

Retirement Income Highlights Problems of State Tax System

Written by Rich Miller
Sunday, 13 March 2011 05:22

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One of the main reasons the Democratic Party did so poorly across the nation last year and lost ground in Illinois was the defection of senior citizens to the Republican Party.

On Election Day 2006, national exit polling showed voters 65 and older split their ballots 49-49 between the two parties. In Illinois, however, senior citizens went with Democrat Rod Blagojevich over Republican Judy Baar Topinka by 10 points, 50-40.

Last year, national exit polling showed Republicans with a huge 59-38 margin over Democrats among seniors. In Illinois, the exit polls showed that Pat Quinn lost the senior-citizen vote to Republican Bill Brady by 17 points, 55-38. Quinn ended up beating Brady by less than 32,000 votes. Blagojevich won his last election by more than 10 times that amount: 367,000. The lost senior vote accounted for more than half the difference between those two margins.

So some Democrats may be forgiven for cringing last week after reading the headlines about how Senate President John Cullerton was floating the idea of taxing retirement income. Their party needs to woo that all-important and rapidly growing demographic back to the fold, not alienate it even more. Those stories probably didn't sit well at all with the oldsters. There's a reason why only five states tax all retirement income, and it ain't fiscal.

To be fair, the headlines didn't tell the whole story. Cullerton told me that he had no intention of moving forward with the proposal unless the Republicans joined him. And, he said, he would only use the new tax revenues to lower rates for everyone. It would have to be revenue-neutral, he said.

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Cullerton also said he was open to limiting the tax to annual retirement income above \$100,000. But the Department of Revenue told the *Chicago Tribune* that taxing only those higher-income seniors would net the state just \$70 million. Revenue that meager wouldn't budge the overall rate at all.

It turns out that the real money is in the low-income brackets. All but a small fraction – \$276 million – of the \$1.9 billion raised by taxing retirement incomes would come from seniors making less than \$50,000 a year, according to *Tribune* numbers obtained from the General Assembly's Commission on Government Forecasting & Accountability.

Chicago's two newspapers both editorialized in favor of it because of the "fairness factor." Why should well-off oldsters get a free ride on income taxes while lots of working families are struggling to stay afloat in these trying times?

There's something to be said for spreading the burden around and lowering overall tax rates.

But exempting lower retirement incomes wouldn't bring in any real money. Not to mention that it probably wouldn't be allowed under the Illinois Constitution, which prohibits graduated rates and is generally held to frown upon exempting lots of income. As a result, Cullerton backed almost totally away from the idea the day after he floated it.

The better idea was passed by Cullerton's Senate two years ago, but it went nowhere in the House. The Senate bill would've broadened our narrow state sales tax to cover more things such as services. If you buy shampoo for your dog, you pay a sales tax. If you take your dog to one of those swank grooming boutiques, you don't pay any sales tax. If you buy disposable diapers for your baby, there's a tax, but diaper service is not taxed.

Keeping the tax base so narrow means that rates have to go up that much higher in a crisis. Widen the base and rates can be stabilized or even lowered. Lots of people don't even know that they currently pay no state sales tax on food and medicine. And I personally know some retired seniors who were furious about this year's income-tax hike even though it didn't cost them a dime.

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The idea would be to spread a little bit of tax “pain” around to lessen the overall sting. But hey, it’s all academic now. The General Assembly raised the income tax 2 percentage points back in January. And a big reason why they they had to jack it up so high to reach the revenue they needed is that our screwed-up tax system exempts so much income and just about all services.

Rich Miller also publishes Capitol Fax (a daily political newsletter) and CapitolFax.com.