CTBA | Center for Tax and Budget Accountability

# Analysis of the Fiscal Year 2008 Illinois Final General Fund Budget

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# CTBA | Center for Tax and Budget Accountability

## *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.

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# Analysis of the Fiscal Year 2008 General Fund Budget

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# INTRODUCTION

After a record overtime sessions, the Illinois Fiscal Year (FY) 2008 budget was enacted on January 4, 2008. The total enacted General Fund budget for FY 2008 was $27.4 billion.[1]

The final General Fund budget for FY 2008 demonstrates the continuation of two significant flaws in the state's overall fiscal system. First, revenue growth will again fail to keep pace with the economy, falling short of inflation. This pattern of revenue underperformance is long standing,[2] and has contributed substantially to Illinois' structural deficit.[3] A "structural deficit" is the term used to describe an ongoing shortfall between the revenues that a tax system generates and the inflationary cost of continuing the same level of public services from one year to the next, without expanding or adding programs.

The state's historic revenue underperformance also has contributed to the second significant flaw demonstrated in the FY 2008 General Fund budget – Illinois will continue to rely on significant infusions of debt and one-time revenue sources to fund services. The projected budget deficit for FY 2008 is currently $4.5 billion.[4] Borrowing and utilization of one-time revenue sources like fund sweeps and deferring payments to medical providers to the next year to pay for current operations has become common practice because the Illinois revenue system cannot cover current public service costs.

***Illinois will continue to rely on significant infusions of debt and one-time revenue sources to fund services.***

# Recap of FY 2008 Budget Process

## Governor's Proposals

In his FY 2008 budget recommendation, Governor Blagojevich proposed to expand health care to include all uninsured Illinoisans, greatly increase funding for education and sell the Illinois Lottery to partially fund the pension unfunded liability. The expansion of health care and education funding was conditional on several revenue raising initiatives including a new tax on business called a Gross Receipts Tax or **"GRT"**. A GRT is a tax imposed on *all income received by a business* without any deductions for costs of doing business, such as wages. GRTs are not based on a company's profit or loss for a given tax year; rather, they are imposed on gross income.[5] It was estimated by the Office of Management and Budget (**"OMB"**) the GRT would have raised an estimated $6 billion annually[6] to cover the Governor's health care and education spending programs. The Governor also proposed a 3.0% payroll tax that employers would have paid on Illinois employee wages. This payroll tax would have been reduced by a credit based upon the employer's contribution to cover health insurance cost for its employees.[7] This proposed healthcare/payroll tax was expected to generate $1.1 billion.[8] (For more information on the GRT see the CTBA Issue Brief on the Gross Receipts Tax at www.ctbaonline.org).

On Wednesday, May 9, 2004, the Illinois House of Representatives held a hearing on the GRT proposal. During the House hearing, opponents and supporters of the GRT proposal made their cases. At the end of the day, House members voted on Resolution 402 to support or oppose the Governor's proposal.

In total, 107 House members voted to oppose the GRT proposal; not a single Representative voted in favor of the proposal. Seven members voted "present". The bill was not called for a vote in the Senate.

## Record Breaking Budget Session

After a record breaking 71 days into the overtime session the General Assembly finally passed the FY 2008 budget bill on August 13, 2007. However, the process was far from complete. The Governor subsequently used his veto power to eliminate about $470 million from 1,504 projects. In October the General Assembly restored only about $8 million of the vetoed programs. (For an in-depth analysis (including a complete list) of the Governor's vetoes of the FY 2008 budget see the CTBA Issue Brief: How Governor Blagojevich's Vetoes Affect Services Across the State of Illinois, available at www.ctbaonline.org).

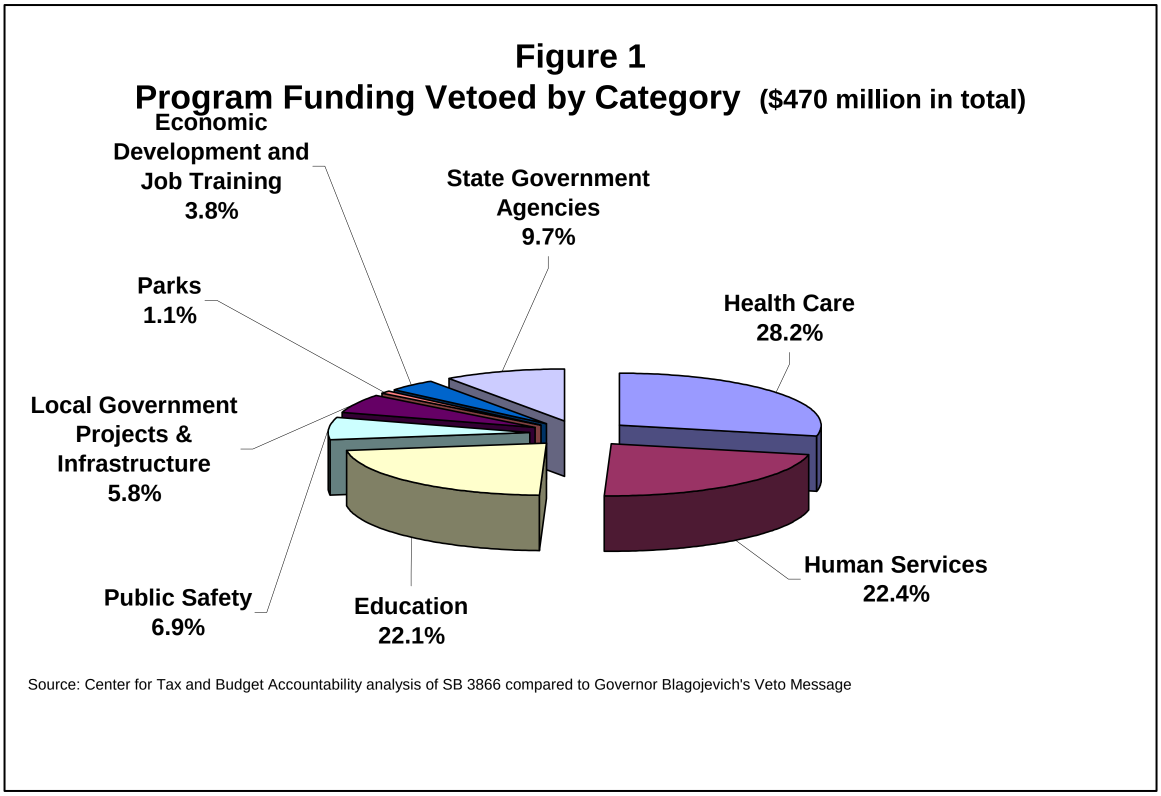
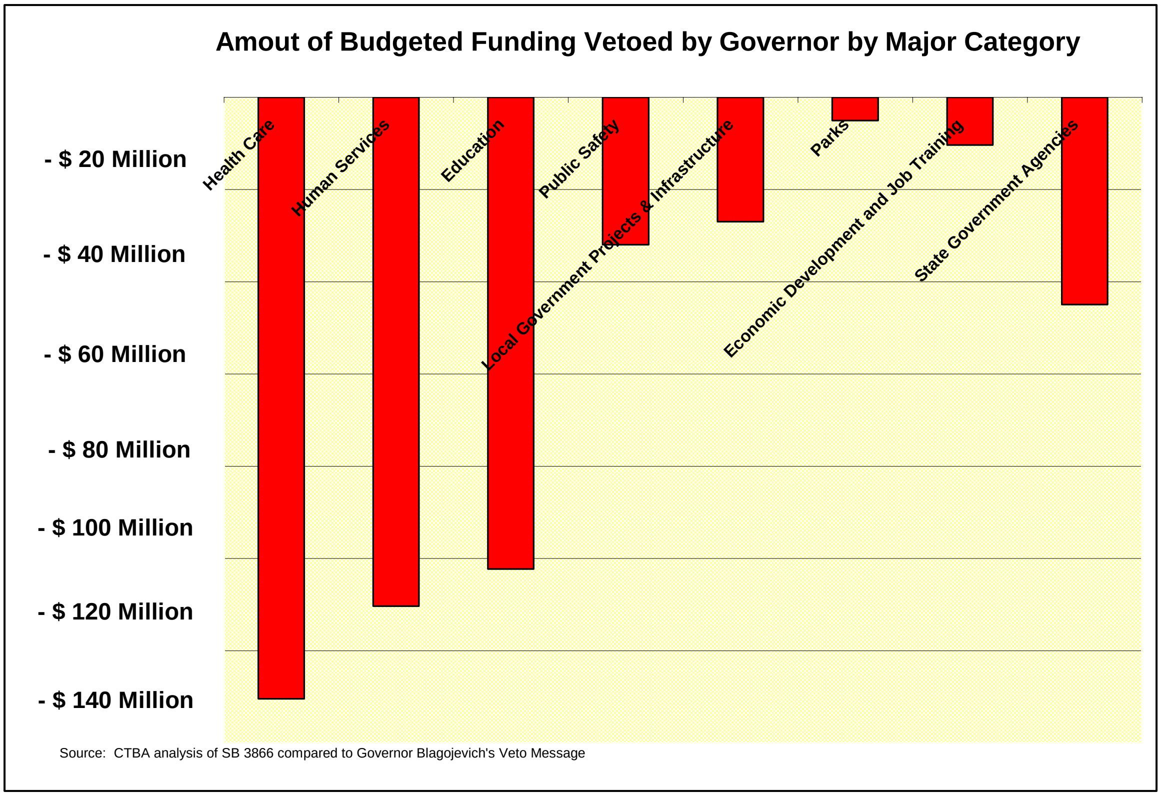


Figure 1
Program Funding Vetoed by Category ($470 million in total)
Economic Development and Job Training 3.8%
State Government Agencies 9.7%
Parks 1.1%
Health Care 28.2%
Local Government Projects & Infrastructure 5.8%
Human Services 22.4%
Public Safety 6.9%
Education 22.1%
Source: Center for Tax and Budget Accountability analysis of SB 3866 compared to Governor Blagojevich's Veto Message

## Figure 2


Amout of Budgeted Funding Vetoed by Governor by Major Category
- $ 20 Million
- $ 40 Million
- $ 60 Million
- $ 80 Million
- $ 100 Million
- $ 120 Million
- $ 140 Million
Health Care
Human Services
Education
Public Safety
Local Government Projects & Infrastructure
Parks
Economic Development and Job Training
State Government Agencies
Source: CTBA analysis of SB 3866 compared to Governor Blagojevich's Veto Message

The FY 2008 budget implementation bill (BIMP), required to authorize new spending from the FY 2008 budget, was sent to Governor Blagojevich for his signature on November 5, 2007. The Governor took action on January 4, 2008, making two revisions to the BIMP regarding funding for special education and the Illinois State Police. The General Assembly unanimously approved the changes on January 10 and the BIMP finally became law. The 60 day delay in the implementation of the BIMP meant that schools had to wait for all new money approved for FY 2008. This required some school districts to take out loans to cover their expenses. While local school districts received their increased FY 2008 funding retroactively, many human service providers rely on Medicaid funding, which can only be paid prospectively. That means programs like those that serve seniors and the developmentally disabled lost funding in FY 2008 due to the delay in the implementation of the BIMP.

# FY 2008 General Fund Budget Highlights

- Overall spending on public services is scheduled to increase in nominal terms by $ 2.18 billion, or 8.4%, from FY 2007 General Fund expenditures. After adjusting for inflation, real spending under the FY 2008 budget will increase by 4.1 %, or $1.12 billion.[9]

- Current revenue growth, however, is projected to increase by only $805 million.[10] This is not sufficient to cover the cost of continuing the public services Illinois provided in FY 2007, adjusting solely for inflation. The inflation-adjusted cost of just maintaining FY 2007 service levels in FY 2008 is $1.057 million. Therefore, projected revenues fall short of projected cost increases for existing programs by at least $252 million, based on the CPI. The shortfall is even greater, increasing to $303 million, when inflationary service costs are adjusted by the more appropriate Employment Cost Index or ECI.

- The FY 2008 budget increases the education foundation level by $400 per pupil.

**FISCAL NOTE: WHY ADJUST FOR INFLATION?**

The answer is simple. It's the only way to determine whether spending on public services and/or revenue growth is increasing in real terms, is just keeping pace with cost increases generated by the economy over time, or is falling behind cost increases generated by the economy. The most common inflation metric is the "Consumer Price Index" or "CPI". The CPI is the rate of inflation based on the change in the cost of all goods and services that collectively constitute the U.S. consumer economy. However, public services, whether education, police protection, healthcare or human service related, are labor intensive endeavors, with labor costs generally comprising over 80% of total cost. Hence the CPI is not the best inflationary metric to use for determining the increased costs of public services annually. The preferred inflation metric is the "Employment Cost Index" or "ECI", which is tied directly to changes in labor market costs.

# SPENDING

Figure 3 illustrates FY2008 General Fund spending by major purpose. In total, health care, education and human services make up over 82 percent of the General Fund budget.

**Figure 3**

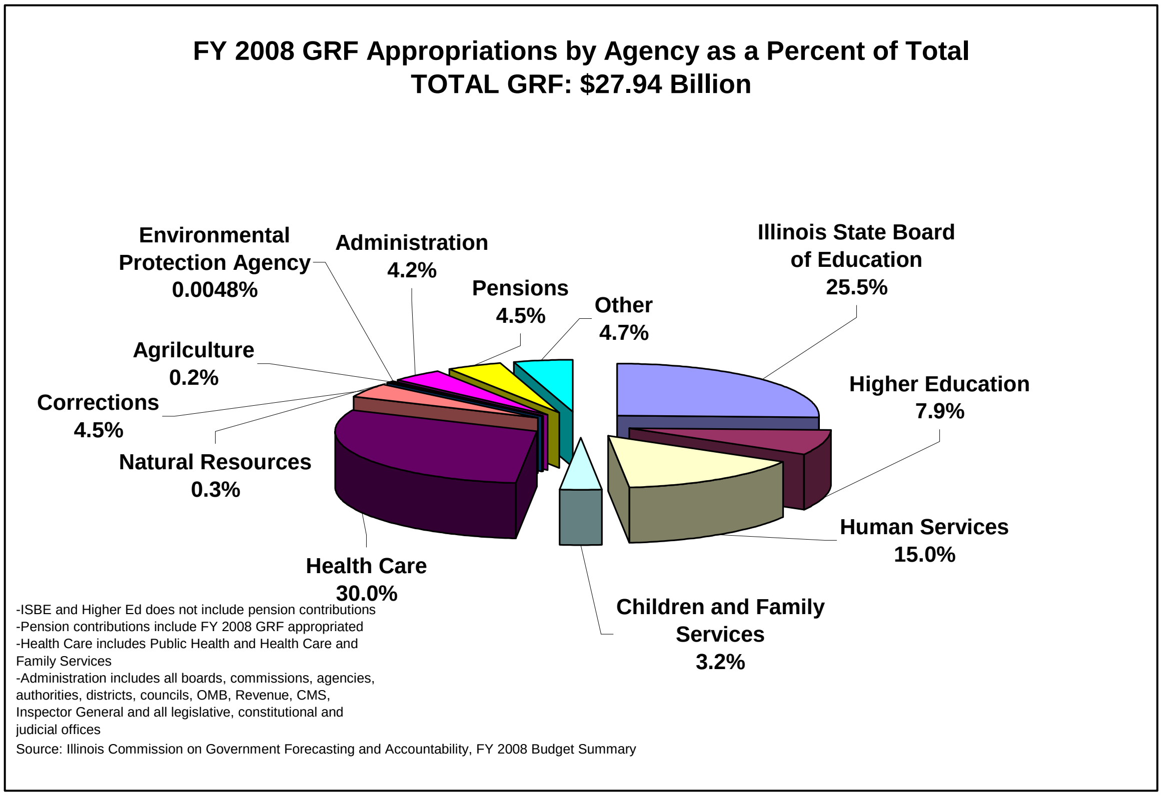



Figure 4 shows: (i) the FY 2007 General Fund budget; (ii) the inflationary cost of just maintaining FY 2007 services levels in FY 2008, using the CPI; (iii) the FY 2008 budget; and (iv) the difference between the FY 2008 budget and the inflationary cost of maintaining FY 2007 services in FY 2008.

**Figure 4: General Fund Spending: FY 2008 Compared to FY 2007 Inflation Adjusted (CPI) ($ in millions)**

| Category | FY 2007 | FY 2007 Inflation Adjusted to FY 2008 | FY 2008 Appropriated | Difference FY 2007 Inflation Adjusted & FY 2008 Appropriated | % Change |
|---|---|---|---|---|---|
| General Revenue Fund Total | $25,772 | $26,829 | $27,949 | $1,120 | 4.18% |

Source: Illinois Commission on Government Forecasting and Accountability

Figure 5 shows the same categories as Figure 2, except the inflation adjustment is based on the more accurate ECI.

**Figure 5: General Fund Spending: FY 2008 Compared to FY 2007 Inflation Adjusted (ECI) ($ in millions)**

| Category | FY 2007 | FY 2007 Inflation Adjusted to FY 2008 | FY 2008 Appropriated | Difference FY 2007 Inflation Adjusted & FY 2008 Appropriated | % Change |
|---|---|---|---|---|---|
| General Revenue Fund Total | $25,772 | $26,880 | $27,949 | $1,069 | 3.98% |

Source: Illinois Commission on Government Forecasting and Accountability

Figure 6 compares the estimated GF FY 2007 spending levels to the FY 2008 proposed spending levels by government department. It also includes the inflation-adjusted cost (CPI based) of maintaining FY 2007 services in FY 2008. After adjusting for CPI, the Illinois State Board of Education is scheduled to receive a real increase of $332 million. The Departments of Human Services, Health Care, DCFS, and Corrections are also scheduled to receive increases. Again, after adjusting for CPI, the Departments of Agriculture and Higher Education is scheduled to be cut in FY 2008.

**Figure 6: Comparison of GRF Spending by Department Inflation Adjusted (CPI): FY 2007 & FY 2008**

| Category | FY 2007 | FY 2007 Inflation Adjusted to FY 2008 | FY 2008 Appropriated | Difference FY 2007 Inflation Adjusted & FY 2008 Appropriated |
|---|---|---|---|---|
| General Revenue Fund Total | $25,772 | $26,829 | $27,949 | $1,120 |
| K-12 Education | $6,532 | $6,800 | $7,132 | $332 |
| Higher Education | $2,154 | $2,242 | $2,221 | -$21 |
| Department of Human Services | $3,994 | $4,158 | $4,183 | $25 |
| Health Care | $7,910 | $8,234 | $8,391 | $157 |
| Department of Corrections | $1,126 | $1,172 | $1,244 | $72 |
| Department of Agriculture | $49 | $51 | $49 | -$2 |
| Department of Children & Family Services | $776 | $808 | $901 | $93 |

Source: Illinois Commission on Government Forecasting and Accountability
Health Care includes Department of Public Health and Department of Health Care and Family Services
FY 2008 payments to the State Employees' Retirement Systems not included in categories

Figure 7 compares GF FY2007 spending levels to FY2008 spending levels by government department, this time adjusting for inflation based on the more accurate ECI.

**Figure 7: Comparison of GRF Spending by Department Inflation Adjusted (ECI): FY 2007 & FY 2008**

| Category | FY 2007 | FY 2007 Inflation Adjusted to FY 2008 | FY 2008 Appropriated | Difference FY 2007 Inflation Adjusted & FY 2008 Appropriated |
|---|---|---|---|---|
| General Revenue Fund Total | $25,772 | $26,880 | $27,949 | $1,069 |
| K-12 Education | $6,532 | $6,813 | $7,132 | $319 |
| Higher Education | $2,154 | $2,247 | $2,221 | -$26 |
| Department of Human Services | $3,994 | $4,166 | $4,183 | $17 |
| Health Care | $7,910 | $8,250 | $8,391 | $141 |
| Department of Corrections | $1,126 | $1,174 | $1,244 | $70 |
| Department of Agriculture | $49 | $51 | $49 | -$2 |
| Department of Children & Family Services | $776 | $809 | $901 | $92 |

Source: Illinois Commission on Government Forecasting and Accountability
Health Care includes Department of Public Health and Department of Health Care and Family Services
FY 2008 payments to the State Employees' Retirement Systems not included in categories

# EDUCATION

For FY 2008, the state increased PreK-12 education by $600 million over FY 2007 in nominal dollars, or $332 million after adjusting for inflation. Figure 8 shows the change in K-12 education funding since FY 2002.

**Figure 8: Historical Change in K-12 Education Funding**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002 - FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $5,297 | $4,965 | $5,444 | $5,809 | $6,110 | $6,532 | $7,132 | $35,993 |
| **Prior Year Inflation Adjusted CPI** | | $5,424 | $5,060 | $5,624 | $6,007 | $6,262 | $6,800 | $35,176 |
| **Difference CPI** | | **-$459** | $385 | $185 | $103 | $269 | $332 | $816 |
| **Percentage Change CPI** | | | | | | | | 2.32% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $5,514 | $5,139 | $5,640 | $6,047 | $6,360 | $6,813 | $35,514 |
| **Difference ECI** | | -$549 | $305 | $169 | $62 | $172 | $319 | $479 |
| **Percentage Change ECI** | | | | | | | | 1.35% |

Source: Illinois Commission on Government Forecasting and Accountability

## Major Education Funding Increases for FY 2008 include:

An increase in the K-12 Foundation Level OF $400, to $5,374 per pupil.

**Figure 9: Change in Foundation Level Since 1995**

| Year | Foundation Level | Change over Previous Year |
|---|---|---|
| FY 1995 | $2,863 | |
| FY 1996 | $2,949 | $86 |
| FY 1997 | $3,061 | $112 |
| FY 1998 | $3,132 | $71 |
| FY 1999 | $4,225 | $1,093 |
| FY 2000 | $4,325 | $100 |
| FY 2001 | $4,425 | $100 |
| FY 2002 | $4,560 | $135 |
| FY 2003 | $4,560 | $0 |
| FY 2004 | $4,810 | $250 |
| FY 2005 | $4,964 | $154 |
| FY 2006 | $5,164 | $200 |
| FY 2007 | $5,334 | $170 |
| FY 2008 | $5,734 | $400 |

- The Foundation Level does not represent total school expenditures per child. It in fact does not include many basic costs, like transportation and special education. Instead, the Foundation Level is just the minimum amount that all school districts are supposed to have to spend per pupil, through a combination of state and local property tax revenue, to cover the cost of core academic programs.
- The current Foundation Level is not based on any objective, measurable standard. It simply represents what the state believes it can afford. The nonpartisan Education Funding Advisory Board or "EFAB", has created a recommended FY 2008 foundation level of $6,974 that ties the per pupil expense to the actual cost of an academic curriculum of sufficient quality to permit an efficiently operated school district to obtain the result of having two-thirds of its non-at-risk children pass the Illinois standardized tests. For more on EFAB and school funding, see the CTBA issue brief, *The Illinois School Funding Formula and the Distribution of General State Aid,* available online at: http://www.ctbaonline.org/Education.htm
- The proposed Foundation Level increase is still $954 short of the FY 2008 Education Funding Advisory Board recommendation of $6,974.

***The current Foundation Level is not based on any objective, measurable standard. It simply represents what the state believes it can afford.***

## Special Education in FY 2008

- An increase in the reimbursement rate for certified special education teachers from $8,000 per teacher (initially set in 1985) to $9,000 per teacher.
- An increase in the reimbursement rate for non-certified personnel of $700 to $3,500 per non-certified personnel.
  - FY 2008 is the first year the special education personnel rate has been increased since it was implemented in 1985. If the rate had kept up with inflation, it would currently be $19,765 per teacher and $6,918 per non-certified staff member.[11]

## Other Programs

- $5 million to reinstate the gifted education program.
- $12 million for a statewide Mentoring programs.
- $3 million in salary incentives to attract teachers to hard to staff schools.
- $30 million increase in nominal dollars for early childhood education. In real inflation adjusted terms, early childhood education received an increase of $16.5 million.
- After school programs were cut by almost $24 million and arts and foreign language education reduced by $4 million.

***For more on EFAB and school funding, see the CTBA issue brief, The Illinois School Funding Formula and the Distribution of General State Aid, available online at: http://www.ctbaonline.org/Education.htm***

**Figure 10: Funding of Selected Education Programs: FY 2005 – FY 2008. Comparison of Funding: FY 2007-FY 2008**

| Category<br>$ in thousands | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Difference in Nominal (non-inflation adjusted) Dollars FY 2007-FY 2008 | Difference in Inflation Adjusted Dollars: FY 2007-FY 2008 |
|---|---|---|---|---|---|---|
| General State Aid | $3,712,331 | $3,927,439 | $4,166,330 | $4,475,200 | $308,870 | $138,050 |
| Fast Growth Districts | $10,000 | $0 | $0 | $7,500 | $7,500 | $7,500 |
| Special Education | $1,153,821 | $1,126,133 | $1,161,174 | $1,316,900 | $155,726 | $108,118 |
| Illinois Free Lunch/Breakfast | $20,500 | $21,000 | $21,000 | $21,000 | $0 | -$861 |
| Transportation - Regular/ Vocational | $261,630 | $261,630 | $286,118 | $317,500 | $31,382 | $19,651 |
| Fast Growth Grants | $10,000 | $0 | $0 | $7,500 | $7,500 | $7,500 |
| Gifted Education | $0 | $0 | $0 | $5,000 | $5,000 | $5,000 |
| Reading Improvement Block Grant | $76,139 | $76,139 | $76,139 | $76,139 | $0 | -$3,122 |
| Early Childhood Education | $243,254 | $372,254 | $318,255 | $347,861 | $29,607 | $16,558 |
| Teacher and Administrator Mentoring and Induction Program | N/A | N/A | N/A | $5,000 | $5,000 | $5,000 |
| Teacher Mentoring | N/A | N/A | N/A | $7,000 | $7,000 | $7,000 |
| Teacher Mentoring Pilot Program | N/A | N/A | $2,000 | $2,000 | $0 | -$82 |
| Alternative Learning/Regional Safe Schools | $17,035 | $18,035 | $18,536 | $18,536 | $0 | -$760 |
| Bilingual Education | $64,552 | $66,552 | $66,552 | $74,552 | $8,000 | $5,271 |
| Extended Learning Opportunities (Summer Bridges) | $22,238 | $22,238 | $22,238 | $22,238 | $0 | -$912 |
| Agricultural Education | $1,881 | $2,381 | $2,881 | $2,881 | $0 | -$118 |
| Career and Tech Ed Programs | $36,062 | $38,062 | $38,562 | $38,562 | $0 | -$1,581 |
| Illinois Governmental Internship Program | $130 | $130 | $130 | $130 | $0 | -$5 |
| Growth Model | N/A | N/A | N/A | $3,000 | $3,000 | $3,000 |
| System of Support | $3,553 | $5,343 | $3,343 | $3,343 | $0 | -$137 |
| School Security ad Bullying Prevention | N/A | N/A | $6,000 | $0 | -$6,000 | -$6,246 |
| Advance Placement Classes | $0 | $1,500 | $1,500 | $1,647 | $147 | $86 |
| After School Programs | $0 | $12,235 | $25,823 | $3,000 | -$22,823 | -$23,882 |
| Arts and Foreign Language | $0 | $2,000 | $4,000 | $0 | -$4,000 | -$4,164 |
| Class Size Reduction Pilot Programs | N/A | N/A | $10,000 | $8,000 | -$2,000 | -$2,410 |
| Hard to Staff School Incentives | N/A | N/A | N/A | $3,000 | $3,000 | $3,000 |
| Healthy Kids/Healthy Minds/ Expanded Vision | $0 | $3,000 | $3,000 | $0 | -$3,000 | -$3,123 |
| Illinois Economic Education | $100 | $250 | $250 | $250 | $0 | -$10 |

Source: Illinois State Board of Education

General State Aid includes GSA Hold Harmless
Special Education includes Extraordinary Services, Orphanage Tuition, Personnel Reimbursement, Private Tuition, Summer School and Transportation

# HIGHER EDUCATION

Fiscal Year 2008 appropriations for higher education in Illinois are $2,221 billion. A $21 million decrease in real terms over FY 2007 funding levels. Figure 11 displays higher education appropriations since FY 2002. Accounting for inflation based on the Consumer Price Index, real spending for higher education has declined $820 million since FY 2002. Accounting for the Employment Cost Index funding has declined $964 million since FY 2002.

**Figure 11: Historical Higher Education Spending**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002 - FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $2,647 | $2,523 | $2,123 | $2,103 | $2,106 | $2,154 | $2,221 | $13,230 |
| **Prior Year Inflation Adjusted CPI** | | $2,711 | $2,571 | $2,193 | $2,175 | $2,159 | $2,242 | $14,050 |
| **Difference CPI** | | -$188 | -$448 | -$90 | -$69 | -$5 | -$21 | -$820 |
| **Percentage Change CPI** | | | | | | | | -5.84% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $2,756 | $2,611 | $2,199 | $2,189 | $2,192 | $2,247 | $14,194 |
| **Difference ECI** | | -$233 | -$488 | -$96 | -$83 | -$38 | -$26 | -$964 |
| **Percentage Change ECI** | | | | | | | | -6.79% |

Source: Illinois Commission on Government Forecasting and Accountability

# HEALTH CARE

Fiscal Year 2008 Appropriations for health care in Illinois (including the Department of Public Health and the Department of Health Care and Family Services) increased $157 million in real terms over Fiscal Year 2007. Figure 12 displays the change in health care appropriations since FY 2002.

**Figure 12: Historical Health Care Spending**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002 - FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal (dollars)** | $5,398 | $5,236 | $5,822 | $6,167 | $7,544 | $7,910 | $8,391 | $41,070 |
| **Prior Year Inflation Adjusted CPI** | | $5,528 | $5,335 | $6,014 | $6,377 | $7,733 | $8,234 | $39,221 |
| **Difference CPI** | | -$292 | $487 | $153 | $1,167 | $177 | $157 | $1,849 |
| **Percentage Change CPI** | | | | | | | | 4.71% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $5,619 | $5,419 | $6,032 | $6,420 | $7,853 | $8,250 | $39,593 |
| **Difference ECI** | | -$383 | $403 | $135 | $1,124 | $57 | $141 | $1,477 |
| **Percentage Change ECI** | | | | | | | | 3.73% |

Source: Illinois Commission on Government Forecasting and Accountability

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,[12] making health care funding one of the state's greatest challenges. For instance, Illinois' Medicaid program grew at an average annual rate of nine percent between fiscal years 2000 and 2004, while state tax revenue grew at an average annual rate of only 2.5 percent over the same period.[13] Skyrocketing Medicaid costs only compound Illinois' annual revenue shortfalls, resulting in cuts to other vital human services and the financing of a greater portion of government operations with debt rather than tax revenue.

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. Rather, the state has dealt with the predicament another way: by delaying payment of Medicaid bills owed to health care professionals, in many cases for months. By deferring these "Medicaid liabilities," the state essentially pushes costs from one fiscal year to the next, making the state budget appear balanced each year 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.

The state's unpaid Medicaid liabilities have increased from $977 million in 2000, to the current past due amount of $3.4 billion.[14]

# Other State Agencies

**Figure 13 compares General Revenue Fund appropriations for the Department of Human Services.**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002 - FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $3,803 | $3,574 | $3,703 | $3,769 | $3,872 | $3,994 | $4,183 | $23,095 |
| **Prior Year Inflation Adjusted CPI** | | $3,894 | $3,642 | $3,825 | $3,897 | $3,969 | $4,158 | $23,385 |
| **Difference CPI** | | -$320 | $61 | -$56 | -$25 | $25 | $25 | -$290 |
| **Percentage Difference CPI** | | | | | | | | -1.24% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $3,959 | $3,699 | $3,836 | $3,924 | $4,031 | $4,166 | $23,614 |
| **Difference ECI** | | -$385 | $4 | -$67 | -$52 | -$37 | $17 | -$519 |
| **Percentage Difference ECI** | | | | | | | | -2.20% |

Source: Illinois Commission on Government Forecasting and Accountability

**Figure 14 compares General Revenue Fund appropriations for the Department of Corrections.**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002- FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $1,303 | $1,207 | $1,270 | $1,191 | $1,163 | $1,126 | $1,244 | $7,201 |
| **Prior Year Inflation Adjusted CPI** | | $1,334 | $1,230 | $1,312 | $1,231 | $1,192 | $1,172 | $7,472 |
| **Difference CPI** | | -$127 | $40 | -$121 | -$68 | -$66 | $72 | -$271 |
| **Percentage Change CPI** | | | | | | | | -3.62% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $1,356 | $1,249 | $1,316 | $1,240 | $1,211 | $1,174 | $7,546 |
| **Difference ECI** | | -$149 | $21 | -$125 | -$77 | -$85 | $70 | -$345 |
| **Percentage Change ECI** | | | | | | | | -4.58% |



Source: Illinois Commission on Government Forecasting and Accountability

Figure 15 compares General Revenue Fund appropriations for the Department of Agriculture.

**Figure 15: Comparison of Historical Department of Agricultural Spending: Inflation-Adjusted CPI & ECI**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002- FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $79 | $52 | $46 | $41 | $45 | $49 | $49 | $282 |
| **Prior Year Inflation Adjusted CPI** | | $81 | $53 | $48 | $42 | $46 | $50 | $320 |
| **Difference CPI** | | -$29 | -$7 | -$7 | $3 | $3 | -$1 | -$38 |
| **Percentage Change CPI** | | | | | | | | -11.92% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $82 | $54 | $48 | $43 | $47 | $51 | $324 |
| **Difference ECI** | | -$30 | -$8 | -$7 | $2 | $2 | -$2 | -$42 |
| **Percentage Change ECI** | | | | | | | | -12.98% |

Source: Illinois Commission on Government Forecasting and Accountability

Figure 16 compares General Revenue Fund appropriations for the Department of Children and Family Services.

**Figure 16: Comparison of Historical Department of Children & Family Services Spending: Inflation-Adjusted CPI & ECI**

| $ in millions | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2008 | Change FY 2002 - FY 2008 |
|---|---|---|---|---|---|---|---|---|
| **Actual Appropriations (nominal dollars)** | $925 | $838 | $819 | $781 | $810 | $776 | $901 | $4,925 |
| **Prior Year Inflation Adjusted CPI** | | $947 | $854 | $846 | $808 | $830 | $808 | $5,093 |
| **Difference CPI** | | -$109 | -$35 | -$65 | $2 | -$54 | $93 | -$168 |
| **Percentage Change CPI** | | | | | | | | -3.29% |
| | | | | | | | | |
| **Prior Year Inflation Adjusted ECI** | | $963 | $867 | $848 | $813 | $843 | $809 | $5,144 |
| **Difference ECI** | | -$125 | -$48 | -$67 | -$3 | -$67 | $92 | -$219 |
| **Percentage Change ECI** | | | | | | | | -4.26% |

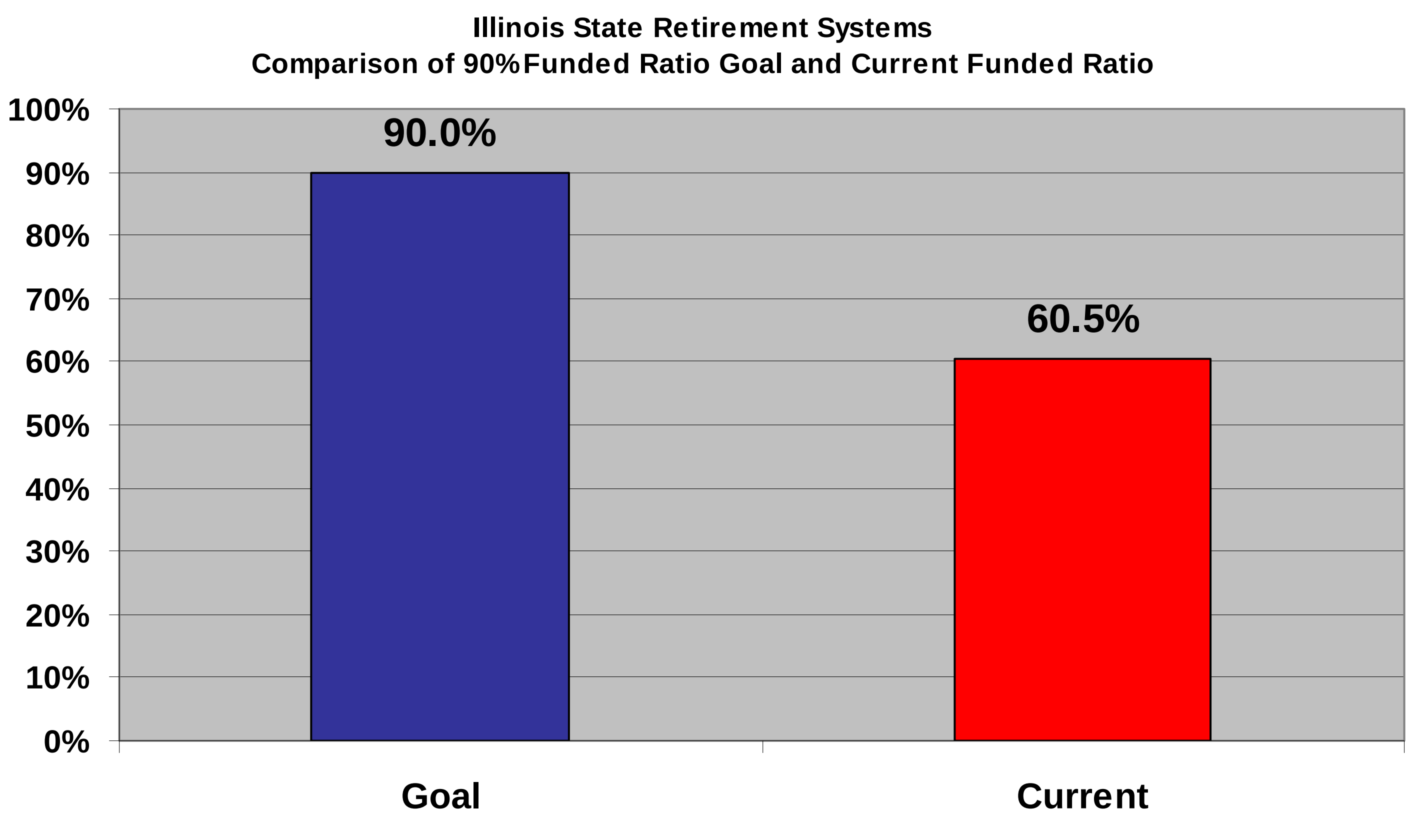
Source: Illinois Commission on Government Forecasting and Accountability

# ILLINOIS STATE RETIREMENT SYSTEMS

The five state employee retirement systems consist of the State Employees' Retirement System (SERS), the State Universities Retirement System (SURS) the Teachers' Retirement System (TRS), the Judges Retirement System (JRS) and the General Assembly Retirement System (GARS). The current unfunded pension liability is $40.7 billion.[15] The "Funded Ratio", for the Illinois Pension System, that is, the percentage of what is required to be funded that has actually been funded, is also one of the worst in the nation. In 2005, Wilshire Associates found that the average national Funded Ratio for a state pension system was 83%.[16] Illinois' Funded Ratio of only 60.5% is significantly below the national average.[17]

Public Act 88-0593 requires the State to make contributions to the State retirement systems such that the funded ratio will equal 90% by Fiscal Year 2045. The contributions are required to be made at a level percent of payroll in Fiscal Years 2011 through 2045, following a phase-in period that began in Fiscal Year 1996.

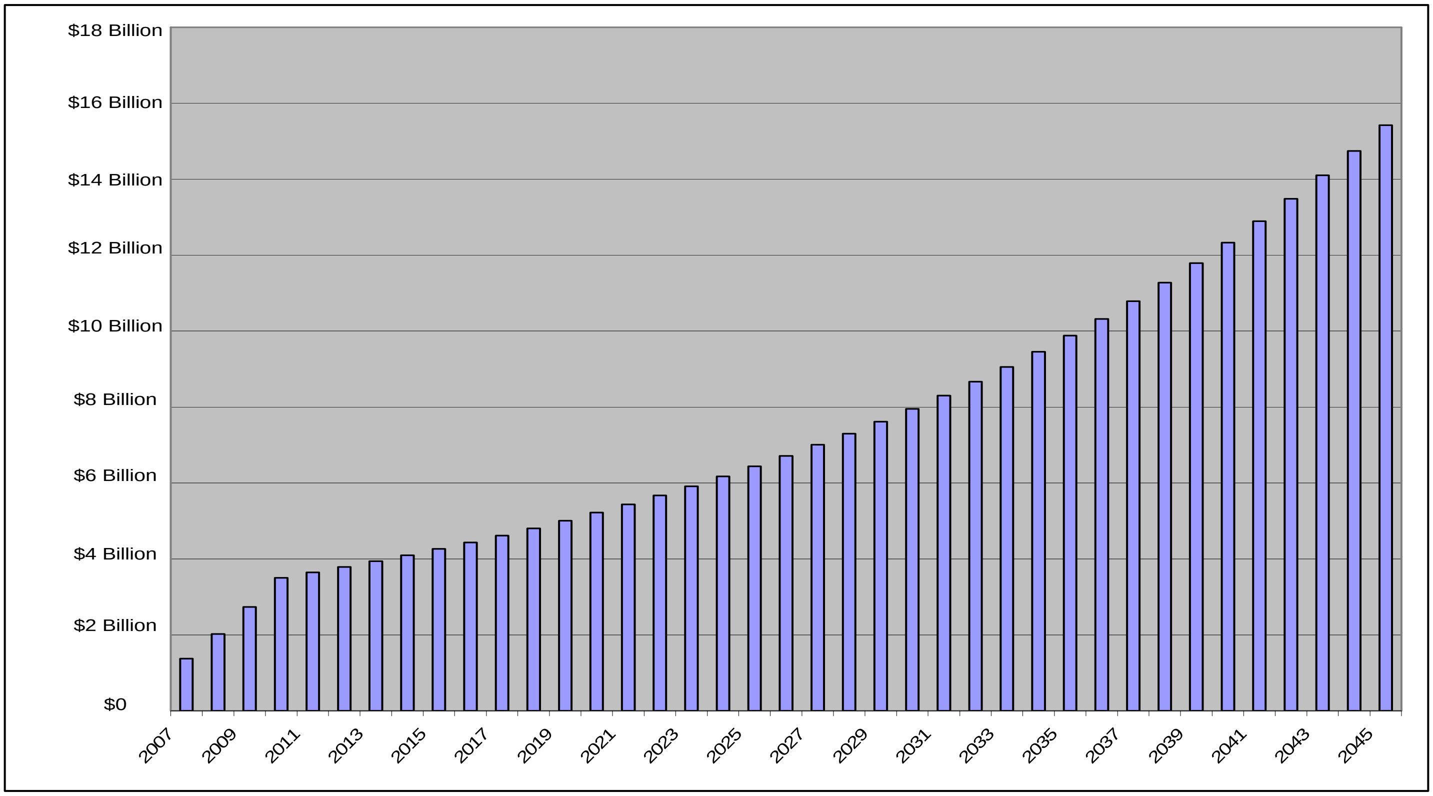
**Figure 17**




Source: Illinois Commission on Government Forecasting and Accountability Report on the Financial Condition of the Illinois Public Retirement System

Looking ahead, it is important to note that the state's required yearly pension payment is scheduled to increase significantly over the next ten years, as shown in Figure 18. Skipping an aggregate of $2.3 billion in required pension contributions in FY 2006 and FY 2007[18] further deferred the state's pension funding problem into the future, threatening the state's ability to continue funding current service levels overtime.

**Figure 18**
**Required Yearly State Pension Payments**




## The FY 2008 Pension Payment

Without modernizing current revenue streams, the state simply will not have the financial capacity to pay its unfunded pension liability plus maintain current services. That said, the pension ramp also is not realistic, so an alternative, long-term payment program makes sense, particularly one that eliminates the ramp and the irresponsible practice of back loading costs.

For FY 2008, the Governor proposed leasing the Illinois lottery at an estimated $10 billion and selling $16 billion in pension obligation bonds to infuse into the pension system and bring the unfunded liability down to $14.7 billion and the funded ratio up to 83 percent. Neither of these proposals were enacted. For more information on the proposals see the CTBA report, *Analysis of the Fiscal Year 2008 Budget Proposal at* [www.ctbaonline.org](www.ctbaonline.org)

***Without modernizing current revenue streams, the state simply will not have the financial capacity to pay its unfunded pension liability plus maintain current services.***

***For more on the Illinois State Pension Systems visit***
***CTBA's special pension research project—The Illinois Retirement Security Initiative:***
***http://www.ctbaonline.org/Pensions.htm***

**Figure 19: FY 2006—FY 2008 Payments to the Illinois State Retirement Systems**

| $ in millions | FY 2006 | FY 2007 | FY 2008 |
|---|---|---|---|
| SERS | | | |
| General Revenue Funds | $220 | $212 | $207 |
| Other State Funds | $0 | $0 | $0 |
| SURS | | | |
| General Revenue Funds | $86,641 | $68,772 | $4,740 |
| Other State Funds | $83,392 | $186,999 | $340,320 |
| TRS | | | |
| General Revenue Funds | $685,039 | $889,140 | $1,185,153 |
| Other State Funds | $0 | $0 | $0 |
| GARS | | | |
| General Revenue Funds | $4,157 | $5,220 | $6,810 |
| Other State Funds | $0 | $0 | $0 |
| JRS | | | |
| General Revenue Funds | $29,189 | $35,237 | $46,873 |
| Other State Funds | $0 | $0 | $0 |
| | | | |
| **Grand Total General Revenue Funds** | **$805,246** | **$998,581** | **$1,243,783** |
| **Grand Total Other State Funds** | **$83,392** | **$186,999** | **$340,320** |
| **GRAND TOTAL** | **$888,638** | **$1,185,580** | **$1,584,103** |

Source: Illinois Commission on Government Forecasting and Accountability, Fiscal Year 2008 Budget Summary.

**Figure 20: Actual Payments to the Illinois Five State Retirement Systems, General Revenue Fund and Other State Funds Combined**

| FY 2006 | FY 2007 | $ Amount Increase Over Previous Year | FY 2008 | $ Amount Increase Over Previous Year |
|---|---|---|---|---|
| $888,638 | $1,185,580 | $296,942 | $1,584,103 | $398,523 |

Source: Illinois Commission on Government Forecasting and Accountability, Fiscal Year 2008 Budget Summary

**Figure 21: Difference in Actual Payments Compared to Required Payments to the Illinois Five State Retirement Systems**

| $ in millions | Required Payment | Actual Payment | Difference |
|---|---|---|---|
| FY 2006 | $2,117 | $889 | -$1,228 |
| FY 2007 | $2,507 | $1,186 | -$1,321 |
| FY 2008 | $2,019 | $1,584 | -$435 |
| Three Year Total | $6,643 | $3,659 | -$2,984 |

Source: Illinois Commission on Government Forecasting and Accountability, Fiscal Year 2008 Budget Summary and Report on the Financial Condition of the Illinois Public Employee Retirement System, July 2007.

# Revenues

As Figure 22 shows, the state will realize $805 million in revenue growth from state and federal sources in FY 2008.

**Figure 22: COGFA Estimated Revenue Growth**

| Estimated Revenue Growth | COGFA |
|---|---|
| From Existing Sources | $704 |
| Federal | $101 |
| **Total Growth** | **$805** |

Center for Tax and Budget Accountability analysis of Illinois Commission on Government Forecasting and Accountability, FY 2009 Economic and Revenue Forecast and Updated FY 2008 Revenue Estimate, March 2008.

Figures 23 and 24 display the difference in the current revenue forecast by COGFA. It illustrates that revenue will not grow sufficiently in FY 2008 to keep pace with the CPI inflation adjusted increases in the costs of simply maintaining FY 2007. The CPI inflation adjusted shortfall in revenues versus costs for FY 2008 projected by COGFA is -$252 million. When adjusting for the more appropriate ECI, the revenue shortfall is worse, increasing to -$303 million.

**Figure 23: FY 2007 Revenue Estimate Comparison (CPI)**

| FY 2008 $ in millions | COGFA |
|---|---|
| **Projected Increase From State Sources** | $704 |
| **Projected Increase From Federal Sources** | $101 |
| **Total Increase** | $805 |
| **Amount Needed to Keep Pace with FY 2007 Inflationary Cost Increases (CPI)** | $1,057 |
| **Difference** | **-$252** |

Source: Center for Tax and Budget Accountability analysis of data from the Illinois Commission on Government Forecasting and Accountability, FY 2009 Economic and Revenue Forecast and Updated FY 2008 Revenue Estimate, March 2008.

**Figure 24: FY 2007 Revenue Estimate Comparison (ECI)**

| FY 2008 $ in millions | COGFA |
|---|---|
| **Projected Increase From State Sources** | $704 |
| **Projected Increase From Federal Sources** | $101 |
| **Total Increase** | $805 |
| **Amount Needed to Keep Pace with FY 2007 Inflationary Cost Increases (CPI)** | $1,108 |
| **Difference** | **-$303** |

Source: Center for Tax and Budget Accountability analysis of data from the Illinois Commission on Government Forecasting and Accountability, FY 2009 Economic and Revenue Forecast and Updated FY 2008 Revenue Estimate, March 2008.

# DEBT AND ONE-TIME REVENUES

Article VIII Section 2 of the Illinois Constitution requires that the state produce a balanced budget each year. The specific constitutional language provides: "Appropriations for a fiscal year shall not exceed funds estimated by the General Assembly to be available during that year."

- This means the revenue forecast for a fiscal year must at least equal all budget appropriations for that year.
- Actually creating a balanced budget has eluded decision makers for decades. Consider last fiscal year, FY 2007 budget: the state used over $4.8 billion in one-time revenues and deficit spending to balance the budget. Put another way, in FY 2007 the state spent $4.8 billion more than it had the revenue to cover.

**Figure 25**
**Effective Deficit Spending FY2007**

| One-Time Revenues and Deficit Spending ($ in millions) | FY 2007 |
|---|---|
| Fund Sweeps | $188 |
| Chargebacks | $98 |
| Deferred Medicaid Payments | $3,400 |
| Underfunding of Required State Pension Contribution | $1,133 |
| **Total** | **$4,819** |

Figure 26 shows Illinois will continue to rely on significant infusions of debt and one-time revenue sources to fund services in FY 2008. For example, the Illinois Comptroller estimates the state will artificially balance its FY 2007 budget by again deferring its obligation to pay providers of Medicaid health care services to FY 2008.[19] Borrowing and utilization of other one-time revenue sources like fund sweeps to pay for current operations has become common practice because the Illinois revenue system cannot cover current public service costs.[20]

Public Act 95-233 or the "Franchise Tax and License Fee Amnesty Act of 2007" should bring in additional revenue in FY 2008 to help offset this deficit. The act allows eligible corporations to pay delinquent license fees and franchise taxes without incurring any statutorily imposed penalty or interest. As reported by the Commission on Government Forecasting and Accountability, the unofficial budget estimate was that this loophole closures may generate up to $90 million in fiscal year 2008.[21]

Further, the Illinois Comptroller's Office reports that Public Act 95-707 (the BIMP) should generate an estimated $268 million in income tax revenue through the re-calculation of Income Tax Refund fund allocations. That Act will also allow the governor the discretion to utilize other education funds to make General State Aid to Education payments, in effect freeing up General Revenue Fund dollars.[22]

**Figure 26**
**FY 2008 Estimated Budget Deficit**

| Category | Dollar Amount |
|---|---|
| Forecasted FY 2008 Revenue Increase | $805 |
| Dollar Amount Necessary to Keep Up with the Inflation Costs of Continuing FY 2007 General Fund Levels | -$1,057 |
| Dollar Increase in the Required FY 2008 Pension Funding Payment Over FY 2007 | -$650 |
| Dollar Amount of Unpaid Medicaid Bills in FY 2007 Carried Over to FY 2008 | -$3,400 |
| Dollar Amount of FY 2007 One Time Revenues Used to Balance Budget (Fund Sweeps and Charge Backs) Not Available in FY 2008. | -$286 |
| **Total Estimated FY 2008 Deficit** | **-$4,588** |

# Historical One-Time Revenues Used to Fund Current Services

To close the gap between revenues and expenditures, the state employs unsound fiscal tactics, which either generate one-time unsustainable revenues or defer current obligations to future fiscal years. In both cases, these tactics ultimately make the situation worse. In fact, rather than actually balance the state's budget in any given fiscal year, utilization of these stratagems merely masks the inability of the state's tax system to generate the revenue necessary to support ongoing services. As Figure 27 details, Illinois has used almost $13 billion in one-time revenue fund sweeps and expenditure deferrals over the past five years to close gaping deficits in the General Funds.

**Figure 27: Unstable, Non-Recurring Tactics Used to Fund Current Services**

| $ in millions | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | TOTAL |
|---|---|---|---|---|---|---|
| Fund Sweeps | $165 | $159 | $260 | $129 | $188 | **$901** |
| Chargebacks | | $269 | $208 | $140 | $98 | **$715** |
| Executive Order 10 | | $6 | | | | **$6** |
| Increased Fee Transfers | | $89 | $38 | $35 | | **$162** |
| Tax Amnesty | | $290 | $100 | | | **$390** |
| Pension Bond Sale | $300 | $1,860 | | | | **$2,160** |
| Cigarette Tax Adjustment | | | $50 | | | **$50** |
| Federal Fiscal Relief | | $675 | | | | **$675** |
| Deferred Medical Payments to Next Fiscal Year | | $1,348.0 | $2,949 | $2,300 | $3,400 | **$6,349** |
| Restructure of ERI Pension Payment | | | $200 | | | **$200** |
| Increase in State Pension Fund Approps | | | $80 | | | **$80** |
| Increase in non-IDOT Road Fund Approps | $95 | $145 | $145 | | | **$385** |
| Pension Underfunding | | | | $1,178 | $1,133 | **$2,311** |
| | | | | | | |
| **Total** | **$560** | **$3,493** | **$4,030** | **$1,482** | **$4,819** | **$14,384** |

## Short Term Borrowing

Short-term borrowing is sometimes appropriate to help with cash flow or to weather one-time revenue shortfalls caused by a recession or unique event (like significant flood damage). Borrowing to pay for public services is problematic, however, if used to cover ongoing revenue shortfalls caused by structural inadequacies in a fiscal system. In such cases, natural revenue growth will never catch-up with both the cost of repaying the debt, plus interest, and the inflationary cost of maintaining public services over time. This is exactly what is happening in Illinois. Over the past six years, the state has short term borrowed over $7.2 billion, mostly to pay Medicaid bills. Prior to FY 2002, the state had not practiced short term borrowing in over five years, since it borrowed $500 million in FY 1996.

**In the three years since FY 2006 alone, the state has paid over $30 million in interest payments on short-term bor-**

**Figure 28: Historical Short-Term Borrowing**

| Fiscal Year Short Term Borrowing | $ Amount in Millions | Reason |
|---|---|---|
| FY 2008 | $1,200 | Medicaid Bills |
| FY 2007 | $900 | Medicaid Bills |
| FY 2006 | $1,000 | Medicaid Bills |
| FY 2005 | $765 | Medicaid Bills |
| FY 2004 | $850 | Medicaid Bills |
| FY 2003 | $1,500 | Medicaid Bills, K-12 State Aid Payments, Income Tax Refunds, Long Term Care Payments |
| FY 2002 | $1,000 | Medicaid Bills, Income Tax Refunds, Long Term Care Payments |
| **Total** | **$7,215.00** | |

Source: Illinois Commission on Government Forecasting and Accountability, 2007 Bonded Indebtedness Report

# CONCLUSION

Overall, the FY 2008 budget continues to show the state is not on sound fiscal footing. Budget stress stemming from increased health care costs and yearly required pension payments make it necessary to modernize how Illinois taxes to raise revenue. However, instead of implementing fair and modern reforms to allow the state to provide necessary public services, the state has again chosen balance the budget by deferring Medicaid payments to providers and sweeping funds.

Implementing comprehensive fiscal reform that modernizes the Illinois tax system is the only way to provide the ongoing revenue necessary to sustain these important programs. Illinois should reform its tax system to comport with the modern economy and assess tax burden more fairly among taxpayers. For further analysis and ideas on how the state should implement these fiscal reforms please visit www.ctbaonline.org

# ENDNOTES

1. Illinois Commission on Government Forecasting and Accountability (COGFA), FY 2008 Budget Summary.
2. Center for Tax and Budget Accountability analysis of historical revenue data compared to the Bureau of Labor Statistics, Con sumer Price Index.
3. *See* Center for Tax and Budget Accountability, *Private Sector Job Trends and the Illinois Structural Deficit*, January 2007.
4. Based on Illinois State Comptroller data on unpaid Medicaid liabilities, COGFA FY 2008 revenue data and COGFA FY 2007 fund sweeps revenue not available in FY 2008.
5. *See* Center for Tax and Budget Accountability, Analysis of the Gross Receipts Tax, April, 2007.
6. COGFA, FY 2008 Revenue Forecast, March 2008.
7. State of Illinois FY 2008 Recommended Budget.
8. Ibid.
9. COGFA, FY 2008 Budget Summary.
10. Center for Tax and Budget Accountability analysis of COGFA FY 2008 revenue projections and FY 2007 final revenue data.
11. Inflation based on Bureau of Labor Statistics, CPI-U.
12. *See* The Kaiser Family Foundation and Health Research and Educational Trust, *Employer Health Benefits 2005 Annual Survey*, September 2005.
13. *See* State of Illinois Comptroller, "Medicaid Continues to Challenge State Budgets," *Fiscal Focus*, May 2005 (Medicaid liability growth); *See* Illinois Commission on Forecasting and Accountability for revenue data.
14. Illinois Comptroller Dan Hynes Fiscal State of the State letter to the Illinois General Assembly, February, 2008.
15. COGFA, *2007 Report on the Public Employee Retirement Systems*, July, 2007.
16. 2005 Wilshire Report on State Retirement Systems: Funding Levels and Asset Allocation.
17. COGFA, *2007 Report on the Public Employee Retirement Systems*, July, 2007.
18. COGFA, Report on the 90% Funding Target of Public Act 88-0593.
19. Illinois Comptroller Dan Hynes Fiscal State of the State letter to the Illinois General Assembly, February, 2008.
20. Center for Tax and Budget Accountability, *Revenue Performance is the Primary Cause of Illinois Chronic Budget Deficits* available at www.ctbaonline.org
21. Illinois State Comptroller, Fiscal Focus, January 2008.
22. Ibid.
23. COGFA, 2007 Bonded Indebtedness Report.