Taxpayer Advocates Win in November

by Sandra Fabry

During this past election cycle, taxpayers gained significant ground as tax hikes were defeated in referenda and more legislators committed themselves to refrain from imposing new taxes.

After the 2002 election, 1,171 state legislators had signed the Taxpayer Protection Pledge, developed in 1986 by Americans for Tax Reform. The pledge is a commitment to “oppose and vote against any and all efforts to increase taxes.” As of December 6, 2004, taxpayers’ interests in the next year were to be represented by 1,245 state Pledge signers, a net increase of more than 6 percent.

**Significant Gains Made**

The increase in pledge signings indicates state legislators are paying close attention to what their constituents want from them: firm commitments, accountability, and no new taxes. A closer look at the 2004 state elections, where the picture initially looked slightly more mixed, shows taxpayers overall can expect a continuation of the previous positive trend.

At the federal level, about 60 million taxpayers (the most votes ever for a candidate for president) gave President George W. Bush a clear mandate for his tax-cutting policies, and Congress will be significantly more taxpayer-friendly. A total of 221 U.S. Representatives and 46 U.S. Senators have signed the Pledge.

**Daschle Ousted**

The biggest congressional victory for taxpayers was the unseating of long-time U.S. Sen. Tom Daschle (D-SD), who had been Senate Minority Leader. Here, the race boiled down to the issue of taxation.

Daschle’s voting record looked dismal from a taxpayer’s perspective. In 2000, Daschle voted against eliminating the corporate income tax.

**GAINS p. 10**

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Congress Lauds Spending Control, Critics Decry Pork Spending

by Steve Stanek

Federal funding for tens of thousands of programs and projects, ranging from road and bridge construction to the study of mariachi music, was contained in a $388 billion omnibus spending bill that overwhelmingly passed both houses of Congress November 20.

Members of Congress praised the bill for holding down spending, but critics say the bill contains thousands of question-

**CONTROL p. 4**

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Outgoing Utah Governor Calls for Tax Reform

by Mike Jerman

Utah would expand its individual income tax and sales tax bases, reduce tax rates, and shift taxes from production to final consumption under a proposal submitted November 22 by outgoing Gov. Olene Walker (R).

Walker’s recommendations are based on the efforts of a group of tax experts she called together one year ago. She promised taxpayers her reform would be revenue-neutral.

**UTAH p. 14**

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Wireless Phone Costs Drop, but Taxes Skyrocket

by Steve Stanek

Taxes on wireless telephone service in the United States have climbed nine times faster than those on general business since January 2003, putting a damper on the growing use of wireless communications, according to Jim Schuler, director of policy at the Cellular Telecommunications & Internet Association (CTIA).

**WIRELESS p. 19**
Isn’t it time you joined a think tank?

The Heartland Institute is a national nonprofit organization devoted to informing elected officials and the public on important public policy issues. It publishes Budget & Tax News, as well as monthly newspapers on taxes, health care, and school reform and other publications addressing a wide range of topics.

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ACCOUNT NUMBER
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This is your share – $24,510.40.

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* Source: Bureau of the Public Debt, U.S. Department of the Treasury

www.heartland.org
Study Shows Big Savings from Competitive Sourcing of Government Functions

by Sean Parnell

A recently released study shows competitive sourcing of government activities has led to significant savings for the federal government. Using baseline costs, the average savings to the federal government was 44 percent over 10 years, for a total savings of $11.2 billion. The report found only 5 percent, or about 3,300, lost their jobs. The total number of government positions reduced was 44 percent lower than its price from the previous year. That was $100,000 a year that GPO could have saved taxpayers any time it chose, but it never chose to do so until it was forced to compete.

Few Jobs Lost

Opposition to competitive sourcing has come primarily from government employees concerned about major job losses, and some department managers concenred about losing control of the work. The research, however, showed those fears to be unfounded.

Of the approximately 68,000 civilian employees at the Department of Defense who faced competitive sourcing, the report found only 5 percent, or about 3,300, lost their jobs. The total number of government positions reduced through competitive sourcing, approximately 25,000, was achieved largely through retirements and transfers into other, vacant positions.

The study also found government employees were able to compete effectively with private contractors when their positions were put up for competitive bidding. Over the 10-year period, private contractors won 56 percent of the competitions, while government employees won the remaining 44 percent.

In recent years, government employees involved in competitive sourcing have become more efficient, according to the report, and have been winning an increasing number of bids. In 2003, government employees were winning nearly two-thirds of all competitively sourced jobs.

Opposition Remains Firm

Regardless of the research results, however, government employee unions and their members remain firmly opposed to competitive sourcing. Carlus Ellerbe, a member of the American Federation of Government Employees, who faced competitive sourcing in his Department of Labor printing shop, voiced his displeasure to Federal Computer Week.

"Regardless of whether the government continues to perform the service or a private company takes over, cost savings are achieved" through competitive sourcing, and "free market forces [in government services] are a catalyst for cost reduction."

Sean Parnell (parnell@heartland.org) is vice president of The Heartland Institute.
able expenditures totaling billions of dollars. Among their complaints: $350,000 for the Rock and Roll Hall of Fame in Cleveland, $75,000 for the Paper Industry International Hall of Fame in Appleton, Wisconsin, and $25,000 to the Clark County, Nevada, school district to study mariachi music.

The omnibus spending bill deals only with nonmilitary discretionary spending, which accounts for about one-seventh of the total amount of federal spending, estimated at $2.3 trillion for fiscal year 2005. The bill funds fiscal year 2005 appropriations bills covering the Departments of Agriculture, Commerce, Education, Health and Human Services, Housing and Urban Development, Interior, Justice, Labor, State, Transportation, Treasury, and Veterans Affairs, as well as numerous agencies and foreign aid. Congress already had approved spending bills for the military, homeland security, and the District of Columbia.

Bill "Held the Line"

"I'm very proud of the fact that we held the line and made Congress make choices and set priorities, because it follows our philosophy," said House Majority Leader Tom Delay (R-TX) during debate on the bill. The $388 billion price tag is about 2 percent more than last fiscal year's. Excluding foreign aid, total spending in the omnibus bill is up about 1 percent, well below the rate of discretionary spending increases the past three years: 10.3 percent in 2002, 9.7 percent in 2003, and 8.3 percent in 2004. The 2004 budget deficit of $415 billion prompted calls to slow spending growth.

Though passed in November, the bill actually funds programs for the budget year that began October 1. The November 2 elections were a factor in the delay, as members of Congress tried to avoid votes that could have been used against them in the days leading up to the election. Congress ordinarily would have approved nine separate spending bills, but instead rolled them into the omnibus bill.

In addition to approving the spending, lawmakers also approved a provision for an $800 billion increase in the government's borrowing limit.

Entitlement Programs Untouched

The omnibus spending bill does not deal with Social Security, Medicare, farm subsidies, or other nondiscretionary "entitlement" programs, which automatically provide government money to beneficiaries. Entitlement spending alone will total about $822 billion in 2005, more than one-third of all federal spending.

Congression already had approved spending bills for the military, homeland security, and the District of Columbia.

"If Congress is truly tightening its belt, then why was it necessary to increase the debt ceiling by $800 billion? There is little purpose to a debt 'ceiling' that can be arbitrarily raised to accommodate the congressional appetite for pork. The boasting over this bill shows that Congress is a long way from passing a truly balanced budget."

TOM SCHATZ, PRESIDENT CITIZENS AGAINST GOVERNMENT WASTE

Congress Not Interested in Real Tax Reform

by Terry Savage

It's tops on the president's agenda, and a very good idea: tax reform. Americans spend an estimated $183 billion every year just to comply with our horrendously complicated federal income tax code.

What's the best way to reform the tax system? There are two leading contenders. Each promises it will replace the current level of tax revenue we need in order to keep our promises to defend our country, pay interest on the national debt, and try to keep Social Security and Medicare solvent. And each promises a greater degree of fairness and transparency, along with a far lower cost of compliance.

The first method is the national sales tax. Let's just get rid of the income tax. And while we're at it, let's get rid of the Internal Revenue Service. The idea is so pleasing that you might be tempted to accept it at face value.

Think again.

"It's tops on the president's agenda, and a very good idea: tax reform."

National Sales Tax

Anational sales tax would definitely eliminate the IRS, along with income taxes and withholding and the annual agony of filing a tax return. In its place, Americans would pay a national sales tax on every purchase of goods and services. It's estimated that a tax of about 20 to 25 percent would be "revenue neutral." That means the new taxes raised would equal the old taxes that would be abolished. And you'd still pay state and local sales taxes.

Proponents call this the "fair tax," because it would apply to all spending. Additionally, recognizing that poor people spend a greater proportion of their income on basic necessities, this plan would send every family an advance rebate that would be equal to spending up to the federal poverty level. That is, a family of four would be able to spend $24,240 annually tax free. They would receive a rebate of $485 every month, or a total of $5,785 annually to offset taxes they pay on their purchases.

How could Americans afford to pay this extra tax? The "fair tax" people at http://www.fairtax.org say the solution is simple. First, people would have more spending money because they don't pay income tax. Secondly, they assume that prices of everything will be lower, with the IRS currently built into prices for goods and services.

That's quite an assumption. But I have a different disagreement with the "fair-
The Flat Tax

Here’s an alternative. Take a postcard and write down how much you earned this year. Then multiply by 20 percent. That’s your tax. Send in the postcard, and use your computer to send your tax payment to the government. Lower-income families would have one simple exemption. Enough money would be collected to make up for our current complicated tax system, and huge costs would be eliminated.

There would be no deductions—not even for mortgage interest or charitable gifts or profits on the sale of your home. No special rates for capital gains or dividends. No more complicated IRA deduction and withdrawal rules, or corporate investment tax credits.

I can hear the squealing now from all the special interests. But isn’t it tempting? No more accountants, no more tax preparers, no more agonizing over the tax implications of simple business decisions.

Flat-taxers predict the economy would double our current growth rate—if we spent less. And that’s The Flat Tax. The power to dole out favoritism in government taxes and spending. A simple tax code would eliminate half that power. And that’s The Savage Truth.

Congressman John Peterson (R-PA), left, and groundhog Punxsutawney Phil, above, defended $200,000 in pork to Phil’s hometown.

The Punxsutawney Weather Discovery Center is a unique museum that presents the history, science, technology, and folklore of weather in an interactive setting that is not only educational for young people, but fun for the whole family. This one-of-a-kind museum will help promote tourism in a beautiful, historic region of the country that has been struggling economically.

As for Punxsutawney Phil, he is best known for emerging from his hole on February 2, Groundhog Day, to look for his shadow. If he sees it, there will be six more weeks of winter. If there is no shadow, spring will soon arrive. In addition to being a skilled weather prognosticator, Phil is also a great burrower of holes in the ground.

“CAGW is disappointed that Phil allowed himself to be used by supporters of the Punxsutawney Weather Discovery Center to burrow holes in taxpayers’ wallets. We hope this does not permanently tarnish the lovable image of meteorological ambassadorship that he has worked so hard to polish.”

By Tom Finnigan

Congressman and groundhog of shadow fame defend weather museum grant

Penn. Congressman and Punxsutawney Phil Named Co-Porkers of the Month

Congressman and groundhog of shadow fame defend weather museum grant

by Tom Finnigan

The nonpartisan, taxpayer-advocacy organization Citizens Against Government Waste (CAGW) named Congressman John Peterson (R-PA) and Pennsylvania’s most famous groundhog, Punxsutawney Phil, as the December Co-Porkers of the Month, for jointly defending a $100,000 federal grant for the Punxsutawney Weather Discovery Center.

After CAGW singled out the project as one of the prime examples of pork in the 2005 omnibus spending bill, Punxsutawney Phil allowed himself to be stirred from his winter slumber and taken to Capitol Hill, where he appeared alongside Peterson and Barry Myers, CEO of the private weather-forecasting firm AccuWeather, in a joint press conference to defend the grant.

Peterson inserted the budget earmark as an Economic Development Initiative (EDI) grant in the Community Development section of the fiscal 2005 Veterans Affairs/Housing and Urban Development Appropriations Act. The project was not requested in the president’s budget, was not the subject of hearings, and appeared only in the House version of the omnibus bill, therefore qualifying as pork under CAGW’s longstanding criteria.

Peterson issued a statement that said, “The Punxsutawney Weather Discovery Center is a unique museum that presents the history, science, technology, and folklore of weather in an interactive setting that is not only educational for young people, but fun for the whole family. This one-of-a-kind museum will help promote tourism in a beautiful, historic region of the country that has been struggling economically.”

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“CAGW is disappointed that Phil allowed himself to be used by supporters of the Punxsutawney Weather Discovery Center to burrow holes in taxpayers’ wallets, said CAGW President Tom Schatz. “We hope this does not permanently tarnish the lovable image of meteorological ambassadorship that he has worked so hard to polish.”

Tom Schatz, President, Citizens Against Government Waste

Myers’ defense of the grant is more serious, of course, but also more troubling, said Schatz, because Myers claims the National Weather Service duplicates work done by the private sector. AccuWeather is the nation’s largest private weather-forecasting operation, part of a $1 billion industry. Schatz said that if Myers thinks so highly of the Punxsutawney Weather Center, he should put up more of his own money for the project, instead of reaching for tax dollars confiscated from other peoples’ paychecks.

The Punxsutawney Weather Center is like hundreds of museums throughout the country that manage to succeed without federal funding, Schatz said.

“Hundreds of poor communities throughout the United States will be taxed to turn Punxsutawney, Pennsylvania, into the ‘Weather Capital of the World,’ simply because its congressman was able to curry favor with the right committee,” said Schatz.

For defending questionable priorities in a time of war, record deficits, and debt; circumventing the budget process; and grabbing $100,000 in federal funding for a pet project, CAGW named Congressman John Peterson and Punxsutawney Phil the December Co-Porkers of the Month.

Tom Finnigan (media@cagw.org) works in media relations for Citizens Against Government Waste.
Massachusetts Lawmakers Eye “New” Cash

Voters’ earlier call for tax cuts ignored

By Frank Conte

After three years of mediocre economic performance and poor job growth in Massachusetts, various economists are projecting the state’s tax revenues will increase significantly in 2005, as the state’s economy improves with the rest of the nation.

The higher tax receipts, however, are likely to lead to greater spending rather than rate cuts, recent budget actions and statements by state legislators suggest.

The Beacon Hill Institute at Suffolk University (BHI) noted the expected revenue increases in fiscal year 2005 and 2006 forecasts it delivered to the Massachusetts legislature’s Joint House and Ways Committee and the Executive Office of Administration and Finance in early December.

“Our Massachusetts lags the national economy, we see strong growth in state tax revenue through the rest of fiscal 2005,” BHI Executive Director David G. Tuerck told the committee.

Strong Economy to Continue

The BHI forecasts anticipate continued strength in the Massachusetts economy. The institute’s forecasts for FY 2005 and 2006 included the following:


For FY 2006 (ending June 30, 2006): $17.555 billion of revenue, for growth of 4.4 percent over the predicted level for FY 2005.

Other observers have made similar estimates. The Massachusetts Taxpayers Foundation, a business-backed research organization, pegged FY 2005 revenues at $16.6 billion. The state’s Executive Office of Administration and Finance estimates FY 2005 revenues will be $16.2 billion.

“The [Beacon Hill Institute] forecasts anticipate continued strength in the Massachusetts economy.”

Pressure for Spending Increases

Republican Governor Mitt Romney will present his budget in January. Although the state has seen strong growth in tax revenues, it remains unclear whether Romney can ignore calls for higher spending and instead hold the line on taxes.

Massachusetts Governor Mitt Romney (center) will present his budget in January. Although the state has seen strong growth in tax revenues, it remains unclear whether Romney can ignore calls for higher spending and instead hold the line on taxes.

By Frank Conte (fconte@beaconhill.org)

is director of communications and information systems at the Beacon Hill Institute at Suffolk University.
Kansas Survives Year Without a Statewide Tax Increase

by Karl Peterjohn

For the first time since 1998, Kansas legislators in 2004 declined to enact a statewide tax hike, one of several reasons 2004 could be considered a historic year for Kansas taxpayers.

That achievement may prove to be short-lived, however, as the Kansas Supreme Court’s school finance decision has yet to be announced. That decision, which will determine whether the aggregate funding provided for public elementary and secondary education is “suitable” under the Kansas Constitution, is likely to shape the proposals and issues taking center stage for 2005 at the statehouse.

High-Taxers Lost Support
Governor Kathleen Sebelius, a Democrat, was a major loser at the ballot box twice in 2004. In November the Democratic minority in the legislature shrank from 55 seats to 52 seats in the Kansas House and Senate.

Sebelius nearly lost three more Senate allies, as three of the Senate races won by Democrats were decided by fewer than 700 votes. The overall Senate balance remains 30 Republicans and 10 Democrats.

Equally bad for the governor was the fate of Republicans who joined her in attempting to raise taxes and spending.

In August, GOP primary election voters defeated several pro-tax Republicans, including Bill Kassebaum, Cindy Neighbor, and even the Senate tax committee chairman, Dave Corbin. As a result of the August Republican primary and November general election, there will be more fiscal conservatives in the Kansas legislature in 2005 than in 2004.

Sales Tax Hike Defeated
In northeast Kansas and northwest Missouri, a proposal for a bi-state, one-quarter percent sales tax hike was defeated in four of the five counties where it appeared on the ballot, stopping it from being enacted anywhere in the bi-state area. The proposal would have applied in Kansas and Missouri counties surrounding Kansas City, to fund renovations of Arrowhead and Kauffman stadiums for the Chiefs and Royals (the city’s professional football and baseball teams), as well as for “cultural” projects.

Although many such tax hikes were defeated, the “carrot-and-stick” approach to raising local sales taxes worked in several Kansas communities.

“In northeast Kansas and northwest Missouri, a proposal for a bi-state, one-quarter percent sales tax hike was defeated in four of the five counties where it appeared on the ballot ...”

The carrot approach of promising property tax relief if the voters would approve a 1 cent local sales tax worked in Pottawatomie County. The tax increase raised the total rate to 6.3 percent effective January 1, 2005.

In an advisory vote in Sedgwick County, the stick was used successfully by tax hike proponents who threatened voters that if they rejected a temporary two-and-a-half year county sales tax hike, the only alternative would be a 20-year property tax hike. A 52 percent majority voted for this increase in the local sales tax, from 6.3 percent (which included a 1 percent county tax) to 7.3 percent. The legislature will have to act to give Sedgwick County the authority to hike its portion of the tax from 1 to 2 percent.

Governor Planning Tax Hikes
Sebelius is being mentioned as a possible national candidate for the Democrats in 2008. In the meantime, she has decided to work toward raising excise taxes on tobacco in addition to her previous requests for higher property, income, and sales taxes. The governor’s push for higher taxes before the Kansas Supreme Court rules on school funding, however, is out of step with the fiscal conservatism projected by a sizable majority of Kansans in the 2004 election.

Karl Peterjohn (kpeterjohn@prodigy.net) is executive director of the Kansas Taxpayers Network.
Pennsylvania Lawmakers Eroding Liberty, Study Finds

by Grant Gulibon

Pennsylvania lawmakers have repeatedly voted in ways that restrict personal and economic liberty, according to a recently released study by the Commonwealth Foundation, a free-market public policy research and educational institute based in Harrisburg, Pennsylvania.


“Rep. Daryl Metcalfe was the top scorer in the General Assembly, and he barely exceeded 50 ... on a 100-point scale. More members, as well as [Gov. Edward] Rendell, had scores of F (111) than the total number of A, B, and C grades (89).”

MATTHEW BROUILLETTE, PRESIDENT COMMONWEALTH FOUNDATION

The Liberty Index evaluates Pennsylvania legislators and Gov. Ed Rendell based on the answer to this question: “Does this Act expand or contract the liberty of the people of Pennsylvania?”

“Unlike most special interest groups that focus only on a handful of laws on selected issues, our analysis considers every single bill that became an Act and every single bill that became a law, earned a Liberty Grade of F- (with an average Liberty Index score of 25.4085).”

As a whole, the General Assembly’s average Liberty Grade was a D (with an average Liberty Index score of 28.4466) and a median Liberty Grade of D-. (with a Liberty Index score of 25.1696). On a party basis, the Republicans scored higher than the Democrats, with an average Liberty Grade of C (with an average Liberty Index score of 23.9408). The Democrats earned an average Liberty Grade of F+ (with an average Liberty Index score of 32.9308). On a caucus-by-caucus basis, the House Republicans had the highest average Liberty Grade, a C (with an average Liberty Index score of 23.9408), while the Senate Democrats had the lowest average Liberty Grade, an F- (with an average Liberty Index score of 20.5464).
Economic Freedom Greatest in Middle America, Study Says

New York, California may be worst places to start a business

by Lawrence J. McQuillan, Robert E. McCormick, and Ying Huang

If you want to start a business but are not sure where to set up shop, should you head for a vibrant megalopolis like New York City? A nucleus of brainpower and venture capital like Silicon Valley? Or a city of flamboyant creativity like Miami?

Actually, whether you’re writing software or whipping up candy bars, chances are you would be better off in Kansas, according to The U.S. Economic Freedom Index: 2004 Report, published by the Pacific Research Institute and Forbes magazine. The report says Kansas is the state with the greatest level of economic freedom in the country, as measured by tax rates, business regulation, the behavior of the courts, and how the government spends its money.

Gauged by these factors, Colorado has the second-greatest level of economic freedom in the country, followed by Virginia, Idaho, and Utah. The states with the least economic freedom, by contrast, are two we often think of as hubs of commerce: California and New York, 49th and 50th respectively.

This means that if you try to bootstrap your fledgling firm in Kansas or Colorado, you will have a serious competitive edge over someone trying to do the same in New York.

Taxes, Regulation Are Key
What should budding capitalists consider when assessing how free they will be to pursue their business dream? Low taxes are an obvious start.

The regulatory environment is also key. Professional licensing requirements, land-use restrictions, and mandated payments to workers’ compensation or insurance funds are just some of the rules that can hamstring businesses trying to get off the ground.

For instance, it’s no surprise California ranks 49th in economic freedom when you consider it makes by far the most onerous workers’ compensation demands in the country. Business owners in the Golden State must pay Sacramento about $6.37 for every $100 of payroll, according to the National Federation of Independent Business. The national average is $2.68.

A third factor in measuring economic freedom is the court system. While citizens must be able to redress grievances in court, in states like Connecticut—48th in economic freedom—civil court awards have gotten out of hand, according to the report, going beyond redressing wrongs to imposing massive punitive damages. States that have introduced legal improvements, like reforming tort law or capping damages, are better places to do business, the report finds.

“While California and New York may be the best places to find fame, fortune is an entirely different matter.”

Wealth Transfers Hurt Economy
Aspiring entrepreneurs should also look at how the state government spends its money. A big public sector is a red flag. If a state has a high number of government workers per citizen, that means not only that it has more tax-funded salaries to pay, but also that it probably has more of a propensity to regulate. Government employees, after all, must have something to do. What better way to stay busy than to create and manage new rules?

Aspirants to the Qwest Communications, which has revenues of $18 billion a year.

New business owners have a lot on their agenda. They must research their markets, fund their ventures, and fine-tune their products, just for a start. Nevertheless, they might want to add another item to their to-do lists: move.

The fortunes created by every one of these companies are in the top 25 of this year’s Forbes 400 “richest Americas” list. They illustrate that while California and New York may be the best places to find fame, fortune is an entirely different matter.

Hence, we shouldn’t be surprised if the next super-company is spawned in Kansas, or in Virginia, home of America Online, or in Colorado, home of five-year-old Qwest Communications, which has revenues of $18 billion a year.

New business owners have a lot on their agenda. They must research their markets, fund their ventures, and fine-tune their products, just for a start. Nevertheless, they might want to add another item to their to-do lists: move.

Lawrence J. McQuillan, Robert E. McCormick, and Ying Huang are the authors of The U.S. Economic Freedom Index: 2004 Report, published by the Pacific Research Institute and Forbes magazine. The authors can be reached at lmaclellan@pacificresearch.org.

INTERNET INFO

Warren Buffett established his first hedge fund in Omaha, Nebraska. Michael Dell started his computer company in Austin, Texas.

Budget & Tax News is free for elected officials. Others may subscribe for $36 for 10 issues!
Gains
Continued from page 1

controlling the marriage penalty, against repealing the death tax, and against tax cuts in the budget resolution. His opponent, former South Dakota Congressman John Thune (R), who represented the state’s only congressional district, voted for tax cuts on all these issues.

Karen Kerrigan, president and CEO of the Small Business and Entrepreneurship Council in Washington, DC, said, “Continuity in political leadership—both in the White House and on Capitol Hill, means our small business and entrepreneurial sector can expect more positive gains on the tax relief and reform front. With respect to future cash flow planning and business investment, small firms now have certainty that tax relief measures signed by President Bush—lower marginal tax rates, increased business expensing, and capital gains [tax rate] reduction, for example—will not be rolled back. In fact, making these tax relief items permanent, including death tax repeal, now has a much greater shot at passage.”

State-Level Victories
At the state level, pro-taxpayer candidates defeated tax hikers at the ballot box in both primary and general elections in several states.

In South Carolina, incumbent pledge signers Henry Brown (R-1) won with 88 percent, Joe Wilson (R-2) won with 65 percent, and Gresham Barrett (R-3) ran unopposed. In the only House race in South Carolina without an incumbent, signer Bob Inglis (R) won Jim DeMint’s seat with 70 percent of the vote.

Perhaps the biggest victory for taxpayers in South Carolina came in the Senate race, where former Congressman Jim DeMint (R) defeated the state’s powerful education superintendent, Inez Tenenbaum (D). Tax reform was arguably the biggest issue in the race, and DeMint won by a convincing 54-44 vote.

Kansas Pro-Taxpayer Success
In Kansas, several steadfast pro-taxpayer legislators who had helped defeat an increase in income, sales, and property taxes in 2004 won reelection. Not only did tax-hikers and like-minded new candidates suffer defeat in the primaries, but the trend continued in the general election, where the following races stood out:

- In Senate District 26, incumbent Sen. Phillip Journey (R), a pledge signer, was challenged by Rep. Daniel Thimesch (D), who had broken the Pledge by voting for income, sales, and property tax increases this year. Journey defeated Thimesch 58 to 42 percent.
- In House District 13, Pledge-signer Forrest Knox (R) defeated his primary election opponent, State Rep. Mary Compton (R), a Pledge signer who had broken her promise by voting for several tax increases over the past few years. She lost the primary election to Knox and challenged him again in the general election, only to lose again and decisively: 68 to 32 percent.
- Former State Rep. Peggy Palmer (R), a Pledge signer with a record of opposing tax increases, had defeated her primary election opponent, State Senate Finance Committee Chairman Dave Corbin (R), who had backed several tax hikes. Palmer then defeated her gener-

“[S]mall firms now have certainty that tax relief measures signed by President Bush—lower marginal tax rates, increased business expensing, and capital gains [tax rate] reduction, for example—will not be rolled back.”
KAREN KERRIGAN, PRESIDENT AND CEO
SMALL BUSINESS AND ENTREPRENEURSHIP COUNCIL

Jim DeMint

Gresham Barrett

Diane Black

JoAnn Graves

Arnold Schwarzenegger

lawyer and big-labor supporter who had voted for an increase in the sales tax.

Similarly, State Rep. Diane Black (R) ousted State Sen. JoAnn Graves (D), the Senate’s Speaker Pro Tem. Graves had voted for an increase in the state’s sales tax. Additionally, several Republican legislators who had supported creation of a state income tax chose to retire rather than seek re-election. All have been replaced by determined anti-taxers. Steve Gill, a radio talk show host and prominent figure in the fight against instituting an income tax in the state, wrote in his weekly column on www.gillreport.com, “Although the income tax itself was not on the ballot this year, Ten-

nessee voters made it clear they are fed up with high taxes. Wheel tax referendums across the state gave voters a chance to speak directly on the issue of higher taxes. Wheel tax referendums across the state gave voters a chance to speak directly on the issue of higher taxes. Wheel tax referendums across the state gave voters a chance to speak directly on the issue of higher taxes.
Georgia Anti-Taxers Carry Day

In 2003, shortly after having been elected the first Republican governor of Georgia since Reconstruction, Governor Sonny Perdue proposed a program of tax increases. At least two of those who supported the governor in that effort saw their careers end in the November elections.

In the 14th House District, newcomer and Pledge-signer Barry Loudermilk (R) defeated incumbent State Rep. Buddy Childers (D), who had signed the Pledge but then broke it by voting for a $180 million tax increase in 2003.

Pledge-breaking State Sen. Joey Brush (R), who also had voted for the $180 million hike, was defeated in the primary election by Pledge-signer Jim Whitehead (R). Several other Pledge breakers who voted for the increase in 2003 decided not to run for re-election.

State Sen. Mike D. Crotts (R), who supported higher taxes, failed to win the Republican nomination for Congress in the 8th District.

A total of 62 Pledge signers will be representing taxpayers’ interests in the upcoming legislative session in Georgia.

With the Republicans taking control of the Georgia House of Representatives for the first time in over 130 years, a Republican-controlled [State] Senate, and a Republican governor, we have an unprecedented opportunity to advance a conservative agenda,” said Loudermilk. “I plan on focusing my efforts to protect the rights of the individual and to reduce the size of government and its ever-extending reach into the lives and pocketbooks of our citizens.”

STATE REP. BARRY LOUDERMILK
R-GEORGIA 14

Utah, Washington Reject Hikes

Utah voters defeated Initiative 1, which would have raised the state sales tax by $195 million over 13 years and increased state debt by $150 million. Washington voters resoundingly rejected Initiative 884, which would have made the state’s sales tax the highest in the nation.

“However, taxpayers suffered a significant loss in New Hampshire, where Governor Craig Benson (R), a Pledge signer, was defeated by challenger John Lynch (D). Lynch has refused to sign the Pledge and has already indicated he may raise taxes. Although Republicans generally tend to be more fiscally conservative, some losses for the Republican Party did not necessarily mean a big loss for taxpayers, as in Colorado, Illinois, Minnesota, and Vermont.

A closer look at the Minnesota election, for example, reveals that those who stayed true to their opposition to higher taxes won. The Taxpayers League of Minnesota points to the following races:

- In 2003, shortly after having been elected the first Republican governor of Minnesota, the clearest case was the race between Rebecca Otto (D) and Matt Dean (R) in House District 52B. Despite the heavy campaigning of former Governor Arne Carlson and Finance Commissioner John Gueyous—both Pledge-breaking State Senator Mike D. Crotts (R) of Wash-ington (who, while still in a dead heat with Democratic opponent Christine Gregoire, is expected to win the recount) and Pledge-signer Barry Loudermilk (R) —ran as strong, fiscally conservative Republicans aligned with Governor Pawlenty,” said David Strum, president of the Taxpayers League of Minnesota. “Running as a fiscally conservative was a winning message, while running away from the Pawlenty message of fiscal responsibility more often than not led to defeat.”

Other States Less Promising

In other states, where the situation may look less promising from a macro-perspective, taxpayer advocates saw some encouraging trends at the local level. According to Dowd Muska of the Yankee Institute in Connecticut, where pro-tax Democrats won a veto-proof majority in the Senate and approached a veto-proof majority in the House, “Taxpayers face good news at the local level. There are now 49 local taxpayer groups fighting to keep Connecticut municipalities’ property taxes, which are some of the highest in the nation, from rising even higher. And in 2004, for the first time ever, more than half of the tax-hiking town budgets that went to referendum were defeated.”

Grover Norquist, president of Americans for Tax Reform, said, “Taxpayers are more critical these days. They constitute an informed electorate, a critical mass who want to see a clear message. Where the tax message is watered down and party lines become blurry as a candidate tries to get comfortable in the ‘middle,’ taxpayers tend to favor the other party’s candidate, as we have seen in the case of Minnesota.”

He added, “In the long run, these election results will serve as a reminder for fiscal conservatives to not abandon the route of fiscal sanity, and to stay on message with regard to ‘no new taxes.’”

Sandra Fabry (sfabry@atr.org) is an associate with Americans for Tax Reform.
by Richard W. Rahn

On November 18, in a speech given at the Finance Ministry in Vienna, Austria, the very highly regarded European economist and first woman president of the Mont Pelerin Society, Professor Victoria Curzon Price, called for eliminating the corporate income tax.

There, in the center socialist Europe, was not only the call to get rid of this destructive tax, but almost everyone in an audience of economists, various government finance officials, and public policy experts appeared to agree.

The idea and practice of the corporate income tax has been dying slowly for the last two decades. The corporate income tax is a highly destructive tax that greatly distorts proper decision making, taxes the same income more than once, is endlessly complex, and provides a declining share of tax revenue in most countries. For instance, in the United States, corporate income tax revenues fell from 4.2 percent of gross domestic product in 1967 to only 1.2 percent of GDP in 2003, though there was minimal change in the tax rate.

Good economists have long known the corporate income tax causes more problems than it solves. Many countries, seeking higher economic growth and employment, have sharply cut their tax rates. Ireland cut its corporate tax rate from 45 percent to only 12.5 percent, attracting investment from around the world and, in turn, becoming not only one of the fastest-growing but one of the wealthiest economies in Europe.

The new market economies of Eastern Europe—seeking high growth and rapid job creation—have also been cutting their corporate tax rates. Slovakia, Lithuania, and Poland have a 19 percent corporate rate; Hungary 16 percent; Slovenia and Latvia 15 percent; and Bulgaria just announced it will move to a 15 percent rate next year. Montenegro, not to be outdone, announced it will go to a 9 percent rate. Estonia has become the champion by going to a zero rate on reinvested profits.

As a result of this competition, even France (34 percent) and Germany (38 percent) have been forced into modest corporate tax reductions, giving them lower rates than corporations face in the United States. American companies now have an average 40 percent rate (including state corporate taxes), and only very poorly performing Japan with its 42 percent rate is higher.

Looking at these numbers, it is easy to understand why corporations doing business around the world elect not to have the United States as their legal home, because it makes them noncompetitive. When running for president, Sen. John Kerry (D-MA) proposed punishing companies for leaving the United States. The correct solution is for the U.S. to abolish the corporate income tax, thereby making it the most desired location on the planet for many companies to incorporate.

Those who oppose eliminating the corporate tax will say we cannot afford the revenue loss. They say such things because they do not think beyond the first order. Think about it for a minute. If you eliminate the corporate tax, corporate profits will increase, causing corporations to hire more workers and/or raise wages and invest more in new and better equipment, and/or increase their dividend payouts. All this will cause the price of corporate stock to rise and the government to receive more in capital gains tax revenues. The government will also receive more tax revenue from the increase in dividends paid and workers hired. If we look at the experience of other countries who have greatly reduced corporate tax rates, like Ireland, it is clear the additional growth in jobs and profits ended up providing the government more, not less, tax revenue.

The U.S. Treasury and Congress’s Joint Tax Committee use very simple-minded static revenue models when estimating proposed tax changes. That is why they almost always get it wrong. I have no doubt a properly constructed dynamic model or, better yet, an actual experiment of eliminating the corporate tax, will prove we are better off without it.

The corporate tax is enormously complex and hence extremely expensive to administer; tends to drive companies to set up operations outside the United States; discourages foreign investment in the U.S., thereby driving down the dollar’s value; taxes capital income more than once, thus reducing the U.S. saving rate, which also drives down the dollar’s value; and makes us less competitive. The corporate rate is also unfair to businesses that need a corporate form as opposed to a single proprietorship, partnership, limited liability company, and real estate investment trust (REIT), which are not burdened with the extra level of taxation.

The president has pledged fundamental tax reform. A first step ought to be eliminating the corporate income tax, because it will greatly simplify the tax code and its enforcement, make U.S. companies more competitive, strengthen the dollar, create many new jobs, and increase economic opportunity. There are still some, but fortunately a diminishing number of mentalistically lightweight leftists, who believe you somehow can tax a corporation without taxing the workers, customers, suppliers, and stockholders (who in many cases are invested in pension funds) of the corporation. When they make the cry, as they surely will, that eliminating the corporate income tax benefits the rich and rewards the greedy, they should be challenged with facts and logic.

Advocates of sound economic policy have too many times allowed themselves to be bullied by loudmouths who claim compassion, yet cause misery. Tax reform is too important to allow ignorance to prevail.

Richard W. Rahn is a senior fellow of the Discovery Institute and an adjunct scholar of the Cato Institute. This essay was first printed on December 1, 2004 by the Washington Times and is reprinted with permission.

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I believe in property rights. What do YOU believe in?

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By Steve Stanek

A state's right to regulate liquor sales and the federal government's right to regulate interstate commerce clashed on December 7 when the U.S. Supreme Court heard arguments over bans on direct-to-consumer sales of wine from out-of-state producers.

Twenty-four states ban out-of-state suppliers from shipping wine directly to consumers within their borders. Three lawsuits centered on the bans were argued before the justices: Granholm v. Heald, 03-1116; Michigan Beer & Wine Wholesalers Association v. Heald, 03-1120; and Swedenburg v. Kelly, 03-1274. The Court's decision is expected to arrive in the next few months.

21st Amendment vs. Commerce Clause

The 24 states argued that the 21st Amendment, which ended prohibition in 1933, gives them the power to control alcohol sales, including restrictions on the importation of liquors from out of state.

The plaintiffs challenged the restrictions by arguing that the Commerce Clause of the Constitution gives the federal government the right to regulate interstate commerce. The Commerce Clause has been interpreted to mean states may not discriminate against out-of-state businesses.

Attorneys general from 36 states have sent friend-of-the-court briefs asserting the right of states to control liquor sales. Associations representing wine producers, beer producers, and wine and spirits wholesalers are at odds over the issue, with the wine producers wanting the bans lifted and the beer producers and wholesalers wanting them left in place.

"California wineries, particularly small, family-run operations, should be able to ship their product directly to customers in all states," said K. Lloyd Billingsley, editorial director of the Pacific Research Institute and author of the new report Wine Wars: Defending E-Commerce and Direct Shipment in the National Wine Market, in a statement issued with the report.

"This clearly is an issue of protectionism, at odds with the Commerce Clause of the Constitution," Billingsley said. "The high court has an historic chance to end the legacy of Prohibition and rule in favor of direct shipping. It should not be a felony, as it is in some states, to buy a bottle of premium wine and ship it to your own home."

However, attorneys for Michigan Governor Jennifer Granholm (D), who defends Michigan's ban on out-of-state wine sales to residents, argued in their filing with the Supreme Court, "The historical basis for the [state] structure, as recognized by this court, is to protect against the collusion, price-fixing, and monopolization problems that existed before Prohibition."

The Michigan governor's attorneys also argued, "the recent proliferation of small-production wineries, whose sole marketing and sales agenda is direct shipment with sales made over the Internet, means that this area of regulation is increasingly important, both to the states from a police power perspective and to wineries and consumers."

Michigan requires out-of-state producers to sell alcohol only through licensed wholesalers or vendors.

Wine Reviewers Sue

Michigan residents Ray and Eleanor Heald, who write wine reviews, had brought the matter to a head when they asked a California winery for a sample bottle to review. The winery informed them that, because of Michigan law, the bottle could not be shipped.

The Healds then sued to overturn the ban. In 2003 the 6th U.S. Circuit Court of Appeals sided with the Healds, ruling the Commerce Clause of the Constitution makes Michigan's law unconstitutional.

New York Ban Challenged

Meanwhile, Juanita Swedenburg, who owns an independent winery in Virginia, wanted to sell her wine to customers outside her home state. She challenged the New York ban on direct sales from out-of-state wineries in 2000. A federal appeals court sided with the state of New York in 2004.

New York allows in-state wineries to ship their wines directly to New York customers. Lawyers for Swedenburg told the Supreme Court she should have the same right to make direct-to-consumer sales in New York as New York wineries have.

The Wine & Spirits Wholesalers of America, which supports state bans on direct-to-consumer sales from out-of-state wineries, estimates that at least $1 billion of liquor is illegally shipped to consumers each year.

The current distribution system prevents illegal trafficking, market manipulation, and access of alcohol to minors, according to an official statement by the organization. The statement also cites "efficient collection of applicable state and local excise taxes" as another reason the Supreme Court should rule in favor of the states.

"WSWA is committed to preserving the integrity of the state-based alcohol control system that has evolved under the 21st Amendment, and which is threatened by illegal direct shipping," the statement says.

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Utah
Continued from page 1

“We have a tax structure in Utah that hasn’t been significantly revised for more than three decades,” Walker said in announcing the recommendations. “Tax reform certainly wasn’t the politically correct thing to do, but it was the right thing to do for the future of the state. It was clear the time had come to take action and bring our tax system into the twenty-first century.”

Incoming Governor Mum on Plan
How far her recommendations will advance is anybody’s guess. Walker leaves office January 3, and incoming Gov. Jon Huntsman Jr. (R), who has said tax reform would be his top priority, has declined to comment on her proposal.

“Tax reform is critical to Utah,” Huntsman said in a statement. “As we work to revitalize the economy, we need to revamp our outdated tax codes and close the loopholes of the past.”

Walker said that because of a shifting economy the state’s overall net tax base is declining. Using the sales tax as an example, Walker said as the economy moves from goods-based to service-based, the state is taxing a smaller share of transactions. A similar problem exists with the income tax, she noted.

“To compound the problem, our school enrollment numbers are growing exponentially,” Walker said. “How will this increase be handled by our tax system if our numbers continue to climb and our tax base continues to decline?”

Prospects Remain Uncertain
Reaction to Walker’s plan has been mixed. Legislative leaders have voiced some concerns about the taxes on services. The Utah Taxpayers Association has not officially endorsed the entire package but has indicated the proposed reforms are worthy of debate and should be the basis for ongoing discussions of tax reform in the state.

“The governor’s new tax proposal does not make any adjustments to provide for the education funding of our children that she and so many others have identified that we need to do,” said State Rep. Steve Mascalzo (R-West Jordan) on the Utah Policymaker Weblog. “I am impressed with the breadth of the tax reform but extremely disappointed to see a lack of commitment to deal with the education funding issue that we continue to fall further behind on.”

However, former State Rep. Craig Call said on the same Weblog, “A flat tax, reform of redevelopment bonding and zoning for dollars, proper equalization of sales taxes between communities, and a broadening of the base to make the system fairer would all be very good moves and help avoid the ongoing negatives of the current structure.”

Public schools and colleges are guaranteed income tax revenues in the Utah Constitution. The proposal would make them more dependent on property and sales taxes because income tax rates would drop.

“We certainly would not want to give up what we have for the uncertainty” of another funding source, Gary Cameron, executive director of the Utah School Superintendents Association, told the Deseret Morning News. “Unless there is some provision to hold education absolutely harmless, of course ... (we’re) nervous.”

Tax Mix Would Change
The proposal would change Utah’s existing income tax system, which has six tax brackets and a current top marginal rate of 7 percent applied to taxable income above $8,626 for a married household. This system would be replaced by a flat tax of 4.9 percent based on federal taxable income.

Because this proposal would generate less revenue than the current state individual income tax, the statewide property tax levy for schools would have to be increased. Walker also has proposed a second option, of taxing federal adjusted gross income at 4.1 percent. At a 4.1 percent tax rate, taxpayers would not be allowed any deductions, including the popular deductions for mortgage interest and charitable contributions.

Both income tax proposals would preclude state-only deductions and credits, which could complicate efforts to allow tuition tax credits for private schools.

Walker also proposes reducing the state sales tax rate from 4.75 percent to 3.75 percent, while expanding the sales tax base to include professional services such as accounting, legal, and medical services. Utah already taxes several types of services, including repair of personal property that is not attached to real property, entertainment, transportation, and cleaning.

Expanding the tax base to include currently untaxed professional services would allow state and local sales tax rates to be reduced by 21 percent.

Would Eliminate Corporate Tax
The governor’s proposal also calls for eliminating the corporate income tax (CIT). Walker cited the volatility of CIT revenues as reason for eliminating the tax. CIT revenues peaked at nearly $190 million at the end of the 1990s’ economic boom and decreased to $119 million during the recent recession. Walker also noted the CIT is slowly being eroded by increased corporate tax sheltering and the increasing popularity of pass-through entities like limited liability corporations and S-corporations, whose incomes are taxed at the individual level.

As a “fallback” proposal, the governor recommends double-weighting the CIT sales factor, as most states already have done. Most states use a three-factor formula—sales, property, and payroll—to determine how much of a multistate corporation’s income should be taxed. Utah still uses an equally weighted formula. Double-weighting the sales factor would shift corporate income taxes from businesses that produce goods and services in Utah to businesses that import goods and services into Utah.

Under Walker’s proposal, the sales tax exemption for purchases of capital equipment currently enjoyed by manufacturers would be extended to all types of businesses. Equipment that can be capitalized under federal income tax law would be exempt from state and local sales taxes.

Exempting business inputs from sales taxes avoids the “pyramiding” effect of imposing taxes on taxes as goods proceed through the production process. Walker noted that taxing business inputs hides the true cost of government by embedding taxes in increased product costs, lower wages and benefits for employees, and reduced rates of return for shareholders. Exempting business inputs also reduces the cost of businesses to improve productivity and expand production.

Protecting School Funding
Walker also proposes allowing school districts to opt out of redevelopment agencies (RDAs). Cities typically use RDAs to offer property tax subsidies, more than half of which are diverted from school districts, to well-connected commercial real estate developers. City officials argue that retail development needs to be subsidized by taxpayers and that RDAs are excellent tools for repairing urban blight, even though such blight is not a serious problem in Utah.

Every year, nearly $40 million in property taxes are diverted from Utah school districts through RDAs, usually to subsidize retail developments, according to Walker’s office.

Mike Jerman (mike@utahtaxpayers.org) is vice president of the Utah Taxpayers Association.

“Tax reform certainly wasn’t the politically correct thing to do, but it was the right thing to do for the future of the state.”

OUTGOING GOVERNOR OLENE WALKER
R-UTAH

INTERNET INFO
Details of the governor’s proposal are contained in “Governor Olene Walker's Recommendations on a Tax Structure for Utah’s Future,” available online at http://www.utahtaxpayers.org/governor.
Chicago City Council overwhelmingly approved on December 15 a $5.08 billion budget for July 1. By a 47-3 vote, the council hiked taxes an estimated $74.6 million. Fees were hiked another $11.1 million.

The approval came despite loud complaints from people in many segments of Chicago’s economy, including hoteliers, restaurateurs, liquor store owners, industrial manufacturers, and retailers, all of whom were already paying the highest taxes and fees in the region.

After the vote, Chicago Mayor Richard Daley (D) warned the city council of more to come. “You think this is difficult? Wait till next year when you want a new school,” Daley said.

Region’s Highest Taxes, Rising Among the increases that passed are these:
- A one-quarter percent rise in the city portion of the retail sales tax, taking it from 8.75 to 9 percent, making it the second-highest sales tax in the United States and the highest among major U.S. cities, including New York and Los Angeles, according to the Chicagoland Chamber of Commerce.
- A tax of 10.25 percent on restaurant meals, up from 10 percent. The state restaurant association believes this is the highest restaurant tax in the nation.
- An increase in the city hotel tax, from 3 to 3.5 percent, giving Chicago a total tax of 15.4 percent, highest in the nation.
- A nearly quadruple increase in the tax on natural gas, from 1.4 cents per therm to 5.2 cents per therm.
- A 25-cent rise in the city’s parking tax, a 12.5 percent increase.
- An increase in the amusement tax from 3 percent to 4 percent on tickets for live performances at venues of at least 750 seats, and from 7 percent to 8 percent for all other amusements, such as professional sporting events. (Tickets at venues that seat fewer than 750 persons are not taxed.)
- A $1 fee for each newly purchased automobile tire.
- A tripling of the city’s cigarette tax, from 16 cents to 48 cents a pack.
- A liquor tax increase, from 30 to 37 cents per fifth-of-a-gallon bottle.

Adding to Chicago’s tax burden is the $1 fee for each newly purchased automobile tire.

Business Community Aghast After Daley announced his budget proposal on November 9, Donovan Pepper, a spokesman for the Illinois Restaurant Association, said, “There’s a 10 percent tax on restaurant meals in Chicago, and the mayor wants to make it 10 and one-quarter percent. Is that amazing or what? Chicago would probably be the highest there is.”

Gregg Durham, a spokesman for the Illinois Manufacturers Association, said Chicago has lost 130,000 manufacturing jobs in recent years. The huge increase in the natural gas tax will further hurt manufacturers in the city, he said.

“Anything that raises the cost of doing business will stifle job creation or encourage people to move out of the area,” Durham said.

Rob Nash, a spokesman for the Chicagoland Area Chamber of Commerce, said, “When you put these tax increases in context with state-level and county-level tax increases in recent years, to come back in a time of crisis and say we need $80 million more, mainly from the business community, is a tough thing to swallow.”

Alderman Pat O’Connor (D) defended the new budget, saying, “This is a good budget for a very bad time,” according to the Chicago Sun-Times.

Laurence Msall, president of the Civic Federation, a Chicago-based government research organization, also defended the budget, telling the Chicago Tribune, “What passed today was a no-property-tax-increase budget that made some important steps to address growing personnel costs.”

More than 80 percent of Chicago’s government costs are related to personnel. The budget includes privatization of some city jobs, such as janitorial work.

Adding to Chicago’s tax burden is the $1 fee for each newly purchased automobile tire.

Though he also supported the park district hikes, Msall told the Chicago Tribune the park district budget is “one of the least transparent budgets of any local government.”

Cook County, where Chicago is located, is also considering a tax hike to help close a $146 million budget gap.

Steve Stanek (stanek@heartland.org) is managing editor of Budget & Tax News.
Bill to Hike Income Tax, Lower Property Tax Stirs Debate

A strong push is underway in Illinois to radically change how taxes are collected and distributed in the state, mainly in response to complaints from educators upset by how public schools are funded.

Ralph Martire, executive director of the Center for Tax and Budget Accountability, an Illinois-based fiscal policy think tank, is a leading spokesperson for the effort.


Reform or Increase?
House Bill 750 would increase the state income tax from 3 to 5 percent and raise other taxes in exchange for a cut in property taxes. Critics say the bill is not revenue-neutral, but rather a tax increase that would send more money to public schools and state budget coffers.

"It’s really a tax policy bill," said Ben Schwarm, associate director of the Illinois Association of School Boards, in the Northwest Herald on November 23. He said the bill "would generate about $7.5 billion not earmarked for education.”

According to Family Taxpayers Network President Jack Roeber, HB 750 "is based on the false premise that the problems with the public school system can be solved with more money."

In a letter to the editor that appeared in the November 22 edition of the suburban Chicago Daily Herald newspaper, Naperville Unit District 203 Superintendent Alan Leis succinctly laid out the bill’s main points and the politics behind it:

- Raise the [personal] income tax to 5 percent [from a current flat 3 percent] on those with incomes above roughly $50,000;
- Eliminate the [personal] income tax exemption on retirement income above $75,000;
- Broaden the [state] sales tax to include services as well as [other] products;
- Increase the [state] corporate income tax by 8 percent [from 4.8 percent];
- Provide a 20 percent to 25 percent [local] property tax rebate.

Tax Cap Frustrates
"For those of us charged with running school systems, the tax cap on what schools receive and the lack of Illinois state education funding (compared to other states) is a constant source of frustration," Leis wrote.

He continued, "The philosophy behind HB 750 is that the only way to fix Illinois' structural deficit, provide additional educational funding to economically impoverished areas, and reduce what many feel is an over-reliance on the property tax for school funding is to do all of those things at once, in one bold move."

As the bill is being tweaked and hearings are being held, groups are lining up on both sides.

"Many education groups are supportive, although the District 203 school board, while encouraging additional debate, opposes the bill in its present form," noted Leis in his letter. "Business and taxpayer groups have voiced strong concerns since the bill is, after all, a tax increase. HB 750 helps education most, but it also devotes $2 billion to ameliorate the structural deficit. Both opponents and supporters note that, in reality, the increase in income tax revenue will come from the collar counties [that surround Chicago] with the bulk of that income then distributed statewide."

Intense Debate Expected
HB 750 appears to have laid the groundwork for debate over significant changes in Illinois tax structure in 2005.

In a recent press statement, State Senator Chris Lauzen (R-Aurora) said, "This legislation promises no improvement in student performance, yet will increase your personal income tax by 67 percent (from 3 percent of your annual income to 5 percent), increase the size of state government by $3 billion, increase your corporate tax by another $600 million, apply a new sales tax on many everyday services by $1 billion, etc. Proponents will put $2 billion into education, 'promise' $2 billion in property tax relief (neither permanent nor substantial), and hand over more than $2 billion to state politicians in general revenue funds to spend however we like."

State Sen. Dan Rutherford (R-Pontiac) told the Associated Press, "the proposal has fired up cash-starved school administrators and supporters note that, in reality, the income then distributed statewide." programs such as Medicaid. He also said the proposal does not include a cap on property tax rates, opening the possibility that property taxes would rise soon after the bill's passage."

"I don't think it has a prayer of passing as it is," Rutherford concluded.

State Sen. Pamela Althoff (R-Mchenry) told the Northwest Herald, "legislators have taken some of the concepts in House Bill 750 and hope to develop a separate bill that deals only with education, removing many other tax-policy issues."

Illinois Governor Rod Blagojevich (D), who was elected in 2002, campaigned on promises not to raise the state income tax or sales tax. He has not taken a public stance on HB 750.

Voters Soundly Defeat Local Property Tax Hikes

Evidence of antipathy toward higher property taxes in Illinois showed up in the November 2 general election when voters across the state rejected 38 of 49 public school district tax-hike referenda.

"Illinois voters rejected two of every three school funding referendums this election, sending administrators back to carve deeper into cash-starved budgets and renewing pleas for more money from Springfield," wrote Associated Press (AP) reporter Jan Dennis on November 5.

State’s Rates Relatively High
About half the property taxes collected in Illinois are used to fund public education. Illinois has one of the nation’s highest property tax burdens, ranking in the top 10 among all states, according to the Washington, DC-based Tax Foundation.

Illinois localities collected $14.45 billion in property taxes in fiscal year 2000, the latest year for which the Census Bureau has published state-by-state data, according to the Tax Foundation. That amounts to $1,166 per capita, or $37 for every $1,000 of personal income.

"Illinois’ local property taxes are 8th highest in the nation by the per-capita measure and 9th highest as a percent of income," says Tax Foundation President Scott Hodge.

Taxpayers Worried About Economy
"The economy [in Illinois] is still relatively shaky, and I think a lot of people are concerned about rising taxes when their own salaries aren’t going up or they’re unemployed,” Robert Bradley, a political science professor at Illinois State University, told AP’s Dennis.

According to Dennis’s report, Fieldcrest, Illinois School Superintendent Michael Stagliano believes “fed-up taxpayers helped sink his district’s bid for a 55-cent education tax increase, its second failed referendum in as many years.”

“What we hear from the man on the street is ‘We’re tired of the taxes, we can’t support any more,’” said Stagliano, whose 1,300-student district stretches through four counties in central Illinois.

Jim Toibin, president of National Taxpayers United of Illinois, told Dennis he "thinks voters are sending a signal that schools should cut costs instead of asking for more money.” He added, “They [pro-taxers] say it’s for the kids when it’s really for the greedy overpaid bureaucrats who provide a mediocre education.”

In a letter published by the Chicago Sun-Times on November 23, Toibin wrote, “Chicago residents deserve tax cuts, not tax increases that fund more wasteful and corrupt government practices.”
Grassroots Battle Brewing Against Illinois Tax Hike

Jim Peschke of Harvard, Illinois, co-founder of Citizens for Reasonable and Fair Taxes (CRAFT), began a full-court press last Fall with other taxpayers and member organizations to defeat the proposed state tax reform bill, HB 750.

According to Peschke, the bill is “a catastrophic piece of legislation for taxpayers, for families, and for those who seek true education reform.” Peschke testified against the bill at an Illinois Senate hearing in the Fall of 2004.

“No-strike” laws are part of the package in HB 750. Peschke said, “More than just a colossal tax hike, HB 750 promotes the status quo of ballooning spending, and minimal accountability. It would be difficult to design legislation more harmful to both taxpayers and public education than HB 750.”

Property Taxes Already High

Judy K. Cocks of Johnsburg, Illinois testified that Illinois residents and businesses already pay plenty of taxes to schools.

“From 1995 to 2003 the total funding, also known as taxes, for education in Illinois rose from $17 billion to $29 billion,” Cocks said. “That is a 70 percent increase. And what was the increase in student population during this time? It was only 7.3 percent,” she told legislators.

Cocks also told the Senate panel, “Illinois ranks 5th highest in the union for total dollars spent on education. Even Education Week states that Illinois spends above the national average (per capita) on education. According to the U.S. Census Bureau, Illinois has the 9th highest per-capita tax burden in the nation. We Illinoisans are not under-taxed nor under-spending for education.”

Chris Jenner, a resident of Cary, Illinois, also testified against HB 750.

“House Bill 750 has an inherent structural problem in that school spending is outpacing the bill’s foundation level increase index, which outpaces the cost of living,” Jenner said. “The bill unquestionably assumes that all school cost and spending increases, no matter how high, must be met with increased funding, i.e. increased taxes.”

School Funding Rising Fast

State funding for Illinois’ public schools has increased by more than $1 billion over the past two years without a tax increase, according to Becky Watts, spokeswoman for the Illinois State Board of Education. She told the Associated Press on November 5 that the additional money totals “about $400 for every student in the state’s 888 public schools.”

“From 1995 to 2003 the total funding, also known as taxes, for education in Illinois rose from $17 billion to $29 billion,“ Cocks said. ‘That is a 70 percent increase. And what was the increase in student population during this time? It was only 7.3 percent,’ she told legislators.”

No Taxpayer Left Behind in Illinois

Citizens for Reasonable and Fair Taxes (CRAFT) believes there is a better way to fund education in Illinois. It supports a program it calls No Taxpayer Left Behind consisting of six elements:

NO-STRIKE LAW
Public school teachers would be forbidden from striking. Most states already ban teachers from striking.

ELIMINATE TENURE
It is next to impossible to remove a teacher that has attained tenure protection. In Illinois, teachers attain tenure after four years of service.

REVISE COLLECTIVE BARGAINING LAWS
Illinois law regarding collective bargaining with teachers is sometimes difficult to follow. When questions arise, the teacher unions are always happy to provide an interpretation. The law requires the school district to negotiate with the union, which has the power to strike, and dictates much of the negotiating. CRAFT argues this is why school boards often cave in to union demands.

SCHOOL CHOICE
Most people’s basic sense of fairness says those who pay for something should have some say in how it works. Being able to remove a child from an under-performing school is a basic right that should not be for the wealthy alone, according to CRAFT.

END STATE SUBSIDY OF THE TRS
Little-known to most taxpayers is the state-run Teacher Retirement System (TRS) fund. In recent years, Illinois has contributed almost $1 billion annually (above and beyond district-level contributions) to curb huge shortfalls in the TRS. Despite this huge influx of taxpayer cash, the TRS continues to lose ground.

Illinois and Utah Move in Opposite Directions over Tax Reform

Here are the major differences (and one similarity) between tax reforms currently being proposed in Illinois and Utah.

**Illinois**
- Reform is being pushed by the education community, not by top lawmakers.
- Reform was proposed by the outgoing governor and recommended by a state government commission.
- Tax reform aims to increase tax revenues.
- Tax reform aims to be tax-revenue neutral.

**Utah**
- Reform would broaden the state sales tax base.
- Reform would broaden the state sales tax base.

**Illinois**
- Personal income tax rate would increase from 3 percent to 5 percent for households earning $50,000 or more.
- Personal income tax rate would drop from a high of 7 percent to a flat 4.9 percent for everyone.
- State sales tax would be increased for certain consumer services, exceeding 9 percent in several localities.
- State sales tax rate would be rolled back one percentage point to 3.75 percent.

**Utah**
- State corporate income tax would be abolished.
- State corporate income tax would be abolished.
- Local property taxes would initially decrease, but there is no assurance they wouldn’t soon start to rise again.
- Local property taxes could increase.
Congress Extends Ban on Internet Taxes

by Steve Stanek

Shortly before adjourning for the Thanksgiving holiday, Congress presented Internet users with an early Christmas present: a three-year extension of the federal ban on Internet taxes. The Internet Tax Nondiscrimination Act, which Congress approved on November 19, blocks state and local governments from taxing Internet connections, including dial-up and DSL. It also blocks multiple state and local taxes from being levied on online purchases and prohibits the creation of taxes unique to the Internet.

“I applaud Congress for their action and for recognizing the significant harm that tax increases can have on the development and deployment of high-tech service offerings,” said Steve Largent, president and CEO of the Cellular Telecommunications & Internet Association. “Broadband will continue to have an enormously beneficial impact on how we as a society access and consume information.

“Broadband holds the promise of revolutionizing the delivery of pertinent information to educators, law enforcement officials, emergency responders, and health care providers all across America,” Largent said. “I am very pleased that this promise will not be interrupted by the imposition of tax increases.”

House Wanted Permanent Ban

The bill was a compromise. The House voted last year to permanently ban Internet taxes, but there was not enough support in the Senate.

The lead sponsor of the original 1998 ban, House Policy Committee Chairman Christopher Cox (R-CA), was also a leader this time around. Cox argued for passage on the House floor by saying, “Republicans and Democrats have come together to say that no matter how we might choose to fund government services, we all agree the worst way to do it would be to create new taxes on the Internet. That would be harmful to consumers, destructive to technological innovation, and bad for our economy.

“The case for allowing Internet access to remain tax-free has never been stronger,” Cox said. “With 200 million Americans now online, a new tax on access would be a tax on working families. Our citizens recognize the danger. Eighty-eight percent of Americans oppose new Internet access taxes, making this legislation among the most popular tax issues in America.”

CHRISTOPHER COX (R-CA)
CHAIRMAN, HOUSE POLICY COMMITTEE

Wisconsin Tax to End

Another leader of the effort was House Judiciary Committee Chairman James Sensenbrenner (R-WI), who insisted his home state of Wisconsin be forced to drop its Internet access tax. Sensenbrenner wanted it dropped immediately, but Sen. Herb Kohl (D-WI) insisted the tax remain in place another two years. The legislation ended up leaving the tax in effect until November 1, 2006.

Wisconsin was one of several states that began taxing Internet access before the original ban in 1998. Those states had been allowed to continue collecting the tax. However, the 1998 ban was enacted before high-speed broadband connections came into use, so the ban did not address those technologies. Several states have levied taxes on high-speed connections. Under the new federal legislation, they will have to phase out those taxes.

“Enacting this legislation is a big win for America Online, one of the world’s largest Internet service providers, said in a statement, ”With adoption of this critical legislation, Congress has recognized the tremendous virtues of an Internet unencumbered by unnecessary and undue taxation and regulation that would impede the growth of the Internet, rather than foster it.”

Sensenbrenner said he pushed for Wisconsin to be forced to drop its 5 percent Internet tax because it was enacted without a vote by the state Assembly. The tax was enacted based on a Wisconsin Department of Revenue interpretation of the 1998 ban’s “grandfather” provision.

In 2002, the state billed Wisconsin Internet users an estimated $24.3 million, according to Sensenbrenner. Some Wisconsin localities also levy up to an additional 1/2 percent tax, he said.

“Whether it’s for checking e-mail, purchasing items online, or researching a subject for school, the Internet has become an integral part of life for many Americans,” Sensenbrenner said. “As one of only a handful of states that taxes Internet access, Wisconsin’s growth and ability to remain competitive in the technology sector are seriously hampered. Removing this tax is a step toward eliminating Wisconsin’s ‘high-tax’ reputation.”

The legislation also updates the definition of Internet access to ensure all types of Internet access are protected from taxation. It also ensures states and municipalities may continue to tax telecommunications services, including VoIP or Voice over Internet Protocol.

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Competition Report

In five states—Florida, Illinois, Nebraska, New York, and Washington—taxes make up more than 20 percent of the bill, said Schuler. Seven other states are nearly at 20 percent.

For most businesses, the tax burden is about 6.5 percent, he said.

“Taxes on wireless service keep piling up,” said Schuler. “The average monthly wireless bill has decreased 37 percent over the past decade, but 19 states now impose double-digit taxation on wireless service, and the trend is increasing.”

Most Competitive Telecom Market

Schuler said the wireless telephone sector is the most competitive in the telecommunications marketplace, a conclusion shared by the Federal Communications Commission (FCC). The Ninth Annual Competition Report of the FCC, released in September 2004, noted that of all areas of the telecom industry, the wireless sector is delivering the lowest prices, the most choices, and the most innovative new services to American consumers.

“We’re an enormously competitive industry, which is what makes these high taxes so bad,” Schuler said. “We don’t have a guaranteed rate base. We must compete for customers. We don’t have a group of customers who are captured and unable to move to competitors. High taxes hurt competition.”

In “The Excessive State and Local Tax Burden On Wireless Telecommunications Service,” published in the July 19, 2004 edition of State Tax Notes, economist Scott Mackey at the Kimbell Sherman Ellis public affairs firms noted, “Many of the taxes imposed by state and local governments are throwbacks to the monopoly telecommunications era. These taxes are levied at rates significantly above those of consumption taxes (typically sales and use taxes) on other goods and taxable services.”

“Despite the fact that congressional policy enabled the U.S. wireless industry to develop as a competitive industry, state and local policymakers continue to impose more than monopoly-era telecommunications taxes on wireless service in the interest of ‘competitive neutrality’ with other types of telecommunications service,” Mackey said. “A more appropriate policy would be the elimination of excessive taxes on wireless service, not the expansion of excessive taxes to wireless service.”

Consumers Sensitive to Prices

Schuler said in the days of monopolistic telephone service, consumers could not significantly change their telephone habits in response to pricing. But with the advent of competition brought about by the development of wireless technology, price has become a major factor in the choices consumers make, Schuler said.

Mackey made a similar point in his article.

“Recent studies have estimated that the price elasticity of demand for wireless service is between -1.12 percent and -1.29 percent, meaning that every 1 percent increase in price reduces demand for the service by between 1.12 percent and 1.29 percent,” Mackey wrote. “When a state like Florida or New York imposes a 16 percent tax on wireless service, demand for wireless service is reduced by between 17.9 percent and 20.7 percent.”

J. Gregory Sidak, resident scholar at the American Enterprise Institute, agrees that the demand for cell phone usage is more price-sensitive than for land-line service.

“When you impose an excise tax on a price-sensitive good, you suppress demand to a greater degree than if you put a tax on a good that is not as price-sensitive,” he said.

Sidak also said regardless of whether wireless phone use is declining, states would tax wireless “because it’s seen as an inviting pot of money.”

State Tax Cash Cow

Sidak said New York state, which in 1991 created a special wireless tax to fund enhanced 911 emergency services. Since then, the state has spent 93 percent of the wireless tax revenues on projects other than 911 emergency services.

“The average wireless customer in New York pays a tax that is nearly double that of the average business tax in New York,” Sidak said.

Schuler said that while the number of wireless subscribers has grown from 16 million to more than 160 million over the past decade, growth would have been faster if taxation of wireless service had been held in check. Offsetting the effect of tax increases were big drops in service costs, from about 47 cents to 10 cents a minute over the past decade.

“Many of the taxes imposed by state and local governments are throwbacks to the monopoly telecommunications era. These taxes are levied at rates significantly above those of consumption taxes (typically sales and use taxes) on other goods and taxable services.”

SCOTT MACKEY, ECONOMIST

KIMBELL SHERMAN ELLIS

Mackey also points out that wireless providers have taken much greater risks than the old Bell Telephone companies did to establish their networks. Those old networks were created in heavily regulated settings, in which rate of return was guaranteed by regulated prices.

“Wireless providers had no such guarantees, and some wireless companies are just now starting to turn profitable after years of losses, while others have yet to break even,” Mackey wrote.

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The Ninth Annual Competition Report of the Federal Communications Commission noted:

- More than 276 million Americans, or 97 percent of the U.S. population, have three or more wireless service providers to choose from in their county.
- The industry is responsible for more than 205,000 jobs, a 7 percent increase from the year prior.
- Capital investment continues to climb, increasing more than 15 percent in 2003.
- 25 percent of wireless subscribers are casual data users, accessing the Web, checking email, downloading ringtones, and sending text messages regularly.

Top 10 Wireless Tax States

Since 1993 the average wireless phone customer’s monthly bill has gone down almost 37 percent, while minutes of use have increased about 300 percent, according to the Cellular Telecommunications & Internet Association. Wireless carriers are providing innovative products and services for less money, but some state legislatures see wireless service as an easy target and are taxing it more and more. Here’s a list of the 10 states with the highest taxes on wireless telephone service:

1. New York 21.70%
2. Florida 21.60%
3. Washington 21.52%
4. Illinois 21.05%
5. Nebraska 20.61%
6. Texas 19.55%
7. Rhode Island 19.55%
8. Pennsylvania 19.05%
9. California 18.66%
10. District of Columbia 18.05%

A full state-by-state breakdown is available online at www.stopaddingtommybill.com/documents/state fedbreakdown.pdf.
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