WSJ OP ED Updated May 26, 2017 8:09 p.m. ET

Illinois's 'Privilege Tax' Proposal Forgets Citizens' Right to Leave
The state can't even pass a budget, but it wants to put a new 20% levy on fees to financial professionals.

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Proponents here call it the "privilege tax." In their continuing quest to punish the productive areas of the economy, liberal groups are pushing legislation in blue states that will force finance professionals to pay up—or move out.

The Illinois bill would put a 20% levy on fees earned by investment advisers. It passed the state Senate in a 32-24 vote Tuesday, and backers are hoping to get it through the House before the legislative session ends May 31.

The new tax is pitched as a way to squeeze more revenue—as much as $1.7 billion a year—from hedge funds and private-equity firms, which purportedly get off easy on their federal taxes because of the "carried interest loophole." But under the current version of the bill, Illinois would keep collecting the privilege tax even if Congress were to cease taxing carried interest at the lower capital-gains rate.

Liberal groups are also hoping—probably in vain—that a multistate agreement will prevent financial firms from simply decamping to friendlier climes. An earlier version of the Illinois proposal included a provision so that the 20% tax would take effect only if and when New York, New Jersey and Connecticut enacted similar measures. But the bill as written now would impose the tax regardless, and lawmakers will simply have to hope other states follow suit.

Yet who says financiers can't do their jobs just as well in Palm Beach, Fla.—or London, Zurich or Hong Kong? The progressives peddling this idea don't understand that Chicago competes for these businesses not only with New York and Greenwich, Conn., but with anywhere that can offer cellphone service and an internet connection. Finance is international and highly mobile.

As often happens when advocates try to work legislation through multiple statehouses, the details have gone down the drain. The Illinois iteration of the privilege tax, for example, is poorly structured in that it fails to account for what's known as apportionment. That means, according to Joseph Henchman of the nonpartisan Tax Foundation, that Illinois would wind up taxing income that's properly taxed by other states.

It's also notable that the states where this "privilege tax" proposal is being seriously pushed are those with the worst grasp on their own finances. Illinois hasn't had a budget in two years, since the Democrats in Springfield continue to insist on more taxes. The state has $267 billion in unfunded retirement liabilities, a $14 billion backlog of unpaid bills, and a $7 billion projected deficit this fiscal year.

Illinois's credit rating is a lackluster Baa2, according to Moody's . New Jersey's rating is only a little better, A3, while Connecticut's is Aa3 and New York's Aa1. Residents are fleeing all four states, Census Bureau data show. On net, tens of thousands left each in 2015-16 alone. The last thing these states need is another 20% tax to drive away money and talent.

Railing against supposed "fat cats" might satisfy progressive groups, but lawmakers shouldn't be in the business of hounding the people who help connect capital with new opportunities for growth. Dynamic entrepreneurship is what makes America great. Rather than focus on how to make everyone miserable together, policy makers should work to increase their states' competitiveness. A start would be to rally against this proposed privilege tax and instead fix the spiraling pension costs and outdated labor rules that are dragging Illinois and other blue states down.

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