CTBA | Center for Tax and Budget Accountability

HIGHIGHTS OF THE ILLINOIS STATE BUDGET PROPOSED FOR FISCAL YEAR 2009

By Chrissy Mancini, Director of Budget and Policy Analysis ***(Updated March 2008)*** February 2008

On Wednesday, Governor Blagojevich submitted his Fiscal Year 2009 budget recommendation to the Illinois General Assembly. Highlights of the budget recommendation include:

Tax Credits and Breaks

Illinois Child Tax Credit - A $300 per child refundable tax credit for each dependent child under age 17, for all "eligible taxpayers". Eligible taxpayers are: (i) individuals with children whose annual incomes are $75,000 or less, and families with annual incomes up to $150,000; provided that (ii) each taxpayer has at least $3,000 in earned income, unemployment or social security in a year. The Illinois Child Tax Credit is estimated to cost approximately $900 million in fiscal year 2009.

- This tax credit is a one-time occurrence and not targeted to those who need relief the most. CTBA recommends that the better policy option would be an increase in the state's Earned Income Tax Credit. This would be ongoing, meaningful tax relief targeted to individuals and families who are in the bottom 40 percent of income earners—a group that has seen their real, inflation-adjusted incomes decline over the last two decades. It would also more effectively reduce the regressivity of Illinois' current tax structure, which places a much greater burden on low and middle income earners than on the affluent.

Business Tax Cut - The Illinois Business Tax Cut will provide eligible Illinois employers with a one-time, 20 percent reduction in their Illinois corporate income taxes for tax year 2008, effective immediately upon becoming law. To be eligible to participate in the Illinois Business Tax Cut, a corporation must

- have paid Illinois corporate income taxes in 2007; and
- not reduce its Illinois based workforce.

The Illinois Business Tax Cut is estimated to cost approximately $300 million in fiscal year 2009.

Funding For Tax Credits and Breaks

It is unclear how these tax credits and breaks will be funded. One avenue that the state proposes to pursue is using one-time revenues generated by the securitization of Illinois' tobacco settlement proceeds.

Capital Program

Illinois Works Capital Program – A $25 billion infrastructure program for transportation, school construction and other capital programs. The initiative would require $11 billion in state funds, with the gap closed by local and matching federal funds. A partial sale/lease of the Illinois state lottery is slated to cover $7 billion of the initiative's funding. The remainder would be financed through bond proceeds. The $300 million debt service on the bond proceeds would be paid for with road fund and other fund transfers.

Privatization of the State of Illinois Lottery - A "partial concession" of the lottery. The State would retain 20% ownership and the ability to regulate the lottery and retain the annual revenue stream that is targeted to education from lottery proceeds. The partial concession is estimated to raise between $10-12 billion, $7 billion of which will be directly used to fund Illinois Works, as identified above.

Pension Funding

State Pension System Funding – Implement enhanced funding of the state's five pension systems (which currently have a collective unfunded liability in excess of $44.2 billion,[1] worst in the nation) by refinancing high interest, unfunded pension liability into lower-interest pension obligation bonds (a **"POB"**).

How the POB Works

The state would issue $16 billion in pension obligation bonds at an interest rate lower than currently applicable to its unfunded liability, and then deposit the proceeds from the bond sale immediately into the pension fund, to pay off some of the current unfunded liability. If structured appropriately, the state would save money because the interest rate paid on the POB would be less than the interest rate normally accruing on the unfunded liability. The state currently pays an 8.0% to 8.5% interest rate on the unfunded liability. If the POB is issued at a 6.0% interest rate, the 2.0% to 2.5% less the state pays on the principal balance of the POB versus the unfunded liability, effectively generates long-term savings to the state. The POB will then be paid out of increased revenue generated for the General Revenue Fund from unidentified tax enhancements, over a set period, such as 30 years. Of course a POB reduces, but does not eliminate, the state's unfunded liability.

Admittedly, the state is already overextended when it comes to debt. But issuing a pension obligation bond will not, in reality, increase the aggregate liability of the state. Illinois constitutionally has the obligation to pay the full $44.2 billion amount by which it has underfunded its employer contribution to the five state pension systems, without diminishment. While the state must pay the principal and interest cost under the POB, the lower interest rate on the POB principal actually lessens the long-term costs of paying it, while creating the discipline that will force the liability to be paid (the state cannot default in a bond payment), and establishing a long-term payment schedule that is feasible.

Of course, to make this option viable, the state still must modernize its existing tax structure through both income and sales tax reforms, to raise enough ongoing revenue to cover both continuation of public services and the new pension bond debt service. However, in that context, appropriate refinancing of the pension debt could save billions.

Funding

Covering the FY 2008 Budget Deficit

The state is projecting an estimated $800 million shortfall[2] in expected revenue for the current Fiscal Year 2008. To address this shortfall, the Governor proposes making $500 million in transfers from special funds to the General Fund, and closing $200 million in corporate loopholes. It is unclear if these proposals will become law.

FY 2009 Revenue

In fiscal year 2009, anticipated revenue growth is expected to be limited. Revenue initially was forecasted to grow by only $630 million,[3] but given the economic downturn, even that low estimate is likely optimistic. Meanwhile, the inflationary cost of just continuing FY 2008 service levels into FY 2009 is over $1.2 billion.[4] This creates a deficit of at least $572 million, between revenue growth and service cost growth. Additionally, the Illinois Comptroller has found that currently the state owes $3.4 billion in unpaid Medicaid bills.[5] It is unclear how much of this Medicaid liability will be paid in FY 2008 and how much deferred to FY 2009. What is clear is the pension ramp is scheduled to increase by $720 million from FY 2008 to FY 2009.[6]

Figure 1
FY 2009 Budget Deficit

Category	Dollar Amount ($ in millions)
Forecasted FY 2009 Revenue Increase	$630
Dollar Amount Necessary to Keep Up with the Inflationary Costs of Continuing FY 2008 General Fund Levels	(-$1,202)
Pension Ramp Increase	(-$720)
Minimum Deficit	(-$1,292)
Plus FY 2008 Medicaid Liabilities deferred into FY 2009	(-$?)

Source: Illinois FY 2009 Budget Book and Illinois Commission on Government Forecasting and Accountability. Inflation based on Bureau of Labor Statistics CPI-U.

According to the Illinois Comptroller in a letter to the General Assembly dated February, 2008, the state currently owes $3.4 billion in unpaid Medicaid liabilities. It is unclear how much of that amount will be paid down in FY 2008.

Spending Cuts

The Governor proposes a three percent across-the-board spending reduction in all areas outside of healthcare, K-12 education, and public safety. Those three line items account for over 60 percent of the General Revenue Fund—meaning the 3 percent cut will hit disproportionately impact other programs.

FY 2009 Budget Spending Proposals

Figure 2 shows: (i) the FY 2008 enacted General Fund budget; (ii) the inflationary cost of just maintaining FY 2008 services levels in FY 2009, using the Consumer Price Index or "CPI"; (iii) the proposed FY 2009 budget; and (iv) the difference between the budget as proposed and the inflationary cost of maintaining FY 2008 services in FY 2009.

Figure 2: General Fund Spending: Proposed FY 2009 Compared to FY 2008 Inflation Adjusted (CPI) ($ in millions)

Category	FY 2008 Appropriated	FY 2008 Inflation Adjusted to FY 2009	FY 2009 Recommended	Difference FY 2008 Inflation Adjusted and FY 2009 Recommended	Percent Change
General Revenue Fund Total	$27,949	$29,095	$28,909	-$186	-0.64%

All spending data based on FY 2009 Budget Book and Illinois Commission on Government Forecasting and Accountability, FY 2008 Budget Summary. Inflation based on Bureau of Labor Statistics, CPI-U.

Figure 3 shows the same categories as Figure 2, except the inflation adjustment is based on the more accurate Employment Cost Index or "ECI". The ECI is more accurate because the primary cost of all public services is labor costs, generally accounting for 80-90 percent of all service costs.

Figure 3: General Fund Spending: Proposed FY 2009 Compared to FY 2008 Inflation Adjusted (ECI) ($ in millions)

Category	FY 2008 Appropriated	FY 2008 Inflation Adjusted to FY 2009	FY 2009 Recommended	Difference FY 2008 Inflation Adjusted and FY 2009 Recommended	Percent Change
General Revenue Fund Total	$27,949	$29,151	$28,909	-$242	-0.86%

Figure 4 compares the estimated GRF FY 2008 spending levels to the proposed FY 2009 proposed spending levels by government department. It also includes the inflation-adjusted cost (CPI based) of maintaining FY 2008 services in FY 2009. After adjusting for CPI, the Illinois State Board of Education, Higher Education, Department of Agriculture, Department of Children and Family Services and the Department of Natural Resources are all scheduled to receive decreases in funding in FY 2009.

Figure 4: Comparison of GRF Spending by Department Inflation Adjusted (CPI): FY 2008 & FY 2009

Category	FY 2008 Approp	FY 2008 Inflation Adjusted to FY 2009	FY 2009 Rec	Difference FY 2008 Inflation Adjusted and FY 2009 Recommended	Percent Change
General Revenue Fund Total	$27,949	$29,095	$28,909	-$186	-0.64%
K-12 Education	$7,132	$7,424	$7,398	-$26	-0.36%
Higher Education	$2,221	$2,312	$2,205	-$107	-4.86%
Department of Human Services	$4,183	$4,355	$4,362	$7	0.17%
Health Care	$8,391	$8,735	$8,883	$148	1.67%
Department of Corrections	$1,244	$1,295	$1,415	$120	8.48%
Department of Agriculture	$49	$51	$40	-$11	-27.52%
Department of Children & Family Services	$901	$938	$902	-$36	-3.98%
Department of Natural Resources	$92	$96	$40	-$56	-139.43%

Figure 5 compares GRF FY 2008 spending levels to FY2009 proposed spending levels by government department, this time adjusting for inflation based on the more accurate ECI.

Figure 5: Comparison of GRF Spending by Department Inflation Adjusted (ECI): FY 2008 & FY 2009

Category	FY 2008 Apprp	FY 2008 Inflation Adjusted to FY 2009	FY 2009 Rec	Difference FY 2008 Inflation Adjusted and FY 2009 Recommended	Percent Change
General Revenue Fund Total	$27,949	$29,151	$28,909	-$242	-0.84%
K-12 Education	$7,132	$7,439	$7,398	-$41	-0.55%
Higher Education	$2,221	$2,317	$2,205	-$112	-5.06%
Department of Human Services	$4,183	$4,363	$4,362	-$1	-0.02%
Health Care	$8,391	$8,752	$8,883	$131	1.48%
Department of Corrections	$1,244	$1,297	$1,415	$118	8.30%
Department of Agrilculture	$49	$51	$40	-$11	-27.77%
Department of Children & Family Services	$901	$940	$902	-$38	-4.18%
Department of Natural Resources	$92	$96	$40	-$56	-139.89%

Health Care

Family Care Expansion - The state will expand the Family Care program, which provides health insurance to Illinois families with children earning up to 400 percent of the federal poverty level, through a sliding premium requirement that allows families of different economic means to purchase coverage at different rates.

Illinois Women's Health Expansions –In fiscal year 2009, the state will continue to fund the costs of breast and cervical cancer screenings and treatment for all uninsured women in Illinois.

Illinois Covered Assist - The state will implement the Illinois Covered Assist program which enhances access to healthcare for Illinoisans living in poverty, who are otherwise ineligible for Medicaid. The Department of Human Services will also accommodate additional patients in its mental health and substance abuse treatment programs under this initiative.

Illinois Covered Rebate – Starting July 1, 2009, the state will ensure affordability by providing insurance premium rebates to adults with incomes between 100 percent and 300 percent of the federal poverty level, to help them pay their health insurance costs. The rebate amount will equal 20 percent of premiums paid by eligible residents.

Illinois Employer Assessment – It is proposed that the costs of Illinois Covered be fully funded in fiscal year 2009 and thereafter, entirely through its own revenue sources, including enactment of a new employer healthcare assessment. The proposed employer assessment, to commence January 1, 2009, will require that all businesses that employ more than 10 workers and that spend less than 4 percent of their payroll costs providing healthcare to employees, pay an assessment of 3 percent of total in-state payroll each pay period. The Employer Assessment is estimated to generate $417 million in fiscal year 2009 and nearly $1 billion per year when fully implemented.

As the number of uninsured in Illinois increases, increasing access to health care is needed. That said, Illinois' chronic fiscal problems make it increasingly difficult for the state to keep up with soaring health care costs, which are growing three times faster than general inflation, making health care funding one of the state's greatest challenges.[7]

While many states have elected to cut Medicaid benefits or restrict eligibility as a way to curtail program costs, Illinois should be applauded for not taking that approach, recognizing that providing basic health care to low-income, uninsured families is an essential public service. Unfortunately, due to an underperforming revenue system, the state has had to delay payment of Medicaid bills owed to health care professionals, in many cases for months. By deferring these Medicaid liabilities from one year to the next, the state makes its budget appear balanced when in fact it is not. This results in long payment delays to hospitals, doctors and pharmacists that treat the most vulnerable in our society. It also acts as a huge disincentive for healthcare providers to actually take on Medicaid eligible patients.

The state's unpaid Medicaid liabilities nearly tripled between fiscal year 2000 and 2005, increasing from $977 million in 2000, to $2.7 billion in 2005. **Currently, the State Comptroller has found past due payments have grown to approximately $3.4 billion.**

Education

In fiscal year 2009, the state proposes to increase K-12 funding by $300 million, subject to additional revenues being approved by the General Assembly. However, as noted previously, after inflation is taken into account, K-12 funding will be cut in real dollars in FY2009.

The $300 million nominal increase, targeted for K-12 education in the fiscal year 2009 will be funded through a proposal to increase tax rates on existing riverboat gaming facilities, as well as through initial recurring revenues generated by the tenth riverboat license, which will be auctioned in early 2009. These new gaming revenues will generate an estimated $300 million in additional revenue.

CTBA will issue a full analysis of the FY 2009 budget recommendation in the coming weeks.

Endnotes

1. Illinois Commission on Government Forecasting and Accountability, *2007 Report on the Condition of the Illinois Public Employee Retire ment Systems*, July, 2007.
2. Illinois Commission on Government Forecasting and Accountability, February 2008 Monthly Briefing.
3. State of Illinois Fiscal Year 2009 Budget Recommendation.
4. Inflation based on Bureau of Labor Statistics, CPI-U. FY 2008 appropriations based on Illinois Commission on Government Forecasting and Accountability, FY 2008 Budget Summary.
5. Illinois Comptroller Dan Hynes, Fiscal State of the State Report to the Illinois General Assembly, February 13, 2008.
6. Illinois Commission on Government Forecasting and Accountability, *2007 Report on the Condition of the Illinois Public Employee Retire ment Systems*, July, 2007.
7. The Kaiser Family Foundation and Health Resource Educational Trust, *Employer Health Benefits 2005 Annual Survey,* September 2005.

About CTBA

Founded in 2000, the Center for Tax and Budget Accountability is a non-profit, bi-partisan research and advocacy think tank committed to ensuring that tax, spending and economic policies are fair and just, and promote opportunities for everyone, regardless of economic or social status.

CTBA uses a data-focused, bipartisan approach to work in partnership with legislators, community groups and other organizations to help change both public policy and perceptions.

Center for Tax and Budget Accountability
70 E. Lake St, Suite 1700
Chicago, IL 60601
Phone: (312) 322-1041
Fax: (312) 578-9258
Www.ctbaonline.org