey results is representative of the region's shopping trips in general, and that the region makes approximately 3,120,000 daily shopping trips for any purpose, as estimated in CMAP's trip generation model.
[2] CMAP analysis of Illinois Department of Revenue data
[3] Regional Transportation Authority, "RTA Files Suit Against Kankakee and Channahon to Recoup More Than $100 Million in Lost Tax Revenue," http://www.rtachicago.com/press-releases-2011/rta-files-suit-against-kankakee-and-channahon-to-recoup-more-than-100-million-in-lost-tax-revenue.html

districts like park districts, sanitary districts, and mosquito abatement districts. Some members thought that many of these special districts that rely heavily on this revenue may have the ability to consolidate operations with other general-purpose governments. However, other members of the Task Force were not in favor of changing the system because the PPRT is a significant source of revenue for local governments that would need to be replaced in some form. The Task Force agreed that local governments should be encouraged to consolidate, and that any future changes to the allocation of PPRT revenue should be based on future study of local government consolidation.

The fact that the PPRT is an additional tax on business and therefore has an effect on the region's tax climate was also discussed. One suggestion was that the PPRT should be phased out over time.

Motor Fuel Tax Revenue Sharing

The Task Force examined the disbursement criteria for the state motor fuel tax. Some Task Force members stated that the system did not always account for actual infrastructure needs. For example, disbursing funds to municipalities based on population does not account for transportation needs due to commercial or industrial activity. Task Force members were also concerned with whether the current system promotes coordination and planning, and the interconnectedness of the region's transportation network. One separate process overseen by the Council of Mayors and CMAP to allocate federal surface transportation funds was brought up as a positive example of current regional coordination; however state MFT funds are not allocated via this process. The degree to which the MFT supports smaller township road districts was also discussed. The Task Force agreed that local governments should consider shared services and consolidation, which may enhance coordination and planning for the region's transportation needs.

Overall Revenue Sharing System and Regional Needs

In reviewing the overall revenue sharing system, the Task Force discussed whether the way state revenues are allocated to local governments has enabled and supported the region's highly decentralized system of local governance. The Task Force also discussed whether this structure promotes accountability to taxpayers to the extent that it results in the expenditure of taxpayer dollars without corresponding levels of service provided in return.

The Task Force was also concerned that the system does not provide support for major regional needs that cross jurisdictional boundaries, such as transportation and water infrastructure. With the existing fiscal challenges at the federal and state government level, more capacity may exist locally to provide for some of these investments. Like many places across the United States, northeastern Illinois faces a considerable financial shortfall in its ability to maintain and expand its existing infrastructure.

The region faces a backlog of billions of dollars annually in infrastructure rehabilitation or "state of good repair" needs. These needs often do not include the enhancements, modernizations, or expansions that are necessary for the region's continued economic prosperity. The Task Force agreed that the CMAP Board should advocate for a funding mechanism and administration structure to support regional infrastructure needs.

Property Tax

GO TO 2040 recommended that the Task Force evaluate the property tax classification system in Cook County as well as the property tax extension limitation law (PTELL). The classification system, in which commercial and industrial property is assessed at a higher percentage of market value than residential property, has resulted in high property tax rates for business taxpayers in many communities in Cook County. This is an important public policy issue for the region because these higher rates not only affect existing taxpayers and service delivery, but also can serve as a barrier to future business development and overall economic activity.

PTELL limits the growth in property tax revenues for certain units of government unless voters approve a referendum allowing additional revenues. GO TO 2040 recommended examining whether constraining a local governments' ability to generate revenue from one source results in a reliance on a less efficient source of revenues, like a municipal non-home rule sales tax or additional general state aid for school districts. In addition, regional economic development may be affected if communities are unable to raise enough revenue to provide the public services necessary to attract residents and businesses.

Classification

The Task Force was concerned about the degree to which commercial and industrial properties are subject to high property tax rates in many Cook County communities. CMAP analysis has shown that these rates are often attributable in large part to classification. For example, in 83 of 129 Cook County municipalities, more than 40 percent of the industrial property tax rate is attributable to classification.[4] The Task Force discussed whether eliminating the classification system over a period of time would lead to a more level playing field with communities with lower property tax rates outside of Cook County, especially border communities. Reducing border effects of differential taxation may result in greater economic efficiency in business location decisions and business activity.

The Task Force was also interested in whether higher property tax rates in Cook County, where there are significant opportunities for infill development, are an obstacle for future infill development as called for in GO TO 2040. Many of these communities have substantial existing infrastructure that is not being supported by the tax base. Eliminating classification would lower property tax rates in many communities with available infill and existing infrastructure and may make these communities more attractive for development.

The Task Force was also concerned that eliminating the classification system would put a greater tax burden on residential property owners. If classification were eliminated, the property tax burden for residential taxpayers would increase by more than 25 percent in 43 municipalities.[5] The Task Force agreed that classification should be phased out, but over a period of years in order to alleviate some of the increased burden on residential taxpayers.

Property Tax Extension Limitation Law

The Task Force discussed PTELL, and agreed that while the policy adds complexity to the property tax system, it also makes the system more predictable for taxpayers. The Task Force agreed that requiring a referendum to raise property tax extensions above the limitation amount is not overly burdensome to local governments and may provide taxpayers with a greater feeling of control over property tax levels. Because PTELL allows for extensions beyond the extension limitation with the approval of a referendum, the Task Force did not believe that PTELL resulted in overreliance on revenue sources that are less efficient than the property tax.

However, some Task Force members were concerned with the method by which the extension limitation is calculated. The PTELL extension is based on the property tax extension from the prior year. This results in an incentive for local governments to increase extension amounts up to the maximum every year. Even if a local government did not need the additional funds in a particular year, they may increase the extension up to the limitation just in case the additional funds were needed in a future year. If a taxing district reduces their extension for the last preceding year, the law does allow the highest aggregate extension in any of the last three preceding levy years to be used.

[4] CMAP analysis of Illinois Department of Revenue data, 2008 and 2009
[5] CMAP analysis of Illinois Department of Revenue data, 2008 and 2009

Sales Tax Rate and Base

GO TO 2040 recommended that the Task Force evaluate expanding the sales tax base to additional services. Currently, most tangible goods but just 17 services are taxed in Illinois. The nation's and the region's economy has become more focused on service industries since Illinois' sales tax was enacted 80 years ago. A tax system that better reflects the region's economy could reduce distortion in the region's tax system and lead to a more stable revenue source for the region's communities.

The Task Force discussed that a modern tax system should reflect present day consumption patterns. Since an increasing proportion of consumption is on services rather than tangible goods, expanding the sales tax base would allow revenues to remain stable as consumer preferences and consumption dynamics shift. By taxing the consumption of goods but not services, the sales tax has moved toward taxing the consumption of a selection of products and away from a tax on the consumption of resources. The tax system would be exerting less influence over consumer choice by taxing both goods and services. For example, under the current system, a person can get upholstery cleaning services tax-free, but must pay a tax to buy upholstery cleaning equipment. In addition, there is some empirical evidence that the focus on taxing goods may have been a contributor of growth in service consumption and decline in the consumption of retail goods.[6] This would constitute an economic distortion, where the tax system is creating inefficiencies through influencing economic activity.

The existing sales tax on goods is highly regressive, owing in part to the relatively high state and local tax rates in Illinois. In Illinois, the poorest 20 percent of taxpayers paid 3.5 percent of their income in sales taxes, while taxpayers in the top 1 percent paid 0.5% of their income in sales taxes.[7] In order to ensure that the sales tax is not made more regressive through a base expansion, products considered essential could be excluded, such as legal services, medical services, or residential leases. In addition, lowering sales tax rates would help to alleviate the regressivity of the sales tax.

The Task Force discussed expanding the sales tax base, and was concerned that expanding the sales tax base to additional services may exacerbate existing problems with taxes on consumption. Under the current system, when a business, such as a retail store, pays a sales tax on a business input, like a cash register or cleaning supplies, the business will pass the cost of this tax on to the customer. When the customer pays a sales tax on their purchase, the result is a tax on a tax, or "cascading taxes." If additional business inputs, such as advertising services, were added to the sales tax base, the cascading nature of the sales tax would be amplified.

The Task Force agreed that the sales tax base should be expanded to some additional services, but the details matter greatly. Some members expressed that the existing rate on goods should be lowered in tandem. The Task Force also expressed that any base expansion should ensure that cascading taxes be limited. To achieve this, businesses-to-business transactions could be exempted from the sales tax. Alternatively, services that are primarily purchased by other businesses could be excluded from the expansion. In a previous analysis, CMAP provided a list of 63 services to the Task Force that may be less problematic to include in the sales tax base.[8] The services included in this list were in the sales tax bases of at least 15 other states and presented fewer problems with cascading.

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[6] Merriman, David and Mark Skidmore. Did Distortionary Sales Taxation Contribute to Growth of the Service Sector? National Tax Journal 53, 1 (2000): 125-142.

[7] Institute on Taxation & Economic Policy, "Who Pays? A Distributional Analysis of the Tax Systems in All 50 States," November 2009, http://www.itepnet.org/whopays3.pdf.

[8] CMAP, "Expanding the Sales Tax Base to Services: Background, Implications, and a Prototypical Example," July 2011, http://www.cmap.illinois.gov/c/document_library/get_file?uuid=c43a4cbf-78d5-4ea8-9bd6-e235f300f958&groupId=20583

Individual Income Tax

GO TO 2040 recommended that the Task Force evaluate the efficiency and equity of the state income tax, including the impact of graduating the State's current flat rate and expanding the base to include retirement income. A broad rather than a narrow tax base would make the region's tax system more efficient and provide a more stable revenue source.

The Task Force discussed the State's income tax exemption for retirement income. Some members were concerned with whether the exemption results in an equitable system of taxation and government service provision. The Task Force agreed that the State of Illinois should treat retirement income for state individual income tax purposes the same way that the federal government treats retirement income for federal income tax purposes. Expanding the state income tax base would provide a more stable tax base as residents age. In order to reduce the effect for low-income taxpayers, the Task Force discussed using federally-taxed retirement income because it would exempt income below a certain threshold.[9]

Tax Capacity

GO TO 2040 recommended that the Task Force evaluate the ramifications of local tax capacity on the region. Some areas within the region have a much larger economic base than others areas, which gives them a greater ability to generate tax revenues from economic activity occurring in their community. For the purposes of this report, tax capacity is defined as property tax base plus sales tax base, per capita. Tax capacity among the region's municipalities varies widely: in 2010, 37 municipalities in the region had tax capacity of less than 50 percent of the regional median, while there were 64 municipalities with tax capacity of 50 percent more than the regional median or greater.[10] Communities on the low end of the spectrum that are unable to raise the revenue required to provide the public services necessary to attract residents and businesses may hinder the economic growth of the region as a whole.

The Task Force discussed various ways to shrink differentials in tax capacity throughout the region. One method would involve placing greater emphasis on a community's population for state revenue sharing criteria. Alternatively, property tax base could be used as criteria for state revenue sharing, which would allow communities with a low property tax base to receive additional state revenue.

A statutory foundation level amount of revenue for municipalities, much like general state aid to school districts, was also discussed. A minimum per capita level of funding for general-purpose governments such as municipalities would be guaranteed by the State. Under such a system, if the local entity cannot provide this level of funding through their property tax base, the State would make up the difference.

In addition, phasing out the Cook County property tax classification system may eventually reduce tax capacity differentials in the region. Currently, many communities in Cook County are at a disadvantage for commercial and industrial development because of high property tax rates. Reducing property tax rates for commercial and industrial properties may result in additional economic activity, which may in turn expand the tax base.

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[9] Under the federal income tax, if half of social security benefits received plus all other income fall between $25,000 and $34,000 for single filers and $32,000 and $44,000 for joint filers, then either half of all income over the threshold or half of the social security benefits (whichever is lower) are subject to the federal income tax. For taxpayers with income above these thresholds, 85 percent of benefits are subject to taxation.

[10] CMAP analysis of CMAP analysis of data from the Illinois Department of Revenue; Cook County Clerk; DuPage County Clerk; Grundy County Clerk; Kane County Clerk; Kendall County Clerk; Lake County Clerk; McHenry County Clerk; Will County Clerk and U.S. Census Bureau decennial census data

2. Recommendations

This section represents a consensus view of the Task Force with respect to its assignment to advise the CMAP Board on carrying out its responsibilities to address issues of tax policy.

In offering these conclusions and recommendations, the Task Force does so with two important caveats:

First, the details matter. The Task Force did not have the time or resources to draft specific proposals, let alone draft legislation. An idea, such as broadening the tax base, may be a sound principle, but it still matters how it is broadened and how the resources will be allocated.

Second, the tax system is a complex and interconnected system. Changing it almost always has unintended as well as intended consequences. The CMAP Board should continue to analyze these issues and consider new solutions with future revenue streams that promote a more efficient and accountable system. Further, changing one part of the tax system almost always results in pressure to change another part. It is important to look at the whole as well as the parts.

1. CMAP should play a leadership role in advocating for a regional perspective to shape tax policy.

With the adoption of GO TO 2040, the CMAP Board has begun to address the tax policy issues that shape the region and influence the implementation of the Plan's goals. The Task Force endorses this commitment and encourages CMAP to take an active role in defining a regional perspective with respect to tax issues and advocating for appropriate changes in tax law.

CMAP's work focuses on the nexus of land use, transportation, and economic development, issues that are directly impacted by tax policies. CMAP should maintain the staff resources and analytical capacity to execute its responsibilities effectively with respect to tax policy. It needs the capacity to move quickly as tax issues emerge in the legislative process.

CMAP needs to develop its own voice, backed by rigorous research and analysis, to become a proponent of tax policies that are in the best interests of the region as a whole, as well as the governments that are an integral part of the region and the residents and businesses that pay the taxes.

2. CMAP should play a leadership role in addressing the following tax policy issues:

The following describes tax policy issues that should be addressed by the CMAP Board. These recommendations are offered as issues that should be addressed, but they are not an implicit or explicit endorsement for a particular solution.

- **Sales Tax Revenue Sharing:** State law provides that local governments receive state sales tax revenues based on local point of sale. While these dollars are used to provide services and infrastructure to support the retail development, in some cases the revenues accrue above and beyond this specific need. This method of distribution contributes to divergences in local tax capacity around the region. While wholesale change to the existing system would be disruptive, particularly if it means taking from existing communities and redistributing to other communities, the CMAP Board should continue to analyze these issues and consider new approaches to the allocation of sales tax revenues when new or increased revenue streams are under consideration.

  In addition, sales tax rebates are employed by some local governments to attract business investment. When the businesses move from one community to another within the State, it

results in no net new revenues or jobs. These tax rebate deals are not always disclosed to the taxpayer. The CMAP Board should support policies that enhance transparency in the sales tax rebate agreements that local governments make with businesses.

- **Personal Property Replacement Tax Revenue Sharing:** This tax generates over $1 billion statewide, and is allocated across nearly all units of local government using a system based on the structure of local taxes and the economy in the late 1970s. It is also the principal source of funds for several special-purpose units of government. Those who pay the tax see little relationship between their tax investments and the services provided, since the allocation system was established over 30 years ago. CMAP should support reform of this outmoded revenue sharing system. It needs to be revised to reflect the region's changing demographics and needs. CMAP should also support and encourage the consolidation of some of the units of government that rely heavily on the PPRT for a principal share of their revenue.

- **Motor Fuel Tax Revenue Sharing:** CMAP should develop an agenda that addresses the efficiency of allocating state motor fuel tax revenue among 375 units of government within the region, all of which are responsible for maintaining an effective and efficient transportation system. Local governments should be encouraged to share services or consolidate, which may enhance coordination and planning for the region's transportation needs.

- **Property Tax Classification System:** Cook County is the only county in the State that assesses commercial and industrial properties at a higher percentage of market value than residential properties. This differential creates a discontinuity in taxation within the region and impedes CMAP's overall development goals. CMAP should support policies that phase out this inconsistency, but over a period of years in order to alleviate some of the increased burden on residential taxpayers.

- **Property Tax Extension Limitation Law:** While this law adds complexity to the tax system, it does place limits on the growth of property tax extensions, and provides a measure of assurance to taxpayers concerning the rate of increase of their tax liabilities. The requirement of a referendum to raise property tax extensions above the limitation amount may provide taxpayers with a greater feeling of control over property tax levels. CMAP should support this law.

- **State Sales Tax Base and Rate:** Combined state and local sales tax rates in the region are generally high compared to national averages. The sales tax is applied to the sale of goods, but only a few services. This system does not reflect changes in purchasing and consumption patterns that have occurred since the sales tax was enacted 80 years ago. CMAP should support tax policies that broaden the tax base by taxing more services as a way to respond to changing consumption patterns and maintain lower rates.

- **Individual Income Tax Base and Rate:** Unlike the federal government and most other states, Illinois exempts retirement income from its income tax base. Broadening the base by treating retirement income for state individual income tax purposes the same way that the federal income tax does would provide a more stable revenue source as the region's demographics change. CMAP should pursue policies that lead to a broadening of the tax base in conjunction with policies that lower tax rates.

- **Motor Fuel Tax:** The CMAP Board should continue its support of an increase in the state motor fuel tax as an efficient way to meet the substantial unmet transportation needs in the region. It

should also support the elimination of the arbitrary 55% to 45% split of transportation funding between the rest of the State and northeastern Illinois.

- **Tax Capacity:** Some areas within the region have a much larger economic base than other areas, which gives them a greater ability to generate tax revenues from economic activity occurring in their community. CMAP should consider that this differential in tax capacity not only affects the communities in question, but also affects the entire region's capacity to attract and maintain business investment

3. CMAP should support policies that provide for regional needs.

Many of the challenges to creating an economically competitive economy, such as modernizing the transportation system, cannot be solved only by the actions of individual local governments. The State, as well as the federal government, appears to be reducing their commitment to the needs of metropolitan areas. Northeastern Illinois should follow the lead of other regions around the country that are pursing regional revenue sources for regional needs.

Other than the Regional Transportation Authority sales tax, which provides funding for transit operations, the region does not have a dedicated source of local funding to provide for regional needs. Transportation infrastructure is integral to the region's prosperity, yet it has fallen behind other industrialized parts of the world, many of which have invested significantly to create and preserve modern systems. CMAP should pursue a source of regional funding to help finance regional infrastructure investments. This funding should be regionally sourced, either through the imposition of a new levy or through repurposing existing resources. CMAP should advocate for a funding mechanism and an administrative structure to support regional infrastructure needs.

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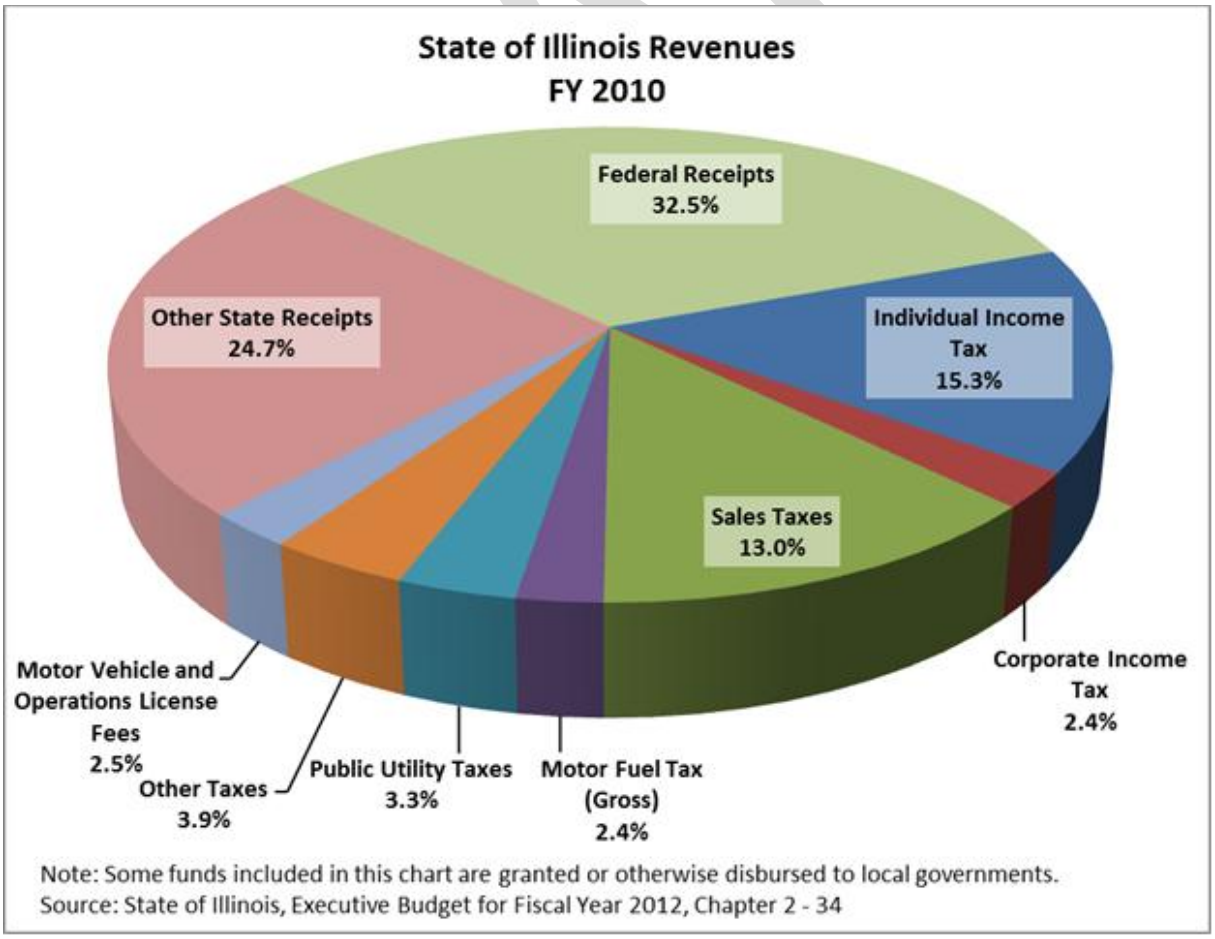
3. Analysis of Existing State and Local Tax Policy Conditions

This section contains a summary of the detailed background information and data used by the Task Force as it deliberated the policy implications of various tax systems.

The State of Illinois derives revenues from state taxes, receipts arising from the provision of specific services, and receipts from the federal government. Not all state revenues are used to fund state government. State statute requires that a portion of certain state taxes be transferred to local governments. In addition, the State passes revenues, including some federal receipts, to local governments and school districts to fund services like education and law enforcement programs. As a result, the structure of state taxes as well as the structure of the state tax revenue sharing system has implications for both the regional economy as well as the fiscal sustainability of local governments. Local governments also have the ability to raise revenues, such as property taxes and local sales taxes.

State Revenues

The State's FY (fiscal year) 2010 budget consisted of $22.5 billion in tax revenue, or 40.4 percent of the total. Primary tax revenue sources for the State include income and state sales tax revenues, which make up over 30 percent of the revenues in the State's budget. State receipts such as motor vehicle license fees and lottery receipts accounted for $15.1 billion or 27.1 percent of the total. Federal receipts like grants and reimbursements for public assistance, social services, and other programs were $18.1 billion or 32.5 percent of the total. Roughly half of the total $55.7 billion revenues were deposited into the State's General Funds, which support public services such as education, health care, and human services. The following chart provides an overview of the revenue sources that fund the State's budget.



Some of the State's budgeted revenues do not stay within state government. Instead, they are granted or disbursed to local governments. In addition to the state tax revenues included above, some state tax revenues do not pass through the State's budget. A portion of the state sales tax is collected by the State but is distributed directly to local governments. The State's personal property replacement tax is also disbursed directly to local governments.

Sales Tax

Taxation of sales became a popular tool in the United States during the Great Depression in response to declining property tax revenues and increasing spending pressures.[11] Illinois first adopted a 2% state sales tax in 1933.[12] The state sales tax rate is currently set at 6.25%, but sales tax rates vary by jurisdiction, depending on whether the RTA sales tax, county or municipal home rule sales taxes, or county or municipal non-home rule sales taxes apply. Currently, combined sales tax rates on general merchandise range from 7 percent in most of Kane, Lake, McHenry, and Will counties to 9.75 percent in a handful of municipalities in Cook County. The following map illustrates combined sales tax rates in the region.

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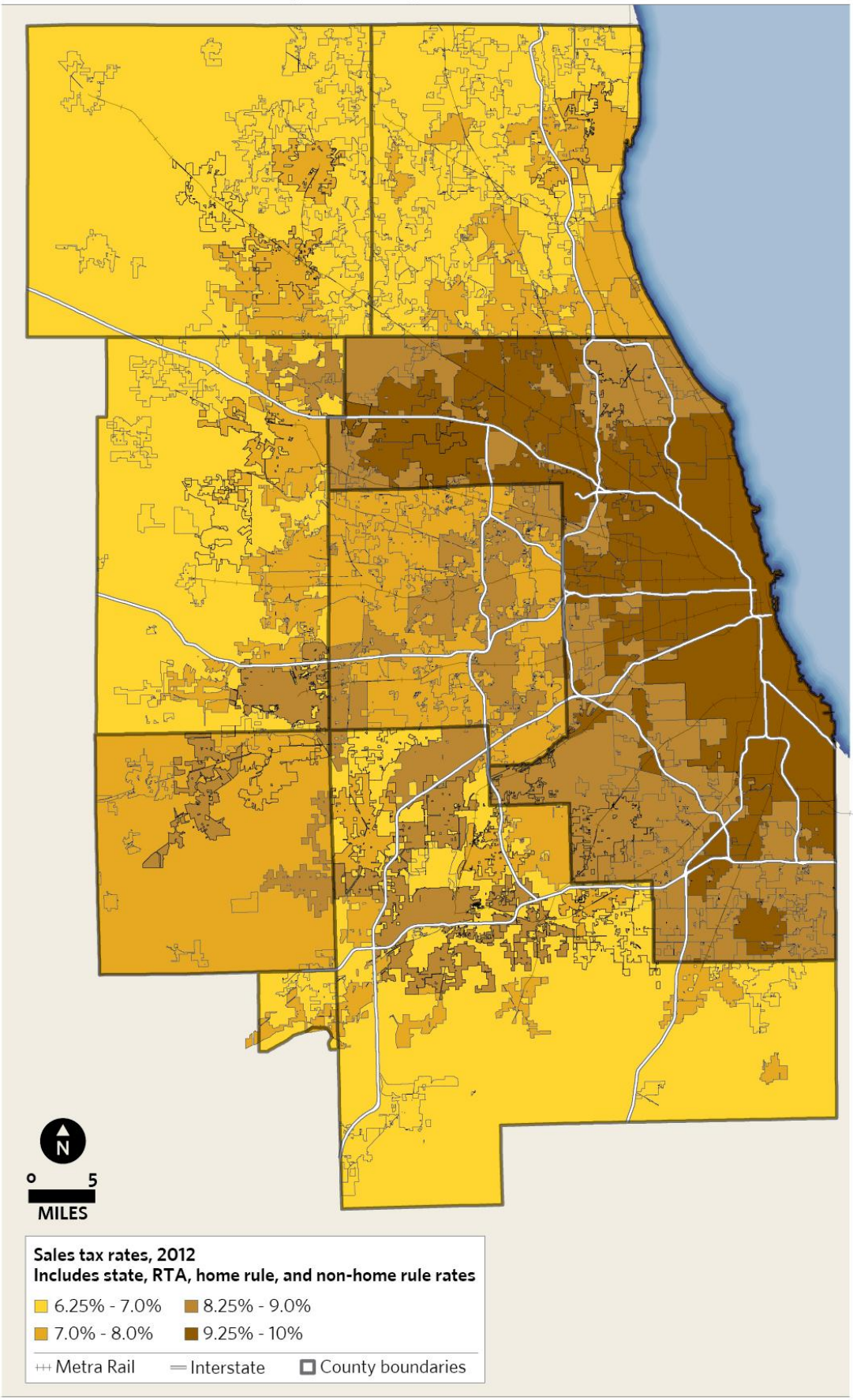
[11] Snell, Ronald, "State Finance in the Great Depression," National Conference of State Legislatures, March 2009, http://www.ncsl.org/print/fiscal/statefinancegreatdepression.pdf.

[12] Legislative Research Unit, "Illinois Tax Handbook for Legislators, 2010, Twenty-Sixth Edition", p 118, http://www.ilga.gov/commission/lru/2010TaxHandbook.pdf.

Combined sales tax rates in metropolitan Chicago



Source: Illinois Department of Revenue
Note: Includes general, special, capital, and debt service funds

During the time that most of these taxes were enacted, the U.S. economy was driven by goods. Illinois' statewide sales tax, primarily applies to tangible personal property.[13] Most tangible goods are subject to the tax under the Retailers' Occupation Tax, Use Tax, Service Occupation Tax, and Service Use Tax, as well as services including prepaid telephone cards, photoprocessing, and canned software or modifications to canned software.[14] There are 14 other services subject to statewide sales taxes at different rates. The State imposes a 6% tax on 94% of gross receipts of short-term hotel and motel rentals.[15] Automobile rentals are also subject to a separate statewide tax of 5%.[16] There are also six telecommunication services taxed under the Telecommunications Excise Tax Act at a rate of 7%.[17] An additional six utility services are taxed under the Gas Revenue Tax Act and the Electricity Excise Tax Law at various rates.[18]

Since the sales tax was enacted, changes in the U.S. economy have resulted in increased consumer income and a shift in demand toward services.[19] Between 1929 and 2010, the U.S. transitioned from an economy based on manufacturing and other goods-producing industries to a services and information-based economy. With this transition came cheaper and more efficiently manufactured goods from within the country and overseas, rising standards of living, and increased disposable income, resulting in increased demand for services. Since the early 1970s, spending on services has exceeded spending on goods. In 2010, consumers spent twice as much on services (66.9 percent of total personal consumption expenditures) as on goods (33.1 percent of total personal consumption expenditures). This shift in the fundamentals of the economy has changed the relationship between consumption and tax revenue. The following chart shows personal consumption expenditures in the United States since 1929.

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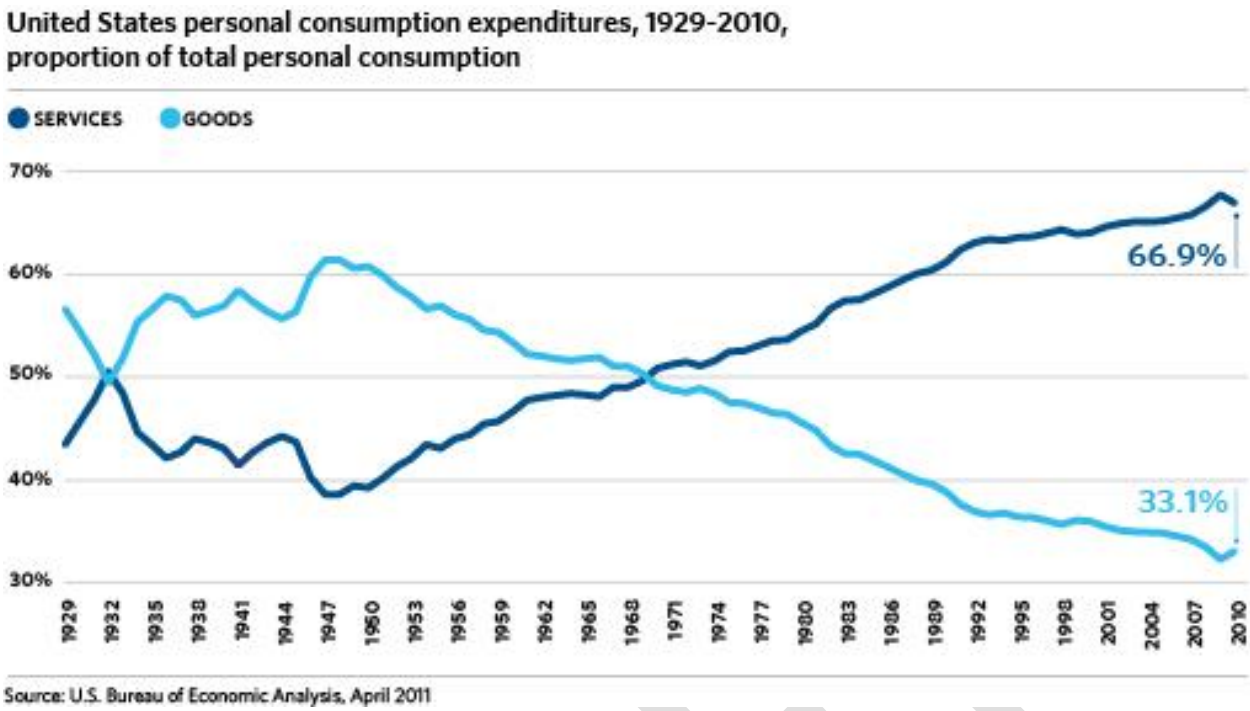
[13] The state sales tax rate for qualifying food, drugs, and medical appliances is 1%.
[14] See 35 ILCS 105/3, 35 ILCS 110/3, 35 ILCS 115/3, 35 ILCS 120/2.
[15] Hotel and motel rentals less than 30 days are subject to a tax of 6% on 94% of gross receipts. See Hotel Operator's Occupation Tax Act, 35 ILCS 145/3.
[16] See Automobile Renting Occupation and Use Tax Act, 35 ILCS 155/3.
[17] 35 ILCS 630
[18] See 35 ILCS 615 and 35 ILCS 640
[19] "The Service Sector: Give it Some Respect," Federal Reserve Bank of Dallas 1994 Annual Report, pp 3-22, http://www.dallasfed.org/fed/annual/1999p/ar94.pdf.



Moreover, there is evidence that services make up an even larger share of GDP, relative to goods, and that the service sector constitutes a large share of the overall regional economy of metropolitan Chicago. In the Chicago-Naperville-Joliet Metropolitan Statistical Area,[20] service-producing industries made up 84 percent of the Gross Regional Product in 2009, up from 80.7 percent in 2001.[21]

Service Industry in Metropolitan Chicago

Northeastern Illinois is home to 165,033 businesses that provide services to consumers and/or other businesses and the public sector. The following table shows the service industries in metropolitan Chicago based on these classifications.[22]

Service Sector Industries in Metropolitan Chicago by Classification

Classification	Number of businesses	Estimated annual sales of services
Consumer services industry	49,516	$13,880,688,267
Consumer/business services industry	88,931	$28,002,725,366
Business services industry	26,586	$23,307,793,017
Total	165,033	$65,191,206,649

Source: Dun and Bradstreet Market Insight, October 2010; U.S. Census Bureau, 2002 Economic Census

A majority of businesses in the region produce services purchased not only by individual consumers, but also businesses and government. These businesses, including landscaping and transportation services

[20] The Chicago-Naperville-Joliet Metropolitan Statistical Area consists of Cook, DeKalb, DuPage, Grundy, Kane, Kendall, McHenry, and Will counties in Illinois, Jasper, Lake, Newton, and Porter counties in northwest Indiana, and Lake and Kenosha counties in Wisconsin.

[21] U.S. Bureau of Economic Analysis, Gross Domestic Product by Metropolitan Area, http://www.bea.gov/regional/gdpmetro, accessed May 10, 2011.

[22] This analysis excludes services already subject to a sales tax, such as restaurants and hotels. The classifications were based off the categories and examples discussed in Michael Mazerov, "Expanding Sales Taxation of Services: Options and Issues," Center on Budget and Policy Priorities, July 2009.

(e.g. privately provided services like limousine, shuttle buses) make up 53.9 percent of the 165,033 service sector establishments in the region. Businesses that provide services primarily to consumers, such as construction, health care, and entertainment, account for approximately 30 percent of service sector establishments. At the same time, almost 27,000 establishments provide services specifically to businesses and government in the region. Most of these services are professional and support services like engineering, architecture, advertising, and administrative services.

Prototypical Example of Expanding the Sales Tax to Services

This section will explore how expanding the sales tax base to the service sector would affect sales tax disbursements in the region.[23] If the base of the 6.25% sales tax were expanded to *all of the service industries* outlined above under current revenue sharing criteria, an additional $814.9 million would be disbursed to local governments in northeastern Illinois. Statewide, this would generate an additional $10 billion in state sales tax revenues for the State[24] and local governments. This estimate includes 118 different service industries and sales to all customers, including individuals, businesses, governments, and nonprofit entities. See the following Methodology section for further detail on the development of the revenue estimates provided in this section. This estimate includes a larger number of services relative to what other states include in their tax bases.

Due to issues with the regressive nature of the sales tax and cascading taxes, taxation of *all services* may be impractical and possibly economically disruptive. In reality, the majority of states tax a narrower array of services. The Federation of Tax Administrators' 2007 survey of sales taxation of 168 services revealed that the median number of surveyed services taxed by each state was 55. Excluding utilities, the median number of states taxing each service was 15.[25] To estimate revenues from a smaller universe of services, 63 services were chosen based on the following criteria:

- Services that are more frequently included in the sales tax base by other states were selected by including services taxed by at least 15 states;
- Services that have been previously proposed for inclusion in the Illinois sales tax base were selected by including several services that had been proposed for taxation in a bill[26] passed by the Illinois Senate in 2009;
- Other services were selected that presented fewer problems with cascading or sourcing the location of sale.

If this smaller universe of 63 services was added to the sales tax base and the tax was imposed for sales to all customers (including businesses, nonprofits, and governments), $210.2 million in additional revenue would be disbursed to location governments in the region under the current revenue sharing system. Statewide, this would generate an additional $2 billion in state sales tax revenues for the State and local governments.

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[23] Disbursements include 16% of sales tax revenue to municipalities (and counties for sales in unincorporated areas) on sales within their borders and 4% of sales tax revenue to the collar counties and the RTA for sales within their borders.

[24] The State receives 80% of sales tax revenues. Revenues fund the following: 25% to Common Schools Special Account Fund, 1.75% to Build Illinois Fund, 3.8% to Build Illinois Fund to retire bonds, 0.27% to Illinois Tax Increment Fund, 80% of revenue on Illinois coal bought by state financed electric generating facility to Energy Infrastructure Fund, and remainder to General Revenue Fund.

[25] Federation of Tax Administrators, Sales Taxation of Services, 2007, http://www.taxadmin.org/fta/pub/services/services.html.

[26] The bill would add 39 services to the Retailers' Occupation Tax Act. See House Bill 174, 96th General Assembly, as passed by the Senate.

Under some proposals and estimates to expand the sales tax, businesses are excluded from paying sales taxes on service purchases in order to lessen cascading taxes. In addition, governments and nonprofit customers are exempt from paying the current sales tax under certain circumstances. Exempting business, government, and nonprofit customers resulted in an estimate of $116.9 million in annual disbursements to the region. This 44.4 percent drop was primarily a result of the reduction in revenues associated with business-focused industries such as travel agencies and janitorial services. If only government customers were exempted, the expanding base would result in an additional $203.8 million to the region. The following table provides a summary of sales tax disbursement estimates.

Estimated revenue disbursements to the CMAP region from taxing 63 services

Disbursements with all customers	Disbursements without government customers	Disbursements without business, nonprofit, and government customers
$210,233,741	$203,841,835	$116,856,984

While some advocate expanding the sales tax base to services in order to raise additional tax revenue, the expansion could also allow the tax rate to be reduced. It is difficult to calculate a tax rate for the broader base that would be completely revenue neutral because there may be future shifts in consumption patterns for goods or services. While it is important to ensure that revenues would be unlikely to drop significantly through any rate reduction, in future years, economic and fiscal benefits may arise from the broader base and the lower rate.

In 2010, over $1.1 billion in state sales taxes was disbursed to municipalities, collar counties, and the RTA. Expanding the sales tax base to 63 additional services would expand the region's tax base subject to a 6.25 percent rate by 21 percent. If the rate on general merchandise was reduced to 5.25 percent and applied to the 63 services, disbursements from general merchandise and qualifying items would be reduced to $1.0 billion and disbursements from services would generate $176.6 million. The region would experience an increase in disbursements of 1.4% in the first year.[27] Depending on how consumption patterns change, this scheme may become revenue neutral or revenue enhancing in future years. In addition, future disbursements may be less volatile due to the expanded base. The following table summarizes revenue estimates under a 5.25% rate.

Estimated total revenue disbursements to the region if 6.25% rate was reduced to 5.25%

	Disbursements with all customers	Disbursements without government customers	Disbursements without business, nonprofit, and government customers
63 Services	$176,596,343	$171,227,142	$98,159,867
Base under current law*	$1,025,951,055	$1,025,951,055	$1,025,951,055
Total	$1,202,547,398	$1,197,178,197	$1,124,110,922
Percent of disbursement retained	101%	101%	95%

*Does not exclude any customer types not already excluded in current law

With no corresponding change in RTA, home rule, and non-home rule sales taxes, a reduction of the state rate from 6.25% to 5.25% would result in a sales tax rate between 6% and 8.75% in most of the

[27] This assumes that the State would continue to receive 80% of the revenues, local governments would continue to receive 20% of the revenues, and the rate on qualifying food, drugs, and medical supplies would remain 1%.

region. The expansion may also allow municipalities to lower home rule and non-home rule sales tax rates, as well as property tax rates.

Methodology

Data on businesses in the CMAP region was obtained from Dun and Bradstreet Market Insight in October 2010. Non-business entities, such as government agencies, were removed from businesses with service industry North American Industry Classification System (NAICS) codes. Businesses addresses were geocoded in order to determine which municipality or unincorporated area each business was located. When businesses were missing sales revenue data, the number of employees at that business was multiplied by the average sales revenue per employee for the business' NAICS code. Businesses with no employee or sales revenue data were considered to have no sales revenue.

To calculate taxable sales, resales of merchandise were excluded from revenue estimates using product line data from the 2007 Economic Census data. For the printing and mining industries, receipt data without resales from the 2007 Economic Census was used and for the construction industry, value added data from the 2007 Economic Census was used. Revenues estimates by customer type were calculated using customer class data from the 2002 Economic Census. The analysis does not subtract revenues to account for compliance rates.

Individual Income Tax

Illinois' individual income tax (IIT) was first enacted in 1969. The rate was originally 2.5 percent, and rose to 3 percent in 1989. In 2011, a temporary increase was enacted, raising the rate to 5 percent through 2014. The rate will then drop to 3.75 percent and will drop again to 3.25 percent in 2025. Pursuant to the 1970 Illinois Constitution's requirement that "a tax on or measured by income shall be at a non-graduated rate,"[28] the income tax applies the same rate to all taxpayers of all income levels.

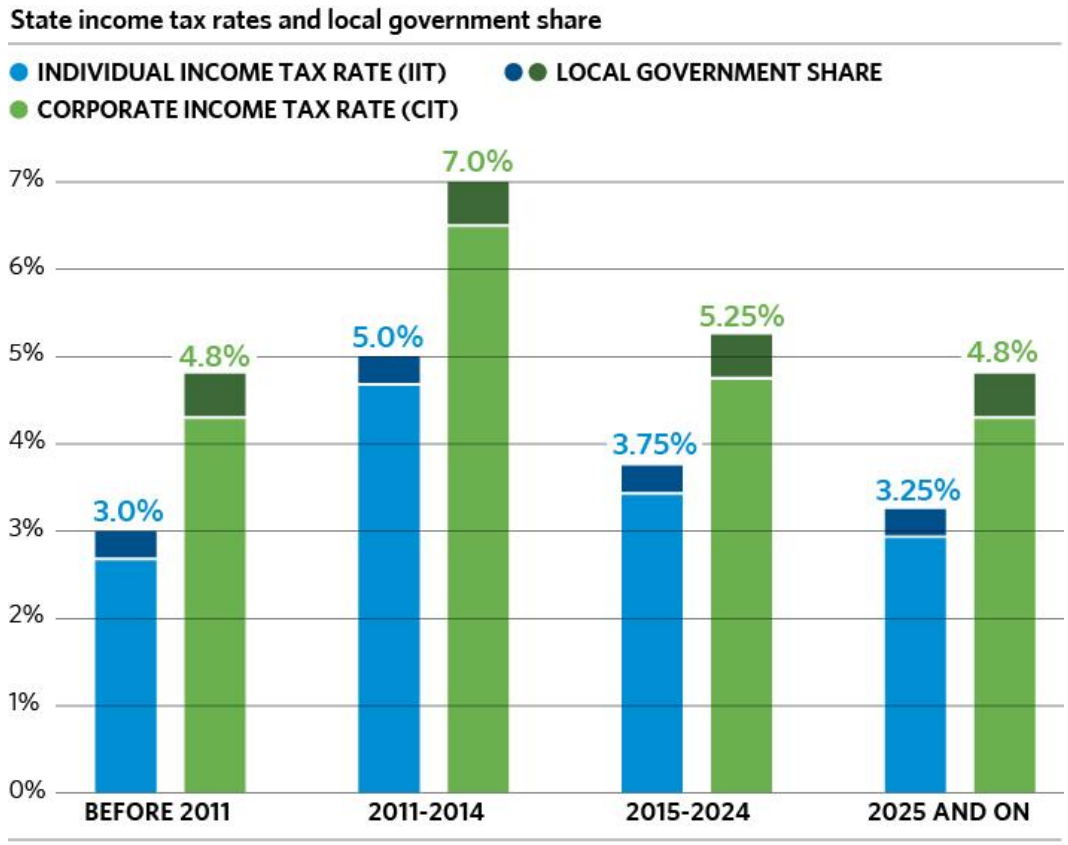
Base income subject to the IIT includes federal adjusted gross income, plus several additions including any interest, dividends, and capital gains that are excluded from federal adjusted gross income. Subtractions from base income include retirement and social security income. Individuals are taxed on base income minus $2,000 for each federally claimed exemption and $1,000 each for any taxpayer or spouse who is 65 years of age or older and/or legally blind.

Individual income tax revenue (along with corporate income tax revenue) is distributed as follows:

- A proportion of gross receipts are deposited into the Income Tax Refund Fund according to a statutory formula that is adjusted annually. In FY2011, 8.75 percent of IIT revenues and 17.5 percent of corporate income tax revenues went to the Refund Fund.
- Of the remainder:
    - 10 percent of the amount generated from the pre-2011 rate to municipalities and counties based on the population in proportion to the total state population;
    - 7.3 percent to the Education Assistance Fund, which funds elementary and secondary education as well as community colleges;
    - The remainder to the General Revenue Fund.

To clarify, municipalities and counties do not receive any additional revenue generated from the 2011 rate increase. Revenue disbursements to local governments are held at previous levels by reducing the percentage disbursed. Local governments receive 10 percent of the ratio of the current rate to the new rate (e.g. 10% of $\frac{3\%}{5\%}$ = 6%). The following chart summarizes the rates and shares to local governments.

[28] Illinois State Constitution of 1970, Article IX, Section 3(a).



Source: CMAP analysis of Public Act 96-1496

Federally Taxed Retirement and Social Security Income

The largest individual income tax expenditure[29] is the deduction for federally taxed retirement and social security income. Under the federal income tax, if half of social security benefits received plus all other income fall between $25,000 and $34,000 for single filers and $32,000 and $44,000 for joint filers, then either half of all income over the threshold or half of the social security benefits (whichever is lower) are subject to the federal income tax. For taxpayers with income above these thresholds, 85 percent of benefits are subject to taxation. However, under the Illinois IIT, social security benefits, as well as income from qualified pension plans, IRAs, state and local government deferred compensation plans, and several other sources of retirement income can be fully deducted. If Illinois subjected the same social security and retirement income to the state income tax as the federal income tax, the State would have received an additional $1.1 billion in revenues in FY2010 (under the 3 percent IIT rate). This is equivalent to 11.5 percent of the total revenues generated from the IIT that year. In 2011, this percentage may stay level, although the amount of the tax expenditure and revenue will rise because of the rate increase from 3 percent to 5 percent. The following table shows the amount that the State would have received, or the tax expenditure, for treating retirement and social security income the same as the federal government for income tax purposes.

[29] According to the Illinois Office of the Comptroller, a tax expenditure is "any exemption, exclusion, deduction, allowance, credit, preferential tax rate, abatement, or other device that reduces the amount of tax revenue that would otherwise accrue to the State."

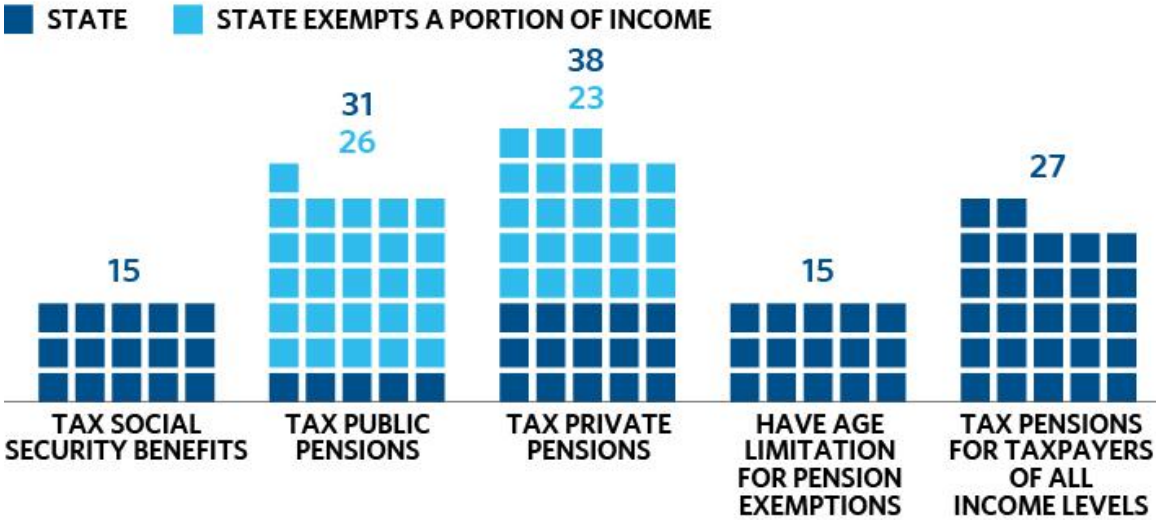
Illinois tax expenditure for federally taxed retirement and social security deduction

FISCAL YEAR	TOTAL INDIVIDUAL INCOME TAX RETURN	TAX EXPENDITURE	EXPENDITURE AS PERCENT OF TOTAL REVENUE
2002	$8,086,000,000	$716,940,000	8.9%
2003	$7,979,000,000	$732,055,000	9.2%
2004	$8,235,000,000	$757,659,000	9.2%
2005	$8,873,000,000	$828,265,000	9.3%
2006	$9,568,000,000	$899,174,000	9.4%
2007	$10,425,000,000	$983,015,000	9.4%
2008	$11,187,000,000	$983,892,000	8.8%
2009	$10,219,000,000	$973,416,000	9.5%
2010	$9,430,000,000	$1,088,858,000	11.5%

Source: Illinois Office of the Comptroller Tax Expenditure Reports and Traditional Budgetary Financial Reports

There are 41 states[30] that impose income taxes. Of these, the majority (26) do not tax social security benefits, but most (38) do tax both public or private pensions at least partially. The following table summarizes how these states treat social security and retirement income.

Tax treatment of social security and pension income among states, 2006



Source: AARP Public Policy Institute, "State Taxation of Social Security and Pensions in 2006"

Personal Property Replacement Tax

The Personal Property Replacement Tax was enacted in 1979 in response to a provision in the Illinois Constitution of 1970 that required the General Assembly to abolish ad valorem (value based) personal property taxes and replace all revenue lost by local governments. Pursuant to this constitutional provision, the statute replaced personal property taxes on businesses with an income tax on businesses

[30] Two states, Tennessee and New Hampshire, are not included in this count, but impose an income tax on dividends and interest income.

and an invested capital tax on public utilities. The PPRT has since been amended and is currently imposed as follows:

Personal property replacement tax rates

TAXPAYER	TAX IMPOSED
Corporations	**2.5%** of taxable income
Partnerships, trusts, and S corporations	**1.5%** of taxable income
Public utilities (gas, electric, water)	**0.8%** of invested capital
Electricity distributors	**Based on amount of kilowatt hours distributed.** The rate increases as the amount distributed per month increases.
Telecommunications services	**0.5%** of all gross charges charged by the telecommunications retailer.

Source: 35 ILCS 5/201(d), 35 ILCS 615/2a.1, 35 ILCS 620/2a.1(b), 35 ILCS 625/3, 35 ILCS 620/2a.1(a), 35 ILCS 635/15.

Partnerships and S corporations pay a PPRT rate, but income tax is paid by the partners or shareholders of the partnership or S corporation. Trusts pay a 5 percent individual income tax rate in addition to the PPRT rate, for a total rate of 6.5 percent. In addition to the PPRT rate on taxable income, corporations currently pay a 7 percent corporate income tax rate.[31] The total rate for corporations of 9.5 percent is one of the highest flat corporate income tax rates in the country. After the corporate income tax rate drops in 2015 to 5.25 percent, the combined rate will be 7.75 percent. The following table compares the income and PPRT tax rates paid by corporations in Illinois with the rates corporations pay in other states with flat rates.

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[31] Until January 1, 2011, the corporate income tax rate was 4.8 percent. On January 1, 2015, it will drop to 5.25 percent.

Corporate income tax rates in states with flat rates

RANK	STATE	FLAT RATE	RANK	STATE	FLAT RATE
1	Pennsylvania	9.90%	16	Arizona	6.97%
2	Minnesota	9.80%	17	North Carolina	6.90%
3	**Illinois**	**9.50%**	18	Montana	6.75%
4	Rhode Island	9.00%	19	Alabama	6.50%
5	Delaware	8.70%	20	Tennessee	6.50%
6	Indiana	8.50%	21	Missouri	6.25%
7	New Hampshire	8.50%	22	Georgia	6.00%
8	West Virginia	8.50%	23	Oklahoma	6.00%
9	California	8.40%	24	Virginia	6.00%
10	Maryland	8.25%	25	Michigan[3]	6.00%
11	Wisconsin	7.90%	26	Florida	5.50%
12	Oregon	7.60%	27	South Carolina	5.00%
13	Idaho	7.60%	28	Utah	5.00%
14	Connecticut[1]	7.50%	29	Colorado	4.63%
15	Kansas[2]	7.00%			

1 Plus a 10% surcharge from 2009 through 2011 on companies with at least $100 million in gross revenue.
2 Plus a surtax of 3.35% of taxable income over $50,000.
3 Beginning on January 1, 2012

Source: "Top State Corporate Income Tax Rates, as of January 1st, 2011", The Tax Foundation; Michigan Public Act 38 of 2011; "Illinois Tax Handbook for Legislators 26th Edition", Legislative Research Unit, March 2010.

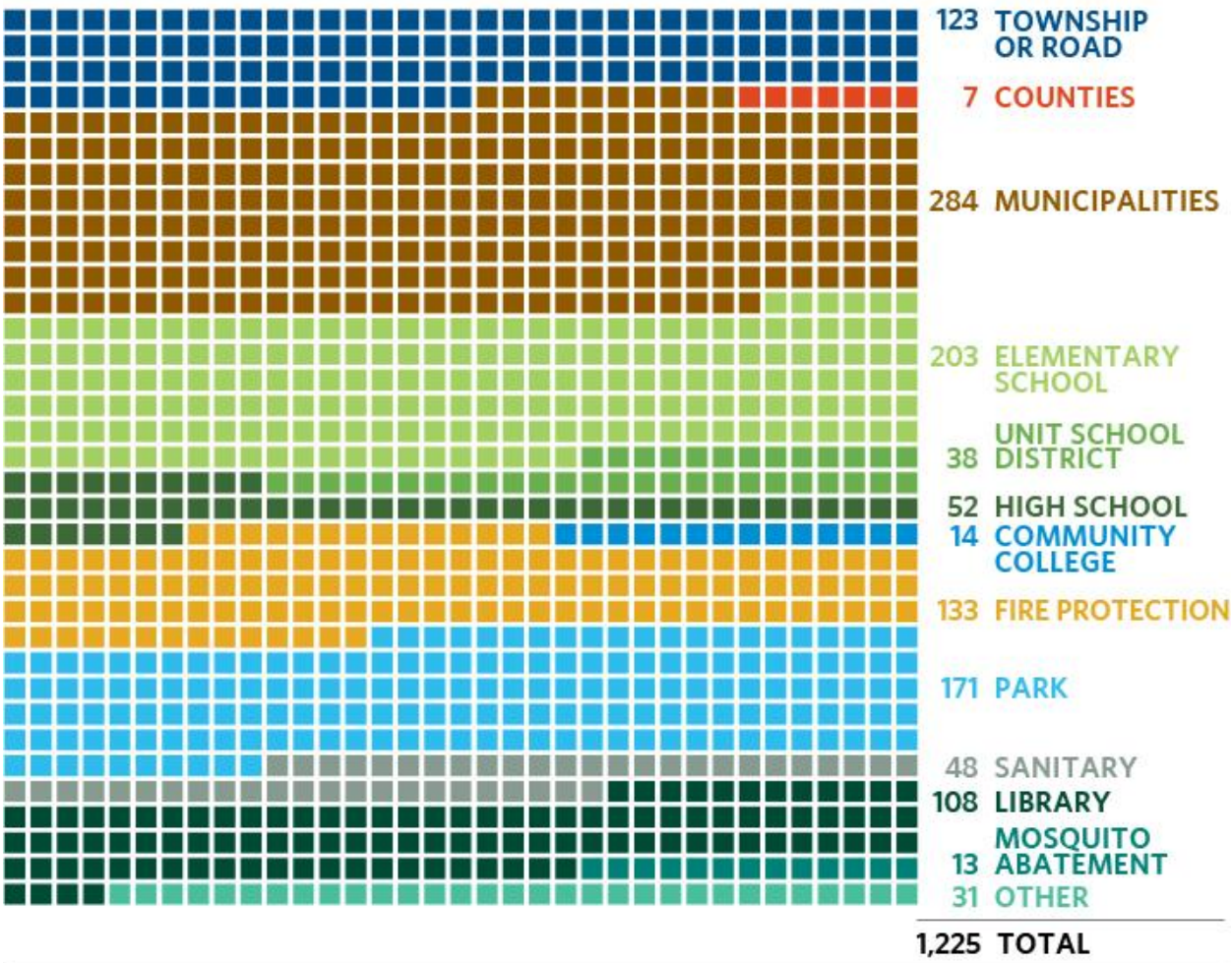
Local Government Revenues

In the seven-county region of northeastern Illinois, 1,225 different units of government collect revenues and provide services to residents, businesses, and visitors. No metropolitan area in the United States has more units of government than Chicago. Illinois has always had permissive incorporation laws for municipalities. By the late 1800's, any community of at least 300 residents could acquire a municipal charter. Many of these municipal governments were transitional in nature, however, and eventually consolidated with the City of Chicago in order to receive services like water, fire, and police protection. Yet, even with these incentives to join up with the City, suburban growth still grew at a faster rate than annexation. By 1910, suburban Cook County already contained 66 municipalities, 30 townships and more than 20 park districts. By 1930, it had 89 municipalities, and by the 1980s, it had 119.[32]

The reason for the proliferation of special district governments has its genesis in the Illinois State Constitution, which from 1870 to 1970 limited the debt municipalities could acquire to 5 percent of assessed valuation.[33] Special districts emerged as a mechanism to work around the constitution, since these districts could borrow an additional 5 percent of assessed value, levy taxes, and provide independent services. The constitution adopted in 1970 removed these limitations. The following chart provides an overview of the types of units of government in northeastern Illinois.

[32] Teaford, John C. 2004. Government, Suburban. The Encyclopedia of Chicago. Chicago: The Newberry Library.
[33] Illinois Office of the Comptroller, "A Brief History of Local Governments in Illinois," *Fiscal Focus*, July 2006

Units of government in northeastern Illinois, 2009

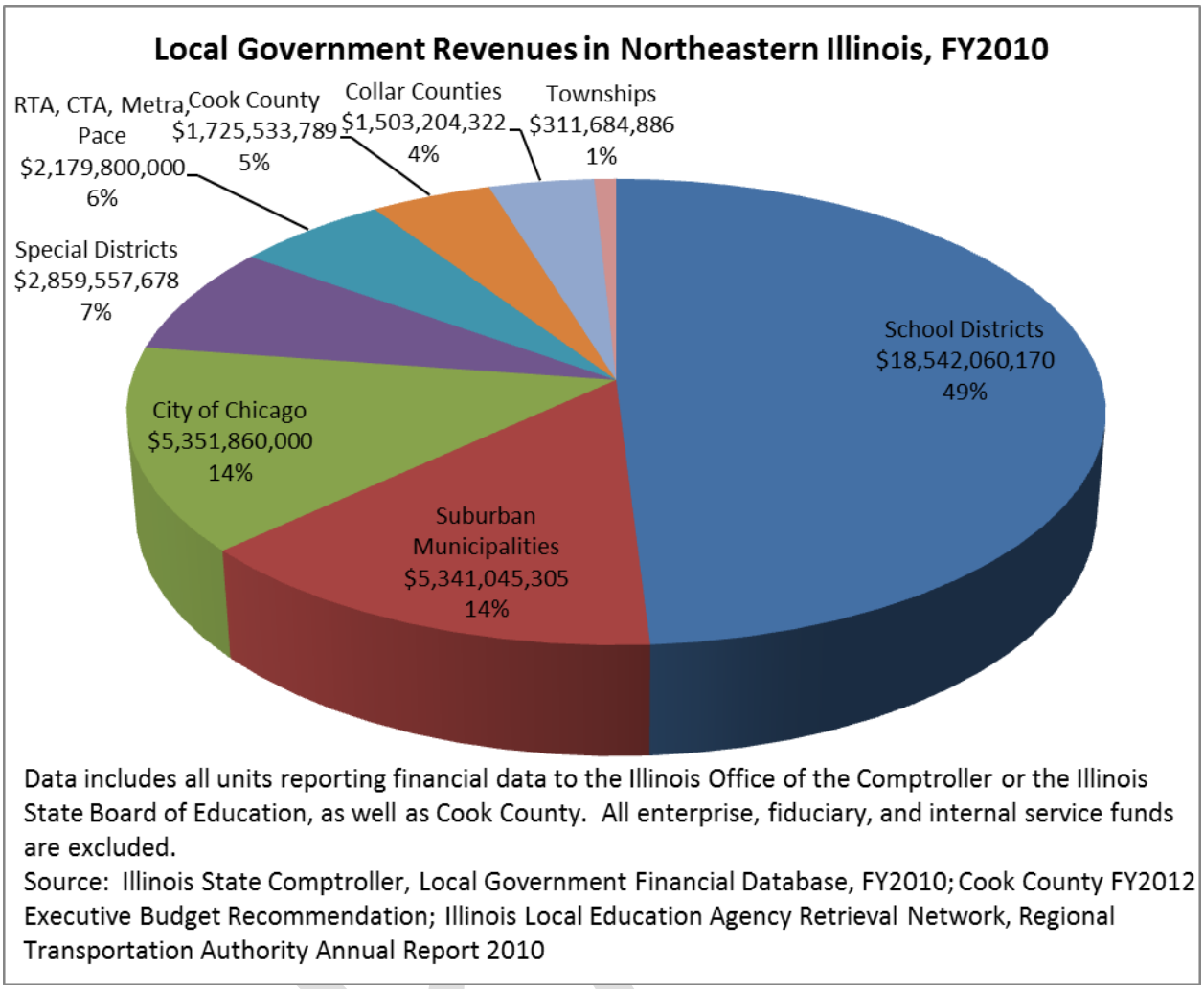


Source: Illinois Department of Revenue

Local governments in northeastern Illinois collected nearly $40 billion in total revenues during FY2010, including tax revenues as well as other receipts.[34] Municipalities collected $10.7 billion in FY2010. About half of those revenues were collected by the City of Chicago. The region's school districts received $18.5 billion in revenues in FY2010. The seven counties in the region accounted for about 10 percent of the local government revenues, with Cook County receiving $1.7 billion in revenue and the collar counties receiving $1.5 billion. Special districts and mass transit districts received $2.9 billion and $2.2 billion, respectively, while townships took in about $311.7 million or 1 percent of local government revenues. The following chart provides an overview of local government revenues in northeastern Illinois. Only revenues for governmental funds are included.[35]

[34] Local governments' fiscal years may start on different dates, although many start on January 1.

[35] Excluded funds: Enterprise Funds for accounting for services where the costs of providing services to the public be recovered through user charges such as parking garages or water utilities; Fiduciary Funds that are held by a government but belong to another entity and account for revenues like pension fund interest income; and Internal Service Funds to account for services provided within a unit of government.

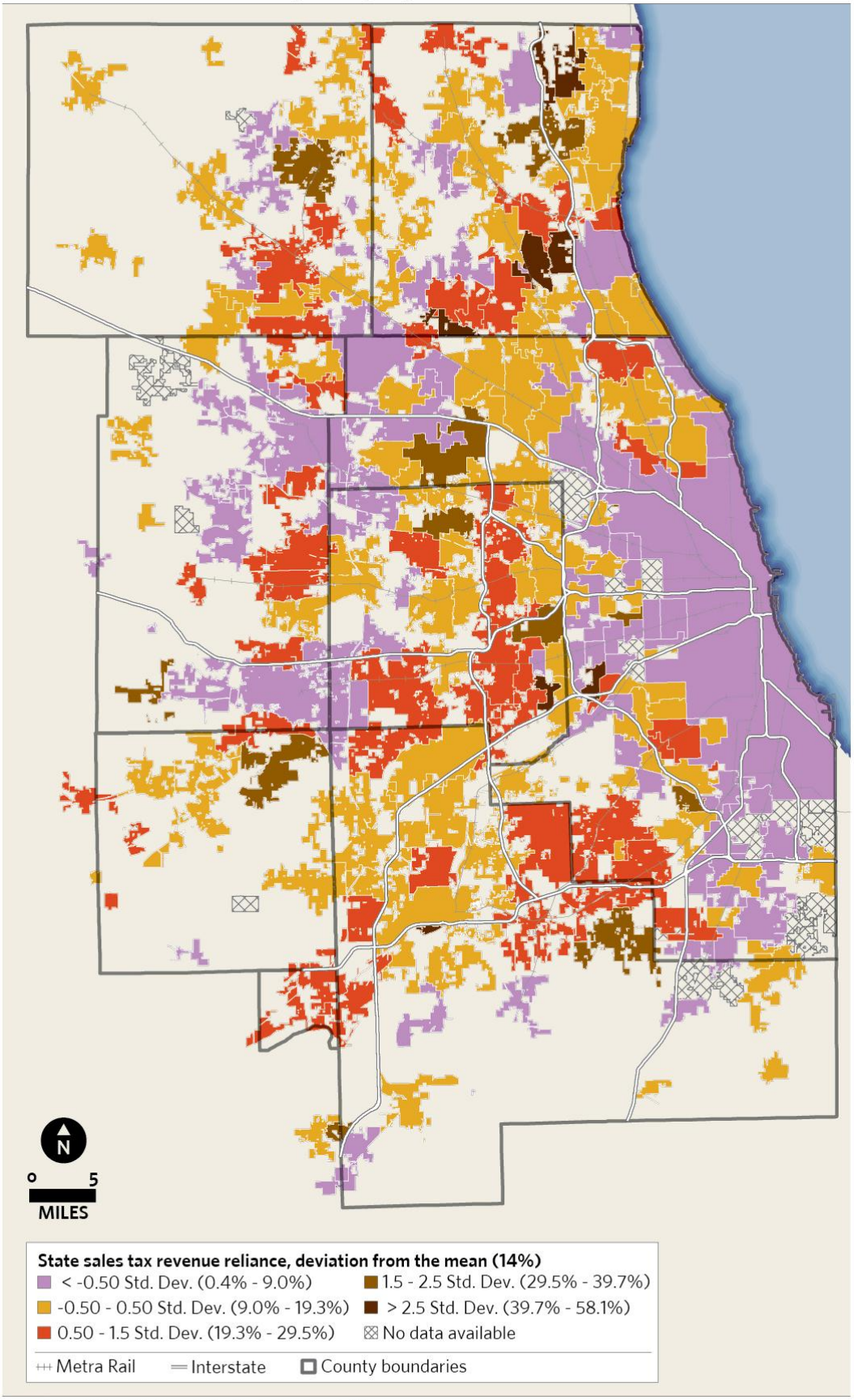


Data includes all units reporting financial data to the Illinois Office of the Comptroller or the Illinois State Board of Education, as well as Cook County. All enterprise, fiduciary, and internal service funds are excluded.
Source: Illinois State Comptroller, Local Government Financial Database, FY2010; Cook County FY2012 Executive Budget Recommendation; Illinois Local Education Agency Retrieval Network, Regional Transportation Authority Annual Report 2010

Revenue sources among these local governments vary considerably. Property tax revenues make up about half of all local government revenues in the region. In the aggregate, property tax revenues are the largest single funding source for local governments' general funds, out of which expenditures for general government operations such as public safety services are made.

State and local sales taxes are a major revenue source for the RTA system (42.7 percent) and suburban municipalities (20.1 percent). Most state and local sales tax revenues in the region accrue to municipalities' general funds. Most of these sales tax revenues come from municipalities' share of the state sales tax. State sales tax revenues account for 14 percent of total revenues for a municipality, on average. However, municipalities' reliance on this revenue source varies widely throughout the region, from 0.4 percent to 58.1 percent of municipal revenues. The following map shows the extent that municipalities deviate from the average state sales tax revenue proportion in the region.

State sales tax revenue reliance, by municipality, FY2010



Source: Illinois Office of the Comptroller; Illinois Department of Revenue
Note: Includes general, special, capital, and debt service funds

For 102 of the 268 of the municipalities for which data was available, sales tax revenue as a proportion of total revenue was within a half of a standard deviation of the mean, or between 9 and 19.3 percent of total revenue. Municipalities falling more than a half of a standard deviation below the mean included Chicago as well as 94 other municipalities distributed throughout the region. The remaining 71 municipalities had sales tax revenue proportions greater than 19.3 percent. Reliance on state sales tax revenues varies throughout the region depending on factors like the retail sales tax base. In addition to state sales tax disbursements, many municipalities also rely on local sales taxes. In northeastern Illinois, 115 home rule municipalities as well as 39 non-home rule municipalities impose a local sales tax.

Home rule authority for some Illinois local governments was implemented when the current state constitution was adopted in 1970. All municipalities with populations greater than 25,000 are automatically granted home rule status.[36] If a municipality's population drops below that threshold, a referendum must be held to determine whether to maintain home rule status. Municipalities with smaller populations may adopt home rule status by referendum, and large municipalities may choose to reject home rule status by referendum. There are 138 home rule municipalities in the region. Cook County has also been granted home rule status through the state constitution, and is currently the only home rule county in the State. Other Illinois counties can become home rule if they adopt, by referendum, a county executive form of government with home rule.[37] School districts, townships, and special districts do not have home rule powers.

Home rule grants local governments authority to expand taxation in ways that would be otherwise unavailable. For example, home rule units may implement local option retail sales taxes, while non-home rule municipalities require a referendum to implement retail sales taxes of up to 1 percent for expenditure on public infrastructure or for property tax relief.[38] Non-home rule counties also require a referendum to implement local sales taxes, and revenues may only be used for public safety, public facilities, or transportation.[39] In the Chicago metropolitan region, only Kendall County has a non-home rule sales tax, for public safety.[40]

In addition, home rule units may exceed statutory caps on property tax levies,[41] and may access a wide variety of other tax bases including the real estate transfer tax and the hotel/motel tax. Home rule units may not tax income. The following map provides an illustration of which home rule and non-home rule municipalities in northeastern Illinois have a local sales tax.

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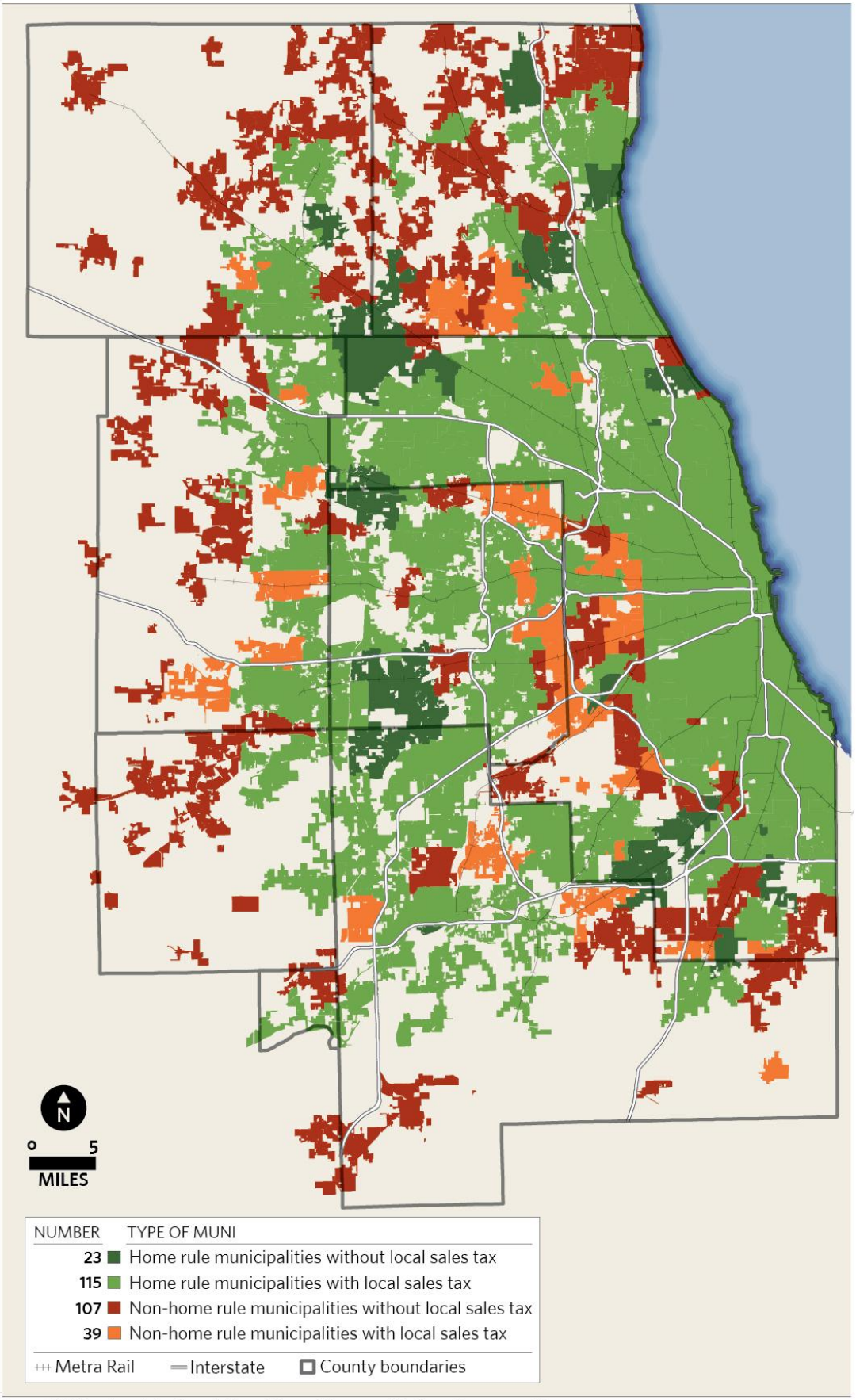
[36] Illinois Legislative Research Unit, *1970 Illinois Constitution Annotated for Legislators, Fourth Edition*, updated 2005.
[37] Ibid.
[38] Both home rule and non-home rule taxes must be imposed in 0.25% increments. See 65 ILCS 5/8-11-1, 65 ILCS 5/8-11-1.3 and 55 ILCS 5/5-1006.
[39] The tax must be imposed in 0.25% increments. See 55 ILCS 5/5-1006.5.
[40] Kendall County implemented a 0.5 percent sales tax rate on January 1, 2002 and increased the rate to 1 percent on July 1, 2007.
[41] The Property Tax Extension Limitation Law, PTELL, limits increases in property tax extensions to the smaller of either inflation (as measured by the CPI) or 5%. See 35 ILCS 200/18.

Home rule status and local sales taxes in northeastern Illinois



Source: CMAP analysis of data from the Illinois Municipal League and the Illinois Department of Revenue

Local Tax Capacity

Some areas within the region have a much greater economic base than others, hence a greater "tax capacity." Since most local governments depend on general revenues like property and state and local sales tax revenues to fund basic services, tax capacity will be defined as the sum of a municipality's equalized assessed value and sales tax base for this analysis. The following map illustrates the per capita tax capacity of the region's 284 municipalities.

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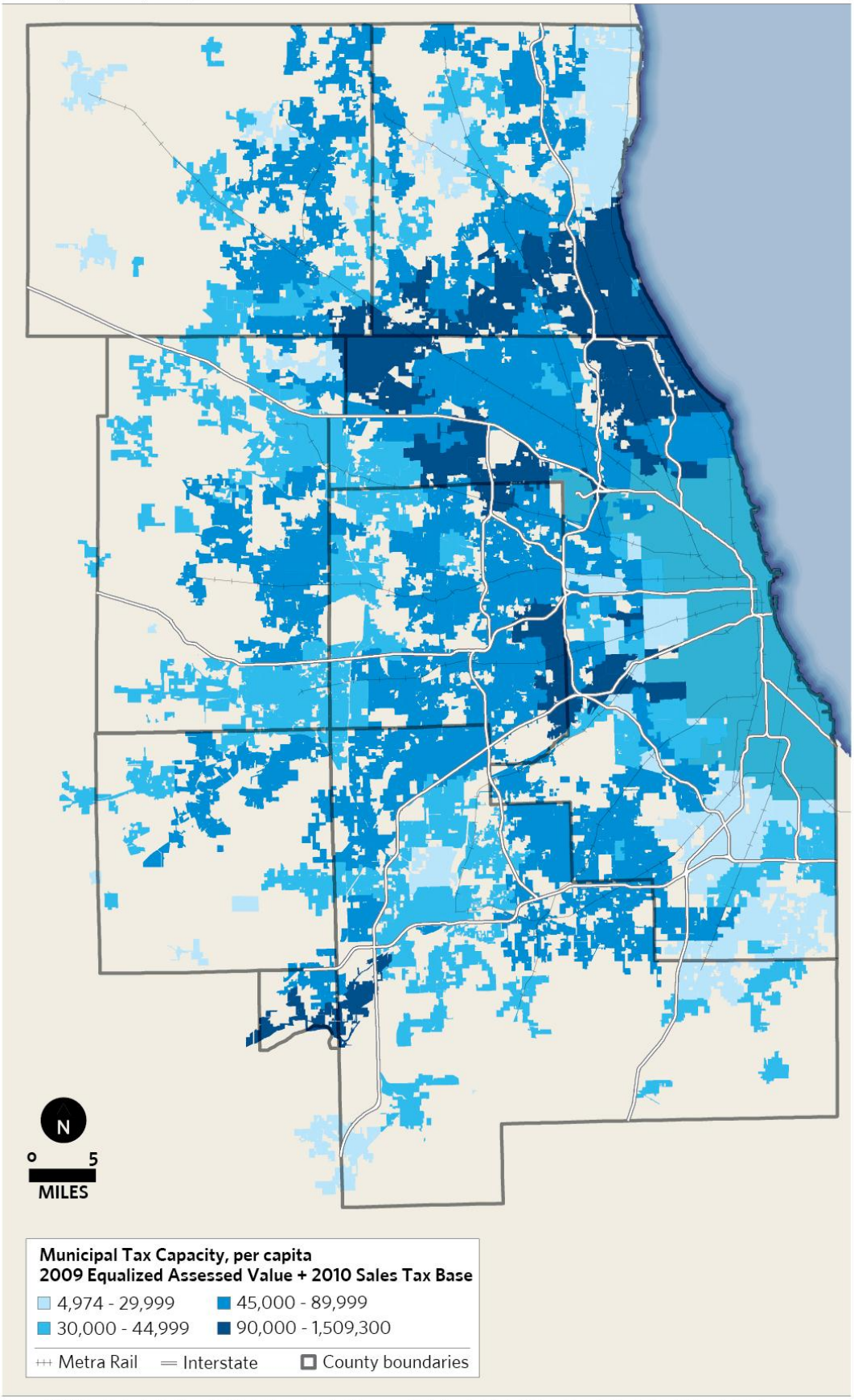
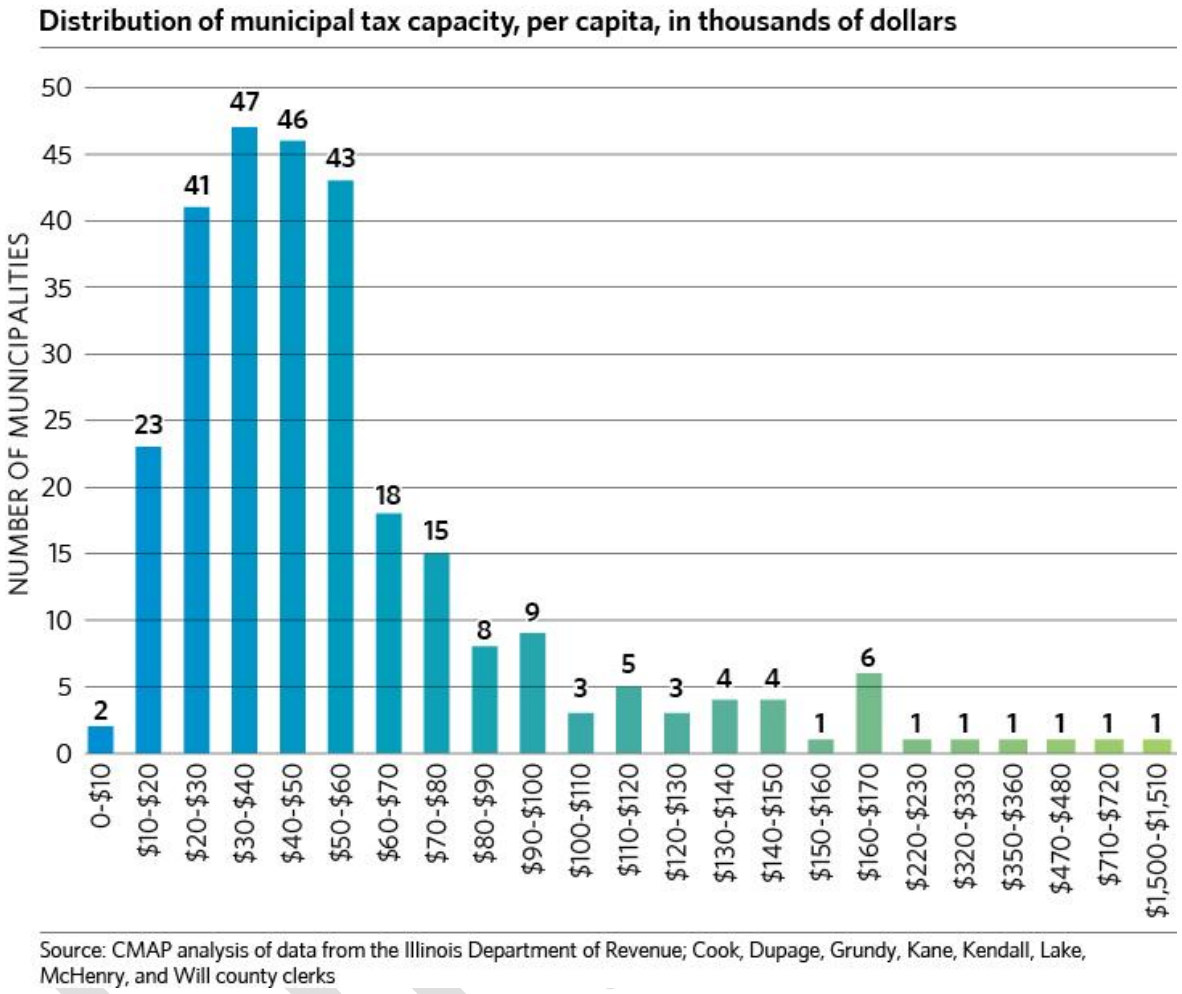
Municipal tax capacity in northeastern Illinois



Source: CMAP analysis of data from the Illinois Department of Revenue; Cook County Clerk; DuPage County Clerk; Grundy County Clerk; Kane County Clerk; Kendall County Clerk; Lake County Clerk; McHenry County Clerk; Will County Clerk; U.S Census Bureau

Median per capita tax capacity among the region's municipalities was $46,174 and ranged from $4,974 to $1.5 million. Relatively high sales tax revenues or greater property valuations allow local governments to maintain lower property tax rates than local governments with minimal tax bases. The following chart illustrates the tax capacity frequency distribution among municipalities.



Source: CMAP analysis of data from the Illinois Department of Revenue; Cook, Dupage, Grundy, Kane, Kendall, Lake, McHenry, and Will county clerks

Of the 284 municipalities, 136 had per capita tax capacity between 30,000 and 60,000. A handful of municipalities were found to have per capita tax capacities far from the region's median. Three outliers with high per capita tax capacity of more than ten times the median had low populations (<600). Two municipalities with tax capacity of less than $10,000 per capita were located in southern Cook County.

While state sales tax revenue disbursements are simply a function of a municipality's sales tax base, home rule municipalities have greater ability to derive additional revenue from their base with a local-imposed sales tax. At the same time, non-home rule taxing districts, such as special districts, school districts, and non-home rule counties and municipalities, are limited in their ability to increase their property tax extension. As a result, these districts are limited in their ability to turn an increase in property valuation into an increase in property tax revenue.

State Revenue Sharing

Pursuant to state statute, the State shares a portion of its tax revenues with local governments. The formulas used to calculate the disbursement of state tax revenues to local governments vary for each tax type. The following table briefly explains some of these state revenue sharing arrangements:

Examples of State Revenue Sharing Arrangements with Local Governments

State Tax Source	How Imposed	Local Governments Receiving Disbursement	Disbursement Formula
Sales Tax	6.25% state rate for retail sales of general merchandise and 1 percent state rate for sales of qualifying food, drugs, and medical appliances	Counties, municipalities, and the Regional Transportation Authority	16% of the state collections from retail sales of general merchandise and 100% of the collections from sales of qualifying food, drugs, and medical appliances are disbursed to the municipal or county government (if unincorporated) where the sale took place. 4% of the tax collected from general merchandise sales is disbursed to county governments (except Cook County) for sales that occurred within county boundaries. For sales made in Cook County, this 4% share is allocated to the RTA.
Income Tax	Individuals, trusts, and estates: 5% of net income. Corporations: 7% of net income	Counties and municipalities	One tenth of total collections minus the amount deposited in the refund fund. The amount that each municipality or county receives is based on its population in proportion to the total state population.
Personal Property Replacement Tax	Corporations: 2.5% tax on income Partnerships, trusts, and S-corporations: 1.5% tax on income Public utilities: 0.8% tax on invested capital Electricity distributors: Based on amount of kilowatt-hours distributed. The rate increases as the amount distributed per month increases. Telecommunications services: 0.5% of all gross charges charged by the telecommunications retailer	All taxing units of government that collected personal property taxes before they were abolished	The total collections are divided into two portions. One portion (51.65%) goes to Cook County. The other portion (48.35%) goes to other counties. The Cook County portion is then distributed to the taxing districts in Cook County based on each district's share of personal property tax collections for the 1976 tax year. (For example, if total taxes collected by all districts were $1 million and District A collected $35,000 of that total, District A's share of any future distributions would be 3.5%.) The downstate portion is distributed similarly, except that the collections from the 1977 tax year are used to calculate each district's share of the distribution.

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State Tax Source	How Imposed	Local Governments Receiving Disbursement	Disbursement Formula
Motor Fuel Tax	$0.19/gallon for gasoline and gasohol, $0.215/gallon for diesel, and $.215/gallon for combustible gases	Counties, municipalities, townships	After a variety of deductions, 54.4% of the balance is allocated to local governments. Of this portion, 49.1% is distributed to municipalities, 16.74% to counties over 1,000,000 in population, 18.27% to counties under 1,000,000 in population, and 15.89% to townships. The municipality's share of the total MFT allocation is based on population. The county share is based on the amount of motor vehicle license fees received. The road district/township share is based on mileage of township roads. MFT funds must be used for transportation purposes.
Source: Information and language directly from the Illinois Department of Revenue was used for this table.			

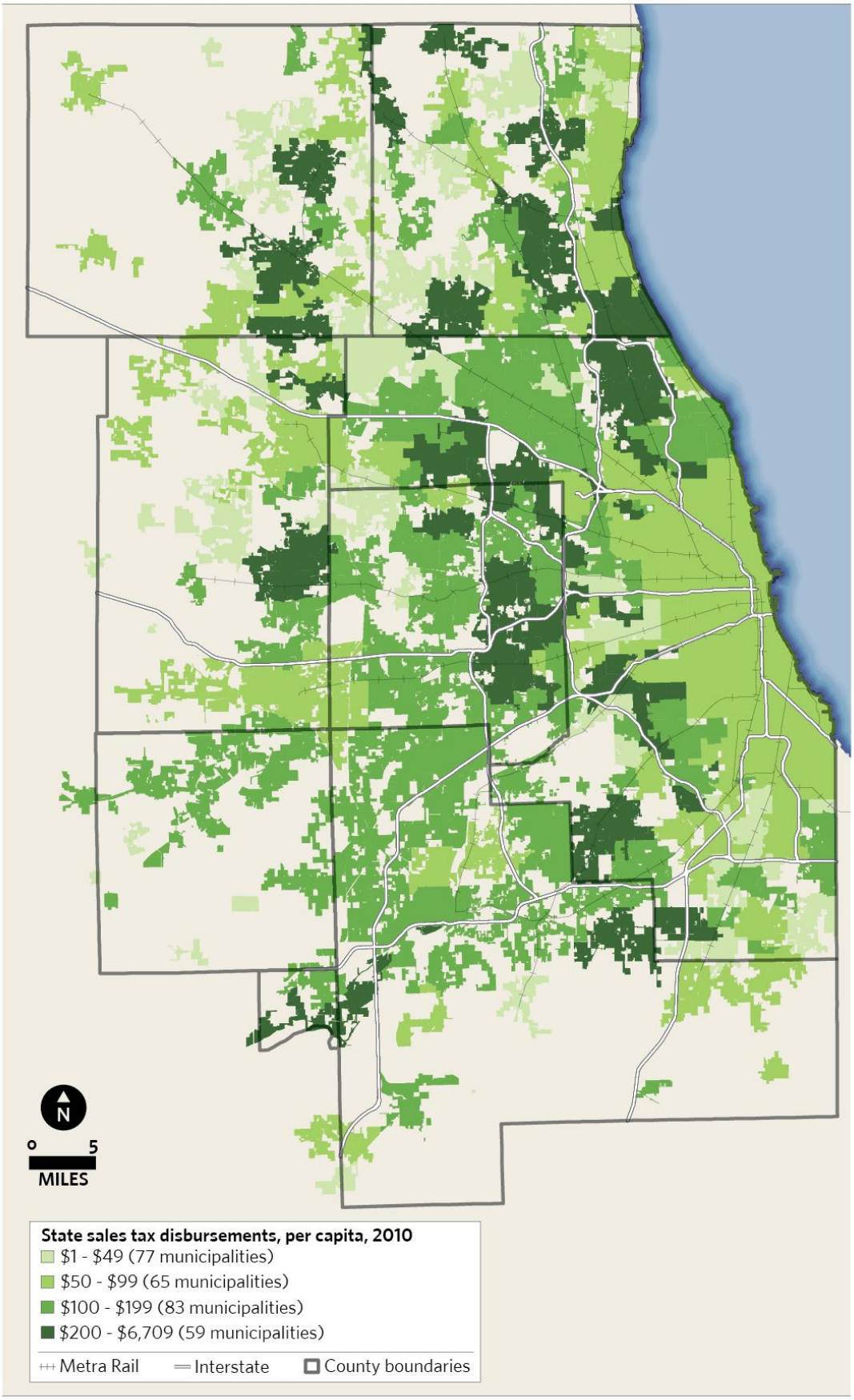
Sales Tax Revenue Sharing

State sales tax disbursements account for the largest portion of state and local revenue sharing. Taxpayers in northeastern Illinois paid a total of $5.2 billion in state sales taxes in 2010. Of that, $4.0 billion or 77.1 percent went to the State, $216.4 million or 4.2 percent went to counties and the Regional Transportation Authority (RTA),[42] and $969.6 million or 18.7 percent went to municipalities.

State sales tax sharing to local governments is based on where the sale took place or where final acceptance of the order occurred. Municipalities (and counties for sales in unincorporated areas) receive 1 percentage point of the 6.25 percent rate on general merchandise sales within their borders. They also receive the full amount of the revenues from the 1 percent state rate on qualifying food, drugs, and medical appliances. Counties receive a quarter of a percentage point of the state rate on general merchandise sales within their borders. The exception is the Cook County share, which is allocated to the RTA. The following map illustrates per capita state sales tax disbursements to municipalities in the region for 2010.

[42] The RTA receives Cook County's share of the state sales tax. The RTA also collects a mass transit district sales tax, which is not included in this data.

State sales tax disbursements to northeastern Illinois municipalities, per capita



Source: CMAP analysis of Illinois Department of Revenue data and U.S. Census Bureau, 2010 decennial census data

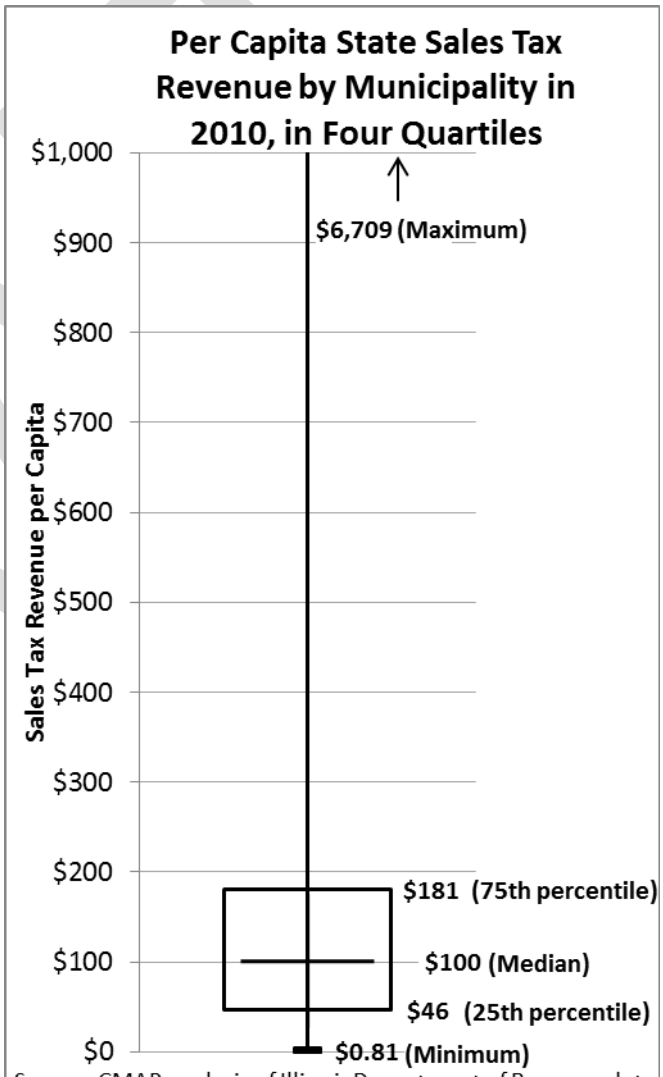
In addition to receiving state sales tax revenues, counties, municipalities, and other units of government can impose local option sales taxes under certain circumstances. This includes municipal home rule sales taxes as well as municipal non-home rule sales taxes that can be adopted through the passage of a referendum up to a maximum rate of 1 percent.

Implications of State Sales Tax Sharing

Highly Varied Distribution

Sharing state sales tax revenue based on location of sale results in highly varied disbursements across the region's municipalities. This creates wide differences in terms of municipal capacity to provide essential services, maintain or expand infrastructure, or attract new residents and businesses. To examine the existing disparities, consider the following 2010 statistics:

- Municipalities covering 26 percent of the region's population received 50 percent of the municipal disbursements.[1] The municipalities of the remaining 74 percent of the population shared the other half.
- Median per capita state sales tax revenue is $100, meaning that half of the municipalities in the region receive less than $100 in state sales tax revenue per resident, while the other half receives between $100 and $6,709. The following chart provides an illustration of this distribution.
- When looking at municipalities in the middle of the pack for state sales tax revenue per resident:
    - The municipality at the 75th percentile receives 79.9 percent more per resident than the municipality at the median.
    - The municipality at the 25th percentile receives 54 percent less than the median municipality.
- When revenues from local sales taxes are taken into account, the revenue differential between municipalities becomes larger:
    - The municipality in the 25th percentile is 57.4 percent less than the median of $130.
    - The municipality at the 75th percentile jumps to 86.1 percent more than the median.



Source: CMAP analysis of Illinois Department of Revenue data; and U.S. Census Bureau, 2010 decennial census data

Impacts on the Provision of Municipal Services and Infrastructure

While high variances exist in terms of sales tax revenues, the expenditure side must also be considered. Shares of sales tax revenue allow municipalities and counties to recoup the cost of providing local government services arising from the revenue generating developments. However, an analysis of a

hypothetical sales tax-generating development in the CMAP region illustrates that average associated municipal expenses amount to much less than the revenues generated. Even without a portion from local option sales taxes, municipalities receive over and above the amount of revenue required to provide these services.

The following table analyses the fiscal impact of a hypothetical retail power center or auto dealership, using data specific to a 30-acre greenfield site in metropolitan Chicago. The analysis compares revenues that would accrue to a municipality as a result of the development, including local taxes and state sales tax disbursements, to municipal expenses that would be required to support the development.

Estimated fiscal impacts on a municipality in the CMAP region for a 30-acre development

	RETAIL POWER CENTER	AUTO DEALERSHIP
REVENUES		
Sales taxes	$1,719,700	$2,696,300
Property taxes	$369,000	$192,500
Telecom taxes	$2,500	$1,000
Electricity taxes	$16,500	$6,500
Natural gas taxes	$4,500	$1,500
Total revenues	**$2,112,200**	**$2,897,800**
EXPENSES		
General administration	$86,000	$34,000
Fire	$70,000	$27,000
Police	$141,000	$55,000
Total Expenses	**$297,000**	**$116,000**
Net fiscal impact	**$1,815,200**	**$2,781,800**

Notes: Assumes sales tax revenues include share of state sales tax, a 0.87% local option sales tax, property taxes of 1.66%, 4.99% telecom tax, 4.34% electricity tax, and 4.35% natural gas tax. Assumes expenses per resident and worker of: General - $140; Fire - $113; and Police - $228.

Source: Analysis of data from Illinois Department of Revenue, Cook County Assessor, DuPage County Assessor, Illinois Department of Commerce and Economic Opportunity, Illinois Comptroller, and S. B. Friedman & Company

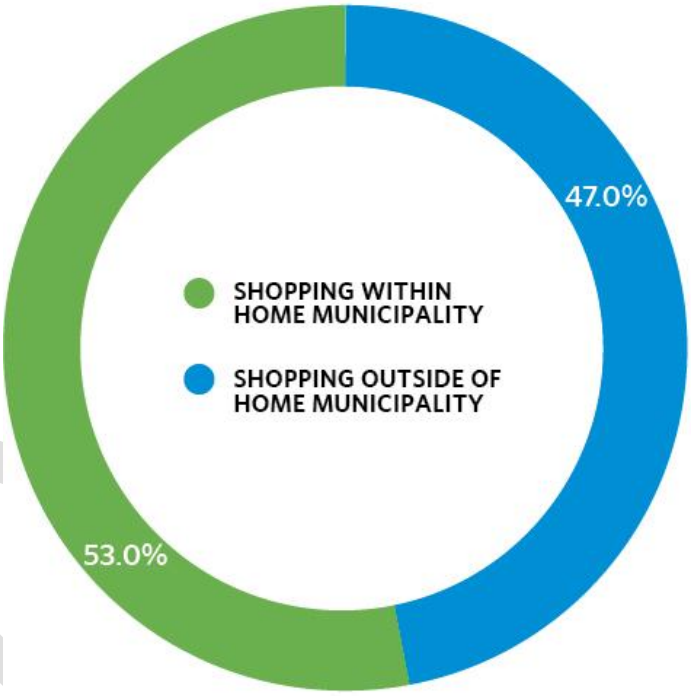
For a retail center, the state and local sales tax revenue generated would be 6 times more than municipal expenses associated with the development, and would be 3 times higher than the state sales tax portion alone. For an auto dealership, the discrepancy is even greater – state and local sales tax revenues are between 23 times municipal service expenses, and 12 times the municipal service expenses for state sales tax disbursements generated. Additionally, the municipality receives property and utility tax revenue that can be utilized to recoup the cost of supporting a development. Municipalities utilize surplus revenue generated from commercial properties to support services to residential areas, which do not typically generate enough tax revenue to support needed government services.[43]

[43] University of Illinois Extension, "Costs of Community Services," Local Government Information and Education Network Fact Sheet 2000-001, http://urbanext.illinois.edu/lcr/pdf/LGIEN2000-0011.pdf, (retrieved on April 29,

While the municipality with the point of sale receives the tax revenue, other nearby municipalities may have to provide services as a result of these developments. Residents shopping outside of their home municipality travel through other municipalities that must provide services or infrastructure associated with that trip. While service and infrastructure costs are likely to be more intense for a municipality with a sales tax generating development, adjacent municipalities also incur these expenses. One of the more visible expenses is the resurfacing or reconstruction of arterial roads, which is done at an average per mile cost of nearly $400,000 (resurfacing), and $5,000,000 (reconstruction).[44]

Analysis of available data clearly demonstrates that residents are not bound by their home municipality when making shopping trips. Using CMAP's trip generation model and information from CMAP's recent Travel Tracker survey, about 1,466,000 (47 percent) daily shopping trips are made to destinations outside of home municipalities and 1,654,000 (53 percent) are made to destinations within home municipalities.[45] This data represents the number of shopping trips made, rather than sales made during shopping trips.

Location of shopping trips in the CMAP region



Source: CMAP analysis of Travel Tracker Survey data

2011; John L. Crompton , "Programs that Work: Parks and Open Space: the Highest and Best Use of Public Land?," *Journal of Park and Recreation Administration* 19, no. 3 (2001): 133-154.

[44] Based on CMAP analysis for GO TO 2040's Financial Plan for Transportation. Figures are derived from reported bids for advertised projects and data acquired directly from municipal and county project implementers. In this context, "per mile" refers to "per centerline mile". As costs obviously vary depending on time and place, these numbers should be treated as illustrative and for planning purposes only.

[45] See http://www.cmap.illinois.gov/travel-tracker-survey for more information on the Travel Tracker Survey. The analysis assumes that the percent of shopping trips made outside the home municipality shown in the Travel Tracker Survey results is representative of the region's shopping trips in general, and that the region makes approximately 3,120,000 daily shopping trips for any purpose, as estimated in CMAP's trip generation model.

Impacts on Land Use and Development

As GO TO 2040 states, the region's development over the last several decades has resulted in a pattern of land use that is not sustainable. These changes have been driven by diverse factors, including infrastructure investment decisions and household preferences. Tax policies, including but not limited to the sales tax, have also played a key role in driving the development patterns for some communities. The sales tax structure often creates an incentive to attract large footprint retail land uses like big box stores and auto dealerships, and may lead many local governments to make land use decisions at odds with their own comprehensive planning goals. The planning term for this incentive is the "fiscalization of land use"—the orientation of land use decisions to maximize municipal revenue streams. From a regional scale, this can encourage a distended rather than compact pattern of development. Other related regional impacts include a disparity between where people work and live, a lack of access to transit, increased energy use and household costs related to transportation, and increasing levels of traffic congestion.[46]

All that considered, it must be emphasized that local governments are simply playing by the rules established by the state. Municipalities have every incentive to maximize certain revenue streams and minimize the tax burdens faced by their own residents. Furthermore, while the "fiscalization of land use" incentive exists, municipalities across northeastern Illinois remain extremely diverse, with their own unique community characters. Many communities do not prioritize the attraction of large footprint retail, and many others have struck a balance between residential and other development priorities. GO TO 2040's emphasis on "livability"—the creation of more walkable communities with access to transportation options – is not a "one size fits all" proposition.

Disbursement Options

This section will analyze a series of different options for disbursing state sales tax revenues. Any of these options could include a multi-year phase-in period or a provision that would prevent a municipality's disbursement from dropping for a set period (hold-harmless). For the purpose of simplicity, analyses of all the following proposals assume that the new disbursement criteria would have begun in 2010.

Population

Instead of location of sale, revenues could be shared on a per capita basis. In other words, sales tax revenues could be shared in the same way as income and motor fuel taxes, which are disbursed to municipalities based on population. Sharing sales tax revenue based on a municipality's population would provide additional funding support to communities with little commercial development. It would also reorient municipal incentives toward maximizing residential population. On a per capita basis, this would result in no variance in state sales tax revenues among municipalities in the region. In 2010, every municipality would receive $122 in state sales tax revenue per capita. In other words, 25 percent of the region's population would live in municipalities collecting 25 percent of the sales tax revenues, and so on. In comparison to disbursing based on location of sale, 172 municipalities would have received higher disbursements in 2010, and 112 municipalities would have received lower disbursements than they otherwise would under location of sale criteria.

Tax Base

Sales tax revenues could be dispersed on a municipality's capacity to raise revenue through its property tax base. This method would likely bring about greater equity in municipal funding sources, as economically depressed areas would be provided with more funding than under a system based on the location of sale.

[46] See GO TO 2040's chapter on "Achieve Greater Livability through Land Use and Housing", p.66.

To estimate the effect of disbursing sales tax revenues using tax base criteria, each municipality's population was multiplied by a ratio of the aggregate equalized assessed value per capita in incorporated areas of the region to the municipality's equalized assessed value per capita.[47] In general, municipalities currently receiving relatively low sales tax revenue per capita would mostly benefit under this new system, while municipalities currently receiving higher disbursements of sales tax revenue per capita would receive less revenue under the new system. Therefore, this change would have the effect of reducing disparity among municipalities. Outcomes of disbursing sales tax revenues using property tax base in 2010 include:

- In comparison to disbursing based on location of sale:
  - 151 municipalities would receive higher disbursements.
  - 133 municipalities would receive lower disbursements.
- Half of the municipalities in the region would receive less than $105 in state sales tax revenue per resident, while the other half would receive between $105 and $917.
- When looking at municipalities in the middle of the pack for state sales tax revenue per resident:
  - The municipality at the 75th percentile would receive 43.5 percent more per resident than the municipality at the median.
  - The municipality at the 25th percentile would receive 30.8 percent less than the median municipality.

Combination Formulas

Criteria for disbursement could include several attributes, including the volume of sales in a municipality's borders, a municipality's population, and the property tax base of a municipality. The following two percentage breakdowns are offered to illustrate hypothetical examples of how a combination formula could be operationalized.

Combination Formula 1

Of total state sales tax disbursements:

70% based on location of sale: 70% × 1% of sales within municipality's borders

20% based on population: $$20\% \text{ of total disbursements } \times \frac{\text{Municipality's population}}{\text{Total population}}$$

10% based on property tax base:

$$10\% \text{ of total disbursements } \times \frac{\dfrac{\text{Aggregate EAV per capita}}{\text{Municipality's EAV per capita}} \times \text{Municipality's population}}{\sum\left(\dfrac{\text{Aggregate EAV per capita}}{\text{Municipality's EAV per capita}} \times \text{Municipality's population}\right)}$$

Disbursing a smaller proportion of revenues based on location of sale results in most municipalities that had been below the median in 2010 doing better. On the other hand, most municipalities above the median of $100 per capita in 2010 would receive lower revenues under this system than they otherwise would have received under a system of allocated all state sales tax revenues based on location of sale. Outcomes of disbursing sales tax revenues using Combination Formula 1 in 2010 include:

- In comparison to disbursing based on location of sale:
  - 162 municipalities would receive higher disbursements
  - 122 municipalities would receive lower disbursements

[47] A similar formula is utilized in the Minneapolis-St. Paul region for sharing property tax revenues.

- Municipalities covering 34 percent of the region's population received 50 percent of the municipal disbursements. The municipalities of the remaining 66 percent of the population shared the other half.
- Half of the municipalities in the region would receive less than $108 in state sales tax revenue per resident, while the other half would receive between $108 and $4,721
- When looking at municipalities in the middle of the pack for state sales tax revenue per resident:
    - The municipality at the 75th percentile would receive 48 percent more per resident than the municipality at the median
    - The municipality at the 25th percentile would receive 31.4 percent less than the median municipality

The next example is based on the following formula:

Combination Formula 2
Of total state sales tax disbursements:
20% based on location of sale: 20% × 1% of sales within municipality's borders

10% based on population: $$10\% \text{ of total disbursements } \times \frac{\text{Municipality's population}}{\text{Total population}}$$

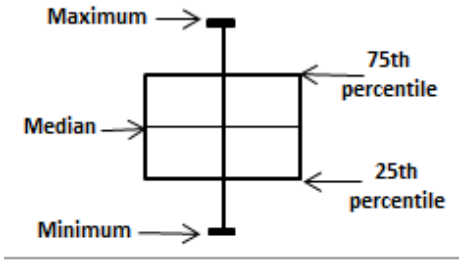
70% based on property tax base:

$$70\% \text{ of total disbursements } \times \frac{\dfrac{\text{Aggregate EAV per capita}}{\text{Municipality's EAV per capita}} \times \text{Municipality's population}}{\sum\left(\dfrac{\text{Aggregate EAV per capita}}{\text{Municipality's EAV per capita}} \times \text{Municipality's population}\right)}$$

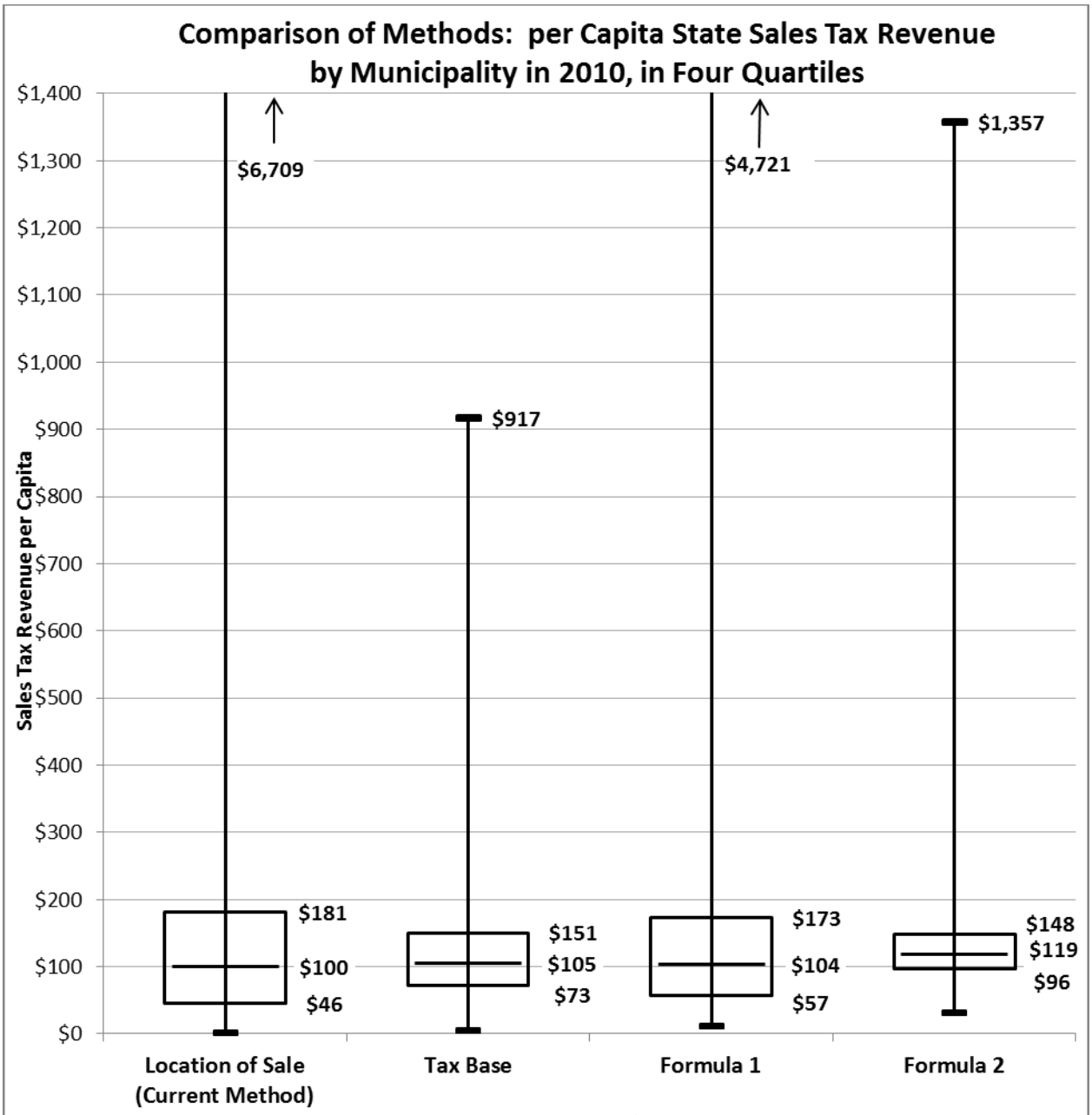
This formula gives more weight to property tax base than the first formula and less weight to location of sale and population. In comparison to disbursements under the current system, most municipalities that had received less than $100 in state sales tax disbursement per capita receive more disbursement under Combination Formula 2 than they would under a system based entirely on location of sale. At the same time, most municipalities above the median in 2010 would receive less than they otherwise would have. Outcomes of disbursing sales tax revenues using Combination Formula 2 include:

- In comparison to disbursing based on location of sale:
    - 154 municipalities would receive higher disbursement
    - 130 municipalities would receive lower disbursement
- Municipalities covering 40 percent of the region's population would receive 50 percent of the municipal disbursements. The municipalities of the remaining 60 percent of the population would share the other half.
- Half of the municipalities in the region would receive less than $119 in state sales tax revenue per resident, while the other half would receive between $119 and $1,357
- When looking at municipalities in the middle of the pack for state sales tax revenue per resident:
    - The municipality at the 75th percentile would receive 24.7 percent more per resident than the municipality at the median
    - The municipality at the 25th percentile would received 19.1 percent less than the median municipality

The following chart provides an illustration of how disbursing revenues using the methods described above would change the variance among municipalities.



How to Read This Chart



Note: The proposal based on population results in a disbursement of $122 per capita.
Source: CMAP analysis of Illinois Department of Revenue data; and U.S. Census Bureau, 2010 decennial census data

Set Aside

Instead of disbursing revenues to municipalities and counties, a portion of sales tax revenues could be set aside for other needs, such as those that impact multiple jurisdictions. Transportation, water, or

other kinds of infrastructure are examples of the types of capital projects that could be financed through such a strategy, though a universe of other options certainly exists. Like many places across the U.S., northeastern Illinois faces a considerable financial shortfall in its ability to maintain and expand its existing infrastructure. Without raising rates, the existing sales tax base for municipalities would obviously be affected, but benefits would be realized by the expenditure of these funds on projects of a multijurisdictional scale.

Permissive

Instead of directly disbursing revenues to municipalities and counties, the State could disburse revenues to other local bodies that would have authority to determine disbursement arrangements based on need. These bodies might also be counties, or sub-regional groups of municipalities. This system could increase local cooperation on shared needs, resolve annexation or land incorporation conflicts between municipalities, or to coordinate government services. Under this system, the effect on municipalities would depend on the formula used.

Personal Property Replacement Tax Revenue Sharing

All taxing districts that collected personal property taxes in 1977, or in 1976 for taxing districts in Cook County, receive PPRT disbursements from the State. Total collections are divided into two portions. One portion (51.65%) goes to taxing districts in Cook County. This portion is distributed to taxing districts in Cook County on the basis of each district's share of total personal property tax collections in Cook County for the 1976 tax year. The other portion (48.35%) is disbursed to taxing districts in the remaining counties based on each district's share of total personal property tax collections in the rest of the State for the 1977 tax year.

The City of Chicago receives 17.9 percent of the PPRT revenues in the region, while suburban municipalities receive 5.5 percent. Park districts receive 6.9 percent, with about three-quarters of the park district funds in the region going to the Chicago Park District. Of the 5 percent of revenues that go to sanitary and water districts, about 90 percent go to the Metropolitan Water Reclamation District. 1,243 taxing districts receive PPRT revenues in the region, while approximately 70 districts, including 21 municipalities, do not receive revenue. Districts that do not receive revenue either were created after 1977 or did not collect personal property taxes. The following chart provides a summary of PPRT allocations in northeastern Illinois by type of district.

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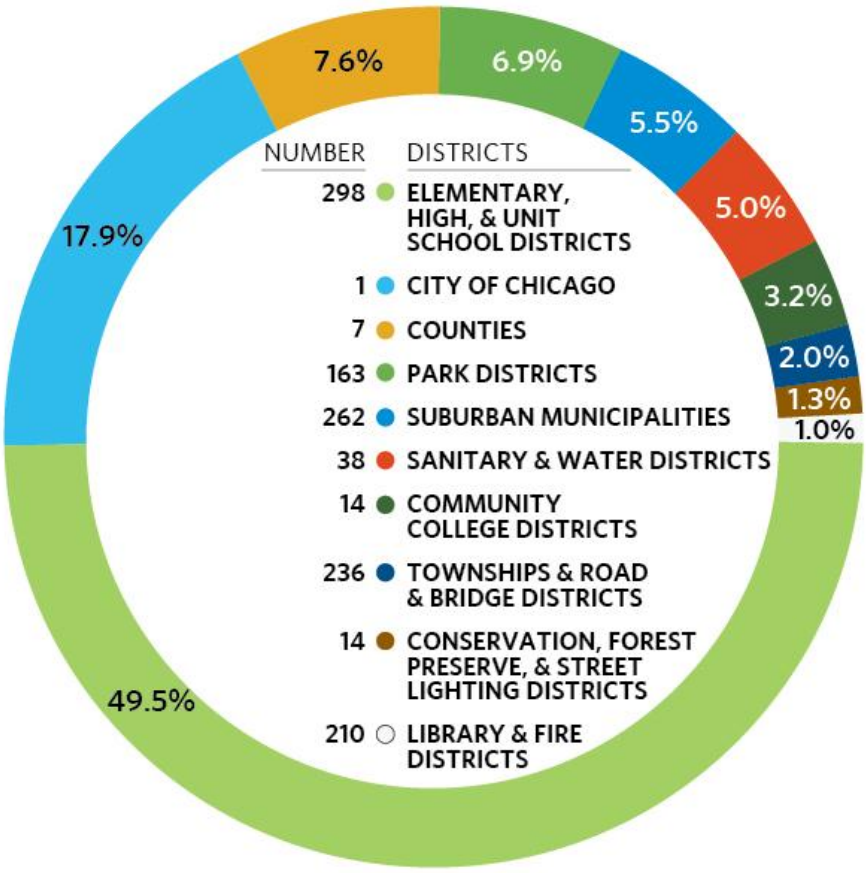
Personal property replacement tax (PPRT) allocations to taxing districts in northeastern Illinois, as a percent of total PPRT revenues to the region



Source: Illinois Department of Revenue

Since the replacement tax was enacted in 1979, local governments have received the same proportion of the total revenue generated every year. However, the demographics and economy of northeastern Illinois have changed fairly extensively during that time. The following chart provides PPRT allocations by the primary county of the taxing district. For comparison, personal property tax collections from 1977 and county populations for 1970 and 2010 are also included.

Personal property replacement tax (PPRT) allocations and personal property tax (PPT) collections compared with population

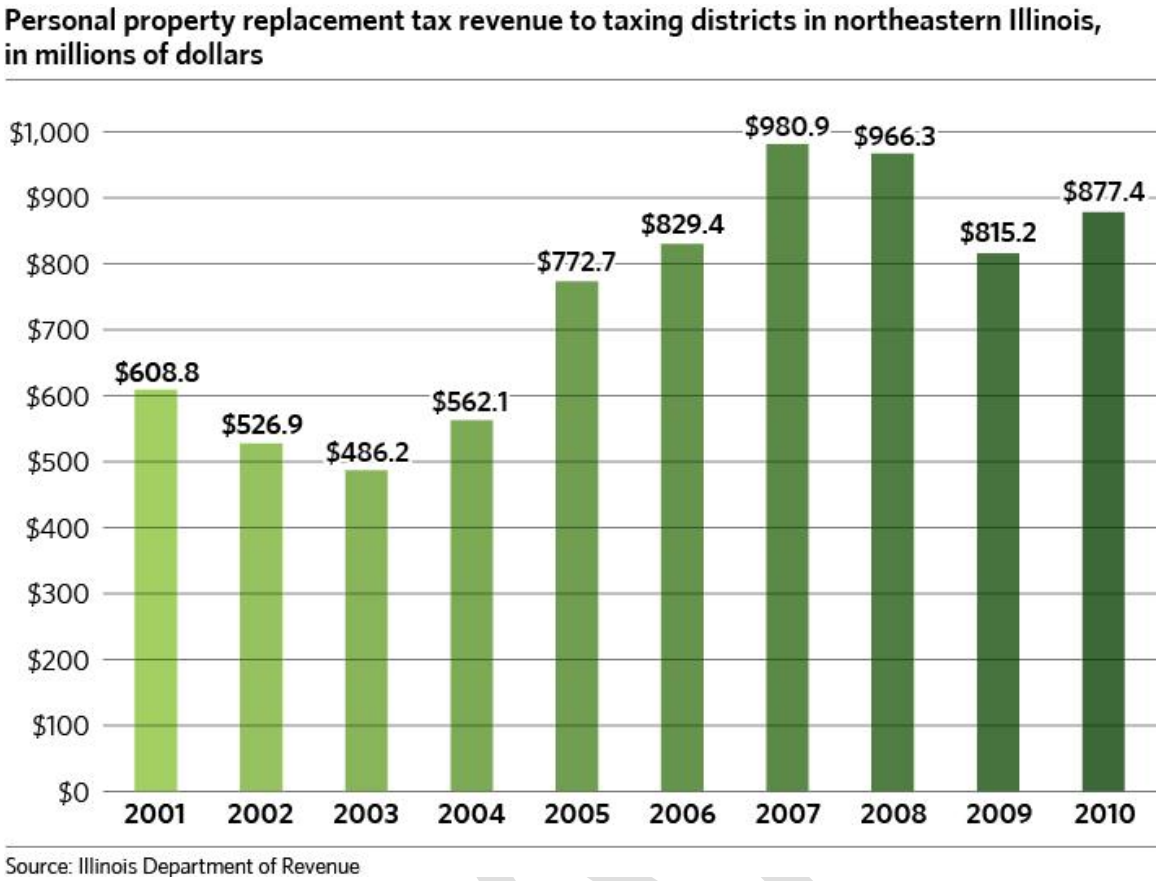
TAXING DISTRICT COUNTY	% OF TOTAL PPRT DISBURSED STATEWIDE TO TAXING DISTRICTS WITHIN COUNTY	PPT COLLECTIONS FOR TAXING DISTRICTS WITHIN COUNTY AS % OF STATE TOTAL	COUNTY POPULATION AS % OF STATE POPULATION	
		1977	1970	2010
COOK	**51.7%**	**48.6%**	**49.4%**	**40.5%**
DUPAGE	**3.4%**	**3.7%**	**4.4%**	**7.1%**
KANE	**1.7%**	**1.9%**	**2.3%**	**4.0%**
KENDALL	**0.4%**	**0.4%**	**0.2%**	**0.9%**
LAKE	**3.0%**	**3.2%**	**3.4%**	**5.5%**
MCHENRY	**0.8%**	**0.9%**	**1.0%**	**2.4%**
WILL	**3.4%**	**3.6%**	**2.2%**	**5.3%**
TOTAL	**64.4%**	**62.3%**	**63.0%**	**65.7%**

Source: Illinois Department of Revenue; U.S. Census Bureau

When examined by county, PPRT allocations to taxing districts are somewhat close to actual personal property tax collections in 1977. However, because Cook County taxing districts receive a set 51.65 percent of PPRT allocations, their allocation does not correspond as well to collections, which accounted for 48.6 percent of the total in 1977 and 48.0 percent in 1976. PPRT allocations were also close to each county's population relative to the state population. However, as the collar counties grew relative to Cook County, Cook County still receives 51.65 percent of PPRT revenues while its population accounts for 40.5 percent of the state population. At the same time, collar counties receive 12.7 percent of the PPRT revenue. This allocation is close to their proportion of the population in 1970 of 13.6 percent. However, in 2010, the collar counties' population accounted for 25.2 percent of the state population.

Revenues

In 2010, taxing districts in northeastern Illinois received $877.4 million in PPRT disbursements. Statewide, taxing districts received $1.4 billion. Statewide revenues were 8.2 percent less than personal property tax collections in 1977 (after adjusting for inflation), which totaled $256.9 million for the 7-county region and $412.1 million statewide. Since 2007 PPRT revenues were actually higher than inflation-adjusted personal property tax collections in 1977, the 2010 drop may be due to the economy. Since the primary revenue source for the PPRT is the income tax on corporations, partnerships, trusts, and S corporations, revenues typically follow economic cycles. Aside from experiencing drops in revenue in 2002 and 2003 and then in 2008 and 2009, PPRT revenue has generally increased between 2001 and 2010. The following chart shows PPRT revenues to the CMAP region for the past ten years.



Even with hundreds of millions of dollars going to local governments in the region from the PPRT, the funds do not make up a large portion of most local governments' budgets. The following chart provides an overview of how much PPRT contributes to local government budgets in the region.

Proportion of revenue from personal property replacement tax (PPRT) revenues, 2010

TYPE OF TAXING DISTRICT	AVERAGE PPRT AS % OF TOTAL REVENUE	NO. OF DISTRICTS WITH PPRT MORE THAN 5% OF TOTAL REVENUE	NO. OF DISTRICTS WITH BUDGET DATA AVAILABLE	TOTAL NO. OF DISTRICTS IN REGION RECEIVING PPRT REVENUE
Elementary, High, and Unit School Districts	2.1%	18	295	298
City of Chicago	2.9%	0	1	1
Counties	0.9%	0	6	7
Park Districts	2.6%	22	140	163
Suburban Municipalities	0.7%	2	240	262
Sanitary and Water Districts	7.2%	4	19	38
Community College Districts	N/A	0	0	14
Townships and Road and Bridge Districts	4.3%	32	118	236
Conservation, Forest Preserve, and Street Lighting Districts	2.5%	1	11	14
Library and Fire Districts	2.0%	17	215	210
TOTAL	**2.2%**	**96**	**1,045**	**1,243**

Note: Total revenues exclude enterprise, fiduciary, and internal service funds.
Source: Illinois Office of the Comptroller; Illinois Department of Revenue; Illinois State Board of Education

Sanitary and water districts have the highest average reliance on PPRT revenue, with an average of 7.2 percent of revenues coming from PPRT. Townships rely on PPRT revenue for 4.3 percent of their revenues, on average. Of the 118 townships for which budget data was available, 32 rely on PPRT for more than 5 percent of total revenues and nine rely on PPRT for more than 10 percent of total revenues. In total, 96 taxing districts in the region rely on PPRT for more than 5 percent of their revenues, while 34 taxing districts rely on PPRT for more than 10 percent of their revenues. The following chart lists taxing districts in the region that rely on PPRT for more than 10 percent of total revenues.

Taxing districts with more than ten percent of revenues from personal property replacement tax (PPRT), 2010

TAXING DISTRICT	TOTAL REVENUE	PPRT	%
Round Lake Sanitary District	$25,202	$19,824	78.7%
Rockdale Elementary School District 84	$2,489,007	$1,161,090	46.6%
West Dundee Fire Protection District	$15,778	$6,187	39.2%
Phoenix Park District	$25,483	$9,639	37.8%
Romeoville Mosquito Abatement District	$74,873	$24,969	33.3%
Forest View Park District	$169,515	$51,653	30.5%
Jackson Township	$463,276	$125,011	27.0%
Laraway Community Consolidated School District 70-C	$7,209,605	$1,826,954	25.3%
Central Stickney Sanitary District	$45,872	$10,123	22.1%
Lockport Township	$3,325,725	$688,991	20.7%
Stickney Township	$7,062,535	$1,412,784	20.0%
Hodgkins Park District	$947,275	$165,416	17.5%
Joliet Township	$3,998,011	$625,560	15.6%
Forest View Village	$2,934,329	$455,370	15.5%
Wilmington Township	$290,267	$44,823	15.4%
Bedford Park District	$2,023,681	$297,896	14.7%
Central Stickney Elementary School District 110	$5,200,035	$763,559	14.7%
Addison Creek River Conservancy District	$164,000	$22,995	14.0%
Ivanhoe Park District	$584,619	$79,398	13.6%
Bedford Park Public Library District	$1,183,621	$156,815	13.2%
Stickney-Forest View Public Library District	$1,149,165	$149,195	13.0%
Little Rock Township	$975,210	$122,307	12.5%
Waukegan Township	$4,879,774	$609,688	12.5%
Berkeley Park District	$205,224	$25,540	12.4%
Broadview Park District	$1,131,205	$135,369	12.0%
Reavis High School District 220	$27,741,798	$3,270,492	11.8%
Ford Heights Elementary School District 169	$11,939,252	$1,357,575	11.4%
Komarek Elementary School District 94	$5,686,666	$644,980	11.3%
Marengo Township	$807,587	$90,763	11.2%
Chicago Park District	$400,062,000	$44,349,000	11.1%
Leyden Fire Protection District	$2,349,678	$259,578	11.0%
Old Town Sanitary District	$52,096	$5,703	10.9%
Veterans Park District	$6,053,386	$650,546	10.7%
Dunham Township	$692,923	$69,927	10.1%

Note: Total revenues exclude enterprise, fiduciary, and internal service funds.
Source: Illinois Office of the Comptroller; Illinois Department of Revenue; Illinois State Board of Education

Most districts that rely heavily on PPRT revenue are also relatively small. Sixteen of the districts have total revenues of less than $1 million, and six districts have total revenues of less than $100,000. However, a handful of school districts and larger townships also rely on PPRT for more than 10 percent of their budget. Of the 34 districts, nine are fully or partially located within the boundaries of Stickney Township. Stickney Township is located in west Cook County and includes the villages of Bedford Park (portion), Bridgeview (portion), Burbank, Forest View, and Stickney and related taxing districts.

Motor Fuel Tax Revenue Sharing

After a variety of deductions, 45.6 percent of state motor fuel tax (MFT) revenues are allocated to the Illinois Department of Transportation's Road Fund and State Construction Fund, and the remaining 54.4 percent are allocated to local governments. This allocation has been in effect since 1999, when the local government portion increased from 41.6 percent to 54.4 percent.[48] In FY2010, about $200 million was deducted off the top for various programs and funds, approximately $500 million to the IDOT Road Fund and Construction Account, and nearly $600 million was allocated to local governments.

State statute divides these MFT allocations into four pots: 49.1 percent to municipalities, 15.89 percent to townships; 18.27 percent to counties with fewer than 1 million residents, and 16.74 percent to counties with more than 1 million residents. These funds are then disbursed to local governments based on formulas that vary depending on the local government pot. While the State began allocating MFT to local governments in 1933, the current proportions were enacted in 1990.[49] The table on the following page describes how the 54.4 percent to local governments are disbursed.

In FY 2010, northeastern Illinois local governments received $347.0 million, which is equal to 59.9 percent of the total funds disbursed statewide. Because such a large portion of the region is incorporated, municipalities received 58.6 percent of the funds disbursed to the region, which is more than 49.1 percent that goes to municipalities statewide. At the same time, townships received 1.6 percent of the revenues to the region. While the region has 124 townships, only 84 received revenue in FY2010 because many road districts property tax levies do not meet the statutory threshold. All but four of the region's townships receiving funds were located in the collar counties. The following map provides an overview of road district miles in FY2010 for northeastern Illinois townships.

Because Cook County received the entire 96.9 million statewide allocation for counties with more than 1 million residents, Cook County received more than a quarter of the revenues disbursed to northeastern Illinois. For the 564-mile Cook County road system, this equates to $171,678 per road mile. The six collar counties received a total of $41.3 million or 11.9 percent of the $347.0 million disbursed to northeastern Illinois. The collar counties have jurisdiction over 1,400 miles of road. This equates to between $17,595 and $56,766 per road mile for each of the six collar counties.

[48] Illinois Public Act 91-20
[49] Illinois Public Act 86-982

State Motor Fuel Tax Disbursements to Local Governments

Type of Local Government	Disbursement Formula	Estimated Revenues FY2010 per Formula Basis	Number of Units Receiving MFT in FY2010		Amount Received in FY2010		Northeastern Illinois Proportion of Statewide Total	Proportion of Total MFT Revenues	
			Statewide	Northeastern Illinois	Statewide	Northeastern Illinois		Statewide (Statutory)	Disbursements to Northeastern Illinois
Municipalities	Based on population	$25.30 per resident	1,298	284	$284,254,974	$203,351,899	71.5%	49.10%	58.6%
Townships	Based on mileage of township roads. Only received if the property tax levied for road and bridge purposes is at least 0.08 percent (or for townships in DuPage County, an amount of at least $12,000 per mile of township road).	$1,297.02 per road mile	1,424 (of 1,509)	84 (of 124)	$91,992,088	$5,393,315	5.9%	15.89%	1.6%
Counties less than 1 million residents	Based on the proportion of motor vehicle license fees received	8 cents per dollar of motor vehicle license fees received	101	6	$105,770,639	$41,298,726	39.0%	18.27%	11.9%
Counties with more than 1 million residents (Cook County)	N/A	N/A	1	1	$96,912,999	$96,912,999	100.0%	16.74%	27.9%
Total			**1,526**	**375**	**$578,930,700**	**$346,952,636**	**59.9%**	**100%**	**100%**

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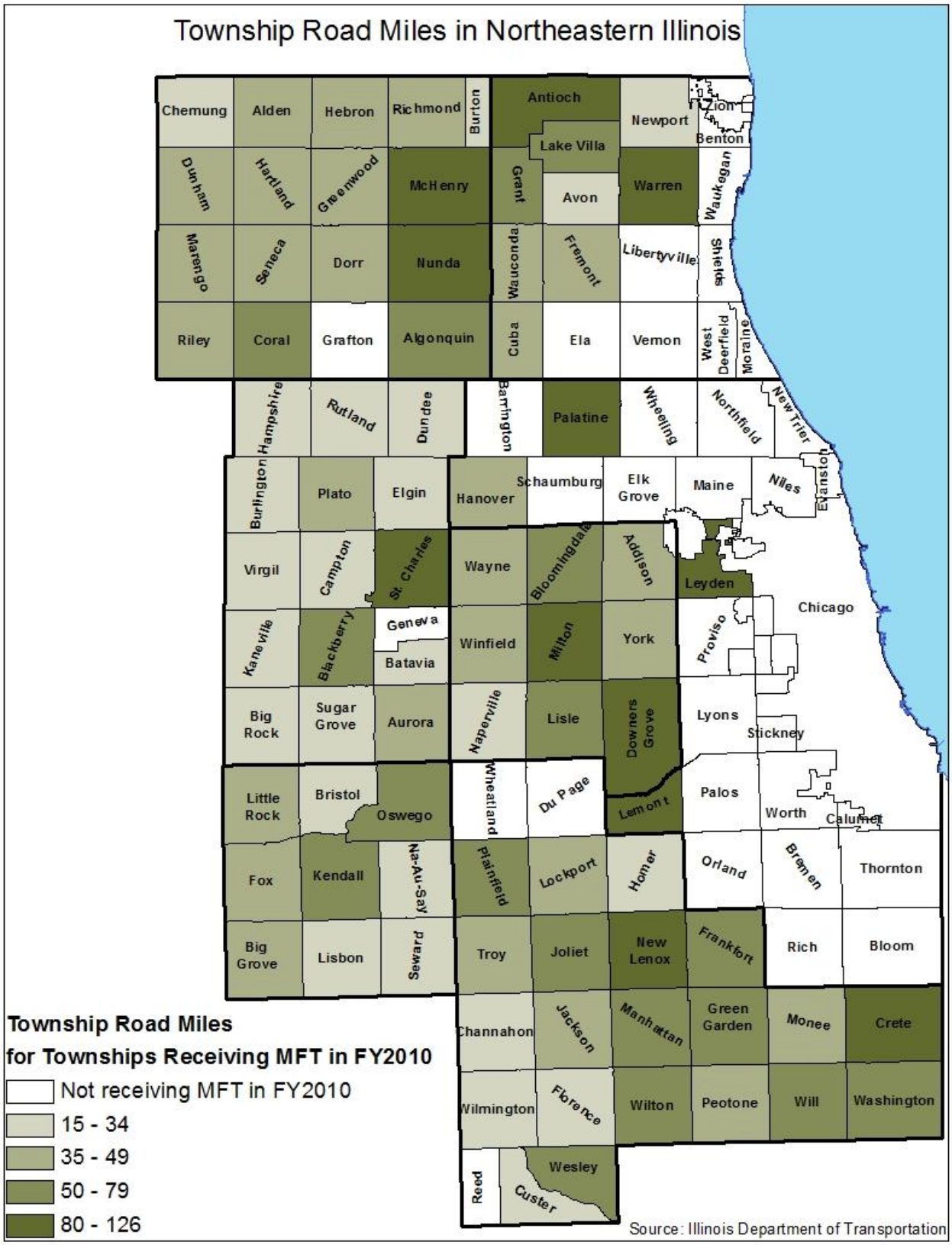
Township Road Miles in Northeastern Illinois
Chemung
Alden
Hebron
Richmond
Burton
Antioch
Newport
Zion
Benton
Lake Villa
Dunham
Hardland
Greenwood
McHenry
Grant
Avon
Warren
Waukegan
Marengo
Seneca
Dorr
Nunda
Wauconda
Fremont
Libertyville
Shields
Riley
Coral
Grafton
Algonquin
Cuba
Ela
Vernon
West Deerfield
Moraine
Hampshire
Rutland
Dundee
Barrington
Palatine
Wheeling
Northfield
New Trier
Burlington
Plato
Elgin
Hanover
Schaumburg
Elk Grove
Maine
Niles
Evanston
Virgil
Campton
St. Charles
Wayne
Bloomingdale
Addison
Leyden
Chicago
Kaneville
Blackberry
Geneva
Batavia
Winfield
Milton
York
Proviso
Big Rock
Sugar Grove
Aurora
Naperville
Lisle
Downers Grove
Lyons
Stickney
Little Rock
Bristol
Oswego
Wheatland
Du Page
Lemont
Palos
Worth
Calumet
Fox
Kendall
Na-Au-Say
Plainfield
Lockport
Homer
Orland
Bremen
Thornton
Big Grove
Lisbon
Seward
Troy
Joliet
New Lenox
Frankfort
Rich
Bloom
Channahon
Jackson
Manhattan
Green Garden
Monee
Crete
Wilmington
Florence
Wilton
Peotone
Will
Washington
Reed
Custer
Wesley
Township Road Miles
for Townships Receiving MFT in FY2010
Not receiving MFT in FY2010
15 - 34
35 - 49
50 - 79
80 - 126
Source: Illinois Department of Transportation

Property Taxes

The vast majority of local governments in northeastern Illinois impose a property tax. Assuming a well-designed system, the property tax is an effective and efficient means of raising local revenues. The virtues of the tax include the stability and reliability of the revenue stream, the ease of administering the tax which contributes to compliance, and the intrinsic connection between the source of the revenue (property) and what is being provided in return (public services). With nearly $20 billion in annual revenues generated, it constitutes the largest funding source for local units of government in the region.

Individual taxing bodies have their own levy rates that are individually determined by the relationship between their annual financial requests and the assessed value of property within their geographical boundaries. Rates can be understood as a function of service provision needs, the value of real property, and other revenue sources. The rates are generally determined according to a simple formula, $\frac{\text{Tax levy}}{\text{EAV}} = \text{Tax rate}$, where "Tax Levy" refers to the funds requested by taxing bodies and "EAV" refers to the equalized assessed value of all properties within a taxing district.

Assessment

The process begins with assessment of all real property. In Cook County, the county assessor initially assesses the fair cash value, or market value, of properties. Cook County is divided into three districts[50] and properties in each district are assessed every three years. In the collar counties, township assessors submit initial assessments to the county assessors. Properties in the collar counties are reassessed every four years. Railroad property and pollution control facilities are assessed by the Illinois Department of Revenue (IDOR).

County assessors convert the market values determined by the assessment to an assessed value by applying assessment ratios. State statute requires that properties be assessed at 33 1/3% of their market value,[51] except in counties allowed to apply property classification. For example, in a county that does not apply property classification, the assessed value for a property with an assumed market value of $150,000 would be $50,000. The state constitution allows counties with more than 200,000 residents to apply different assessment ratios depending on the type of property, as long as highest class does not exceed 2.5 times the level of assessment of the lowest class.[52] Counties that would like to apply property classification must enact an ordinance.[53] Currently, only Cook County has enacted an ordinance providing for property classification.[54]

After the assessed values are determined, property owners receive assessment notices. Property owners may appeal assessments to the county assessor's office and/or to the county Board of Review based on uniformity, overvaluation, or property description error.[55] County Boards of Review evaluate property assessment appeals by both property owners as well as taxing districts that may contest a valuation on the basis that a property is undervalued. In collar counties, the county assessor or the Board of Review may provide intra-county equalization multipliers for each township, which are applied

[50] The three districts are Chicago, suburban townships north of North Avenue, and suburban townships south of North Avenue.
[51] 35 ILCS 200/9-145
[52] Illinois State Constitution, Article IX, Section 4
[53] 35 ILCS 200/9-150
[54] Cook County Ordinances Sec. 74-60 through Sec. 74-71
[55] Assessment decisions by the Board of Review may be appealed to the Illinois Property Tax Appeal Board or to the county circuit court.

to assessments to equalize the median level of assessment across townships or classes or property within the county.[56] Finally, the Board of Review certifies the assessment rolls to the county clerk.

State Equalization

The next step in the process is inter-county equalization by the IDOR. The purpose is to equalize assessments such that the median level of assessment across counties within the State, including Cook County, is 33 1/3%. Farms, as well as properties assessed by the State such as railroads, are not subject to equalization. Without equalization, assuming equal rates and market values, a property taxpayer in one county may pay more property tax than the tax paid by a property taxpayer in another county. In addition, it is important to control for underassessment and overassessment because the property tax base is utilized for other functions, like calculating state funding to school districts.

The IDOR is responsible for determining an equalization factor for each county in the State. To do this, the IDOR compares assessment data with actual real estate sale data from Real Estate Transfer Declarations for sales representative of market values that are "arms' length" transactions. Using this data, the median ratio of assessed value to market value, called the median level of assessment, is computed for each county. To calculate the multiplier for each county used to adjust assessments to the statutory level, 33 1/3% is divided by the average median level of assessment for the previous three years. The assessed property value after equalization is called the Equalized Assessed Value (EAV). For example, if a county was found to have an average median level of assessment for the previous three years of 28%, then the assessed values of all properties in the county would be multiplied by 1.2. In this county, the property in the previous example with an assessed value of $50,000 would have an EAV of $59,524. Cook County was the only county in northeastern Illinois to be issued an equalization multiplier in 2009. Due to classification, the multiplier required to bring Cook County's median level of assessment to 33 1/3% was 3.3701.

In addition to providing a median level of assessment, IDOR also provides other measures, such as a coefficient of dispersion (COD). The COD is a calculation of the assessments' average deviation from the median level as a percent of the median level. This figure is used to determine uniformity of assessment ratios within each county. For Cook County, CODs vary by class, and the COD for residential property is significantly lower than the COD for commercial and industrial property.

When assessments are not uniform, taxpayers may have taxes extended on a property assessment that diverges from 33 1/3% of market value, even after equalization. As a result, taxpayers with equal market values and property tax rates may not pay the same in property taxes. In addition, there is evidence that uniformity also varies by property value. Specifically, assessment ratios as well as ratio variability may decrease as the market value of the property rises.[57]

Exemptions

Finally, applicable exemptions are applied to the property value. Properties used for educational, religious, governmental, or charitable purposes are exempt from the property tax. In addition, several other exemptions are available for residential properties. These residential property tax exemptions reduced the property tax base in northeastern Illinois by $34.2 billion in 2008.

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[56] 35 ILCS 200/9-205, 35 ILCS 200/9-210, 35 ILCS 200/16-60

[57] McMillen, Daniel P., "Assessment Regressivity: A Tale of Two Illinois Counties," *Land Lines*, January 2011.

Together, the general and alternative general homestead exemptions make up the largest amount of property value exempted from the tax base in the region. Other exemptions serve to reduce property taxes for specific taxpayers, such as seniors or veterans. However, exemptions also reduce the overall property tax base on which the extension can be levied. If the property tax base decreases, the rate must rise in order to achieve the same level of revenue. This higher rate is imposed on all taxpayers, including those that did not benefit from an exemption. While exemptions provide property tax relief to homeowners, the tax burden is shifted from homeowners with exemptions to other property owners.[58]

Tax Base and Rates

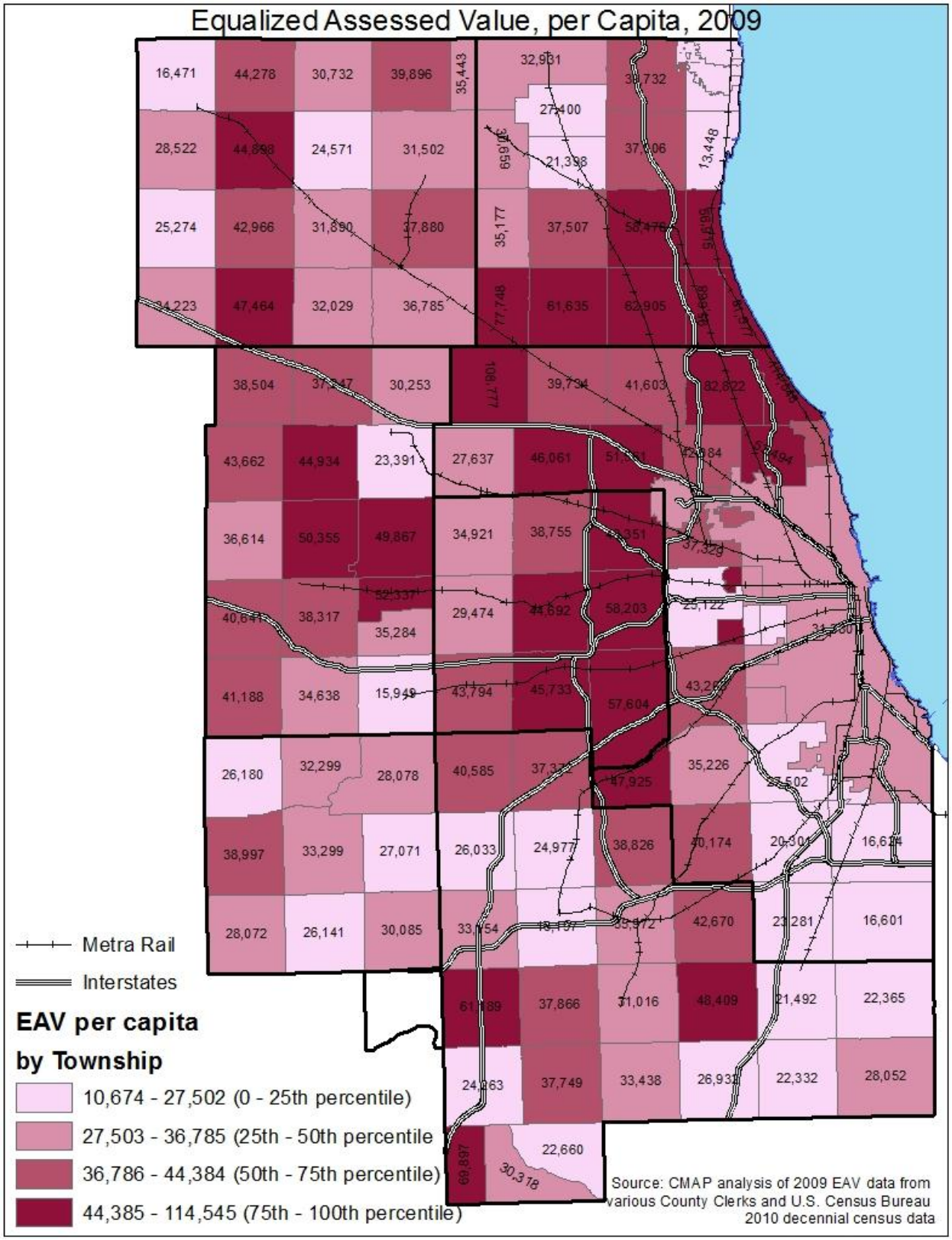
Each county clerk calculates the tax base for each taxing district located within the county using the EAV minus any exemptions. The tax base also includes the value of railroad property and pollution control facilities that had been assessed by the IDOR. Taxing districts submit property tax levy requests to the County Clerk. Tax levies are requested for specific purposes, or funds, such as the corporate fund, bond funds, retirement, police, or library. The County Clerk determines a property tax rate for each fund that will generate the revenues necessary to meet the levy request. This rate is subject to adjustments based on rate limits and extension caps.

Certain units of government must limit rates extended for specific purposes to maximum rates set forth in various state statutes. For example, non-home rule municipalities are limited to a 0.4375 percent rate for their corporate funds, while forest preserve districts are limited to a 0.06 percent rate for their corporate funds. However, many taxing districts' property tax rates do not come close to meeting the maximum statutory rate. One reason may be the property tax extension limitations required by the Property Tax Extension Limitation Law (PTELL).[59] PTELL limits property tax extensions for most non-home rule governments in the region, including municipalities, townships, and school districts. Growth in property tax extensions is limited to 5 percent or the increase in the Consumer Price Index, whichever is less. New properties are exempt from the limit.

The relationship between property tax extensions and tax bases results in rate differentials throughout the region. Relatively high property valuations typically allow local governments to maintain lower property tax rates than those with smaller tax bases. On a per capita basis, the property tax base in townships across northeastern Illinois varies widely-- from $10,674 EAV per capita to $114,545 EAV per capita. This has a direct impact on the quantity and quality of local government services provided to residents and businesses.

Variations in property tax base affect units of government differently in terms of ability to generate the revenues necessary to provide public services. A unit of government that primarily relies on the property tax base to generate revenues would be negatively affected by a low property tax base more than a unit of government that derived the majority of their revenues from other sources. Some units of government, such as counties and municipalities, generate revenues from a variety of sources while many special districts and townships generate nearly all of their revenues through the property tax. The following map illustrates EAV per capita in 2009, by township.

[58] See Appendix B and C for information on studies regarding exemptions.
[59] 35 ILCS 200/18-185 through 35 ILCS 200/18-245


Equalized Assessed Value, per Capita, 2009
Metra Rail
Interstates
EAV per capita
by Township
10,674 - 27,502 (0 - 25th percentile)
27,503 - 36,785 (25th - 50th percentile
36,786 - 44,384 (50th - 75th percentile)
44,385 - 114,545 (75th - 100th percentile)
Source: CMAP analysis of 2009 EAV data from various County Clerks and U.S. Census Bureau 2010 decennial census data

The composite rate extended to each taxpayer depends on the set of taxing districts that encompass the property. As a result, two properties located in the same municipality may be extended different levy rates. Composite tax rates include the sum of any rates extended by the county, township, municipality, school district, and special districts. Composite tax rates in the region also vary widely, from less than 4 percent of EAV in Oak Brook, to 20.6 percent in south suburban Ford Heights. The following map illustrates composite property tax rates levied for a typical or average taxpayer in each municipality in the region. The rates included on the map are inclusive of rates levied by counties, municipalities, school districts, and special districts, but exclude rates levied by Special Service Areas. Where available, the rate paid by most taxpayers in a municipality is shown. Otherwise, the rate shown is the unweighted-average of the composite rates of each tax code located in the municipality.

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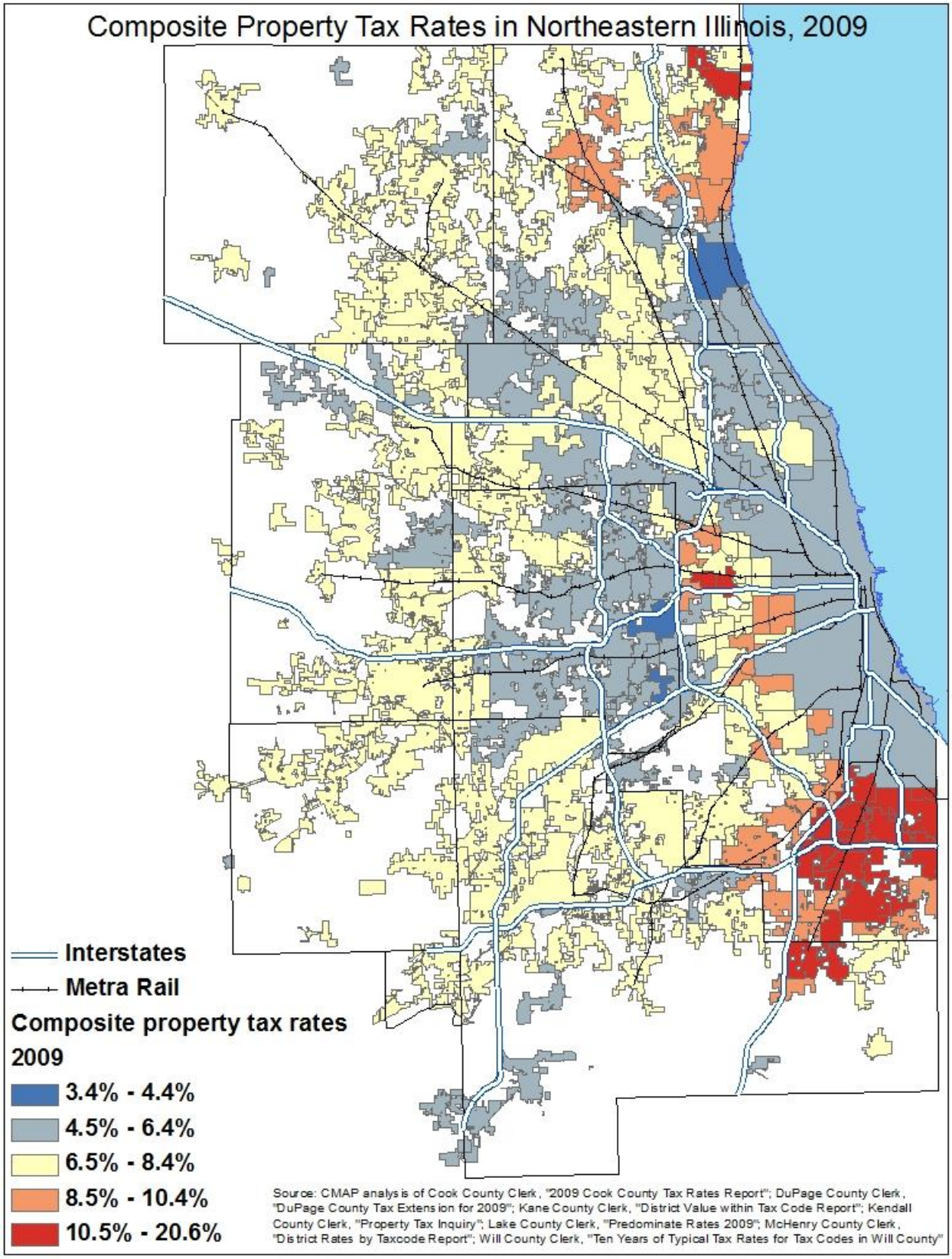
Composite Property Tax Rates in Northeastern Illinois, 2009
Interstates
Metra Rail
Composite property tax rates
2009
3.4% - 4.4%
4.5% - 6.4%
6.5% - 8.4%
8.5% - 10.4%
10.5% - 20.6%
Source: CMAP analysis of Cook County Clerk, "2009 Cook County Tax Rates Report"; DuPage County Clerk, "DuPage County Tax Extension for 2009"; Kane County Clerk, "District Value within Tax Code Report"; Kendall County Clerk, "Property Tax Inquiry"; Lake County Clerk, "Predominate Rates 2009"; McHenry County Clerk, "District Rates by Taxcode Report"; Will County Clerk, "Ten Years of Typical Tax Rates for Tax Codes in Will County"

Property Tax Extension Limitation Law

The Property Tax Extension Limitation Law (PTELL)[60] was first enacted in 1991 for taxing districts in DuPage, Kane, Lake, McHenry, and Will counties. The law was proposed in response to concerns about how fast growth in collar county property values was affecting property tax bills. Taxing districts in Cook County were added to the statute for the 1994 assessment year. In 1996, the statute was amended to authorize the remaining counties 96 counties in Illinois to hold a referendum on whether to implement PTELL. Between 1996 and 2003, 42 counties have held referendums. These referendums passed in 33 of the counties, including Kendall County. No referendums have been held since 2003.

The statute requires that non-home rule taxing districts in PTELL counties limit the annual increase in property tax extensions to the lesser of five percent or the increase in the Consumer Price Index for all urban consumers. The law allows increases above this amount to account for new properties added to the tax rolls. Most taxing districts in PTELL counties are subject to the limitation because most taxing districts do not have home rule authority. Some municipalities and Cook County have home rule authority. School districts, townships, and special districts do not have home rule powers.

The following simple example shows how PTELL affects a taxing district's extension for a unit (K-12) school district with less than 500,000 residents that levies a property tax for educational purposes.

A	Equalized Assessed Value of all property	$100,000,000
B	Equalized Assessed Value of new property only	$1,000,000
C	Levy request	$4,500,000
D	Rate (C/A)	4.5000%
E	Maximum statutory rate	4.0000%
F	Extension (prior to PTELL) (E * A)	$4,000,000
G	Prior year extension	$3,750,000
H	CPI	2%
I	PTELL extension on base property (G + (G * H))	$3,825,000
J	**Limiting rate (I/(A-B))**	**3.8636%**
K	PTELL extension on new property (J * B)	$38,636
L	**Total extension (I + K)**	**$3,863,636**

In the example, Equalized Assessed Value (EAV) totals $100 million, with $1 million being new property, which includes the EAV added by new improvements to a parcel of land or additions to existing improvements. The school district is requesting a $4,500,000 property tax levy for its education fund. Such a tax levy would result in a tax rate of 4.5 percent. However, most types of units of government are subject to longstanding state statutes that dictate the maximum property tax rates that can be levied for each fund type. For the education fund of a unit school district with less than 500,000 residents, state statute does not allow more than a 4.0 percent tax rate.[61] Under the maximum rate, the extension would have been $4,000,000.

[60] 35 ILCS 200/18-185 through 35 ILCS 200/18-245

[61] 105 ILCS 5/17-3

For a school district in a non-PTELL county, this would be the final rate and extension. However, in a PTELL county, the growth in the extension from the prior year is constrained. In the example, the prior year extension totaled $3,750,000. The Consumer Price Index was 2 percent, which is less than 5 percent. Thus, the extension, excluding new property, cannot grow by more than 2 percent. To determine the final rate, or the limiting rate, the prior year extension increased by 2 percent is divided by the EAV, minus new property. The final rate equals 3.8636 percent. This rate is applied to the total EAV, including new property, to get a final property tax extension of $3,863,636. This extension is 3.4 percent lower than the extension would have been without PTELL.

Statutory maximum property tax rates had long been the method limiting a taxing district's ability to generate property tax revenues.[62] However, in PTELL counties, the slower growth in property tax extensions relative to EAV has meant that maximum rates are not usually a factor in limiting property taxes. In the example, the extension would be limited to $3,863,636 regardless of the maximum rate.

Taxing districts under PTELL have a number of means to generate property tax revenue beyond what is authorized under PTELL. Funds used to pay off bonds approved by referendum are excluded from PTELL. In addition, taxing districts may hold a referendum asking for approval of a higher tax rate than what would be allowed under PTELL. The new rate approved is imposed for the number of years approved by voters, up to four years. Alternatively, a taxing district can hold a referendum on allowing a higher extension growth rate than the growth allowed under PTELL. Lastly, for counties that are subject to PTELL through the approval of a referendum, PTELL may be rescinded via referendum.

Assessment Classification

Cook County assesses commercial and industrial property at a higher percentage of market value than residential property. On the whole, this results in a higher property tax burden for business taxpayers, although the magnitude of the impact varies from place to place. This classification system does not exist in the collar counties, where businesses and residents with similar property market values typically share similar tax burdens.

Overview of Classification

State statute requires that properties be assessed at 33 1/3% of their market value,[63] except in counties allowed to apply property classification. The Illinois State Constitution of 1970 authorized counties with more than 200,000 residents to apply different assessment ratios depending on the type of property, as long as highest class does not exceed 2.5 times the level of assessment of the lowest class.[64] Counties that would like to apply property classification must enact an ordinance.[65] These provisions allowed Cook County to enact an ordinance to legally classify property for assessment purposes, a practice it had been employing for many years prior to its legal authorization. Currently, Cook County is the only county in the State that has enacted an ordinance providing for property classification.

The classes as well as the levels of assessment for each class have changed since the first ordinance was enacted in 1974. The most recent amendment reduced levels to 10 percent for residential property and

[62] See http://tax.illinois.gov/localgovernment/Propertytax/NewMaxRates.pdf for a compilation of statutory maximum rates.
[63] 35 ILCS 200/9-145
[64] Illinois State Constitution, Article IX, Section 4
[65] 35 ILCS 200/9-150

25 percent for commercial and industrial property beginning with the 2009 tax year.[66] For multi-family residential properties, this change was phased in between 2009 and 2011. In addition to general residential, commercial, and industrial categories, classification includes various incentive classes that reduce the level of assessment on certain properties for a period of years. The following chart provides a recent history of classes and assessment levels.

Cook County Assessment Classifications

Class	Description	2008	2009	2010	2011
1	Vacant	22%	10%		
2	Farm, single family or residential building with 6 units or fewer	16%	10%		
3	All other multi-family residential property	20%	16%	13%	10%
4	Not-for-profit	30%	25%		
5a	Commercial	38%	25%		
5b	Industrial	36%	25%		
6b	Industrial development incentive 1st 10 years and for any subsequent 10-year renewal periods Year 11 Year 12	 16% 23% 30%	 10% 15% 20%		
C	Industrial or commercial incentive for brownfield redevelopment	1st 10 years: 16% Year 11: 23% Year 12: 30%	1st 10 years: 10% Year 11: 15% Year 12: 20%		
7a/7b	Commercial incentive for development				
8	Commercial or industrial incentive for development in areas in communities in need of revitalization 1st 10 years and for any subsequent 10-year renewal periods Year 11 Year 12	 16% 23% 30%	 10% 15% 20%		
9	Multifamily incentive for new or redeveloped buildings with 35% of units leased at rents affordable to low- or moderate-income persons or households. Incentive for 10-year period and renewable upon application for additional 10-year periods.	16%	10%		
S	Multifamily incentive for Section 8 contract renewal. Incentive is for the term of the contract under the mark up to market option and for any additional terms of renewal.	16%	10%		
L	Landmark incentive				

[66] Cook County Ordinance Number 08-O-51

	1st 10 years and for any subsequent 10 year renewal periods (commercial properties are not renewable)	16%	10%
	Year 11	23%	15%
	Year 12	30%	20%
Source: Cook County Ordinances Sec. 74-63 and 74-64; Cook County Assessor			

Effect on Property Tax Rates

Due to classification, Cook County property taxpayers pay a different effective tax rate depending on the class of property. While property tax rates are calculated as the tax levy divided by the Equalized Assessed Value (EAV), *effective* tax rates refer to the property tax extension as a percent of *market value*. Examining property taxes through a property's actual market value rather than the EAV allows for analysis across property classes and analyzes tax rates and extensions from the perspective of the taxpayer. Assuming "all else equal" in terms of local tax levy and market value, and assuming no other exemptions or deductions, a taxpayer with commercial or industrial property in Cook County pays more than they would in a county without classification. Meanwhile, a taxpayer with residential property in Cook County pays less than they would in a county without classification.

The following maps illustrate effective composite property tax rates levied for a typical or average taxpayer in each municipality in the region. The rates included on the map are inclusive of rates levied by counties, municipalities, school districts, and special districts, but exclude rates levied by special service areas. Where available, the rate paid by most taxpayers in a municipality is shown. Otherwise, the rate shown is the unweighted-average of the composite rates of each tax code located in the municipality.

The map providing rates for residential property shows effective rates below 4 percent across most of the region. Rates above 4 percent are primarily in southern Cook County. In the maps showing commercial and industrial property rates, effective rates remain the same in the collar counties (primarily under 4 percent) because they do not employ classification. However, for the majority of Cook County, commercial and industrial properties rates are more than 4 percent. Many of the areas of Cook County with residential effective rates above 4 percent show effective rates for commercial and industrial of more than 8 percent. At the same time, effective tax rates for commercial and industrial properties in the collar counties are all less than 8 percent.

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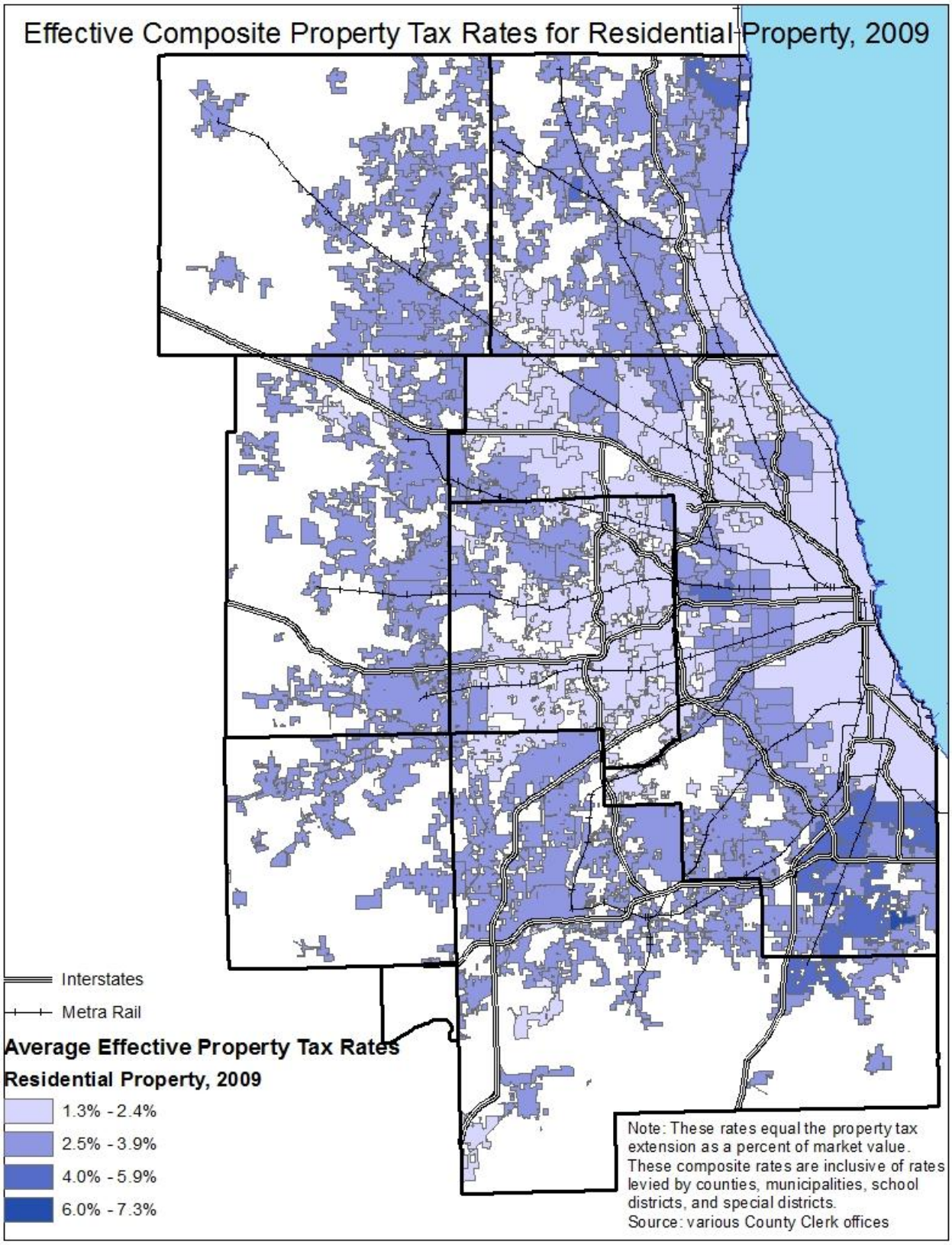
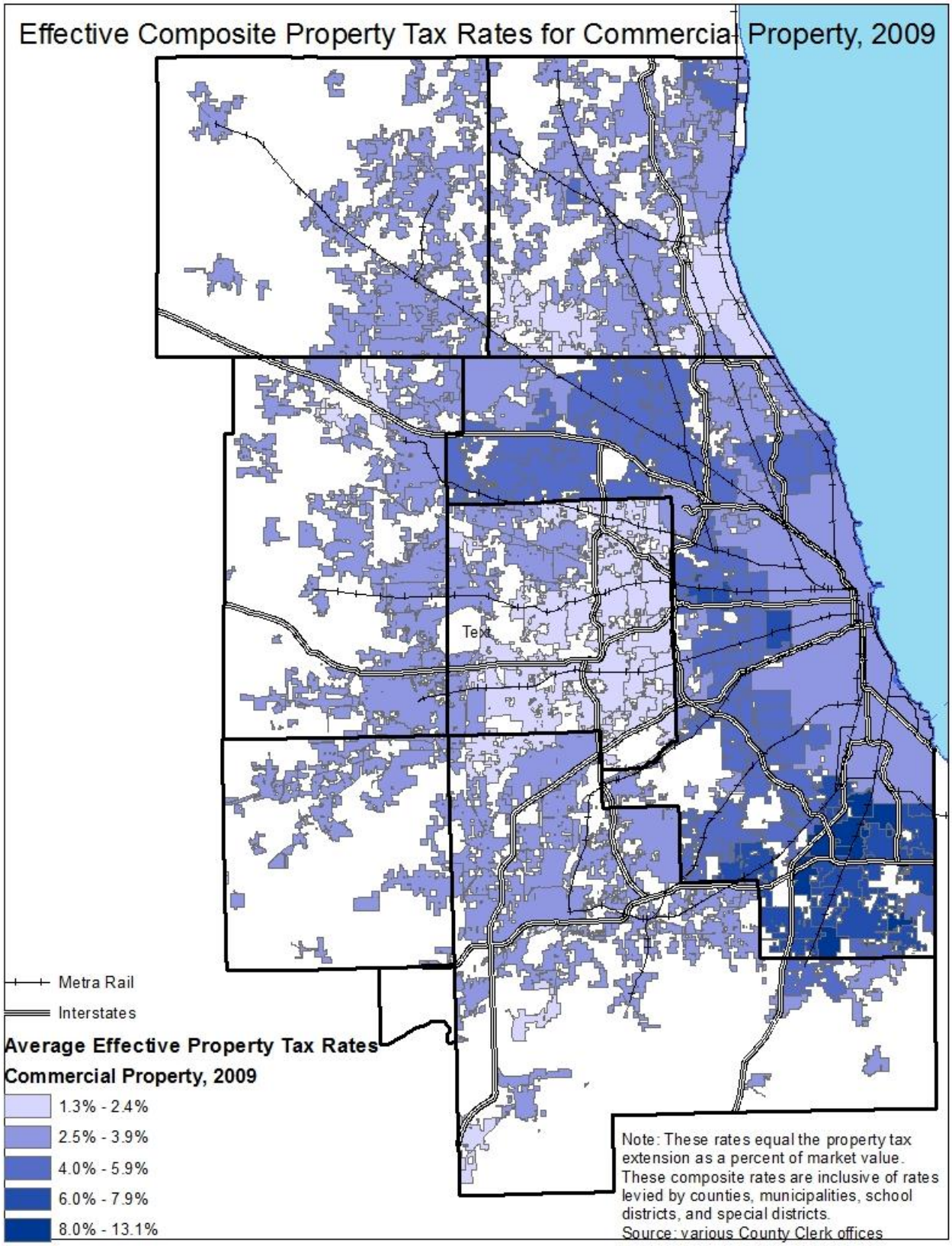
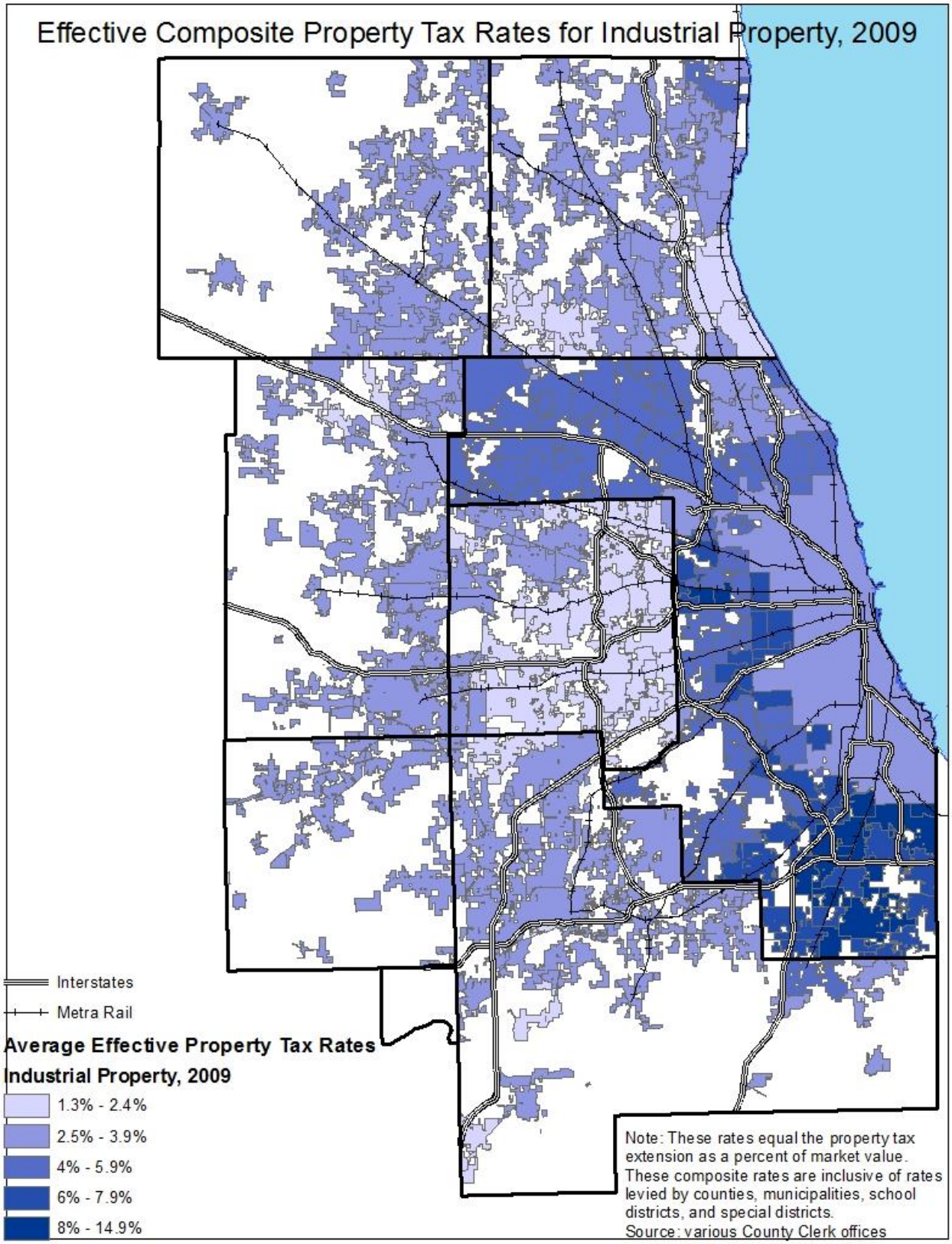

Effective Composite Property Tax Rates for Residential Property, 2009
Interstates
Metra Rail
Average Effective Property Tax Rates
Residential Property, 2009
1.3% - 2.4%
2.5% - 3.9%
4.0% - 5.9%
6.0% - 7.3%
Note: These rates equal the property tax extension as a percent of market value. These composite rates are inclusive of rates levied by counties, municipalities, school districts, and special districts.
Source: various County Clerk offices


Effective Composite Property Tax Rates for Commercial Property, 2009
Text
Metra Rail
Interstates
Average Effective Property Tax Rates
Commercial Property, 2009
1.3% - 2.4%
2.5% - 3.9%
4.0% - 5.9%
6.0% - 7.9%
8.0% - 13.1%
Note: These rates equal the property tax extension as a percent of market value. These composite rates are inclusive of rates levied by counties, municipalities, school districts, and special districts.
Source: various County Clerk offices


Effective Composite Property Tax Rates for Industrial Property, 2009
Interstates
Metra Rail
Average Effective Property Tax Rates
Industrial Property, 2009
1.3% - 2.4%
2.5% - 3.9%
4% - 5.9%
6% - 7.9%
8% - 14.9%
Note: These rates equal the property tax extension as a percent of market value. These composite rates are inclusive of rates levied by counties, municipalities, school districts, and special districts.
Source: various County Clerk offices

Under classification, effective tax rates for all classes rise as the proportion of commercial and industrial property in a taxing district declines. The extent to which a taxpayer pays more or less under classification in a particular taxing district depends on whether a particular class of property dominates the property values in that taxing district. The following chart shows how the effect of Cook County's classification system on tax rates is dependent on the makeup of the taxing district.

Row	Hypothetical Taxing Districts in Cook County	1 (primarily residential)	2 (50/50)	3 (primarily commercial/ industrial)
A	Property Tax Levy (what is requested by taxing districts for service provision)	$1,000,000	$1,000,000	$1,000,000
B	Total Market Value of Taxable Properties	$100,000,000	$100,000,000	$100,000,000
B_1	Residential portion	$90,000,000	$50,000,000	$10,000,000
B_2	Commercial/Industrial portion	$10,000,000	$50,000,000	$90,000,000
C	Assessed Value (assuming 2009 levels of assessment)	$11,500,000	$17,500,000	$23,500,000
C_1	Residential portion (10% of B_1)	$9,000,000	$5,000,000	$1,000,000
C_2	Comm/Ind portion (25% of B_2)	$2,500,000	$12,500,000	$22,500,000
D	Equalized Assessed Value (assuming equalization factor=3)	$34,500,000	$52,500,000	$70,500,000
D_1	Residential portion (C_1 x 3)	$27,000,000	$15,000,000	$3,000,000
D_2	Comm/Ind portion (C_2 x 3)	$7,500,000	$37,500,000	$67,500,000
E	Rate (A/D)	2.9%	1.9%	1.4%
F	Extension			
F_1	Residential (E x D_1)	$782,609	$285,714	$42,553
F_2	Commercial/Industrial (E x D_2)	$217,391	$714,286	$957,447
G	Effective Rates			
G_1	Residential (F_1/ B_1)	0.9%	0.6%	0.4%
G_2	Commercial/Industrial (F_2/ B_2)	2.2%	1.4%	1.1%
Rate and Extension assuming no classification (as if taxing districts were not in Cook County)				
H	Effective Rate with no classification (A/B)	1.0%	1.0%	1.0%
I	Extension with no classification			
I_1	Residential (H x B_1)	$900,000	$500,000	$100,000
I_2	Commercial/Industrial (H x B_2)	$100,000	$500,000	$900,000

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Taxing district 1 is primarily residential. As a result, eliminating classification would increase the effective tax rate for residential from 0.9 percent to just 1 percent, because the effect of reducing the tax burden for commercial/industrial is spread out among the large residential tax base. Moreover, because commercial/industrial makes up a small portion of the tax base, the overall extension increase for the residential portion of the tax base is smaller.

The reduction in tax burden for commercial/industrial gets smaller and the increase in tax burden for residential gets larger when classification is eliminated for taxing district 2. Since half of the market value in taxing district 2 is commercial/industrial, reducing the effective tax rate means that a larger proportion of the overall $1 million tax levy is shifted from commercial/industrial to residential than in taxing district 1. As a result, the residential rate in taxing district 2 also increases more than in taxing district 1 - from 0.6 percent to 1 percent. Also, the rate for commercial/industrial decreases less in taxing district 2 (2.2 percent to 1 percent) than in taxing district 1 (1.4 percent to 1 percent).

In taxing district 3, most of the market value consists of commercial/industrial property. As a result, these taxpayers were already paying most of the tax levy, thus eliminating classification does not have as large of an impact on the effective rate for commercial/industrial – from 1.1 percent to 1 percent. Because of the predominance of commercial/industrial property with a higher level of assessment, the residential effective tax rate was lower than the other taxing districts under classification – 0.4 percent. Thus, eliminating classification increases the residential rate more than in the other taxing districts.

In general, Cook County's classification system results in higher tax rates for commercial/industrial property taxpayers and lower tax rates for residential taxpayers than if all properties were assessed at the same level. However, these examples show that the impact of eliminating classification on effective tax rates varies by community. In some communities, especially where there is a large amount of commercial/industrial property, effective property tax rates for commercial/industrial property are primarily functions of the tax levy and base and not of classification's differential levels of assessment. In these same communities, low residential rates are a function of classification because the concentration of commercial/industrial property, which is assessed at a higher level, shoulders much of the tax burden. Therefore, eliminating classification would increase the residential tax burden in these communities more than in communities with relatively less commercial/industrial property.

The reverse is also true – communities with low concentrations of commercial/industrial property have effective tax rates for commercial/industrial property that may have resulted from classification and effective tax rates for residential that are primarily attributable to the actual tax levy. As a result, eliminating classification in these communities would not have as large of an impact on the residential tax burden or effective rates. The following maps illustrate how classification affects property tax rates in Cook County communities. The map on the left shows the extent that industrial tax rates are affected by classification and the map on the right shows the extent that residential property taxpayers would see an increase in property taxes without classification.

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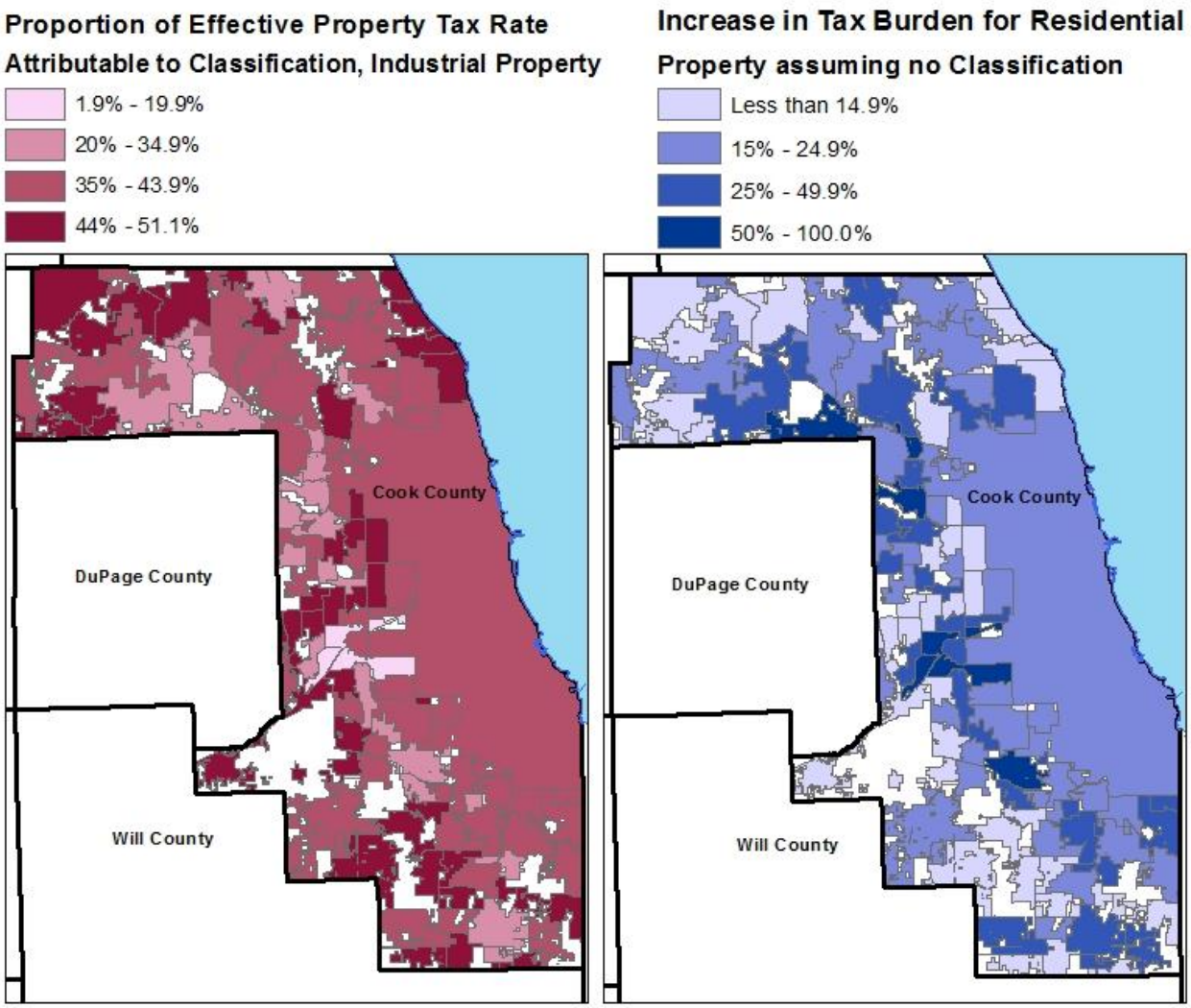
Effects of Property Tax Classification in Cook County, by Municipality



Implications for Economic Development

As shown in the tax rate maps earlier in this report, many Cook County communities have higher effective tax rates for commercial/industrial property taxpayers than communities in the collar counties. These higher rates are partially attributable to classification. In general, taxation, including property tax rates, affects economic development. Other factors both unrelated and related to taxation, such as the provision of government services and infrastructure, play a role in business location decisions. However, tax differences appear to have a larger impact on business activity within metropolitan regions rather than across them.[67] Businesses that can move relatively cheaply within a metropolitan region may do so in order to take advantage of lower tax rates. Given this, business development in Cook County may be affected by the classification system to the extent that it results in a greater tax burden for businesses.

[67] Wasylenko, Michael, "Taxation and Economic Development: The State of the Economic Literature," New England Economic Review, March/April 1997.

There has not been conclusive empirical evidence that classification, which has been done in some form since the 1920s in Cook County,[68] has affected economic development.[69] However, while engaged in local planning efforts, CMAP staff has interacted with community officials that believe economic development in their communities have been negatively affected by classification. Many businesses find that locating in areas with high property taxes would be a risk without adequate financial returns. In addition, many communities have used the classification system as an opportunity to pursue Cook County businesses to relocate to collar county communities.

Development in northeastern Illinois has expanded outward into the collar counties. As a result, the property tax base grew faster in Kane, Kendall, and Will counties than in Cook County between 1999 and 2009. However, EAV growth throughout the region varied considerably, with EAV in some communities within the same county growing faster than their neighbors. In addition, several collar county communities on the Cook County border have experienced higher EAV growth than neighboring Cook County areas. The following map illustrates EAV growth rates for northeastern Illinois by township.

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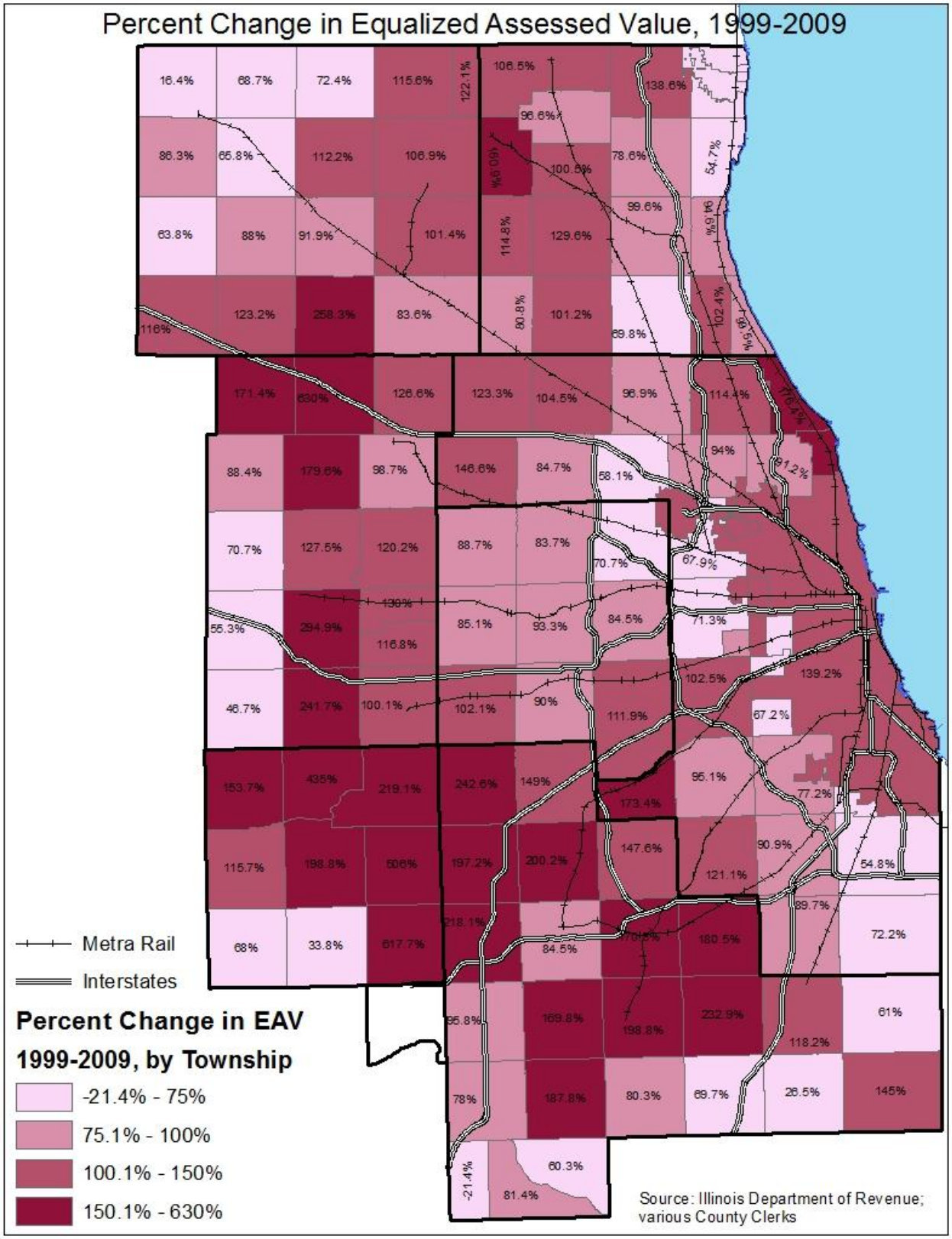
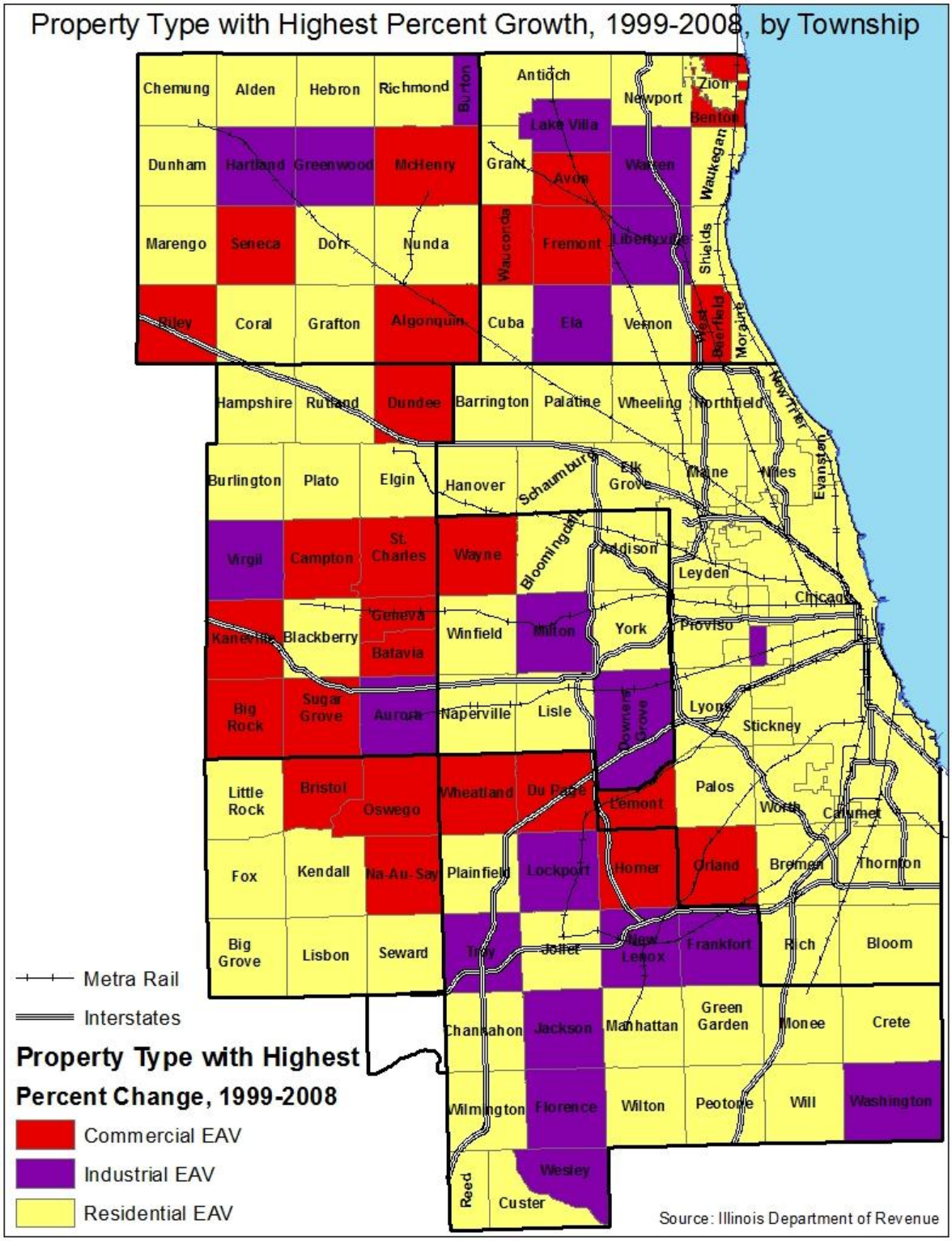
[68] The Civic Federation. "The Cook County Property Assessment Process." April 2010.
[69] Dye, Richard F., Therese J. McGuire, and David F. Merriman. "The Impact of Property Taxes and Property Tax Classification on Business Activity in the Chicago Metropolitan Area." Lincoln Institute of Land Policy. 1999.


Percent Change in Equalized Assessed Value, 1999-2009
Metra Rail
Interstates
Percent Change in EAV
1999-2009, by Township
-21.4% - 75%
75.1% - 100%
100.1% - 150%
150.1% - 630%
Source: Illinois Department of Revenue; various County Clerks

The property tax base may be growing at faster rates in certain areas for several reasons. Population growth in suburban and exurban areas may have resulted in increases in residential property values. In addition, business and economic activity may have accelerated in these areas. The following map illustrates which property class exhibited the largest growth in each township between 1999 and 2008.



The townships that have experienced the highest percentage growth in commercial or industrial EAV are primarily located in the collar counties. Just three out of the 46 townships that experienced more commercial or industrial EAV growth than residential EAV growth were in Cook County.

In addition, it appears that higher commercial and industrial property tax rates in Cook County may have driven down commercial rental rates. In an analysis of several pairs of border communities,[70] rental rates in Cook County communities have been lower on average over the past 15 years than rental rates on the other side of the Cook County border. This phenomenon may be the market correcting for higher property tax rates. However, this means that property developers may receive lower rents from lessees in Cook County. This may discourage property development or redevelopment in Cook County. In addition, this likely results in lower commercial and industrial property values in Cook County. Lower property values mean that the property tax base is also lower. Given a particular tax levy, a smaller tax base translates to higher property tax rates. To the extent that higher tax rates for commercial and industrial properties and lower rental rates may affect business location or property development decisions, Cook County may be at a disadvantage for future development.

Cook County has 55,512 acres of land that are either vacant parcels or underutilized commercial and industrial properties.[71] These parcels provide the opportunity to redevelop within existing communities rather than develop in areas where infrastructure is not already available. Higher property tax rates in Cook County, where there are significant opportunities for infill development, may be an obstacle for future sustainable development in the region. Eliminating classification would lower property tax rates in many communities with available infill and may make these parcels more attractive for development.

While sustaining and expanding economic development is dependent on a variety of factors, tax rates matter. Currently, and in the future, businesses in high tax rate areas may choose to locate in northeastern Illinois but outside of Cook County communities with high tax rates to reduce their tax burden. Eliminating the classification system would put a greater tax burden on residential property owners. However, keeping a system that may result in relatively low growth in the property tax base would put a greater tax burden on both residents and businesses.

[70] Buffalo Grove and Wheeling, Burr Ridge, Elmhurst and Northlake.
[71] CMAP, "Infill Regional Snapshot," March 2008, http://www.cmap.illinois.gov/documents/20583/b5a220e4-a7fe-4909-8cde-bb922883b2a9.