The Institute for Illinois' Fiscal Sustainability

AT THE CIVIC FEDERATION

STATE OF ILLINOIS FY2011 RECOMMENDED OPERATING AND CAPITAL BUDGETS:

Analysis and Recommendations

April 26, 2010

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The Civic Federation is an independent, non-partisan government research organization working to maximize the quality and cost-effectiveness of government services in the Chicago region and State of Illinois.

The Civic Federation
would like to express its gratitude
to the John D. and Catherine T. MacArthur Foundation,
whose generous grant to fund
the Institute for Illinois' Fiscal Sustainability at the Civic Federation
made the research and writing of this report possible

ACKNOWLEDGEMENTS

The Civic Federation would like to express our appreciation to David Vaught, director of the Governor's Office of Management and Budget, and his staff for their assistance with this report. We also appreciate the assistance provided by the Commission on Government Forecasting and Accountability and the Department of Healthcare and Family Services.
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EXECUTIVE SUMMARY

The Civic Federation **opposes** Governor Pat Quinn's $52 billion FY2011 recommended operating budget for the State of Illinois because it is unbalanced and does too little to address the State's fiscal crisis. The Governor's recommended budget borrows billions to pay for operations while continuing to ignore the massive backlog of unpaid bills, which will make the State's financial condition worse.

Although the Civic Federation is **encouraged** that Governor Quinn has signed significant pension reform legislation and recommends some reductions in spending, we **cannot support** his FY2011 State of Illinois operating budget because it does not effectively stabilize state finances or substantially reduce the State's $12.9 billion deficit going into FY2011.

The Governor's FY2011 budget recommendation would create a $10.6 billion deficit, consisting of an operating deficit of $4.7 billion and a carry forward deficit of $5.9 billion from the prior year. The recommended budget proposes borrowing $4.7 billion to close the operating deficit. Even after borrowing to pay for the operating deficit, the State will end FY2011 with the same carry forward deficit of $5.9 billion.

Due to the carry forward deficit, the Governor proposes pushing over $6.2 billion in bills into the next fiscal year. There is also a possibility that the State might borrow to pay its statutorily required pension contributions in FY2011 rather than contributing to the retirement systems through operating funds. The Civic Federation **opposes** borrowing to pay for pensions because pensions are an annual operating expense and the use of debt is not sustainable and adds to the State's mounting debt service burden, increasing future pressures on the operating budget.

The Governor's recommended FY2011 budget includes a $1.5 billion net reduction in appropriations to departments, consisting of $2.2 billion in departmental cuts that are partially offset by $636.8 million in departmental increases. The recommended cuts are heavily concentrated in education and reduce the base level per pupil funding for schools. The Governor's FY2011 budget also decreases the share of existing income tax proceeds passed to local governments. The Civic Federation has great reservations about an approach to reducing state expenditures that shifts costs to other governments, which may accelerate the need to raise property taxes and other local taxes.

In his budget address on March 10, 2010, Governor Quinn suggested that a one-percentage point increase in the personal income tax rate could be used to avert his proposed reductions in education spending, pay down outstanding education bills and restore local government funding through the income tax. However, the Governor did not include any details of this proposal in his formal budget recommendation.

Six weeks after his budget address, the Governor's Office of Management and Budget provided further information on a possible income tax increase in a proposal to legislative leaders. The alternative budget plan reduces the FY2011 year-end deficit from $5.9 billion to $2.9 billion.[1]

[1] Email communication between Civic Federation and Governor's Office of Management and Budget, April 20, 2010.

The alternative plan also increases total borrowing for operations by $1 billion, including borrowing to pay the State's pension contributions. The plan makes unspecified additional cuts and suggests raising additional revenue through a series of consumer and business tax changes. The Civic Federation continues our opposition to the Governor's alternative plan because it relies even more heavily on borrowing and proposes to raise taxes primarily to avert spending cuts rather than to pay down the deficit or reduce the State's other growing liabilities.

At the same time that the Governor's budget recommendation does little to address the State's massive deficit in FY2011, his capital budget proposes reauthorization and expansion of state spending on capital projects. The Civic Federation **opposes** the heavily debt-funded $30.5 billion capital budget because it is not based on a transparent and comprehensive capital improvement plan and will increase state debt costs well beyond the new revenues passed to support it. It is fiscally irresponsible to borrow $19 billion of new debt to fund capital projects over the next five years without a strategic plan for the infrastructure investments and while the State cannot afford to pay its current operating expenses.

Although the Civic Federation has serious concerns about many aspects of the FY2011 operating and capital budgets, we **commend** the Governor and General Assembly for taking a significant step towards meaningful pension benefit reform. In addition, the Governor's plan in the FY2011 budget to require all retirees to pay a share of their health insurance premiums is a much needed reduction of a relatively generous benefit.

The Civic Federation offers the following key findings on the State of Illinois' FY2011 budget:

- The Governor expects total General Funds revenues of $27.4 billion, which represents a projected $210 million state-source revenue increase from FY2010 and a drop of $711 million in federal-source revenues;
- The increased federal Medicaid match is scheduled to expire on December 31, 2010, but the Governor's budget includes roughly $450 million in General Funds revenues from the extension of the enhanced Medicaid match for the entirety of FY2011;
- The FY2011 recommended operating budget totals $52.0 billion, of which $24.8 billion are General Funds appropriations;
- The Governor recommends $2.2 billion in total General Funds departmental cuts from the FY2010 enacted budget. The cuts include $1.2 billion to elementary and secondary education, $94.3 million to higher education and $254.5 billion to the State's contributions for retiree health care;
- **The proposed General Funds cuts of $2.2 billion to 61 departments and agencies, mainly to education and human services, are offset by $636.8 million in increases to 15 other departments, mostly in the State's Medicaid agency. In total, this results in net cuts of $1.5 billion;**
- In addition to appropriations reductions, the Governor recommends reducing local governments' share of the income tax from 10% to 7%, a cut of $308 million;
- The Governor proposes to reduce FY2011 required contributions to the retirement systems certified under the 1995 law by $267 million based on a "pension stabilization"

plan that involves a two-tier pension system. Legislation to implement the plan was enacted on April 14, 2010;[2]
- Total recommended General Funds expenditures, including debt service and other statutorily required transfers, are $32.1 billion;
- The General Funds budget deficit going into FY2011 is $12.9 billion, composed of a $7.0 billion operating deficit in FY2011 and a $5.9 billion carryover deficit from FY2010;
- After the Governor's recommended budget cuts, the FY2011 projected operating deficit is $4.7 billion. The Governor proposes to borrow to fund the operating deficit, but no information on the cost or term of the borrowing notes is included in the FY2011 budget;
- The Governor's budget does not address the $5.9 billion deficit carried forward from FY2010; and
- The Governor's capital budget recommends new appropriations of $4.3 billion in FY2011 on top of the $26.2 billion reappropriated from FY2010. Excluding the State's user fee-funded road and transit program and federally-funded capital projects, the State will increase new capital spending by $2.2 billion in FY2011, $1.6 billion of which will be debt funded.

The Civic Federation **opposes** the following components of the Governor's recommendations in the FY2011 operating and capital budgets:
- Borrowing $4.7 billion to fund operations including the contributions to the retirement systems and not addressing the State's $6.2 billion backlog of bills;
- Reauthorization of the heavily debt funded $26.2 billion in capital reappropriations and the proposed $4.3 billion increase in new capital spending because it is not based on a comprehensive capital improvement plan (CIP) and the revenues approved are not enough to support the estimated $19 billion in borrowing over the next five years;
- A reduction of $267 million in the State's pension contributions in FY2011 unless the retirement systems certify that the new contribution levels comply with statutory funding requirements;[3] and
- Although it is not included in the formal budget proposal, the Governor suggests that the personal income tax rate be increased from 3% to 4% to offset cuts to education spending, pay down some education bills and restore local government funding through the income tax. The Civic Federation opposes the one-percentage point increase to the income tax because it does not effectively address the State's financial crisis, and it is not tied to significant reductions in state spending and comprehensive pension reform.

The Civic Federation is **supportive of some aspects** of the Governor's FY2011 operating budget:
- The pension reforms enacted by the General Assembly in Public Act 96-0889 as a significant first step toward reforming state pension costs by reducing benefits for future employees, but to reduce its substantial unfunded pension liabilities the State needs to address the benefits of current employees;

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[2] After the pension reform legislation was enacted, the Governor increased his estimate of FY2011 savings on the State's pension contributions to $382 million, according to an email communication between the Civic Federation and the Governor's Office of Management and Budget on April 15, 2010.
[3] Ibid.

- The Governor's proposed net cuts to state appropriations totaling $1.5 billion, but significantly more reductions are needed;
- Reduction of $254.5 million to the State's costs by requiring increased participant contributions for retiree health care;
- Medicaid-related state spending cuts of $70 million by increasing participant contributions to the Illinois Cares Rx program, which is not federally funded;
- The Governor's initial steps to implement a managed care pilot program for disabled and elderly Medicaid recipients; and
- The Governor's initiation of a performance management system as enacted last year by the Public Accountability and Performance System Act.[4]

The Civic Federation offers a number of recommendations intended to improve the State's financial condition, institute sound management practices and reduce costs:

- Implement additional pension reforms including funding state contributions at the certified amount from existing operating revenues;
- Address the benefits and contributions of current employees to reduce the State's substantial unfunded pension liabilities;
- Other pension reforms needed include applying the cost-of-living-adjustment provisions of the pension reform bill to the General Assembly and Judges' pension funds, and requiring balance on pension boards between employees, management and taxpayers;
- Develop alternatives to institutional care for recipients of Medicaid and other state aid, which would be in line with court rulings;
- Develop and implement a formal long-term financial planning process that is shared with and/or reviewed by key policymakers and stakeholders;
- Implement a capital improvement plan to explain prioritization of projects in the capital budget or the overall needs assessment for all state-owned assets;
- Improve the budget document format by including comprehensive data with respect to the State's personnel expenses; and
- Consolidate special purpose funds in order to have maximum flexibility in allocating resources to meet policy priorities.

[4] 30 ILCS 25/3 (2009).

CIVIC FEDERATION POSITION

The Civic Federation **opposes** the FY2011 State of Illinois operating budget of $52.0 billion because it is unbalanced and fails to effectively stabilize state finances or improve the fiscal crisis that has led to a $12.9 billion deficit going into FY2011. Governor Quinn's FY2011 recommended budget would create an operating deficit of $4.7 billion, which the Governor proposes to close through borrowing. In addition, the State would still end FY2011 with a deficit of $5.9 billion carried forward from the prior year, even after borrowing to pay for the operating deficit. Due to the carry forward deficit, the Governor proposes continuing to delay payment on a balance of $6.2 billion in bills for another entire fiscal year.

The Governor's budget staff has indicated that the State may borrow to pay the statutorily required pension contributions in FY2011, as was done in FY2010. Such pension borrowing would add to the State's mounting debt service burden and increase future pressures on the operating budget. The Civic Federation **opposes** borrowing to pay for pensions because debt is not a sustainable funding source and adds to the State's mounting debt service burden, increasing future pressures on the operating budget.

The Governor's recommended FY2011 budget includes a $1.5 billion net reduction in appropriations to departments, consisting of $2.2 billion in departmental cuts that are partially offset by $636.8 million in departmental increases. The recommended cuts are heavily concentrated in education and reduce the base level per pupil funding for schools. The Governor's FY2011 budget also decreases the share of existing income tax proceeds passed to local governments. The Civic Federation has great reservations about an approach to reducing state expenditures that shifts costs to other governments, which may accelerate the need to raise property taxes and other local taxes.

In his budget address on March 10, 2010, Governor Quinn suggested that a one-percentage point increase in the personal income tax rate could be used to avert the proposed reduction in education spending, pay down outstanding education bills and restore local government funding through the income tax. However, the Governor did not include any details of this proposal in his formal budget recommendation.

Six weeks after his budget address, the Governor's budget office provided further information on a possible income tax increase in a proposal to legislative leaders. The alternative budget plan reduces the FY2011 year-end deficit from $5.9 billion to $2.9 billion.[5] The alternative plan also increases total borrowing for operations by $1 billion, including borrowing to pay the State's pension contributions. The plan makes additional cuts and raises additional revenue through a series of consumer and business tax changes. The Civic Federation **opposes** the alternative budget plan because it continues to rely too heavily on borrowing for operations and the proposed tax increase is aimed primarily at reversing spending cuts rather than paying down the deficit or other growing state liabilities.

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[5] Email communication between Civic Federation and Governor's Office of Management and Budget, April 20, 2010.

Although the Civic Federation has serious concerns about many aspects of the FY2011 operating and capital budgets, we **commend** the Governor and General Assembly for taking a significant step towards meaningful pension benefit reform. The pension reform legislation signed by the Governor on April 14, 2010 includes reasonable reductions in retirement benefits for new employees that will substantially decrease the State's pension liabilities and expenses over time.[6] However, the enacted pension reforms do not apply to the benefits of current employees, so they do not address the existing unfunded pension liabilities of the State. Further, the reforms do not effectively address the State's inability to fund the statutorily required contributions to the retirement systems from existing operating resources. In addition, the Governor's plan in the FY2011 budget to require all retirees to pay a share of their health insurance premiums is a much-needed improvement to a very expensive state health insurance program.

Issues the Civic Federation Opposes

The Civic Federation opposes the following aspects of the Governor's recommendation for the FY2011 State of Illinois operating and capital budgets.

Borrowing $4.7 Billion for Operating Expenses

The Governor's FY2011 budget recommendation depends heavily on borrowing to pay for operating expenses. The budget includes a proposal to borrow $4.7 billion in "voucher payment notes," which have not been effectively defined or statutorily authorized. Fundamentally, the Federation opposes borrowing schemes that allow operating expenditures to exceed available revenues and push the cost of these operating liabilities into future budget years. Borrowing for operations increases the strain on the State's future finances by increasing mandatory debt service payments and does not address structural budgetary imbalances.

The Civic Federation cannot support a budget for Illinois that continues to borrow to pay for operating expenses. The State borrowed $3.5 billion in FY2010 to make its statutorily required pension contributions, thus freeing up funds for additional state spending. The funds made available for operations through pension borrowing amounted to 11.9% of total General Funds expenditures in FY2010. The State will now have to pay $803 million in debt service on the FY2010 pension bonds and set aside an additional $345 million for a statutory transfer of pension bond debt service in FY2011. The State will pay an additional $800 million in debt service on the FY2010 pension bonds for the next five years in order to cover contributions to the retirement systems for one year.

Even before any of the proposed new debt for operations is issued, debt service will increase by 41.7% from FY2010 to FY2011, to a historic high of $2.9 billion. The $4.7 billion of debt-funded operations represents 14.5% of total General Funds expenditures in FY2011. Despite the proposed borrowing, the State would still end FY2011 without paying an estimated $6.2 billion in unpaid bills carried over from FY2010.

The State provides no information in the FY2011 budget documents detailing the term or costs of the proposed "voucher payment notes." However, the State currently does not appear to have

[6] Public Act 96-0889.

authority to issue bonds for longer than one year to pay directly for operating costs or current bills. The State would need to approve a new statute by a three-fifths vote of the General Assembly to authorize this new type of borrowing. This would set a dangerous precedent for future borrowing for operations and would likely be viewed negatively by the financial markets and credit rating agencies. All three major debt-rating agencies have downgraded the State's debt rating due to inaction on addressing the structural deficit in FY2010 and currently have the State on a negative watch. The rating agencies' reports on Illinois call for the State to address its structural deficit in a meaningful and permanent way or face further downgrades. Borrowing to fund operations does not address the State's structural deficit in a meaningful or permanent way.

Borrowing for Pensions

Nearly half of the State's total $28.0 billion in outstanding debt is attributed to pension borrowing. In addition to the $3.5 billion that was borrowed in FY2010, the State borrowed $10 billion in FY2003 to help pay down unfunded pension liabilities and finance required retirement systems contributions in FY2003 and FY2004. The Governor's budget recommendation does not refer to additional pension borrowing in the FY2011 budget, but the Governor's staff has publicly advocated issuing additional Pension Obligation Bonds as part of a "strategic" borrowing plan being considered by the Governor's office.[7]

The cost of funding the State's retirement systems is an operating cost that should be paid for with operating revenues. Borrowing compounds the cost of state pension programs because of the debt service costs associated with the bonds.

The State's retirement systems are severely underfunded, with unfunded liabilities of $62.4 billion as of June 30, 2009 and a combined funded ratio of 50.6%.[8] According to the Pew Center on the States, Illinois' retirement systems had the lowest funded ratio among all states as of June 30, 2008.[9] Increasing the pressure on the State's General Funds by issuing more pension debt will make it more difficult for Illinois to fund its pensions in future years and will accelerate the State's financial deterioration.

The Civic Federation opposes any further borrowing by the State of Illinois to make its required annual contributions to the retirement systems.

Failure to Pay $6.2 Billion in Unpaid Bills

In order to carry forward a budget deficit from one fiscal year into the next, the State defers the payment of bills into the first two months of the next fiscal year, paying them with the available cash

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[7] Presentation by David Vaught, Director of the Governor's Office of Management and Budget, to members of the Civic Federation Board of Directors, April 5, 2010.
[8] Commission on Government Forecasting and Accountability, Report on the Financial Condition of the Illinois Retirement Systems as of June 30, 2009, March 2010, p.18. These numbers are based on an asset smoothing calculation method, required by Public Act 96-0048, that averages unexpected investment gains and losses over five years. Under the market value method previously used by the State, unfunded liabilities totaled $77.8 billion and the funded ratio stood at 38.5%.
[9] Pew Center on the States, *The Trillion Dollar Gap*, February 2010, p. 5, http://downloads.pewcenteronthestates.org/The_Trillion_Dollar_Gap_final.pdf (last visited on April 13, 2010).

from next year's revenues.[10] The State ended FY2009 with $4.0 billion backlog of unpaid bills in order to carry forward a $3.7 billion General Funds budget deficit and maintain a year-end positive cash balance. The Governor's recommendation shows the State will increase its backlog of bills by $2.2 billion to $6.2 billion by the end of FY2010 in order to carry forward a $5.9 billion deficit. However, under the Governor's recommendation, the State would continue to hold a $6.2 billion backlog of bills at the end of FY2011 in order to carry forward a $5.9 billion deficit into FY2012. The Civic Federation cannot support an unbalanced budget proposal that continues to rely on ignoring such a massive backlog of unpaid bills.

Many residents, public employees, social service agencies and local governments are facing substantial difficulties because of the State's financial problems.[11] Illinois' backlog of unpaid bills has risen to unprecedented levels and the lag time in paying bills has nearly doubled from a year earlier.[12] The delay in paying bills was as long as 92 business days at the end of December, compared with at most 48 days a year earlier. Transfers to Other State Funds from General Funds were delayed as much as 122 days at the end of December.

At the end of March of 2010, the backlog of unpaid bills at the Illinois Office of the Comptroller stood at $4.5 billion, up from $3.4 billion at the same time a year earlier.[13] Some social service agencies that rely on state funding are facing severe financial stress.[14] Record payment delays are also affecting grants to local school districts and payments to universities, local governments and transit districts.[15] The estimated growth in the backlog of bills to $6.2 billion will only increase payment delays and worsen the effect on agencies that provide services for the State or rely on state funding.

Expanding and Reauthorizing the Capital Budget

Even as the State of Illinois struggles to cope with a massive backlog of unpaid bills and growing a General Funds deficit, the Governor proposes continued expansion of the State's capital budget funded mostly by issuing more long-term state debt. Last year, the Civic Federation opposed the Governor's proposed $26.0 billion *Illinois Jobs Now!* capital budget because it was not based on a comprehensive capital improvement plan (CIP) and was unaffordable over time. However, the General Assembly passed a $30.5 billion capital budget for FY2010 based on the Governor's

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[10] As part of the Governor's suggested alternative plan offered to legislative leaders on April 20, 2010 to raise the income tax and borrow more for operations, the Governor also proposes extending the lapse period from two months to six months.

[11] For further discussion on the impact of payment delays, see The Civic Federation, *A Fiscal Rehabilitation Plan for the State of Illinois*, February 22, 2010, http://civicfed.org/sites/default/files/IllinoisFiscalRehabilitationPlan.pdf.

[12] Illinois Office of the Comptroller, "Fiscal Position Continues Downward Slide," *Comptroller's Quarterly,* January 2010, p. 1, at http://www.ioc.state.il.us/ioc-pdf/CQJanuary10.pdf (last visited on January 25, 2010).

[13] Illinois Office of the Comptroller, "Cash Position Deteriorates as State Begins to Repay Short-Term Borrowing," Comptroller's Quarterly, April 2010, p. 1, at http://www.apps.ioc.state.il.us/ioc-pdf/CQ_35.pdf (last visited on April 12, 2010).

[14] AARP Illinois, "State $200 Million Behind in Payments to Agencies Providing Care to Thousands of Older Illinoisans," news release, December 10, 2009, at http://www.aarp.org/community/portfolio/journals/getBlogEntryByMonth.jsp?membername=AARPIL&monthNum=11&year=2009 (last visited on January 22, 2010).

[15] Illinois Office of the Comptroller, Illinois Office of the Comptroller, "Fiscal Position Continues Downward Slide," *Comptroller's Quarterly,* January 2010, p. 2.

proposal, which included approximately $14 billion in new debt-funded capital projects. In FY2011, the Governor proposes a capital budget that reauthorizes $26.2 billion in unspent appropriations and expands the capital budget by an additional $4.3 billion. Of the total $30.5 billion in appropriations proposed for FY2011, new debt funded capital projects increase by $1.6 billion and reappropriated projects total $16.8 billion, bringing the total estimated bond-funded projects to $18.4 billion over the next five years. Although the State will retire an estimated $5.5 billion in debt over the same period, the State's total capital debt will increase by $12.9 billion, or 83%.

The Civic Federation recognizes the need for infrastructure investment in Illinois to maintain the current state-owned assets for the safety of residents and to ensure a vital state economy. **However, the Federation cannot support capital spending that is not directly linked to a comprehensive CIP and supported by reliable revenue to pay for bonds needed to support these projects.** The Civic Federation opposes the reauthorization of the debt-funded portion of the capital budget and the increase in debt funded spending until the State establishes a transparent and needs-based CIP for all capital spending.

The Governor's recommendation does not indicate the prioritization of projects or when projects approved will receive funding. The largest portion of the capital funding, totaling $20.6 billion, is designated by purpose and is not tied to specific projects goals, cost estimates or completion timelines.

The proposed capital borrowing will increase the State's annual debt service payment by $1.2 billion, or 81.8%, between FY2010 and FY2016. Although some revenues were passed in FY2010 to support the new capital borrowing, the sources appear insufficient to support long-term debt service needs. The revenue for the capital bill included an increase in vehicle and license fees, expanding the sales tax to candy, sweetened beverages and some personal hygiene products, a lease of the marketing operations for the state lottery, increased tax on alcoholic beverages and taxing legalized video poker. The State's estimates of the annual revenue that will be produced from these sources have dropped considerably. The largest decrease is attributed to more than 50 communities and the City of Chicago opting not to legalize video poker, which is estimated to reduce the annual revenue for capital by $100.2 million to $189.7 million for debt service. Despite approving $5.8 billion in new borrowing to begin the capital program in FY2010, the State had only sold $1.9 billion in capital bonds and spent $394 million on actual projects as of February 28, 2010, demonstrating an overall lack of planning and the subsequent inefficiency in the capital program.

Without the proper planning and transparency provided by a CIP, the residents of Illinois cannot be assured that the *Illinois Jobs Now!* program will properly address the capital needs of the State. At the same time, the new proposed debt levels will put a stranglehold on any further capital borrowing for decades to come. Citizens of Illinois deserve a concrete multi-year plan before being asked to support an extremely high level of indebtedness that will limit any additional borrowing for decades to come and result in higher fees and taxes to support the capital budget.

Issues the Civic Federation Supports

The Civic Federation supports several components of the Governor's recommended FY2011 budget.

Expenditure Reductions

The Governor proposes reducing state appropriations by $1.5 billion, net of increases, in FY2011. The Civic Federation is supportive of the Governor's initial efforts to cut spending but considerably more is needed and we encourage more reductions. However, the proposed cuts also shift some costs to other governments, such as a $613 million reduction in General State Aid to elementary and secondary education. In addition to appropriations cuts, the Governor recommends reducing the local share of the income tax revenue from 10% to 7% in order to reduce the budget deficit by $308 million. The Civic Federation is concerned that these reductions pass expenses from one government to another, putting added pressure on local property taxes and other local resources.

The State provides funding to local school districts through General State Aid that may be used for any purpose and other grants that must be used for specific purposes. The distribution of General State Aid to school districts is largely based on the number of pupils, the amount of local property tax base and the poverty level of the districts' students. The Governor recommends reducing General State Aid to local school districts by $613.1 million, or 13.3%, from $4.6 billion in the FY2010 enacted budget to $4.0 billion in the FY2011 recommended budget. Under these appropriations, the Foundation Level falls to $5,669 per pupil in FY2011 from $6,119 in FY2010. This cut does not reduce or eliminate taxpayer-supported programs. Instead, each school district determines how they will operate with a reduction in General State Aid funds.

The State Revenue Sharing Act requires that 10% of personal and corporate income tax proceeds be transferred from General Funds to the Local Government Distributive Fund (LGDF), for distribution to counties and municipalities based on population. Local governments may use these funds for any purpose. Local governments have already experienced LGDF reductions proportionally to the State's decline in income tax revenue due to the recession. The Governor's proposal to change the local share to 7% will cut transfers to the LGDF from $1.0 billion that it would receive under current law to $718 million in FY2011. Reducing the local share by 30% might not reduce or eliminate taxpayer-supported programs, because each municipality and county would have the ability to raise additional revenue through property tax rate increases.

In total, local resources account for a significant portion of school district, county and municipality revenues.[16] These local revenues are generated primarily from property taxes.[17] If a

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[16] Illinois State Board of Education, *Annual Report 2009*, p. 6, http://www.isbe.state.il.us/reports/annual09/report.pdf (last visited on April 15, 2010); U.S. Census Bureau, State and Local Government Finance, 2007 Local Government, http://www.census.gov/govs/estimate (last visited on April 15, 2010).

drop in state funding results in a property tax increase, government spending does not decline. Instead, the spending resources are shifted from one taxpayer-supported source to another taxpayer-supported source. Home-rule governments may also raise revenues through other taxes.

Pension Reform

The Governor's FY2011 budget, issued on March 10, 2010, does not contain specific proposals to fix the State's severely underfunded retirement systems. The budget states that the Governor will work with the General Assembly to achieve pension stabilization and that the changes are expected to reduce the State's required pension contribution in FY2011 by $267 million.[18]

On March 24, 2010, after the budget was released, the General Assembly passed pension reform legislation that creates a second tier of reduced benefits for employees hired after January 1, 2011. The Governor signed Public Act 96-889 on April 14, 2010. The Governor's Office said the measure will reduce the State's pension liabilities by $220 billion, from $537.2 billion to $312.7 billion, in 2045, and save the State $67 billion on pension contributions through 2045.[19] According to the Governor's Office, the legislation will save the State $382 million on pension contributions in FY2011.[20] The legislation also covered some local government retirement systems, although not police and firefighters' funds.

The Civic Federation supports these important first steps by the Governor and General Assembly toward comprehensive public pension reform for future employees in Illinois and urges state leaders to act now to address the immediate pension funding crises facing state and local government. To reduce its substantial unfunded pension liabilities, the State will need to address the contributions and benefits of current employees.

Provisions of Public Act 96-0889

The Civic Federation has long advocated many of the reforms contained in the legislation that will reduce the future cost of most public pension programs in the State. Downstate and Chicago police and fire and Illinois Municipal Retirement Fund sheriff pensions are exempted. Public Act 96-0889 creates a second tier of reduced pension benefits for new employees hired after January 1, 2011.

Highlights:

- Raises the retirement age to 67 with 10 years of service for full retirement. Some retirement plans currently allow full retirement at age 55 or even lower.

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[17] Illinois State Board of Education, *Annual Report 2009*, p. 7, http://www.isbe.state.il.us/reports/annual09/report.pdf (last visited on April 15, 2010); U.S. Census Bureau, State and Local Government Finance, 2007 Local Government, http://www.census.gov/govs/estimate (last visited on April 15, 2010).
[18] Illinois State FY2011 Budget, p.2-10 and p. 3-2.
[19] State of Illinois, Governor's Office, "Governor Quinn Signs Historic Illinois Public Pension Reform Law," news release, April 14, 2010, at http://www.illinois.gov/gov/ with http://www.illinois.gov/publicincludes/statehome/gov/documents/Pension%20Reform%20Background.pdf (last visited on April 15, 2010).
[20] Email communication between the Civic Federation and the Governor's Office of Management and Budget, April 15, 2010.

- Raises the early retirement age to 62 with 10 years of service for a reduced benefit.
- Limits the maximum pensionable salary to the 2010 Social Security wage base of \$106,800. Previously there was a limit of \$245,000 for employees hired on or after January 1, 1996; there was no limit for employees hired before that date.[21]
- Final average salary will be calculated as the average of the highest eight consecutive salary years out of the previous ten years. This reform has the effect of reducing the salary from which a worker's pension is calculated and helps mitigate the practice of artificially inflating a worker's salary in her final years of service to increase her pension.
- Cost of living adjustment (COLA) to pensions for all affected pension plans *except General Assembly and Judges* will be calculated with simple interest rather than compound interest.
- COLA will be the lesser of 3% or ½ of the inflation rate—*except for General Assembly and Judges*—and for all plans will only be applied after age 67.[22]
- Maximum General Assembly and Judges' annuities will be 60% of average salary, down from 85%.
- Eliminates "double-dipping" by suspending the pension of any retiree who goes to work for a government that participates in another pension system until that employment ends.

<u>Shortcomings of Public Act 96-0889</u>

The Civic Federation supports Public Act 96-0889 as a solid step in the right direction on pension reform in Illinois. However, there is much more that the General Assembly and Governor must do to put state and local public pensions on the path to sustainability.

- Public Act 96-0889 does **NOT** reform Chicago or downstate police and firefighters' pension funds, which are some of the worst-funded in Illinois. They are also among the most generous in the State. Chicago and other municipalities in Illinois will still face the budget-busting pressures to fund these plans.
- The legislation allows Chicago Public Schools to take a partial pension holiday totaling more than a billion dollars over the next three years. CPS faces a significant budget deficit in FY2011 due in large part to pension pressures. Public Act 96-0889 also extends the District's 50-year funding schedule to 2060. *The Civic Federation strongly opposes pension holidays for any pension fund. The partial pension holiday will worsen the long-term condition of the Chicago Teachers Pension Fund*.
- The reforms do not include increases to either employer or employee contributions to the pension funds. Past underfunding of pensions on the part of employers and employees across Illinois is a key factor in the terribly underfunded state of those funds.
- The General Assembly and Judges' retirement funds are exempted from many of the provisions of the reform bill that apply to every other pension fund.
- The legislation does not ensure that certified pension contributions are made from existing operating revenues. Continued failure to fund the pensions from current revenues will expedite the need for reducing benefits for existing employees.

[21] 40 ILCS 5/1-117.
[22] For the General Assembly and Judges' systems, the COLA will be the lesser of 3% or the inflation rate.

Retiree Health Insurance Reforms

The Civic Federation supports the Governor's proposal to reduce state costs by requiring all state retirees to contribute toward the cost of their health insurance premiums. Under Illinois law, retirees with at least 20 years of service and their survivors are not required to pay any portion of their health insurance premiums.[23] Currently 90% of retirees pay no premiums, according to the Department of Healthcare and Family Services (HFS).[24]

State retirees overwhelmingly choose the State's most expensive health insurance plan—a traditional indemnity or fee-for-service plan, while most employees and dependents select less costly managed care plans. In FY2010, 68.4% of retirees chose the indemnity plan, compared with 23.9% of employees and 25.3% of dependents.[25] The State's average cost per participant in the traditional plan is 29.4% higher than its average cost per participant in the managed care plans.[26]

In his FY2011 budget, Governor Quinn proposes that the State limit its share of retiree health insurance premiums to $300 per month per participant. The change would mean that Medicare-eligible retirees, for whom the state plan serves as supplemental insurance, would pay between $4 per month and $50 per month, depending on which insurance plan they chose. For retirees not yet on Medicare, the cost would be between $290 per month and $500 per month.[27]

The proposal, which requires a change in state law, follows the premium-sharing practices of the federal government and most private businesses.[28] The Civic Federation acknowledges that the proposal would require some retirees to either pay significantly higher costs for their insurance or switch to less costly health plans. The Civic Federation supports the proposal as a reasonable way for the State to moderate the growth in its healthcare spending.

Medicaid-Related Reforms

The Civic Federation supports the Governor's efforts to control costs in the complicated and expensive Medicaid program.

In the FY2011 budget, the Governor is planning to reduce by half—from $140 million to $70 million—spending on a prescription drug program called Illinois Cares Rx. The program

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[23] State Employee Group Insurance Act of 1971, 5 ILCS 375/10.
[24] Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 10, 2010, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).
[25] Email communication between the Civic Federation and the Commission on Government Forecasting and Accountability, April 8, 2010.
[26] Ibid, p.10.
[27] Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 10, 2010, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).
[28] U.S. Office of Personnel Management, *Insurance Programs/Retirees/Health* ,at http://www.opm.gov/insure/retirees/index.asp?ProgramId=1 (last visited on April 19, 2010); Kaiser Family Foundation and Hewitt Associates, Retiree Health Benefits Examined: Findings from the Kaiser/Hewitt 2006 Survey on Retiree Health Benefits, December 2006, p. 16, at http://www.kff.org/medicare/upload/7587.pdf (last visited on April 19, 2010).

provides assistance to seniors to supplement coverage in the Medicare Part D drug program. Expenditures for the Illinois Cares Rx program do not qualify for federal reimbursement. The State intends to save money by requiring seniors to pay a greater share of the costs, rather than by cutting enrollment. The Civic Federation supports cutbacks in this program as a reasonable way to limit state spending. In addition, federal healthcare legislation is scheduled to eliminate the gaps in Medicare Part D coverage over the next 10 years.

The Governor is also implementing a pilot program to place about 40,000 disabled and elderly Medicaid recipients into health maintenance organizations (HMOs). This program marks the first time that Illinois has required Medicaid recipients to enroll in HMOs. State officials have said the plan will save roughly $200 million over the first five years, although this number includes both federal and state savings. The State believes that the program can both improve care and reduce costs. Although advocates for the disabled are concerned that vital services might be cut, the Civic Federation supports the Governor's efforts to manage healthcare more efficiently. The Civic Federation urges the State to establish incentives for HMOs to provide necessary care.

Performance Measurement System

The Civic Federation supports the Governor's efforts to create and improve performance metrics under the Public Accountability and Performance System Act.[29] We encourage the Governor to enhance the quality and effectiveness of the performance data collected, presented, and utilized. Optimally, this would include stated goals as well as more outcome measures of efficiency, effectiveness, and service quality.

Currently, the FY2011 budget includes five years of performance metrics for each agency. Some agencies provide outcome measures, such as cost per unit. However, most of these metrics are indicators of output, or workload measures. These are counts of the number or percentage of activities undertaken or services delivered. In addition, goals are not provided for the statistics that are being measured. A lack of articulated goals makes it impossible to determine if agencies are meeting, exceeding, or falling short of program and policy targets or if they have such targets.

Civic Federation Financial Management Recommendations

In February of 2010, the Civic Federation published *A Fiscal Rehabilitation Plan for the State of Illinois*, a report that described the basis of Illinois's fiscal crisis and presented the Civic Federation's a plan for rehabilitating the State's finances.[30] The Civic Federation's plan called for expenditure cuts of $2.5 billion from the FY2010 level and substantial pension reforms, including creation of a two-tier system with reduced benefits for new employees and increased employee contributions. The report opposed cuts to General State Aid to elementary and secondary education and reductions in the Medicaid program that would jeopardize the State's receipt of federal recovery funds.

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[29] 30 ILCS 25/3 (2009).

[30] The Civic Federation, *A Fiscal Rehabilitation Plan for the State of Illinois: An Analysis of the State's Fiscal Crisis and Actionable Recommendations for Governor Pat Quinn and the Illinois General Assembly*, February 22, 2010, at http://www.civicfed.org/iifs/publications/afiscalrehabilitationplanforillinois (last visited on April 16, 2010).

Only after these conditions were met, the *Fiscal Rehabilitation Plan* proposed an income tax increase to be used exclusively to pay down the State's outstanding liabilities, including its unfunded pension liabilities. Governor Quinn has said he supports a one-percentage point increase in the personal income tax rate, from 3% to 4%, although the proposal does not appear in the Governor's FY2011 budget. The Civic Federation cannot support the Governor's proposal because its conditions regarding spending cuts and pension reforms have not been met. In addition, the Governor proposes to use much of the new revenue to eliminate a recommended reduction in education spending. The Civic Federation's support for new tax revenue is inextricably linked to the State's overriding responsibility to use such revenue to first pay down outstanding liabilities.

In addition to its recommendations in the *Rehabilitation Plan*, the Civic Federation offers the following policy proposals intended to improve the State's financial condition, institute sound management practices, and reduce costs.

Continue to Reform Funding and Governance of Pension Systems

Fund State Pension Systems at Certified Contribution Amount for FY2011

Previous pension reform legislation that took effect in 1995 established a 50-year schedule of funding requirements to achieve a 90% funded ratio by 2045.[31] The state retirement systems calculate and certify the amounts needed each year to meet the requirements of this funding schedule. Each retirement system must certify the contribution for the following fiscal year by November 15. The Civic Federation does not support any reduction in the State's pension contributions in FY2011, which were certified in November of 2009, unless the retirement systems certify that the new contribution levels comply with the funding requirements.

Additional Pension Reforms

The General Assembly and Governor Quinn must immediately implement further critical reforms to State and local government pension funds. It is imperative that our political leaders realize that the reforms implemented in Public Act 96-0889 do not *solve* Illinois' pension debacle. There is much more work to be done before public pensions in Illinois are made solvent and sustainable.[32]

- The General Assembly should pass and Governor Quinn should sign into law reforms to Chicago and downstate Police and Fire pension funds, including the creation of a second tier of reduced pension benefits for new hires.
- The General Assembly and Governor Quinn must not allow any pension funding holidays and must require that certified pension contributions be made with existing operating revenue.

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[31] Public Act 88-593.

[32] For a complete list of the Civic Federation's recommended pension reforms, see the pension reform section of our *Status of Local Pension Funding Fiscal Year 2008* report at http://www.civicfed.org/civic-federation/publications/fy2008statuslocalpensions, starting on page 53.

- Funding for many local public pension funds in Illinois is not tied to the financial needs of those funds. Future pension reforms should tie contributions by both employers and employees to the funding needs of the pensions.
- The General Assembly and Governor should apply the COLA provisions of the pension reform bill to the General Assembly and Judges' pension funds.
- The State should require a balance of employee, management and taxpayer interests in the governance of its retirement system Boards. Board seats should be set aside for members with professional expertise or certification in financial asset investment, and all members who do not already possess such expertise should be required to receive some relevant training on an annual basis.
- Continued failure to fund the pensions with current revenues will eventually necessitate reducing benefits for existing employees.

Develop Alternatives for Institutionalized Recipients of Medicaid and Other State Aid

The Civic Federation believes that the State can do much more to improve the quality and efficiency of services in the Medicaid program. In particular, Illinois has historically lagged behind other states in developing alternatives to costly institutional care. Illinois must speed up its efforts to serve the elderly, disabled and mentally ill in less restrictive settings.

Implement a Formal Long-Term Financial Planning Process

The National Advisory Council on State and Local Budgeting (NACSLB) and the Government Finance Officers Association (GFOA) both recommend that all governments formally adopt a long-term financial plan as a key component of a sound budget process.[33] Internally, the State of Illinois currently employs many of the techniques of a long-term financial planning process, including the projection of multi-year revenue trends and modeling of various revenue and expenditure options. However, the State does not develop a formal plan that is shared with and/or reviewed by key policymakers and stakeholders. The Civic Federation recommends that the State develop and implement a formal long-term financial planning process.
Personnel data should be aggregated in one section of the budget and include positions across all funds and for all departments. This data should be based on the Governor's recommended

Implement a Capital Improvement Plan

The Civic Federation urges the State of Illinois to establish a comprehensive capital improvement plan (CIP) that is updated and published annually. The citizens of Illinois deserve to know the overall condition and maintenance needs of all state-owned assets and how projects in the capital budget are prioritized to meet those needs. Although a list of nearly 9,000 appropriations accompanies the capital budget document, no planning documents are available to explain the prioritization of projects or estimates of total capital needs for the State. Very little has been publicized about the selection of projects approved in FY2010 or the new projects proposed for FY2011. Although the capital budget book describes a process coordinated by the Capital Development Board and the Governor's Office of Management and Budget to assemble and prioritize the projects in the capital program, no documentation of the process or final

[33] See National Advisory Council on State and Local Budgeting and Government Finance Officers Association.

ranking of projects was included the budget.[34] Some of the important elements of a CIP missing from the Governor's proposed capital budget include:[35]

- A comprehensive inventory of all state owned assets, with description of useful life and current condition;
- A five-year summary list of all projects and expenditures per project as well as funding sources per project;
- Criteria for projects to earn funding in the capital budget, including a description of an objective and needs-based prioritization process;
- Information about the impact of capital spending on the annual operating budget of each project;
- Brief narrative descriptions of individual projects, including the purpose, need, history, and current status of each project; and
- Expected timeframe for completing each project and a plan for fulfilling overall capital priorities.

A well-organized and annually updated CIP ensures efficient and predictable execution of capital projects. The State's capital budgeting process should use a more transparent process of determining the specific goals of infrastructure investments and the availability of pay-as-you-go funding versus leveraging the bonding authority to complete projects.

Revise the Budget Document Format

The State's annual budget document contains useful features, but the Civic Federation recommends that its content be improved to provide readers with more information.

The budget document format provides a user guide for the reader, as well as a budget summary that outlines the policy goals and objectives for the fiscal plan. Both of these sections are well done and provide the public and policy makers with useful knowledge regarding the State's finances.

However, the State's information regarding personnel expenses is severely lacking. A small chart depicting employee headcount and an accompanying descriptive paragraph is the only aggregate information for state personnel data in this year's budget document. It only contains headcount information for agencies under the Governor, leaving headcounts for constitutional officers, the General Assembly, and the judicial branch excluded. Nowhere in the budget is an aggregate total for personnel salary costs; as a result, it was necessary for the Civic Federation based our personnel cost calculations in this document on data provided by the State in response to a request.

Personnel data should be aggregated in one section of the budget and include positions across all funds and for all departments. This data should be based on the Governor's recommended appropriations for all state departments and agencies, including constitutional officers, the

[34] Illinois State FY2011 Capital Budget, pg. 5.
[35] Vogt, A. John, *Capital Budgeting and Finance: A Guide for Local Governments*, International City/County Management Association, 2004, p. 62.

General Assembly, and the judicial branch. The data in the personnel section should be broken down by payroll, health insurance and pension expenditures. A two- and five-year comparison should be provided for the reader, along with a five-year cost projection that takes into account annual cost of living increases. This expenditure data should be cross-referenced with actual personnel counts for each department that are summarized in one convenient chart.

Consolidate Special Purpose Funds

The vast majority of the State's more than 300 Special State Funds were created to receive earmarked revenues that are only used for a designated purpose. Over time, the number of special funds has increased, consuming ever larger portions of the state budget. In most cases, segregating revenues into special purpose funds is a practice that should only be adopted for certain high priority or mandatory programs. The State should be afforded maximum flexibility in allocating resources to meet policy priorities.

ECONOMIC OVERVIEW AND REVENUES

The following section provides an overview of the current economic situation in Illinois. It also details revenue trends for the State of Illinois' operating budget.

Economic Overview

The State of Illinois continues to be affected by the national economic recession that began in December of 2007.[36] The economic recession has contributed significantly to Illinois' poor fiscal health.

The Illinois unemployment rate has more than doubled since the beginning of the recession, rising from 5.5% in December of 2007 to 11.4% in February of 2010.[37] Due to rising unemployment and other effects of the recession, statewide personal income dropped by 1.8% from calendar year 2008 to 2009. Calendar year 2009 marked the first drop in Illinois' personal income since at least 1969, the first year that data were available.[38] Diminished personal income and reduced consumer confidence have a negative effect on personal consumption.

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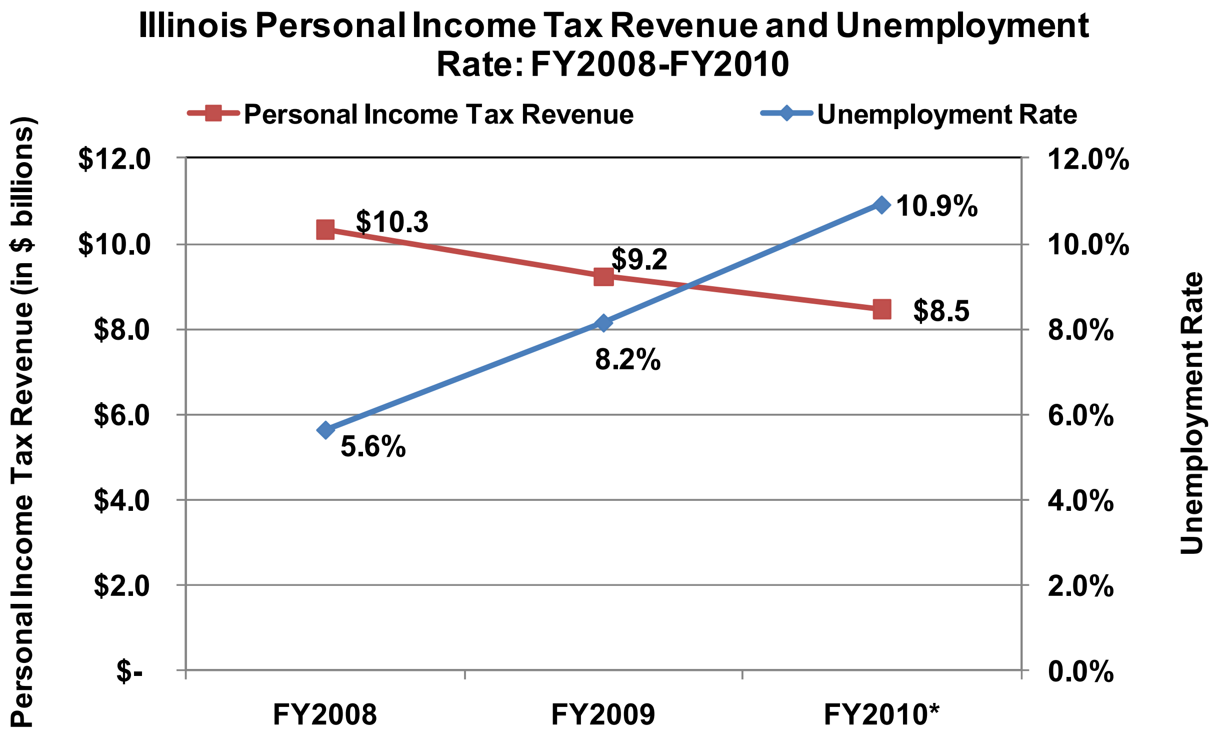
[36] National Bureau of Economic Research, "Determination of the December 2007 Peak in Economic Activity," December 1, 2008.
[37] U.S. Bureau of Labor Statistics, Local Area Unemployment Statistics, http://www.bls.gov (last visited March 31, 2010).
[38] U.S. Bureau of Economic Analysis, State Annual Personal Income, http://www.bea.gov/regional/spi (last visited April 5, 2010).

The decline in consumer spending affects business income and activity. Illinois' Gross State Product declined for the first time this decade in 2009, dropping by 2.6% from $516.1 billion in 2008 to $502.7 billion.[39] Since state tax revenue in Illinois depends heavily on personal and corporate income taxes and the state sales tax, the recession resulted in a decline in state revenues. The following chart compares the decline in personal income tax revenue with the increase in the unemployment rate since FY2008, which began July 1, 2007, prior to the start of the recession.



*Personal Income Tax Revenue for FY2010 are projections as of March 2010. The FY2010 unemployment rate is the average unemployment rate for the first eight months of FY2010.
Source: State of Illinois, Illinois State Budget Fiscal Year 2011, p. 2-29; U.S. Bureau of Labor Statistics, Local Area Unemployment Statistics, http://www.bls.gov (last visted March 31, 2010).

The recession began in the middle of FY2008, but Illinois' unemployment rate did not begin to accelerate until the end of the fiscal year. The unemployment rate increased from 5.6% during FY2008 to 8.2% during FY2009, a 2.6 percentage point increase. For the first eight months of FY2010, the unemployment rate averaged 10.9%, a 2.8 percentage point increase over FY2009. As the unemployment rate rose, personal income tax revenues declined from $10.3 billion in FY2008 to $9.2 billion in FY2009, and the Governor projected another drop for FY2010 to $8.5 billion. In FY2010, the personal income tax is projected to generate 18.0% or $1.9 billion less revenue than in FY2008.

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[39] Moody's Economy.com, *State of Illinois Economic Forecast Report*, February 2010, http://www.ilga.gov/commission/cgfa2006/Upload/2010FebMoodysEconomyILforecast.pdf (last visited April 5, 2010).

Illinois was not alone; most other states experienced a drop in revenue during the recession. While Illinois' personal income tax revenue dropped 3.3% from the second quarter of FY2009 to the second quarter of FY2010, personal income tax revenue for all U.S. states declined by 4.7% during the same period.[40] Illinois second quarter state sales tax revenues declined by 11.7% between FY2009 and FY2010, a much larger decline than the national state sales tax revenues which declined 2.9% during the same period.[41] States utilized federal funds provided through the American Recovery and Reinvestment Act of 2009 to offset declining state revenues during FY2009 and FY2010.

Due to positive economic forecasts for Illinois, revenue growth is expected in FY2011. While the calendar year 2010 unemployment rate forecast is 11.4%, the rate is projected to drop during 2011 to 10.5%.[42] Likewise, personal income is projected to increase by 1.6% in 2010 and an additional 2.7% in 2011.[43] Total state-source General Funds revenues are projected to increase by $562 million or 2.7% in FY2011.[44]

However, this growth is not sufficient to offset a General Funds baseline deficit of $1.2 billion, which is the budgetary imbalance before any changes to revenues and expenditures. In addition to this baseline deficit, Illinois faces a budget gap in FY2011 due to the loss of one-time revenues, including federal recovery funds, the proceeds from the sale of five-year pension notes and sweeps from special funds. Additional required expenditures including debt service on the pension notes and an increase in the State's statutorily required contribution to the retirement systems add to the FY2011 budget gap. The FY2011 deficit of $12.9 billion also includes the $5.9 billion gap projected to be carried forward from FY2010. The following table outlines the contributors to the $12.9 billion budget deficit in FY2011.

State of Illinois General Funds Budget Gap: FY2011 (in $ millions)	
Carry-forward of FY2010 Deficit	$ (5,918)
FY2011 Baseline Deficit	$ (1,200)
Loss of Federal Recovery Funds	$ (947)
Fund Sweeps Included in FY2010 Revenue	$ (352)
Borrowing FY2010 Contributions to Retirement Systems	$ (3,466)
Increase in Statutory Contributions to Retirement Systems	$ (691)
Pension Bond Repayment	$ (803)
Statutory Transfer of Pension Bond Debt Service	$ (345)
FY2011 Revenue Growth	$ 798
FY2011 Total Budget Gap	**$ (12,923)**

Source: Illinois State FY2011 Budget, p. 2-10, 4-16, 4-17.

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[40] U.S. Census Bureau, Quarterly Summary of State and Local Government Tax Revenue, March 30, 2010, http://ftp2.census.gov/govs/qtax/information_sheet.pdf (last visited April 5, 2010).
[41] Ibid.
[42] Moody's Economy.com, *State of Illinois Economic Forecast Report*, February 2010, http://www.ilga.gov/commission/cgfa2006/Upload/2010FebMoodysEconomyILforecast.pdf (last visited April 5, 2010).
[43] Ibid.
[44] Illinois State FY2011 Budget.

The Governor's FY2011 budget recommendation includes various measures to reduce this $12.9 billion deficit. The measures outlined in the budget recommendation do not include any new or increased revenues for FY2011. Instead, the Governor proposes budget reductions, borrowing $4.7 billion to cover the operating deficit and carrying the $5.9 billion FY2010 deficit over into FY2012. However, as part of his budget address to the General Assembly, the Governor proposed a one-percentage point increase in the personal income tax as an alternative to education cuts included in the FY2011 budget recommendation.[45] However, this proposal does not appear in the Governor's budget document. The next subsection examines the Governor's revenue projections for FY2010 and FY2011.

Revenues

Projections for the State of Illinois' operating revenues indicate that FY2010 revenues will be lower than estimated in the Governor's FY2010 budget recommendation and lower than the estimates included in the budget enacted by the General Assembly in July 2009. This continued downward revision is due to the continuing effects of the economic recession. While the Governor projects a modest rebound in revenues for FY2011, it will not be enough to offset the loss of federal recovery funds.

Reductions in economically sensitive revenues have particularly affected General Funds revenues, which support the regular operating and administrative expenses of most state agencies and are the funds over which the State has the most control and discretion. The State's other operating revenues consist of Other State Funds, which are accounts for activities funded by earmarked revenue sources that may only be used for special purposes, and Federal Funds, other than those designated for General Funds, that support a variety of state programs.

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[45] Governor Pat Quinn, "FY 2011 State of Illinois Budget Address," March 10, 2010, http://www2.illinois.gov/budget/Documents/FY%202011%20Transcript.pdf (last visited April 5, 2010). Six weeks after the Governor's recommendations were released, the Governor provided further information on how this income tax rate increase and cigarette, consumer and business tax changes would reduce the FY2011 budget deficit as part of a proposal to legislative leaders. Email communication between the Civic Federation and the Governor's Office of Management and Budget, April 20, 2010.

Governor's Recommended General Funds Revenues: FY2010 and FY2011

The Governor's recommended budget includes revenues totaling $52.8 billion for FY2011, a reduction from the $55.5 billion projected in the Governor's recommended budget for FY2010. The Governor's revenue estimates for FY2011 includes $27.4 billion in General Funds revenues. This is $5.6 billion or 17.0% less than the $33.1 billion General Funds revenues projected in his FY2010 budget recommendation. However, the reduction resulted primarily from revenue increases recommended in FY2010, including an income tax increase, that were not adopted by the General Assembly. Projected General Funds revenues before increases actually dropped from $26.8 billion to $26.5 billion, a decline of $250 million or 0.9%. The following chart provides a comparison of the Governor's projected General Funds revenues for FY2010 and FY2011.

Governor's Projections of State of Illinois Revenues for General Funds: FY2010 and FY2011 (in $ millions)				
	FY2010 (proj.)	FY2011 (proj.)	$ change	% change
Base Revenues				
State Sources				
Income Taxes (Net)	$ 9,968	$ 10,256	$ 288	2.9%
Personal	$ 8,925	$ 8,686	$ (239)	-2.7%
Corporate	$ 1,043	$ 1,570	$ 527	50.5%
Sales Taxes	$ 6,394	$ 6,290	$ (104)	-1.6%
Public Utility Taxes	$ 1,150	$ 1,144	$ (6)	-0.5%
Cigarette Taxes	$ 350	$ 350	$ -	0.0%
Liquor Taxes	$ 161	$ 161	$ -	0.0%
Inheritance Taxes	$ 275	$ 278	$ 3	1.1%
Insurance Taxes & Fees	$ 325	$ 350	$ 25	7.7%
Corporate Franchise Fees & Taxes	$ 205	$ 205	$ -	0.0%
Interest on State Funds and Investments	$ 80	$ 35	$ (45)	-56.3%
Cook County Intergov. Transfer	$ 240	$ 243	$ 3	1.3%
Other State Sources	$ 430	$ 372	$ (58)	-13.5%
Transfers-In				
Lottery	$ 645	$ 636	$ (9)	-1.4%
Riverboat Gaming Taxes	$ 478	$ 428	$ (50)	-10.5%
Other Transfers	$ 480	$ 664	$ 184	38.3%
10th Riverboat License	$ 50	$ -	$ (50)	-100.0%
Subtotal State Sources	**$ 21,231**	**$ 21,412**	**$ 181**	**0.9%**
Federal Sources	$ 5,555	$ 5,124	$ (431)	-7.8%
Subtotal Base Revenues	**$ 26,786**	**$ 26,536**	**$ (250)**	**-0.9%**
Increases to Base Revenues				
Federal Recovery	$ 1,882	$ 908	$ (974)	-51.8%
Fund Sweeps	$ 364	$ -	$ (364)	-100.0%
Income Taxes	$ 3,207	$ -	$ (3,207)	-100.0%
Cigarette Taxes	$ 365	$ -	$ (365)	-100.0%
Equity Charges	$ 287	$ -	$ (287)	-100.0%
Titles and Fees	$ 185	$ -	$ (185)	-100.0%
Subtotal Increases to Base Revenues	**$ 6,290**	**$ 908**	**$ (5,382)**	**-85.6%**
Total Revenues for General Funds	**$ 33,076**	**$ 27,444**	**$ (5,632)**	**-17.0%**

Note: The FY2011 federal recovery funds projection assumes an extension of the American Recovery and Reinvestment Act's 62% Medicaid match beyond the currently scheduled expiration date of December 31, 2010. That extension will require action by the U.S. Congress.
Sources: Illinois State FY2010 Budget, p. 2-33; Illinois State FY2011 Budget, p. 2-29 and 4-17.

Projected base General Funds revenues decrease from FY2010 to FY2011 by $250 million or 0.9%. The Governor does not recommend increases to base revenues for FY2011,[46] and includes $908 million from available federal recovery funds. In FY2010, the Governor recommended increasing revenues by a total of $6.3 billion, which included $3.2 billion through increasing the personal income tax from 3% to 4.5% and the corporate income tax from 4.8% to 7.2% and $1.9 billion in federal recovery funds. The Governor also proposed to raise cigarette taxes, tax sweetened tea and coffee drinks at the same sales tax rate as soft drinks, and tax all grooming and hygiene products at the same sales tax rate. In addition, the Governor recommended eleven sales, income and other tax changes on business activities to generate $478.0 million.[47]

In FY2010, the Governor also estimated federal recovery funding would total $1.9 billion and $364 million would be available from fund sweeps, which are statutory transfers of excess moneys from special funds to General Funds. The budget enacted by the General Assembly approved $352 million in fund sweeps for FY2010 and appropriated the federal recovery funds.[48] Additionally, the General Assembly enacted the expanded sales tax on sweetened drinks and hygiene products as well as candy in FY2010, but used the revenue to fund the capital program rather than the operating budget.[49] No action was taken by the General Assembly on the other FY2010 revenue increases proposed by Governor Quinn.

FY2010 General Funds Revenues: Enacted and March 2010 Estimates

The FY2010 operating budget as enacted in July 2009 included General Funds revenues of $29.3 billion. Since the budget's enactment, revenue projections have continued to decline. In the FY2011 budget proposal, the Governor's FY2010 revenue estimates show $27.9 billion General Funds revenue. This projection represents a General Funds decline of $1.4 billion or 4.6%, primarily due to reduced personal income tax and sales tax collections. Personal income tax projections drop from $9.2 billion to $8.3 billion, a decline of 8.1% or $745 million. Projections of state sales tax receipts were $6.4 billion when the budget was enacted in July 2009. The State projects $6.2 billion from the state sales tax, a drop of $194 million or 3.0% in the Governor's proposed budget.

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[46] As part of his budget address to the General Assembly, the Governor proposed a one-percentage point increase in the personal income tax as an alternative to education cuts included in the FY2011 budget recommendation. Governor Pat Quinn, "FY 2011 State of Illinois Budget Address," March 10, 2010, http://www2.illinois.gov/budget/Documents/FY%202011%20Transcript.pdf (last visited April 5, 2010). Six weeks after the Governor's recommendations were released, the Governor provided further information on how this income tax rate increase and cigarette, consumer and business tax changes would reduce the FY2011 budget deficit as part of a proposal to legislative leaders. Email communication between the Civic Federation and the Governor's Office of Management and Budget, April 20, 2010.

[47] For a discussion of the Governor's recommended FY2010 revenues, see The Civic Federation, *State of Illinois FY2010 Recommended Operating & Capital Budgets*, May 11, 2009, http://civicfed.org/sites/default/files/civicfed_294.pdf (last visited March 22, 2010).

[48] 30 ILCS 105/8.49 (2009).

[49] Public Act 96-34.

Additionally, the Governor reduced federal revenue for the General Funds in FY2010 by 5.4%. The enacted budget included $7.1 billion in federal revenues for the General Funds including federal recovery funds, but the Governor now projects $6.7 billion in federal revenues for General Funds. Corporate income tax projections for FY2010 increased from $1.1 billion to $1.3 billion since the budget was enacted, an increase of $178 million or 15.7%. The following table provides a comparison of FY2010 General Funds revenue projections when the budget was enacted in July 2009 and the Governor's March 2010 estimate.

State of Illinois Revenues for General Funds: FY2010 Enacted and Estimated (in $ millions)

	Enacted July 2009	Estimate March 2010	$ change	% change
Base Revenues				
State Sources				
Income Taxes (Net)	$ 10,337	$ 9,770	$ (567)	-5.5%
Personal	$ 9,205	$ 8,460	$ (745)	-8.1%
Corporate	$ 1,132	$ 1,310	$ 178	15.7%
Sales Taxes	$ 6,394	$ 6,200	$ (194)	-3.0%
Public Utility Taxes	$ 1,150	$ 1,115	$ (35)	-3.0%
Cigarette Taxes	$ 350	$ 350	$ -	0.0%
Liquor Taxes	$ 161	$ 161	$ -	0.0%
Inheritance Taxes	$ 275	$ 278	$ 3	1.1%
Insurance Taxes & Fees	$ 325	$ 350	$ 25	7.7%
Corporate Franchise Fees & Taxes	$ 205	$ 205	$ -	0.0%
Interest on State Funds and Investments	$ 80	$ 35	$ (45)	-56.3%
Cook County Intergov. Transfer	$ 240	$ 243	$ 3	1.3%
Other State Sources	$ 430	$ 378	$ (52)	-12.1%
Transfers-In				
Lottery	$ 645	$ 625	$ (20)	-3.1%
Riverboat Gaming Taxes	$ 470	$ 420	$ (50)	-10.6%
Other Transfers	$ 704	$ 670	$ (34)	-4.8%
10th Riverboat License	$ 50	$ 50	$ -	0.0%
Subtotal State Sources	**$ 21,816**	**$ 20,850**	**$ (966)**	**-4.4%**
Federal Sources	$ 5,165	$ 4,888	$ (277)	-5.4%
Subtotal Base Revenues	**$ 26,981**	**$ 25,738**	**$ (1,243)**	**-4.6%**
Increases to Base Revenues				
Federal Recovery	$ 1,966	$ 1,855	$ (111)	-5.6%
Fund Sweeps	$ 352	$ 352	$ -	0.0%
Subtotal Increases to Base Revenues	**$ 2,318**	**$ 2,207**	**$ (111)**	**-4.8%**
Total Revenues for General Funds	**$ 29,299**	**$ 27,945**	**$ (1,354)**	**-4.6%**

Sources: Commission on Government Forecasting and Accountability, State of Illinois Budget Summary Fiscal Year 2010, p. 18, 29, 136; Illinois State FY2011 Budget, p. 2-29, 4-16 and 4-17. FY2010 projected Riverboat Gaming Taxes reflect the text on 4-16 and not the table on 2-29.

Estimated FY2010 and FY2011 Revenues: All Funds and General Funds

The Governor's recommended budget estimates $52.8 billion in total revenues, a reduction of $1.4 billion or 2.5% from total projected FY2010 revenues of $54.2 billion. This reduction is primarily due to a 23.4% decrease in federal recovery funds that the State receives through the American Recovery and Reinvestment Act of 2009 from $4.0 billion to $3.0 billion. Federal authorization for these funds expires July 1, 2010 for certain purposes and December 31, 2010 for the enhanced Medicaid match. The FY2011 revenues projected by the Governor assume that the enhanced Medicaid match will be extended until June 30, 2011. The reduction in federal recovery funds of $930 million along with the $513 million reduction in other federal receipts is actually more than the total revenue reduction. The reduction in federal recovery funds is partially offset by an expected recovery in state tax revenue. The following chart compares FY2010 projected state revenues with the revenues projected by the Governor for FY2011.

State of Illinois Revenues for All Funds: Estimated FY2010 and Projected FY2011 (in $ millions)

	FY2010 (est.)	FY2011 (proj.)	$ change	% change
State Taxes				
Income Taxes (Net)	$ 9,770	$ 10,256	$ 486	5.0%
Individual	$ 8,460	$ 8,686	$ 226	2.7%
Corporate	$ 1,310	$ 1,570	$ 260	19.8%
Sales Taxes	$ 7,023	$ 7,125	$ 102	1.5%
Motor Fuel Tax (Gross)	$ 1,360	$ 1,368	$ 8	0.6%
Public Utility Taxes	$ 1,880	$ 1,929	$ 49	2.6%
Cigarette Taxes and Tobacco Products Taxes	$ 562	$ 558	$ (4)	-0.7%
Liquor Gallonage Taxes	$ 161	$ 161	$ -	0.0%
Inheritance Tax	$ 278	$ 278	$ -	0.0%
Insurances Tax and Fees	$ 450	$ 450	$ -	0.0%
Corporate Franchise Taxes and Fees	$ 212	$ 212	$ -	0.0%
Riverboat Gaming Taxes and Fees	$ 494	$ 505	$ 11	2.2%
Subtotal State Taxes	**$ 22,190**	**$ 22,842**	**$ 652**	**2.9%**
Other Receipts				
Motor Vehicle and Operations License Fees	$ 1,285	$ 1,296	$ 11	0.9%
Interest Income	$ 66	$ 61	$ (5)	-7.6%
Revolving Fund Receipts	$ 741	$ 761	$ 20	2.7%
Lottery	$ 1,039	$ 1,124	$ 85	8.2%
Assessment Funds Receipts	$ 1,555	$ 1,602	$ 47	3.0%
Intergovernmental Receipts	$ 1,312	$ 1,279	$ (33)	-2.5%
Group Insurance Receipts	$ 1,464	$ 1,279	$ (185)	-12.6%
Tobacco Settlement Receipts	$ 315	$ 324	$ 9	2.9%
Other Taxes, Fees, Earnings and Net Transfers	$ 4,805	$ 4,297	$ (508)	-10.6%
Subtotal Other Receipts	**$ 12,582**	**$ 12,023**	**$ (559)**	**-4.4%**
Federal Sources	$ 15,438	$ 14,925	$ (513)	-3.3%
Federal Recovery	$ 3,977	$ 3,047	$ (930)	-23.4%
Subtotal Federal Receipts	**$ 19,415**	**$ 17,972**	**$ (1,443)**	**-7.4%**
Total	**$ 54,187**	**$ 52,837**	**$ (1,350)**	**-2.5%**

Note: The FY2011 federal recovery funds projection assumes an extension of the American Recovery and Reinvestment Act's 62% Medicaid match beyond the currently scheduled expiration date of December 31, 2010. That extension will require action by the U.S. Congress.

Sources: Illinois State FY2011 Budget, p. 2-28; E-mail communication between the Governor's Office of Management and Budget and the Civic Federation, March 26, 2010.

The Governor's recommendation projects $22.8 billion in state tax revenues for all funds in FY2011, an increase of $652 million or 2.9% from projected FY2010 state tax revenues of $22.2 billion. The majority of this increase occurs in economically sensitive revenues such as income and sales taxes. The Governor projects that personal income tax receipts will increase from $8.5 billion in FY2010 to $8.7 billion in FY2011, an increase of $226 million or 2.7%. Despite the estimated increase, personal income tax revenues would remain significantly below FY2009 levels of $9.2 billion and FY2008 levels of $10.3 billion.

Corporate income tax revenues are projected by the Governor to rise from $1.3 billion in FY2010 to $1.6 billion in FY2011, an increase of $260 million or 19.8%. Despite this increase, corporate income taxes would still be less than collections during FY2008 and FY2009. Sales tax revenues are expected to increase by $102 million or 1.5%. Projected FY2011 sales tax receipts of $7.1 billion are still greater than the $7.0 billion projected for FY2010, but they remain lower than collections in FY2006 through FY2009. Interest income is projected to drop from $66 million to $61 million, a reduction of $5 million or 7.6%. This level of interest income is the lowest experienced in the past ten years.

General Funds are projected to drop from $27.9 billion in FY2010 to $27.4 billion in FY2011. The FY2011 projection would be the lowest General Funds revenues in five years. This $501 million or 1.8% decline in General Funds revenues is primarily due to the $947 million or 51.1% reduction in federal recovery funds. The drop is largely because the State allocated all available federal fiscal stabilization funds during FY2009 and FY2010. The Governor estimated Illinois would receive $908 million in federal recovery funds for FY2011. This is based on the assumption that the U.S. Congress will pass an extension to the enhanced federal Medicaid match, which expires on December 31, 2010. If the extension of the match is not approved, projected FY2011 revenues will drop by approximately $450 million.

The decline in federal recovery funds is partially offset by the recovery of income and sales tax revenues. Projected state source General Funds revenues rose from $20.9 billion for FY2010 to $21.4 billion for FY2011, an increase of $562 million or 2.7%. The following table shows how the Governor's recommended FY2011 General Funds revenues compare with projected FY2010 revenue.

State of Illinois Revenues for General Funds: Estimated FY2010 and Projected FY2011 (in $ millions)				
	FY2010 (est.)	FY2011 (proj.)	$ change	% change
Base Revenues				
State Sources				
Income Taxes (Net)	$ 9,770	$ 10,256	$ 486	5.0%
Personal	$ 8,460	$ 8,686	$ 226	2.7%
Corporate	$ 1,310	$ 1,570	$ 260	19.8%
Sales Taxes	$ 6,200	$ 6,290	$ 90	1.5%
Public Utility Taxes	$ 1,115	$ 1,144	$ 29	2.6%
Cigarette Taxes	$ 350	$ 350	$ -	0.0%
Liquor Taxes	$ 161	$ 161	$ -	0.0%
Inheritance Taxes	$ 278	$ 278	$ -	0.0%
Insurance Taxes & Fees	$ 350	$ 350	$ -	0.0%
Corporate Franchise Fees & Taxes	$ 205	$ 205	$ -	0.0%
Interest on State Funds and Investments	$ 35	$ 35	$ -	0.0%
Cook County Intergov. Transfer	$ 243	$ 243	$ -	0.0%
Other State Sources	$ 378	$ 372	$ (6)	-1.6%
Transfers-In				
Lottery	$ 625	$ 636	$ 11	1.8%
Riverboat Gaming Taxes	$ 420	$ 428	$ 8	1.9%
Other Transfers	$ 670	$ 664	$ (6)	-0.9%
10th Riverboat License	$ 50	$ -	$ (50)	-100.0%
Subtotal State Sources	**$ 20,850**	**$ 21,412**	**$ 562**	**2.7%**
Federal Sources	$ 4,888	$ 5,124	$ 236	4.8%
Subtotal Base Revenues	**$ 25,738**	**$ 26,536**	**$ 798**	**3.1%**
Increases to Base Revenues				
Federal Recovery	$ 1,855	$ 908	$ (947)	-51.1%
Fund Sweeps	$ 352	$ -	$ (352)	-100.0%
Subtotal Increases to Base Revenues	**$ 2,207**	**$ 908**	**$ (1,299)**	**-58.9%**
Total Revenues for General Funds	**$ 27,945**	**$ 27,444**	**$ (501)**	**-1.8%**

Note: The FY2011 federal recovery funds projection assumes an extension of the American Recovery and Reinvestment Act's 62% Medicaid match beyond the currently scheduled expiration date of December 31, 2010. That extension will require action by the U.S. Congress.
Source: Illinois State FY2011 Budget, 2-29, 4-16 and 4-17. FY2010 projected Riverboat Gaming Taxes reflect the text on 4-16 and not the table on 2-29.

Five-Year Revenue Trends: All Funds and General Funds

The State of Illinois' total revenues have risen over the past five years despite declines in state tax revenues. The Governor's budget recommendation estimated FY2011 revenues of $52.8 billion, which is $4.0 billion or 8.2% more than FY2007 revenues of $48.8 billion. This increase is a result of a $5.0 billion projected increase in federal receipts, from $13.0 billion in FY2007 to $18.0 billion in FY2011. The increase in federal funds offset a decline in state tax revenue.

The FY2011 budget projects revenues from state taxes to decrease by 7.0% or $1.7 billion from FY2007. This drop from $24.6 billion to $22.8 billion is primarily a result of the $902 million or 8.1% drop in personal and corporate income tax revenues. Personal income tax receipts have dropped from $9.4 billion in FY2007 to $8.7 billion projected for FY2011 and corporate income tax receipts have dropped from $1.8 billion to $1.6 billion.

Sales tax receipts in FY2011 are projected to be $506 million or 6.6% lower than in FY2007, a decline from $7.6 billion to $7.1 billion. Riverboat gaming taxes and fees have dropped from $772 million in FY2007 to $505 million in FY2011, a decline of $267 million or 34.6%. The largest percentage reduction occurred in interest income, which has dropped from $202 million in FY2007 to a projection of $61 million for FY2011, a decline of $141 million or 69.8%.

State of Illinois Revenues for All Funds: Actual FY2007 and Projected FY2011 (in $ millions)

	FY2007	FY2011 (proj.)	$ change	% change
State Taxes				
Income Taxes (Net)	$ 11,158	$ 10,256	$ (902)	-8.1%
Individual	$ 9,408	$ 8,686	$ (722)	-7.7%
Corporate	$ 1,750	$ 1,570	$ (180)	-10.3%
Sales Taxes	$ 7,631	$ 7,125	$ (506)	-6.6%
Motor Fuel Tax (Gross)	$ 1,454	$ 1,368	$ (86)	-5.9%
Public Utility Taxes	$ 1,884	$ 1,929	$ 45	2.4%
Cigarette Taxes and Tobacco Products Taxes	$ 639	$ 558	$ (81)	-12.7%
Liquor Gallonage Taxes	$ 156	$ 161	$ 5	3.2%
Inheritance Tax	$ 264	$ 278	$ 14	5.3%
Insurances Tax and Fees	$ 412	$ 450	$ 38	9.2%
Corporate Franchise Taxes and Fees	$ 201	$ 212	$ 11	5.5%
Riverboat Gaming Taxes and Fees	$ 772	$ 505	$ (267)	-34.6%
Subtotal State Taxes	**$ 24,571**	**$ 22,842**	**$ (1,729)**	**-7.0%**
Other Receipts				
Motor Vehicle and Operations License Fees	$ 1,288	$ 1,296	$ 8	0.6%
Interest Income	$ 202	$ 61	$ (141)	-69.8%
Revolving Fund Receipts	$ 623	$ 761	$ 138	22.2%
Lottery	$ 957	$ 1,124	$ 167	17.5%
Assessment Funds Receipts	$ 1,529	$ 1,602	$ 73	4.8%
Intergovernmental Receipts	$ 1,319	$ 1,279	$ (40)	-3.0%
Group Insurance Receipts	$ 1,310	$ 1,279	$ (31)	-2.4%
Tobacco Settlement Receipts	$ 285	$ 324	$ 39	13.7%
Other Taxes, Fees, Earnings and Net Transfers	$ 3,748	$ 4,297	$ 549	14.6%
Subtotal Other Receipts	**$ 11,261**	**$ 12,023**	**$ 762**	**6.8%**
Federal Sources	$ 12,999	$ 14,925	$ 1,926	14.8%
Federal Recovery	$ -	$ 3,047	$ 3,047	N/A
Subtotal Federal Receipts	**$ 12,999**	**$ 17,972**	**$ 4,973**	**38.3%**
Total	**$ 48,831**	**$ 52,837**	**$ 4,006**	**8.2%**

Note: The FY2011 federal recovery funds projection assumes an extension of the American Recovery and Reinvestment Act's 62% Medicaid match beyond the currently scheduled expiration date of December 31, 2010. That extension will require action by the U.S. Congress.

Sources: Illinois State FY2010 Budget, 2-32; Illinois State FY2011 Budget, 2-28; E-mail communication between the Governor's Office of Management and Budget and the Civic Federation, March 26, 2010.

The Governor projected General Funds revenues of $27.4 billion for FY2011, a drop of $1.4 billion or 4.8% since FY2007. FY2011 General Funds revenue estimates include $21.4 billion from state sources, a reduction from $23.9 billion from state sources included in the total FY2007 General Funds revenue of $28.8 billion. This decline in state sources of $2.5 billion or 10.5% is partially offset by a $1.3 billion increase in funds from federal sources. This increase is primarily due to the $908 million in federal recovery funds the Governor projected the State will receive in FY2011.[50] FY2007 General Funds revenues also included fund sweeps, which were not included in the Governor's FY2011 budget.[51] The following chart compares FY2011 General Funds revenue projections to actual FY2007 revenues.

State of Illinois Revenues for General Funds: Actual FY2007 and Projected FY2011 (in $ millions)

	FY2007	FY2011 (proj.)	$ change	% change
Base Revenues				
State Sources				
Income Taxes (Net)	$ 11,159	$ 10,256	$ (903)	-8.1%
Personal	$ 9,409	$ 8,686	$ (723)	-7.7%
Corporate	$ 1,750	$ 1,570	$ (180)	-10.3%
Sales Taxes	$ 7,136	$ 6,290	$ (846)	-11.9%
Public Utility Taxes	$ 1,130	$ 1,144	$ 14	1.2%
Cigarette Taxes	$ 349	$ 350	$ 1	0.3%
Liquor Taxes	$ 156	$ 161	$ 5	3.2%
Inheritance Taxes	$ 264	$ 278	$ 14	5.3%
Insurance Taxes & Fees	$ 310	$ 350	$ 40	12.9%
Corporate Franchise Fees & Taxes	$ 193	$ 205	$ 12	6.2%
Interest on State Funds and Investments	$ 204	$ 35	$ (169)	-82.8%
Cook County Intergov. Transfer	$ 307	$ 243	$ (64)	-20.8%
Other State Sources	$ 482	$ 372	$ (110)	-22.8%
Transfers-In				
Lottery	$ 623	$ 636	$ 13	2.1%
Riverboat Gaming Taxes	$ 685	$ 428	$ (257)	-37.5%
Other Transfers	$ 935	$ 664	$ (271)	-29.0%
Subtotal State Sources	**$ 23,933**	**$ 21,412**	**$ (2,521)**	**-10.5%**
Federal Sources	$ 4,702	$ 5,124	$ 422	9.0%
Subtotal Base Revenues	**$ 28,635**	**$ 26,536**	**$ (2,099)**	**-7.3%**
Increases to Base Revenues				
Federal Recovery	$ -	$ 908	$ 908	N/A
Fund Sweeps	$ 188	$ -	$ (188)	-100.0%
Subtotal Increases to Base Revenues	**$ 188**	**$ 908**	**$ 720**	**382.2%**
Total Revenues for General Funds	**$ 28,823**	**$ 27,444**	**$ (1,379)**	**-4.8%**

Note: The FY2011 federal recovery funds projection assumes an extension of the American Recovery and Reinvestment Act's 62% Medicaid match beyond the currently scheduled expiration date of December 31, 2010. That extension will require action by the U.S. Congress.
Sources: Illinois State FY2010 Budget, 2-33; Illinois State FY2011 Budget, 2-29 and 4-17.

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[50] This assumes an extension of the enhanced Medicaid match beyond the currently schedule expiration date of December 31, 2010.

[51] For a discussion of the history of fund sweeps and other statutory mechanisms for transferring special funds to General Funds, see The Civic Federation, *A Fiscal Rehabilitation Plan for the State of Illinois*, February 22, 2010, http://civicfed.org/sites/default/files/IllinoisFiscalRehabilitationPlan.pdf.

APPROPRIATIONS

Facing a budget deficit of nearly $13 billion in FY2011, Governor Quinn recommended spending cuts to many areas of state government. Most of the proposed spending reductions are concentrated in the area of elementary and secondary education. However, some of the recommended cuts are offset by increased appropriations to other agencies, making it more complicated to get a clear picture of budgetary trends. This section examines the Governor's recommended appropriations and assesses their overall impact on state spending authority.

The Governor's FY2011 operating budget recommends total appropriations of $52.0 billion. This total consists of $24.8 billion in General Funds, $17.4 billion in Other State Funds and $9.7 billion in Federal Funds. General Funds is the largest fund group, representing 47.7% of total recommended appropriations. General Funds support the regular operating and administrative expenses of most state agencies and are the funds over which the State has the most control and discretion. Other State Funds are accounts for activities funded by earmarked revenue sources that may only be used for special purposes. Federal Funds are funds from the federal government other than those designated for General Funds and support a variety of state programs.

Appropriations by Funds

Total appropriations decline by 3.3%, or $1.8 billion, from $53.7 billion in the FY2010 enacted budget to $52.0 billion in the FY2011 recommended budget. General Funds appropriations decline by 5.8%, or $1.5 billion, from $26.3 billion to $24.8 billion. In this report, projected General Funds savings of $267 million due to pension reform legislation are not included in FY2011 operating appropriations.[52] Further information on the State's five retirement systems is contained in the Personnel and Retirement Systems section on page 52.

State of Illinois Appropriations by Fund: FY2010 Enacted - FY2011 Recommended (in $ thousands)

	FY2010 (enacted)	FY2011 (rec.)*	$ Change	% Change
General Funds	$ 26,308,589	$ 24,775,432	$ (1,533,157)	-5.8%
Other Funds	$ 17,479,967	$ 17,436,135	$ (43,832)	-0.3%
Federal Funds	$ 9,913,567	$ 9,739,807	$ (173,760)	-1.8%
Total	**$ 53,702,123**	**$ 51,951,374**	**$ (1,750,749)**	**-3.3%**

Source: Illinois State FY2011 Budget, p. 2-26.
*The General Funds number for FY2011 does not include projected savings of $267.0 million on pension contributions.

[52] Public Act 96-0889, signed into law by Governor Quinn on April 14, 2010.

The $1.5 billion reduction in FY2011 General Funds appropriations represents the net result of the Governor's departmental cuts. Total cuts amount to $2.2 billion to 61 departments or universities but are partially offset by $636.8 million in budget increases to 15 departments.

State of Illinois General Funds Net Appropriations Cuts to Departments: Enacted FY2010 to Recommended FY2011 (in $ thousands)		
Appropriations Cuts to Departments	$	(2,168,759)
Appropriations Increases to Departments	$	636,790
Net Appropriations Changes	**$**	**(1,531,969)**

Source: Illinois State FY2011 Budget, pp. 2-17 to 2-26.

The next table shows departments with reductions of $10 million or more in the Governor's recommended FY2011 General Funds appropriations.

State of Illinois Agencies with Decreases in Recommended General Funds Appropriations: FY2010 Enacted - FY2011 Recommended (in $ thousands)*

Agency	FY2010 (enacted)	FY2011 (rec.)	$ Change	% Change
State Board of Education	$ 7,307,877	$ 6,081,057	$ (1,226,820)	-16.8%
Department of Healthcare & Family Services Group Insurance	$ 1,000,000	$ 675,000	$ (325,000)	-32.5%
Department of Human Services	$ 4,036,885	$ 3,886,884	$ (150,001)	-3.7%
Office of the Governor	$ 94,024	$ 4,605	$ (89,419)	-95.1%
University of Illinois	$ 743,420	$ 697,057	$ (46,363)	-6.2%
Department on Aging	$ 656,214	$ 613,799	$ (42,415)	-6.5%
Supreme Court	$ 285,840	$ 244,993	$ (40,847)	-14.3%
Office of the Secretary of State	$ 260,277	$ 220,627	$ (39,650)	-15.2%
Department of State Police	$ 287,366	$ 255,359	$ (32,007)	-11.1%
Office of the Comptroller	$ 106,791	$ 85,807	$ (20,984)	-19.6%
Department of Central Management Services	$ 90,040	$ 74,829	$ (15,211)	-16.9%
Southern Illinois University	$ 234,167	$ 219,564	$ (14,603)	-6.2%
Department of Public Health	$ 143,266	$ 130,573	$ (12,693)	-8.9%
Others	$ 1,336,988	$ 1,224,242	$ (112,746)	-8.4%
Total	**$ 16,583,155**	**$ 14,414,396**	**$ (2,168,759)**	**-13.1%**

Source: Illinois State FY2011 Budget, pp. 2-17 to 2-26
*Includes universities.

The majority of cuts in appropriations were recommended for the State Board of Education, with reductions representing $1.2 billion, or 56.6%, of the Governor's total recommended General Funds cuts of $2.2 billion. Recommended General Funds appropriations to the State Board of Education decline 16.8%, from $7.3 billion in the FY2010 enacted budget to $6.1 billion in the FY2011 recommended budget. The University of Illinois' General Funds appropriation is reduced by $46.4 million, or 6.2%, from $748.0 million to $701.1 million. Education funding is discussed on page 42.

Recommended General Funds appropriations to the State Employees' Group Insurance Program decline $325.0 million, or 32.5%, from $1.0 billion to $675.0 million. The reductions in group insurance costs are largely based on the Governor's proposal to require all state retirees to pay part of the bill for their healthcare insurance premiums. The cuts also include $70 million in negotiated cost savings for current employees under an agreement with Local 31 of the American Federation of State, County and Municipal Employees in January of 2010.[53] State health insurance costs are discussed in the State Employee and Retiree Health Insurance section on page 56.

The Governor is also recommending major cuts to social services programs funded by the Department of Human Services (DHS) and the Department on Aging, where the General Funds budgets decline by $150.0 million and $40.8 million, respectively. Cuts to the DHS budget, including reductions in appropriations to community mental health clinics and programs for the developmentally disabled, are expected to affect 178,000 children and adults.[54]

The FY2011 General Funds appropriation to the Department of State Police is reduced by $32.0 million, or 11.1%, from $287.4 million to $255.4 million. The State Police's total recommended appropriation decrease of $58.1 million is expected to come from a 30% reduction in the number of state troopers.[55] However, the Governor recently suggested that he might avoid State Police cuts that would require the Chicago Police Department to assume primary responsibility for patrolling Chicago area expressways.[56]

The Office of the Governor shows a cut of $89.4 million, or 94.1%, from $94.0 million to $4.6 million. The reduction relates to the unusual FY2010 budget passed by the General Assembly, which gave the Governor authority to allocate lump-sum appropriations to departments rather than making line-item appropriations in the budget bills.[57] By comparison, the FY2009 actual expenditure by the Governor's Office was $7.0 million.

Included in the $2.2 billion in departmental cuts are $133 million in personnel-related reductions that affect employees across a number of state agencies.[58] These include furlough days, renegotiated employee contracts and travel restrictions. Council 31 of AFSCME agreed to many of the reductions in its deal with the State in January of 2010 in order to avert all except approximately 200 of 2,600 layoffs that had been planned by the State.[59] The labor union also agreed to a voluntary furlough plan and deferred pay increases in exchange for the State's pledge not to lay off any state employees or close any state facilities (not previously slated for closure)

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[53] Council 31 AFSCME, AFSCME, *State Reach Mediated Resolution on Layoff Grievances*, January 27, 2010, at http://www.afscme31.org/news?id=0011, (last visited on April 7, 2010).
[54] Illinois Department of Human Services, *FY2011 Budget Request Agency Budget Briefing*, March 10, 2010, p.5, at http://www.dhs.state.il.us/page.aspx?item=49098 (last visited on April 3, 2010).
[55] Dean Olsen, "State Budget Cut Pain Shared by Many," The State Journal-Register, March 28, 2010, at http://www.sj-r.com/news/x38421208/State-budget-cut-pain-shared-by-many (last visited on April 3, 2010).
[56] Fran Spielman, "Governor May Keep State Cops on Local Expressways," *Chicago Sun-Times*, April 7, 2010, at http://www.suntimes.com/news/cityhall/2144258,CST-NWS-quinn07web.article (last visited on April 7, 2010).
[57] Illinois State FY2011 Budget, p. 10-3.
[58] Governor Pat Quinn, *Fighting for Illinois: Fiscal Year 2011 Budget*, March 10, 2010, at http://www.state.il.us/budget/FY2011/FY2011_Budget_Briefing.pdf (last visited on April 7, 2010). This document gives a personnel savings number of $203 million, which is reduced above to $133 because $70 million in negotiated savings on employee health insurance is included in the previously cited health insurance savings of $325 million.
[59] Council 31 AFSCME, AFSCME, *State Reach Mediated Resolution on Layoff Grievances*, January 27, 2010, at http://www.afscme31.org/news?id=0011 (last visited on April 7, 2010).

through the end of FY2011. The agreement states that wage deferrals will be restored if legislation that raises significant tax revenues is enacted.[60]

The Governor's recommended cuts are partially offset by increases to 15 departments. The table below provides a breakdown of departments with recommended increases in General Funds appropriations of $1.0 million or more.

State of Illinois Agencies with Increased Recommended General Funds Appropriations: FY2010 Enacted - FY2011 Recommended (in $ thousands)				
Agency	**FY2010 (enacted)**	**FY2011 (rec.)**	**$ Change**	**% Change**
Department of Healthcare & Family Services	$ 6,808,586	$ 7,324,861	$516,275	7.6%
Teachers' Retirement System	$ 116,678	$ 157,594	$ 40,916	35.1%
Department of Corrections	$ 1,151,335	$ 1,186,647	$ 35,312	3.1%
Department of Children & Family Services**	$ 980,115	$ 994,639	$ 14,524	1.5%
Executive Ethics Commission	$ 334	$ 8,271	$ 7,937	2376.3%
Court of Claims	$ 45,206	$ 52,926	$ 7,720	17.1%
Department of Transportation	$ 78,042	$ 83,335	$ 5,293	6.8%
Department of Veterans' Affairs	$ 60,449	$ 65,156	$ 4,707	7.8%
Property Tax Appeal Board	$ -	$ 2,382	$ 2,382	***
Illinois Guardianship & Advocacy Commission	$ 8,873	$ 9,897	$ 1,024	11.5%
Others	$ 7,291	$ 7,991	$ 700	9.6%
Total	**$ 9,256,909**	**$ 9,893,699**	**$636,790**	**6.9%**

Source: Illinois State FY2011 Budget, pp. 2-17 to 2-26
**The Department of Juvenile Justice is being merged into the Department of Children & Family Services.
***Percentage increase can not be calculated.

The largest proposed increase is to the Department of Healthcare and Family Services (HFS), the state agency that oversees Illinois' Medicaid program. The Medicaid program, which is funded jointly by the federal and state governments, is discussed on page 47. The Teachers' Retirement System sees a $40.9 million increase in General Funds appropriations. The increase reflects the State's return to traditional levels of funding the pension system of the Chicago Public Schools after reducing its contribution in FY2010.[61] The recommended General Funds appropriation to the Department of Corrections increases by 3.1%, or $35.3 million, to $1.2 billion, reflecting increased staffing to reduce future overtime costs.[62]

The Department of Children and Family Services (DCFS) receives an increase of $14.5 million. The Governor plans to merge the Department of Juvenile Justice into DCFS—a plan that comes shortly after a legislative audit found problems with management of the Department of Juvenile Justice since it was split off from the adult prison system in 2006.[63] Council 31 of AFSCME has opposed the merger and, at the labor union's urging, 33 state lawmakers signed a letter to the Governor asking him not to issue an executive order implementing the merger.[64] On April 1, 2010, the Governor issued an executive order that does not provide for immediate

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[60] Ibid.
[61] Illinois State FY2011 Budget, 5-8.
[62] Illinois State FY2011 Budget, 7-1.
[63] Kurt Erickson, "Governor Wants to Move Juvenile Justice Department Under Department of Children and Family Services, " *Herald & Review*, March 11, 2010, at http://www.herald-review.com/news/state-and-regional/article_4c67a0cb-85fd-529f-913c-b953b5412676.html (last visited on April 5, 2010).
[64] Council 32 AFSCME, "Legislators Seek to Delay DJJ Merger," April 1, 2010, at http://www.afscme31.org/news?id=0046 (last visited on April 5, 2010.)

implementation of the merger but establishes an interagency planning process and calls for enabling legislation.[65]

The Governor recommends an increase of $4.7 million for the Department of Veterans' Affairs, which will see its staffing grow by 7% or 87 workers to 1,328.5 full-time equivalents (FTEs).[66] The funding increase is aimed at reducing staff overtime and treating seriously ill patients at the State's four veterans' homes.[67] The largest percentage growth in recommended appropriations is to the Executive Ethics Commission, the agency that oversees ethics compliance by executive branch employees. The agency's budget will increase nearly 25 times from $334,000 to $8.3 million, while its headcount will grow from 10.0 FTEs in FY2010 to 72.0 in FY2011.[68] The expansion is recommended to allow the Commission to implement new legislative authority to oversee and review procurement processes.[69]

In the case of the Property Tax Appeal Board, an increase in General Funds is part of a shift in funding sources. In the FY2010 enacted budget, the agency got all of its funding—$2.8 million—from Other State Funds. In the FY2011 recommended budget, its total funding is $2.4 million, and all of it comes from General Funds.

Appropriations Trends

A direct comparison can be made between operating appropriations in the FY2010 enacted budget and the FY2011 recommended budget because in both budgets departmental appropriations include no General Funds contributions to the State's five retirement systems. In the FY2010 enacted budget, most of the State's contributions were made by borrowing, rather than from General Funds. In the FY2011 recommended budget, pension contributions are not included in the General Funds budgets of state agencies.[70] Instead, the $4.2 billion in projected pension contributions from General Funds is recorded in the FY2011 budget on a separate line following operating appropriations.

However, comparing the FY2011 recommended budget with the Governor's original recommended budgets in FY2010 and prior years is problematic. In recommended budgets for FY2010 and prior years, the State's General Funds pension contributions are included in departmental appropriations.

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[65] State of Illinois Executive Department, *Executive Order Commissioning A Plan for Integrating the Department of Juvenile Justice into the Department of Children and Family Services*, April 1, 2010, at http://www.illinois.gov/gov/execorders/docs/execorder2010-05.pdf (last visited on April 7, 2010).
[66] Illinois State FY2011 Budget, p. 6-60.
[67] Email communication between the Civic Federation and the Governor's Office of Management and Budget, April 16, 2010.
[68] Ibid, p. 10-56.
[69] Public Act 96-795, enacted on November 3, 2009.
[70] FY2011 recommended appropriations do include approximately $419 million in retirement systems contributions from Other State Funds. See Commission on Government Forecasting and Accountability, *Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009*, p. 87; and Illinois State FY2011 Budget, 2-10.

The following table shows recommended appropriations for FY2010 and FY2011. Total recommended appropriations decrease by 1.7%, from $52.9 billion to $52.0 billion, and General Funds recommended appropriations decline by 12.7%, from $28.4 billion to $24.8 billion.

State of Illinois Recommended Appropriations by Fund: FY2010-FY2011 (in $ thousands)				
	FY2010	FY2011*	$ Change	% Change
General Funds	$ 28,390,541	$ 24,775,432	$ (3,615,109)	-12.7%
Other Funds	$ 15,645,633	$ 17,436,135	$ 1,790,502	11.4%
Federal Funds	$ 8,836,464	$ 9,739,807	$ 903,343	10.2%
Total	**$ 52,872,638**	**$ 51,951,374**	**$ (921,264)**	**-1.7%**

Source: Illinois State FY2010 Budget, p. 2-30; Illinois State FY2011 Budget, p. 2-26.
*FY2011 figures do not include project savings of $267.0 million on pension contributions.

However, as explained above, these comparisons are somewhat misleading. The FY2010 recommended budget included a total of $1.5 billion in pension contributions, mostly from General Funds, while the FY2011 recommended budget includes no General Funds contributions to the retirement funds.

The table below compares the recommended FY2011 budget with the recommended FY2007 budget. Over the five-year period, total recommended appropriations increase by 14.4%, from $45.4 billion to $52.0 billion, and recommended General Funds appropriations drop by 3.6%, from $25.7 billion to $24.8 billion.

State of Illinois Recommended Appropriations by Fund: FY2007-FY2011 (in $ thousands)				
	FY2007 (rec.)	FY2011 (rec.)*	$ Change	% Change
General Funds	$ 25,711,790	$ 24,775,432	$ (936,358)	-3.6%
Other Funds	$ 14,125,477	$ 17,436,135	$ 3,310,658	23.4%
Federal Funds	$ 5,590,405	$ 9,739,807	$ 4,149,402	74.2%
Total	**$ 45,427,672**	**$ 51,951,374**	**$ 6,523,702**	**14.4%**

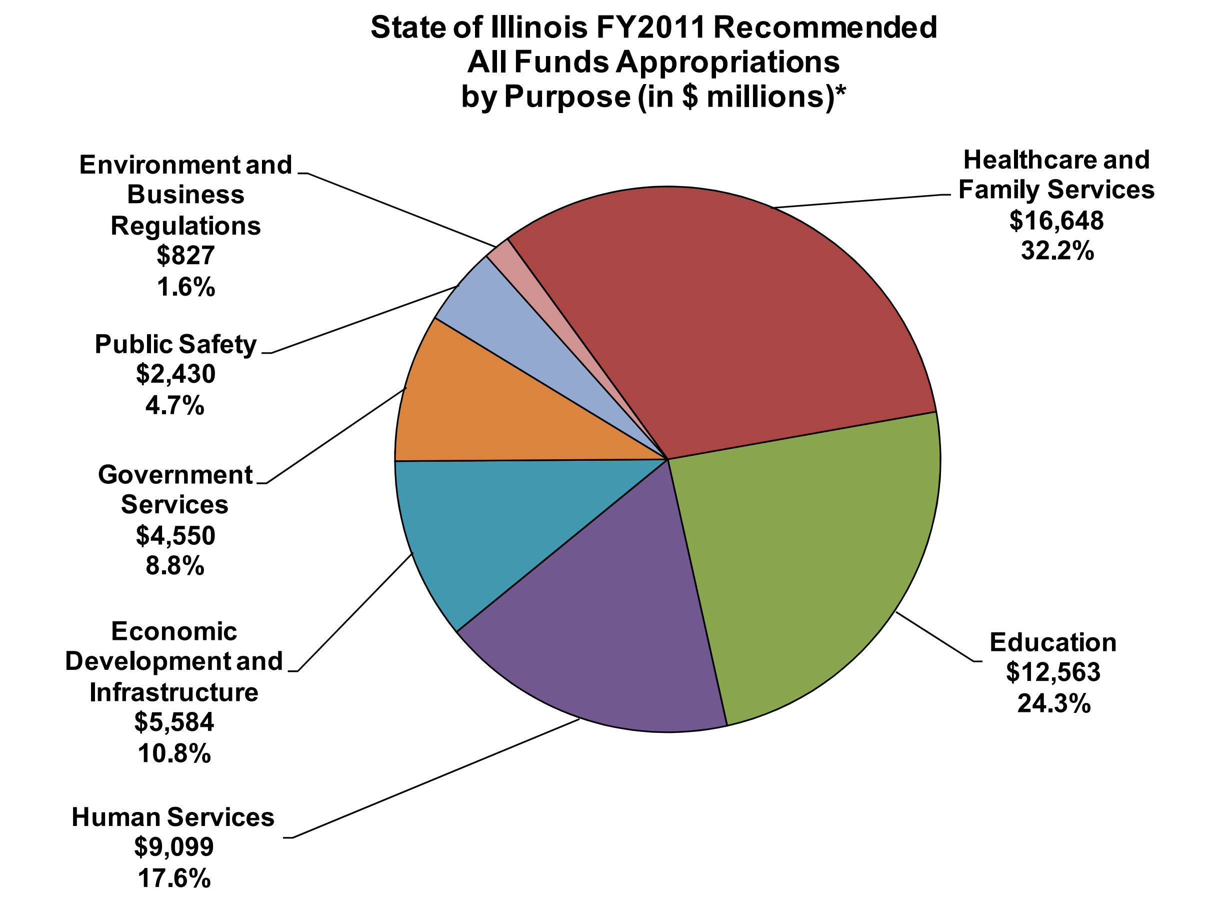
Source: Illinois State FY2011 Budget, p. 2-26; FY2007 Budget, p. 2-32.
*The General Funds number for FY2011 does not include projected savings of $267.0 million on pension contributions.

Again, the comparisons are not entirely appropriate. The FY2007 budget included $1.4 billion in pension contributions, mostly from General Funds.[71]

[71] Public Act 94-0004.

Appropriations by Purpose

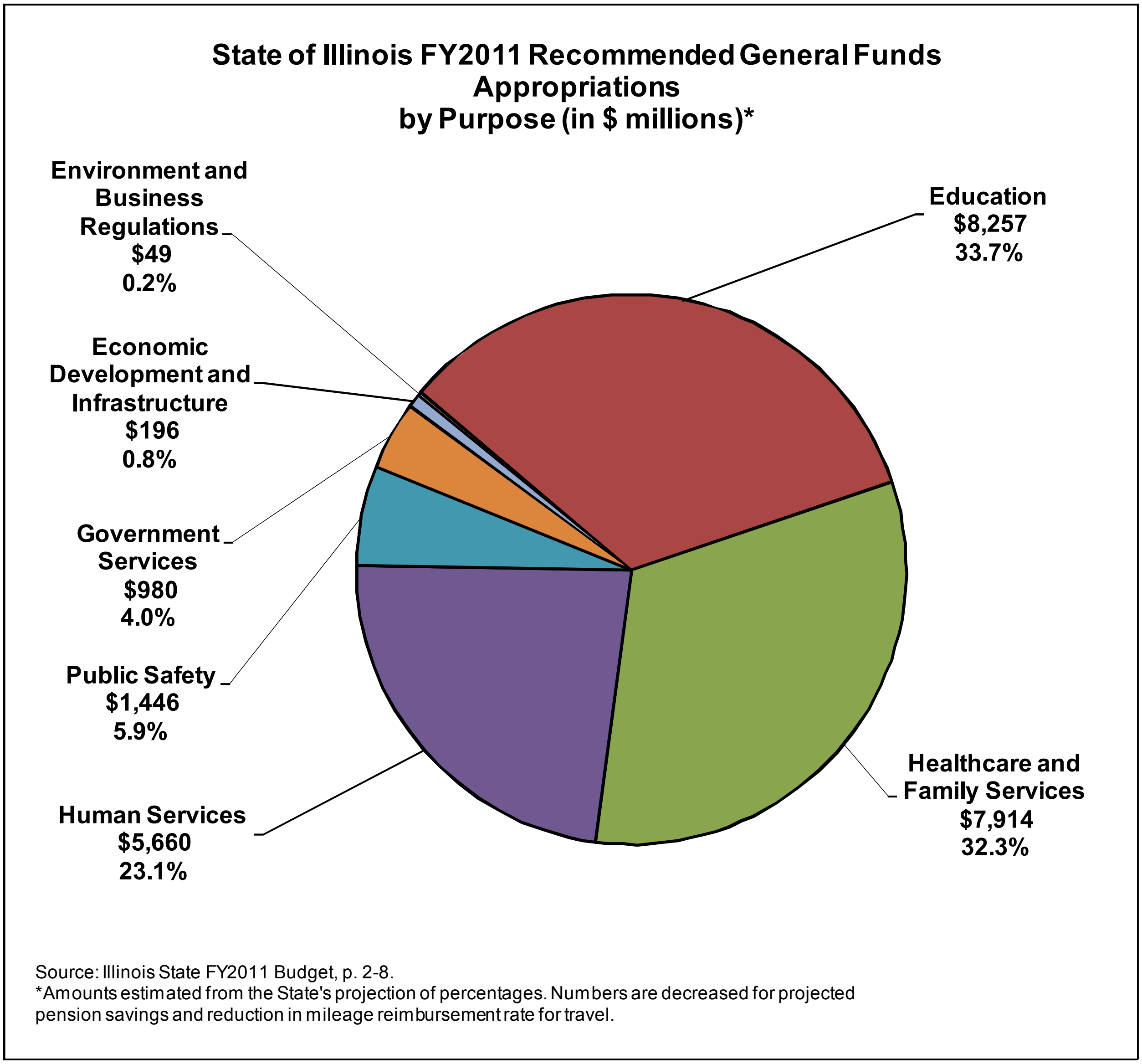
The following chart shows how FY2011 recommended appropriations are allocated across all funds according to major purpose. The numbers in this chart do not correspond to departmental figures or totals presented elsewhere in this section because they are reduced for the projected $267 million in pension savings discussed above, as well as for a reduction in mileage reimbursement rates for travel and for revolving funds. Revolving funds finance the operations of state agencies that provide services to other state agencies on a cost reimbursement basis.



Source: Illinois State FY2011 Budget, p. 2-8.
*Amounts estimated from State's projections of percentages. Figures are decreased for projected pension savings, reduction in the mileage reimbursement rate for traveland revolving funds.

The Department of Healthcare and Family Services, including the State Employees' Group Insurance Program, accounts for 32.2% of the total budget. Spending for elementary, secondary and higher education is the second largest category, representing 24.3% of all appropriations. Appropriations for human services account for 17.6% of the total.

The next chart shows FY2011 recommended General Funds allocation by major purpose. Similar to the chart above, the numbers below do not correspond to numbers elsewhere in this section because of the decreases for projected pension savings and the reduction in the mileage reimbursement rate for travel.



Education accounts for 33.7% of recommended FY2011 General Funds appropriations, while the Department of Healthcare and Family Services represents 32.2% and human services require 23.1% of the budget. The other categories make up smaller percentages of General Funds appropriations because they rely more heavily on funding from Other State Funds and Federal Funds.

Appropriations by Category

The following table shows changes in appropriations from the FY2010 enacted budget to the FY2011 recommended budget by agency category.

State of Illinois Appropriations by Agency Category: FY2010 Enacted - FY2011 Recommended (in $ thousands)				
Type	**FY2010 (enacted)**	**FY2011 (rec.)**	**$ Change**	**% Change**
Agencies Under the Governor				
Governor's Agencies Total	**$ 39,735,638**	**$ 39,719,582**	**$ (16,056)**	**0.0%**
General Funds	$ 15,706,180	$ 15,674,055	$ (32,125)	-0.2%
Other State Funds	$ 18,159,602	$ 18,440,586	$ 280,984	1.5%
Federal Funds	$ 5,869,856	$ 5,604,941	$ (264,915)	-4.5%
Elementary & Secondary Education				
Elementary & Secondary Education	**$ 11,106,273**	**$ 10,018,850**	**$ (1,087,423)**	**-9.8%**
General Funds*	$ 7,424,555	$ 6,238,651	$ (1,185,904)	-16.0%
Other State Funds	$ 44,268	$ 54,099	$ 9,831	22.2%
Federal Funds	$ 3,637,450	$ 3,726,100	$ 88,650	2.4%
Higher Education				
Higher Education Total	**$ 2,801,983**	**$ 2,591,955**	**$ (210,028)**	**-7.5%**
General Funds*	$ 2,211,471	$ 2,117,212	$ (94,259)	-4.3%
Other State Funds	$ 209,604	$ 88,865	$ (120,739)	-57.6%
Federal Funds	$ 380,908	$ 385,878	$ 4,970	1.3%
Elected Officials & Elections				
Elected Officials & Elections Total	**$ 2,592,684**	**$ 2,286,215**	**$ (306,469)**	**-11.8%**
General Funds	$ 523,065	$ 361,071	$ (161,994)	-31.0%
Other State Funds	$ 2,057,777	$ 1,914,304	$ (143,473)	-7.0%
Federal Funds	$ 11,841	$ 10,840	$ (1,001)	-8.5%
Judicial Agencies				
Judicial Agencies Total	**$ 419,884**	**$ 376,608**	**$ (43,276)**	**-10.3%**
General Funds	$ 364,156	$ 324,412	$ (39,744)	-10.9%
Other State Funds	$ 42,216	$ 39,661	$ (2,555)	-6.1%
Federal Funds	$ 13,512	$ 12,535	$ (977)	-7.2%
Legislative Agencies				
Legislative Agencies Total	**$ 103,601**	**$ 83,349**	**$ (20,252)**	**-19.5%**
General Funds	$ 79,162	$ 61,217	$ (17,945)	-22.7%
Other State Funds	$ 24,439	$ 22,132	$ (2,307)	-9.4%
Federal Funds	$ -	$ -	$ -	0.0%

Source: Illinois State FY2011 Budget, p. 2-17 to 2-26.

*FY2010 enacted General Funds appropriations for Elementary and Seconday Education and for Higher Education are reduced by $834.8 million and $8.5 million, respectively, to account for reimbursement of required pension contributions made from continuing appropriations.

Total proposed spending for agencies under the Governor,[72] the largest appropriations category, remains nearly flat at $39.7 billion. Total appropriations for elementary and secondary education, the next largest category, decline by 9.8% to $10.0 billion, while higher education drops by 7.5% to $2.6 billion. The largest percentage decline involves legislative agencies, with total appropriations reduced by 19.5% to $83.3 million.

[72] The Governor's agencies include over 55 departments that oversee agriculture, criminal justice, health, human services, economic development, environment and business regulation and finance issues across the State.

Appropriations by Largest Agency

The next table compares appropriations for the ten largest agencies in the FY2010 enacted budget and the FY2011 recommended budget.

State of Illinois Top Ten Largest Agencies FY2010 Enacted-FY2011 Recommended (in $ thousands)				
Agency	**FY2010 (enacted)**	**FY2011 (rec.)**	**$ Change**	**% Change**
Department of Healthcare and Family Services	**$ 15,278,949**	**$ 15,920,104**	**$ 641,155**	**4.2%**
General Funds	$ 6,808,586	$ 7,324,861	$ 516,275	7.6%
Other State Funds	$ 8,270,363	$ 8,395,243	$ 124,880	1.5%
Federal Funds	$ 200,000	$ 200,000	$ -	0.0%
State Board of Education	**$ 10,989,595**	**$ 9,861,256**	**$ (1,128,339)**	**-10.3%**
General Funds	$ 7,307,877	$ 6,081,057	$ (1,226,820)	-16.8%
Other State Funds	$ 44,268	$ 54,099	$ 9,831	22.2%
Federal Funds	$ 3,637,450	$ 3,726,100	$ 88,650	2.4%
Department of Human Services	**$ 6,224,149**	**$ 6,346,019**	**$ 121,870**	**2.0%**
General Funds	$ 4,036,885	$ 3,886,884	$ (150,001)	-3.7%
Other State Funds	$ 755,467	$ 744,549	$ (10,918)	-1.4%
Federal Funds	$ 1,431,798	$ 1,714,586	$ 282,788	19.8%
Department of Healthcare and Family Services Group Insurance	**$ 3,194,403**	**$ 2,939,865**	**$ (254,538)**	**-8.0%**
General Funds	$ 1,000,000	$ 675,000	$ (325,000)	-32.5%
Other State Funds	$ 2,194,403	$ 2,264,865	$ 70,462	3.2%
Federal Funds	$ -	$ -	$ -	-
Department of Transporation	**$ 2,512,168**	**$ 2,512,338**	**$ 170**	**0.0%**
General Funds	$ 78,042	$ 83,335	$ 5,293	6.8%
Other State Funds	$ 2,430,253	$ 2,424,957	$ (5,296)	-0.2%
Federal Funds	$ 3,873	$ 4,046	$ 173	4.5%
Department of Commerce and Economic Opportunity	**$ 2,670,213**	**$ 2,389,531**	**$ (280,682)**	**-10.5%**
General Funds	$ 50,325	$ 44,051	$ (6,274)	-12.5%
Other State Funds	$ 272,564	$ 331,420	$ 58,856	21.6%
Federal Funds	$ 2,347,323	$ 2,014,060	$ (333,263)	-14.2%
Office of the State Treasurer	**$ 1,743,160**	**$ 1,730,926**	**$ (12,234)**	**-0.7%**
General Funds	$ 16,918	$ 14,346	$ (2,572)	-15.2%
Other State Funds	$ 1,726,242	$ 1,716,580	$ (9,662)	-0.6%
Federal Funds	$ -	$ -	$ -	-
Department of Children & Family Services*	**$ 1,412,587**	**$ 1,439,451**	**$ 26,864**	**1.9%**
General Funds	$ 980,115	$ 994,639	$ 14,524	1.5%
Other State Funds	$ 424,404	$ 436,744	$ 12,340	2.9%
Federal Funds	$ 8,068	$ 8,068	$ -	0.0%
Department of Corrections	**$ 1,279,388**	**$ 1,305,163**	**$ 25,775**	**2.0%**
General Funds	$ 1,151,335	$ 1,186,647	$ 35,312	3.1%
Other State Funds	$ 128,052	$ 118,516	$ (9,536)	-7.4%
Federal Funds	$ -	$ -	$ -	-
Department of Revenue	**$ 1,396,818**	**$ 1,210,576**	**$ (186,242)**	**-13.3%**
General Funds	$ 142,504	$ 134,537	$ (7,967)	-5.6%
Other State Funds	$ 903,263	$ 996,312	$ 93,049	10.3%
Federal Funds	$ 346,050	$ 79,727	$ (266,323)	-77.0%

Source: Illinois State FY2011 Budget, 2-17 to 2-26.

*The Department of Juvenile Justice is being merged into the Department of Children & Family Services.

Several large agencies with decreases in FY2011 recommended General Funds appropriations were not included separately in the earlier table showing agencies with the biggest cuts because the reductions are less than $10 million. The Department of Commerce and Economic Opportunity (DCEO) shows a decline of $6.3 million, or 12.5%, in General Funds appropriations from $50.3 million to $44.1 million. DCEO's total recommended appropriations decline by $280.7 million, or 10.5%, from $2.7 billion to $2.4 billion, primarily due to a drop in Federal Funds.

The Office of the State Treasurer receives a $2.6 million decrease in recommended General Funds appropriations, from $16.9 million to $14.3 million. The Office of the Treasurer's overall funding declines by $12.2 million due to a reduction in Other State Funds. The Department of Revenue sees a drop of $8.0 million in General Funds appropriations, from $142.5 million to $134.5 million. The department's total appropriations are down $186.2 million, or 13.3%, from $1.4 billion to $1.2 billion, because of a decline in Federal Funds.

Education Appropriations

Education—including elementary, secondary and higher education—is the largest component of the FY2011 recommended General Funds budget, accounting for more than 33% of appropriations. Education is also the area where Governor Quinn has proposed $1.3 billion in cuts, or nearly 60% of the total $2.2 billion in recommended reductions in General Funds appropriations. This section gives a brief overview of education funding and examines the Governor's proposed education cuts.

Elementary and Secondary Education

Funding for elementary and secondary education is appropriated to the Illinois State Board of Education (ISBE), which distributes funding to more than 800 school districts in the State. The ISBE's largest spending program is for General State Aid. General State Aid provides funding to every school district largely based on the number of pupils, the amount of local property tax base and the poverty level of the districts' students.

General State Aid payments are based on a Foundation Level of funding that is established annually by statute. The Foundation Level is the minimum per child expenditure a school district is supposed to make. General State Aid is designed to help fill the gap between the Foundation Level and the amount a district can provide from local property tax revenues and other local resources.[73] The ISBE also provides school districts with categorical grants, which provide the majority of funding for services mandated by state and federal programs, such as special education; and targeted grants, which provide funding for specific populations and purposes to school districts throughout the State.[74]

The following table compares appropriations to the State Board of Education in the FY2010 enacted and FY2011 recommended budgets. This chart does not include operating appropriations for the Teachers' Retirement System (TRS), the retirement system for Illinois teachers outside the City of Chicago.[75] The Board of Education's budget is typically considered as a separate

[73] Illinois State Board of Education, *General State Aid – FY2010 Overview*, at http://www.isbe.state.il.us/funding/pdf/gsa_overview.pdf (last visited on April 7, 2010).
[74] Illinois State FY2011 Budget, p. 5-2.

component of the total budget for elementary and secondary education, which is composed of only two components: the Board of Education and TRS.

State of Illinois Appropriations to State Board of Education by Fund: FY2010 Enacted-FY2011 Recommended (in $ thousands)				
	FY2010 (enacted)	FY2011 (rec.)	$ Change	% Change
General Funds	$ 7,307,877	$ 6,081,057	$ (1,226,820)	-16.8%
Other State Funds	$ 44,268	$ 54,099	$ 9,831	22.2%
Federal Funds	$ 3,637,450	$ 3,726,100	$ 88,650	2.4%
Total	**$ 10,989,595**	**$ 9,861,256**	**$ (1,128,339)**	**-10.3%**

Source: Illinois State FY2011 Budget, p. 2-24.

As discussed above, Governor Quinn proposes a reduction of $1.2 billion, or 16.8%, in the State Board of Education's General Funds appropriations, from $7.3 billion in the FY2010 enacted budget to $6.1 billion in the FY2011 recommended budget. The Governor has said that the cuts are likely to cause nearly 17,000 teachers to lose their jobs.[76] According to the Governor, the cuts are necessary because of the loss of nearly $1.0 billion in funding from the federal American Recovery and Reinvestment Act of 2009.[77] In FY2009 and FY2010, those federal stimulus funds were used by the ISBE to make General State Aid payments.[78] The graph on the following page shows the Foundation Level for elementary and secondary education dating back to FY2007.

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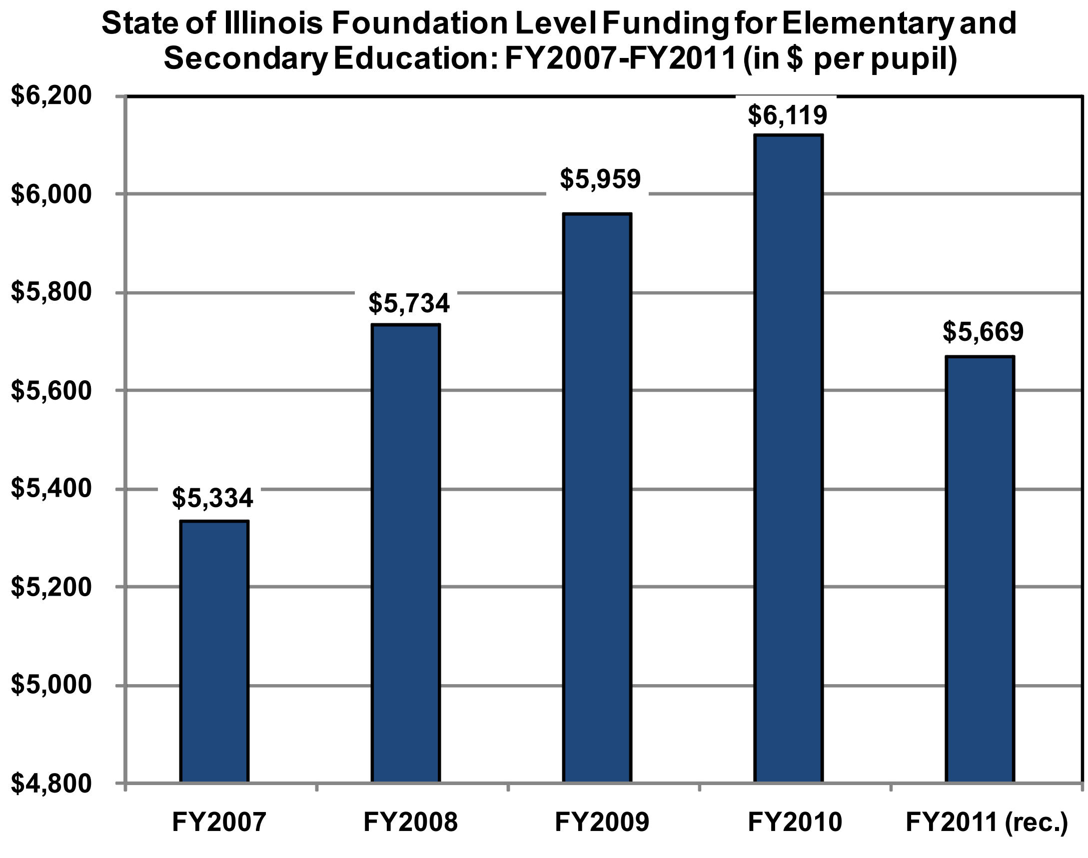
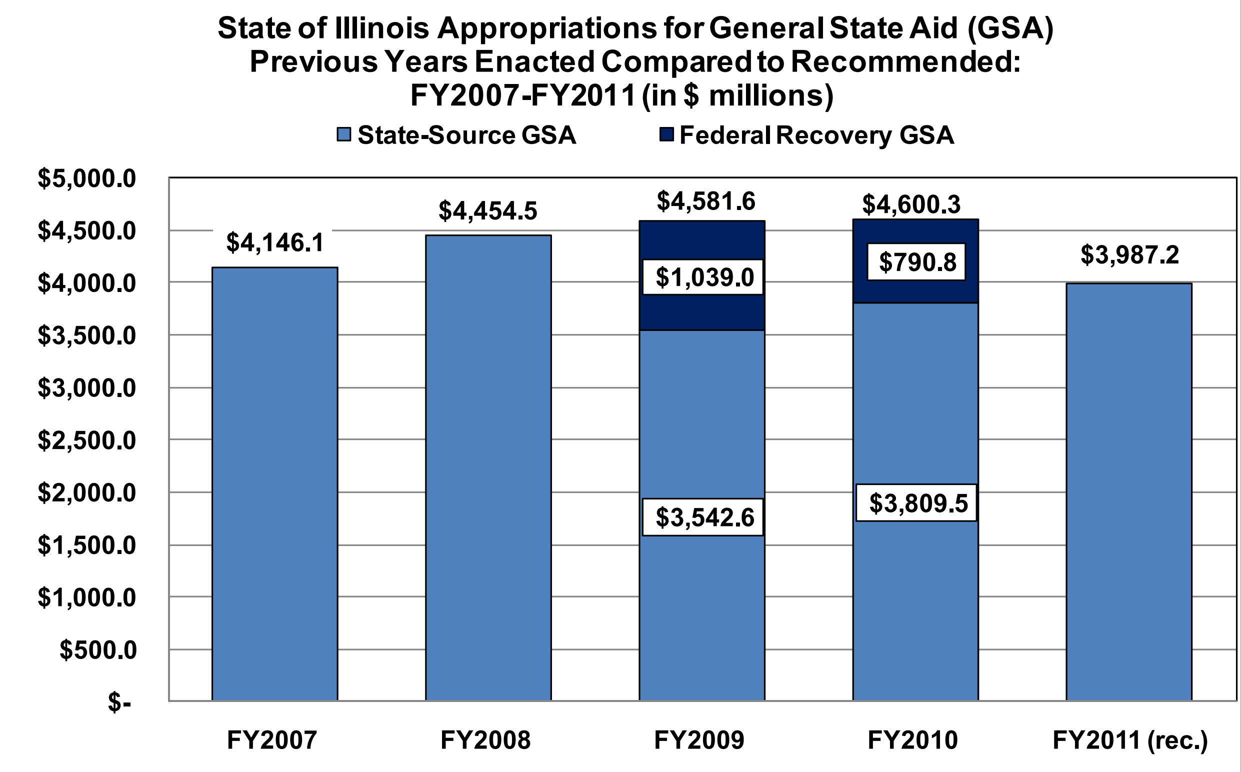
[75] Operating appropriations to the Teachers' Retirement System totaled $116.7 million in the FY2010 enacted budget (after reimbursement to General Funds of $834.9 million in pension contributions from continuing appropriations) and $157.6 million in the FY2011 recommended budget.
[76] Stephanie Banchero and Noreen Ahmed-Ullah, "State Deficit Casts a Shadow that Leaves Educators in the Dark," *Chicago Tribune*, March 14, 2010.
[77] Governor Pat Quinn, *FY2011 State of Illinois Budget Address*, March 10, 2010, at http://www2.illinois.gov/budget/Documents/FY%202011%20Transcript.pdf (last visited on April 7, 2010).
[78] Illinois State Board of Education, "State Board Focuses on Core Agency Mission by Reallocating Funds to Maintain Foundation Level*," news release*, January 14, 2010, at http://www.isbe.net/news/2010/jan14.htm (last visited on April 7, 2010).

Under the Governor's recommended budget, the Foundation Level falls to $5,669 per pupil in FY2011 from $6,119 in FY2010.



Source: Illinois State Board of Education, email communication with Civic Federation, March 24, 2010;

General State Aid to local school districts declines by $613.1 million, or 13.3%, from $4.6 billion in the FY2010 enacted budget to $4.0 billion in the FY2011 recommended budget. The chart below shows that most of the difference involves federal recovery funding.



Source: Illinois State FY2009 Budget, p. 6-3; FY2010 Budget, p. 5-4; and FY2011 Budget, pp. 5-3 and 5-4.

The ISBE recommended that the Foundation Level remain at the FY2010 level of $6,119, which would require an increase of $43 million in General State Aid to offset decreased corporate and residential property taxes.[79]

The Governor, as part of his budget address to the General Assembly, proposed a one-percentage point increase in the personal income tax to avert education cuts and make overdue state payments to school districts and universities.[80] However, the budget document does not include projected revenues from a tax increase or any plan reflecting how additional revenues would be used.

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[79] Illinois State Board of Education, "State Board Focuses on Core Agency Mission by Reallocating Funds to Maintain Foundation Level*," news release*, January 14, 2010, at http://www.isbe.net/news/2010/jan14.htm (last visited on April 7, 2010).

[80] Governor Pat Quinn, *FY2011 State of Illinois Budget Address*, March 10, 2010, at http://www2.illinois.gov/budget/Documents/FY%202011%20Transcript.pdf (last visited on April 7, 2010).

Higher Education

The Illinois higher education system consists of nine public universities, 48 community colleges, 97 private, not-for-profit institutions and 22 out-of-state institutions approved to offer degree programs in Illinois.[81] The higher education system is supported by a number of agencies, including the Illinois Board of Higher Education, the statewide coordinating board for higher education; the Illinois Community College Board, which provides statewide coordination for community colleges; the Illinois Student Assistance Commission, which administers student financial aid programs; and the Illinois Mathematics and Science Academy, a secondary school serving students across the State.

The next table compares appropriations to the higher education system in the FY2010 enacted and FY2011 recommended budgets. The numbers below include operating appropriations for the State Universities Retirement System (SURS), which covers employees at universities and community colleges.[82] Because the Board of Higher Education is just one of 15 components of the higher education system, each of the components, including SURS, is usually considered in analyzing the budget for higher education.

State of Illinois Appropriations to Higher Education by Fund: FY2010 Enacted-FY2011 Recommended (in $ thousands)

	FY2010 (enacted)	FY2011 (rec.)	$ Change	% Change
General Funds*	$ 2,211,471	$ 2,117,212	$ (94,259)	-4.3%
Other State Funds	$ 209,604	$ 88,865	$ (120,739)	-57.6%
Federal Funds	$ 380,908	$ 385,878	$ 4,970	1.3%
Total	**$ 2,801,983**	**$ 2,591,955**	$ (210,028)	-7.5%

Source:Illinois State FY2011 Budget, p. 2-25.
*FY2010 appropriation reduced by $8.5 million for reimbursement of General Funds continuing appropriations for pension contributions.

Governor Quinn proposes a reduction of $94.3 million, or 4.3%, in General Funds appropriations to the higher education system, from $2.2 billion in the FY2010 enacted budget to $2.1 billion in the FY2011 recommended budget. General Funds appropriations to public universities are cut by 6.2% across the board, or a total of $87.0 million. The Illinois Board of Higher Education (IBHE) attributes this decrease, and a drop of $6.9 million in community college base operating grants, to a loss of federal stimulus funds.[83]

General Funds appropriations for IBHE grants and to the Illinois Math & Science Academy and IBHE remain at the FY2010 levels. Total appropriations to the Illinois Student Assistance Commission grow by $27.5 million, or 3.4%, from $803.4 million in FY2010 to $830.9 in FY2011 because of an increase in Other State Funds.

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[81] Illinois State FY2011 Budget, 5-10.
[82] Operating appropriations to the State Universities Retirement System totaled $4.1 million in the FY2010 enacted budget (after reimbursement to General Funds of $8.5 million in pension contributions from continuing appropriations) and $4.2 million in the FY2011 recommended budget.
[83] Illinois Board of Higher Education, *Overview of Governor Quinn's Fiscal Year 2011 Budget Recommendation*, at http://www.ibhe.state.il.us/Fiscal%20Affairs/PDF/FY2011BudgetRecommendation.pdf (last visited on April 7, 2010).

Medicaid

The FY2011 budget recommends continued growth in Medicaid, the joint federal-state program that finances healthcare services for low-income people, including children, parents, the elderly and the disabled. This section provides an overview of the State's Medicaid program and an analysis of Medicaid-related appropriations in the FY2011 budget.

Medicaid financing is complex. As a program involving several state agencies, Medicaid has no specific designation in the state budget. The Department of Healthcare and Family Services (HFS) is the agency that oversees Medicaid spending in Illinois, but nearly 20% of expenditures are made by other agencies, including the Department of Human Services, the Department on Aging and the Department of Children and Family Services. In addition, although HFS' Medical Assistance Program is often considered equivalent to Medicaid, about 10% of the Medical Assistance budget is outside the Medicaid program. Recognizing these limitations, this section uses HFS' Medical Assistance program to represent Medicaid because it is the only readily available budget category.

Governor Quinn recommends total FY2011 Medical Assistance appropriations of $15.5 billion, an increase of $632.0 million, or 4.2%, from $14.9 billion in the FY2010 enacted budget.[84] General Funds appropriations for Medical Assistance rise by $517.4 million, or 7.8%, from $6.7 billion in the FY2010 enacted budget to $7.2 billion in the FY2011 recommended budget.[85] In addition to General Funds, other Medical Assistance appropriations come from the University of Illinois Hospital Services Fund, the County Provider Trust Fund, the Long Term Care Provider Fund, the Hospital Provider Fund, the Drug Rebate Fund, the Tobacco Settlement Recovery Fund and the Healthcare Provider Relief Fund.

Medicaid is jointly funded by states and the federal government. A state spends money for healthcare services and is then reimbursed by the federal government for a portion of the expenditures. The reimbursement rate has typically varied nationally from 50% to 83%, depending on a state's wealth. However, the American Recovery and Reinvestment Act of 2009 (ARRA) temporarily raised federal reimbursement rates, beginning in October of 2008. Illinois is currently being reimbursed at a rate of 61.88%, up from 50.32% before the federal stimulus law.[86] To receive the enhanced reimbursement, states must not decrease Medicaid eligibility and must meet federal prompt payment requirements. Most claims from doctors, hospitals and nursing homes must be paid within 30 days.

The enhanced reimbursement rate is scheduled to end on December 31, 2010 but would be extended through June 30, 2011 under a bill passed by the U.S. Senate.[87] Illinois' FY2011 budget recommendation assumes that the enhanced reimbursement rate will be extended for six months.[88] Approximately $450 million of the $908 million in federal recovery funds for

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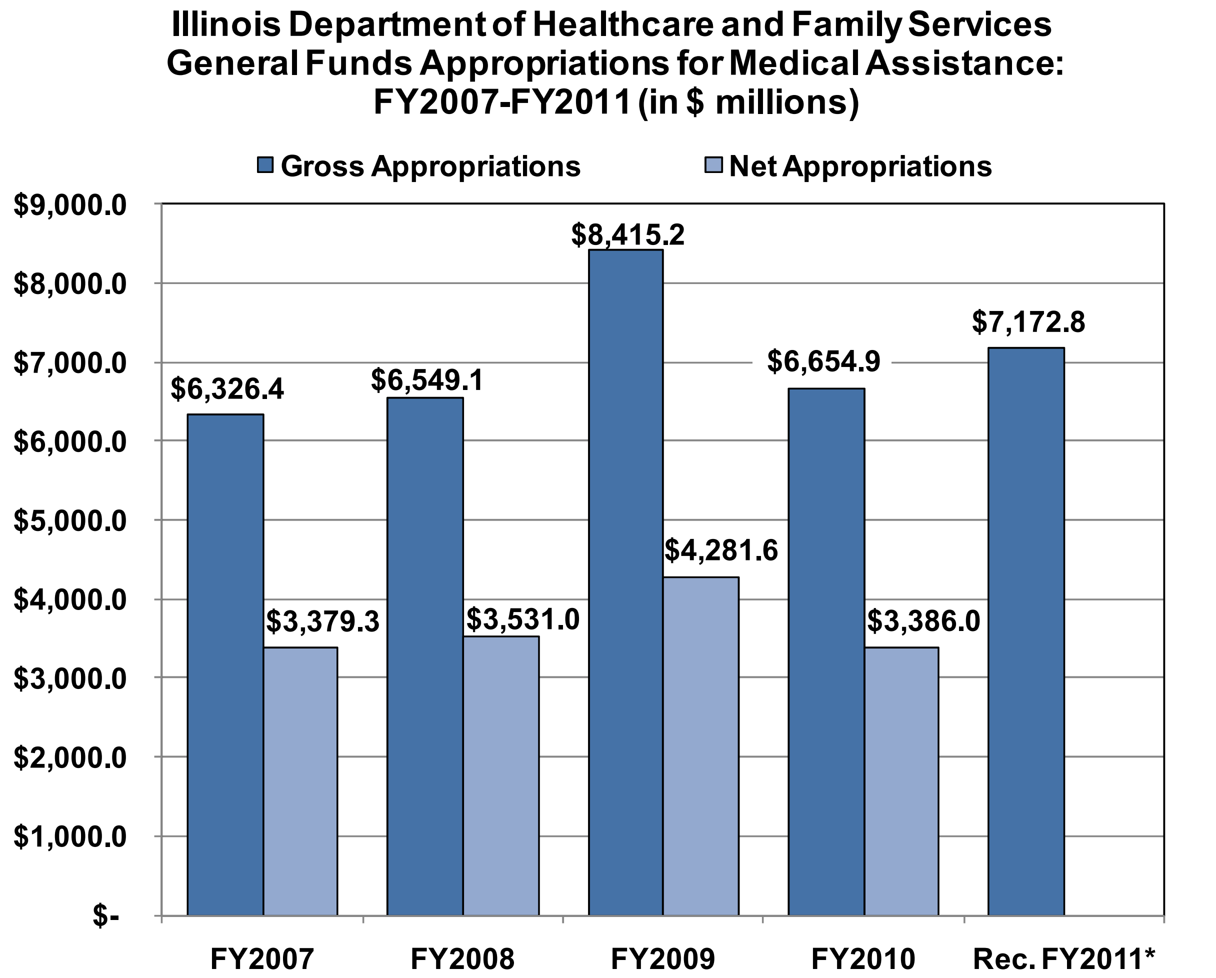
[84] Illinois State FY2011 Budget, p. 6-18.
[85] Illinois Department of Healthcare and Family Services, *Fiscal Year 2011 Budget Overview*, March 10, 2010, p. 15, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).
[86] Department of Healthcare and Family Services, *Highlights of the American Recovery and Reinvestment Act of 2009*, at http://hfs.illinois.gov/recovery/ (last visited on April 13, 2010).
[87] HR 4213, The American Workers, State, and Business Relief Act of 2010, as amended, passed by the U.S. Senate on March 10, 2010.
[88] Illinois State FY2011 Budget, p. 4-17.

Medicaid included in FY2011 projected General Funds revenues are based on the expected extension.[89]

The following chart shows General Funds appropriations to Medical Assistance from FY2007 to FY2011. The chart provides both gross appropriations, or total state-source General Funds appropriations, and net appropriations, or state funding after subtracting federal reimbursements.



Source: Email communication between Civic Federation and HFS, April 13, 2010.
*Net appropriations not available for FY2011.

Gross General Funds appropriations rose to $8.4 billion in FY2009 largely because the State appropriated a supplemental Medicaid amount of $1.5 billion to comply with the prompt payment requirements of the federal recovery program.[90] In FY2010, gross General Funds appropriations dropped to $6.7 billion because fewer bills needed to be paid down to meet the

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[89] Email communication between the Civic Federation and officials of the Department of Healthcare and Family Services, April 13, 2010.
[90] State of Illinois, $1 Billion General Obligation Bonds Taxable Build America Bonds, Series 2010-1, *Official Statement*, January 28, 2010, p.16.

prompt payment requirements and because the General Assembly reduced by about half appropriations to medical services providers not covered by the prompt payment standards.[91]

It has often been difficult to understand Medicaid spending trends by reviewing appropriations because increases can reflect the payment of overdue bills rather than new program initiatives. Illinois law allows the State to pay outstanding Medicaid bills from a future year's appropriations.[92] As a result, the State has repeatedly carried over substantial Medicaid liabilities to balance its budget.[93] HFS prefers to focus on liabilities, which are not dependent on when bills are paid. Medical Assistance General Funds liabilities and related obligations are expected to increase by $804.0 million, or 8.2%, from $9.8 billion in FY2010 to $10.6 billion in FY2011.[94]

The FY2011 recommended General Funds appropriation of $7.2 billion keeps the time to process bills from doctors, hospitals and nursing days at 30 days, as required by ARRA, and reduces the payment lag for other medical services providers to 60 days.[95] The payment delay for other providers, such as pharmacies and home health agencies, is currently 90 to 120 days, according to HFS officials.[96]

Medicaid Enrollment and Eligibility

The increased FY2011 appropriation also reflects growth in Medicaid enrollment.[97] The number of recipients grew 19.7% from 2,152,089 in 2007 to an estimated 2,575,886 in FY2010, according to HFS officials.[98] The program covers approximately 20% of the State's 12.9 million residents.[99] State officials said the recent rise in enrollment stems from increased participation in the program by people who were previously eligible but not enrolled, rather than an expansion of program eligibility. More people typically turn to Medicaid during economic recessions, as they are laid off or lose employer-sponsored health insurance.[100] Federal law requires states to cover certain segments of the population in order to receive federal matching funds for Medicaid.[101] Currently states must cover pregnant women and children under age 6 with family income below 133% of the Federal Poverty Level (FPL); children ages 6 to 18 below 100% of the FPL; parents below states' July 1996 welfare eligibility levels (often below 50% of the FPL); and most elderly and disabled people receiving Supplemental Security Income, for which income eligibility equates to 74% of the FPL for an individual. The FPL is now $10,830 for a single person and

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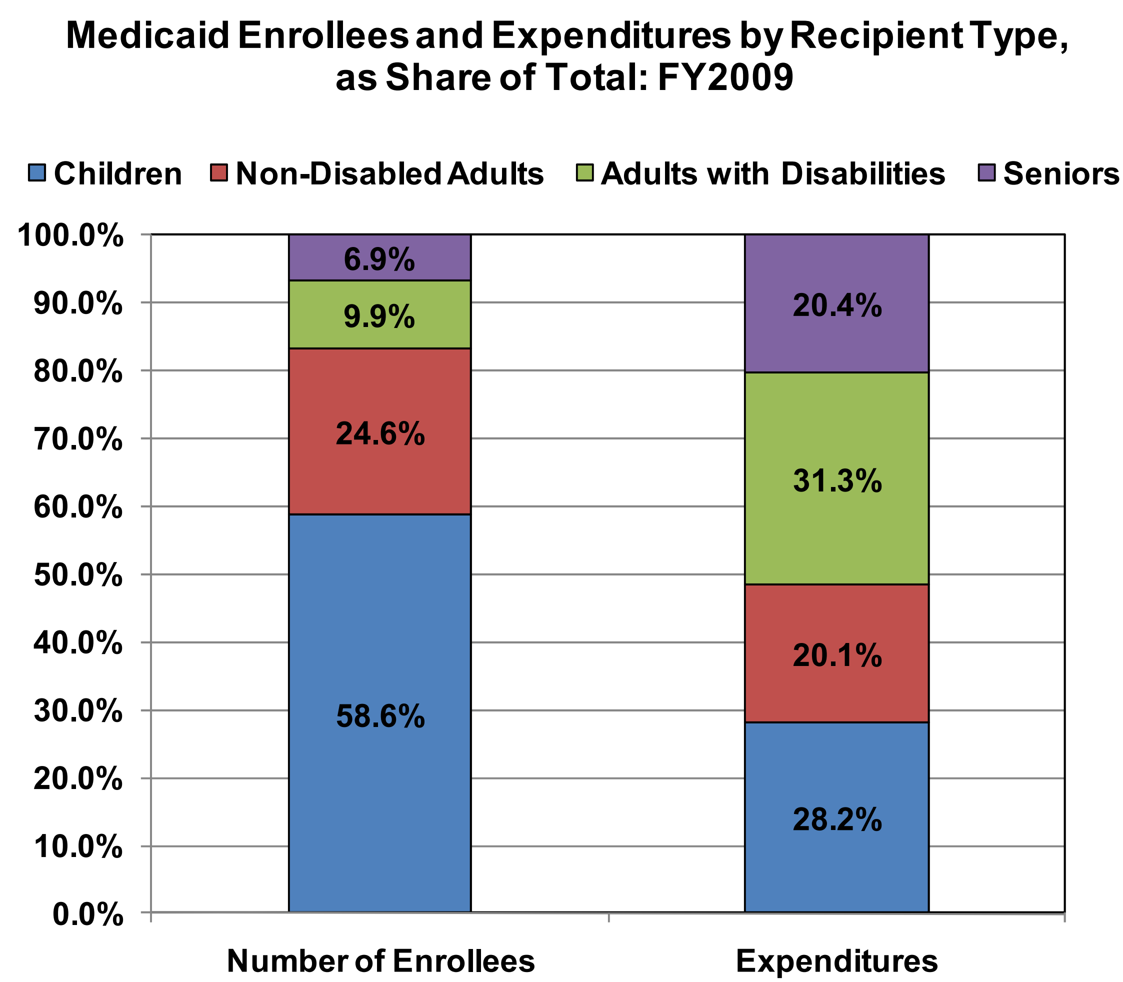
[91] Email communication between the Civic Federation and HFS officials, April 13, 2010.
[92] 30 ILCS 105/25(2007).
[93] Illinois State Comptroller, *Fiscal Focus*, July 8, 2008, p. 7 at http://www.apps.ioc.state.il.us/ioc-pdf/FFWeb0708.pdf (last visited on April 14, 2010).
[94] Email communication between the Civic Federation and HFS officials, April 13, 2010.
[95] Illinois Department of Healthcare and Family Services, *Fiscal Year 2011 Budget Overview*, March 10, 2010, p. 5, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 14, 2010).
[96] Phone communication between the Civic Federation and HFS, April 1, 2010.
[97] Ibid.
[98] Email communication between the Civic Federation and HFS, April 13, 2010.
[99] U.S. Census Bureau, Population Division, National and State Population Estimates, at http://www.census.gov/popest/states/NST-ann-est.html (last visited on April 13, 2010).
[100] The Kaiser Family Foundation, "Kaiser Analysis Finds Record Medicaid Enrollment Growth in 2009," *news release*, February 18, 2010.
[101] The Kaiser Family Foundation, Medicaid A Primer 2009, January 2009, p. 5, at http://www.kff.org/medicaid/upload/7334-03.pdf (last visited on April 14, 2010).

$22,050 for a family of four.[102] Regardless of income level, non-elderly adults without dependent children are excluded unless they are disabled or pregnant.

States have also been allowed to expand Medicaid eligibility to optional groups. Illinois, for example, receives federal matching funds for covering elderly and disabled people with incomes up to 100% of the FPL, children with family incomes up to 200% of the FPL and parents of low-income children up to 185% of the FPL.

Like other states, Illinois spends the most per recipient on the disabled and elderly. The next chart compares the breakdown of total Medicaid enrollment in FY2009 with the breakdown of total expenditures. For that year, total enrollment was 2,434,972 participants and total spending was estimated at $14.5 billion.[103]



Source: Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 2010, p.7.

[102] U.S. Department of Health & Human Services, *The 2009 HHS Poverty Guidelines*, at http://aspe.hhs.gov/POVERTY/09poverty.shtml (last visited on April 14, 2010).
[103] Email communication between the Civic Federation and HFS, April 13, 2010; National Association of State Budget Officer, *State Expenditure Report 2008*, Fall 2009, p. 47.

Medicaid-Related Cost-Saving Proposals

To better control costs for the most expensive Medicaid recipients, the State plans to place roughly 40,000 disabled and elderly recipients in health maintenance organizations (HMOs). The pilot program, scheduled to start in October of 2010, will be the first time that the State's Medicaid program has required mandatory enrollment in HMOs. The program is expected to save $200 million over the first five years.[104] That figure represents gross savings, before federal reimbursements. The HMOs will be paid a monthly fee from the State for each Medicaid recipient. HFS officials said the fee will be 5% below the amount the State is currently paying for medical services for the recipients.[105] The HMOs are expected to be able to deliver more efficient healthcare by eliminating duplicative drug prescriptions and lowering hospital readmission rates. State officials have not said how much the pilot program is expected to save in FY2011. The plan has been opposed by many advocates for the disabled, who have expressed concern that HMOs will save money by restricting needed services.[106]

The State is also reducing by half—to $70 million from $140 million—spending on a prescription drug program for seniors called Illinois Cares Rx, which provides supplemental benefits to fill in gaps in coverage under Medicare Part D. Illinois Cares Rx does not receive federal funding because recipients' income levels exceed federal eligibility limits.[107] HFS plans to cut costs by requiring participants to pay more for coverage rather than by reducing enrollment in Illinois Cares Rx.[108] There were 172,000 participants in the program as of May of 2009.[109] Federal health legislation signed into law on March 23, 2010 includes provisions to close the Medicare prescription drug gap—known as the "doughnut hole"—over 10 years.[110]

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[104] State of Illinois Department of Healthcare and Family Services, "Proposals Sought for Innovative Care Program," news release, February 8, 2010 http://www.illinois.gov/PressReleases/ShowPressRelease.cfm?SubjectID=2&RecNum=8235 (last visited on April 14, 2010).

[105] Phone communication between the Civic Federation and HFS officials, April 1, 2010.

[106] Access Living, "Access Living Opposes Managed Care Program Announced by State of Illinois," *news release*, February 10, 2010, at http://www.accessliving.org/index.php?tray=release&tid=top683&cid=2al86 (last visited on April 15, 2010); The Arc of Illinois, "Arc Testimony on Managed Care," *news release*, January 11, 2010, at http://www.thearcofil.org/documents/documentdetails.asp?did=2104 (last visited on April 15, 2010).

[107] Illinois Cares Rx is budgeted as a Medical Assistance program, rather than a Medicaid program, because it does not receive federal reimbursement.

[108] Illinois Department of Healthcare and Family Services, *Fiscal Year 2011 Budget Overview*, March 10, 2010, p. 10, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 14, 2010).

[109] Illinois Department of Healthcare and Family Services, *Response to Questions from the Taxpayer Action Board Medicaid Subcommittee*, May 5, 2009.

[110] Tara Parker-Pope, "What You Need to Know in the First Year," *The New York Times*, March 30, 2010.

PERSONNEL AND RETIREMENT SYSTEMS

This section describes the State's personnel-related expenditures and liabilities, including salary costs, health insurance costs, contributions to the retirement systems and pension obligations.

State Employee Payroll

Expenditures on state employee salaries historically have made up approximately 8% of the State's total appropriated expenditures and 10% of the State's General Funds appropriated expenditures. A relatively small proportion of the State's budget is spent on salaries because many state services and operations are not performed by state employees. State government in Illinois provides many services through funding for local governments, health care providers and human services providers, rather than having state employees perform and provide those services.

FY2010 Enacted and FY2011 Recommended Payroll

The Governor's budget recommends increasing the number of authorized full-time equivalent (FTE) positions from 63,857.2 in FY2010 to 64,236.4 in FY2011. The FY2011 headcount includes the Governor's headcount recommendation for agencies under the Governor. However, for agencies not under the Governor,[111] the headcount does not reflect the Governor's recommendation; rather, it reflects the appropriations these agencies requested from the Governor. The net increase of 379.2 FTEs or 0.6% consists of various increases that are partially offset by reductions elsewhere, including a reduction in state employees dedicated to public safety. The Governor recommends cutting 464.0 FTEs from the Department of State Police in FY2011 by closing three district headquarters. The next table compares the FY2010 estimated state employee headcount with the FY2011 headcount recommended by the Governor.[112]

State of Illinois FTE Headcount: FY2010-FY2011

	FY2010 Estimated	FY2011 Recommended	# Change	% Change
Education	916.0	918.0	2.0	0.2%
Human Services	23,395.0	23,691.5	296.5	1.3%
Public Safety	15,534.5	15,071.5	(463.0)	-3.0%
Environment and Business Regulations	3,931.7	3,969.4	37.7	1.0%
Economic Development and Infrastructure	8,530.0	8,831.0	301.0	3.5%
Government Services	11,550.0	11,755.0	205.0	1.8%
Total	**63,857.2**	**64,236.4**	**379.2**	**0.6%**

Source: Illinois State FY2011 Budget.

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[111] Agencies not under the Governor include the State Board of Elections, General Assembly agencies, judicial agencies and the offices of the Executive Inspector General, the Attorney General, the Secretary of State, the State Comptroller and the State Treasurer.

[112] Includes members of the General Assembly, but excludes General Assembly staff. Excludes employees of the State's nine public universities and the Illinois Math and Science Academy. Data in the FY2011 Government Services category is not congruent with appropriations data in this report for agencies not under the Governor. The headcount for agencies not under the Governor reflects the amount these agencies requested that the Governor include in the FY2011 budget recommendation, rather than an amount based on the Governor's recommended appropriations. The salary cost data and the headcount data do not completely correspond because the cost data include personnel costs for some employees that are not included in the headcount and the headcount data include some employees that are not in the cost data.

The 301.0 FTE increase in employees dedicated to economic development and infrastructure is primarily due to a 262.0 FTE increase in Department of Transportation employees. The Department of Transportation has the largest recommended increase in headcount increase for FY2011 of any department or agency. The 296.5 FTE increase in human services employees consists of an additional 87.0 FTEs for the Department of Veterans Affairs to add staff at veterans' homes and 208.0 FTEs for the Department of Children and Family Services (DCFS). DCFS is adding 95.0 FTEs for a juvenile aftercare program to reduce recidivism among juvenile offenders leaving institutions that would be funded with federal recovery funds. The child welfare and child protection divisions also would increase headcount by 69.0 FTEs.

The 205.0 FTE increase in government services employees primarily consists of an additional 75.0 FTEs in the Department of Revenue, which include new tax auditors to pursue uncollected tax liability and 62.0 FTEs for the Executive Ethics Commission to implement its new legislative authority to oversee and review procurement processes.[113]

While the state employee headcount rises by 0.6% in the Governor's FY2011 recommended budget, salary costs rise by 4.0% or $158.1 million. The FY2010 budget includes $4.0 billion for salary costs and the FY2011 Governor's recommendation includes $4.2 billion. However, for agencies not under the Governor,[114] salary costs corresponding to the Governor's recommended appropriations are not available. The salary costs for agencies not under the Governor reflect the budget requests made by those agencies to the Governor. The total increase in salary costs is primarily due to a $100.2 million increase in salary costs for human services employees. The following chart lists FY2010 enacted and FY2011 recommended salary costs by category for all funds.[115]

State of Illinois Salary Costs for All Funds: FY2010-FY2011
(in $ thousands)

	FY2010 Enacted	FY2011 Recommended	$ Change	% Change
Education	$ 55,003.0	$ 55,403.3	$ 400	0.7%
Human Services	$ 1,302,622.4	$ 1,402,796.8	$ 100,174	7.7%
Public Safety	$ 1,020,655.7	$ 1,025,070.4	$ 4,415	0.4%
Environment and Business Regulations	$ 219,840.5	$ 215,482.4	$ (4,358)	-2.0%
Economic Development and Infrastructure	$ 602,593.8	$ 627,387.8	$ 24,794	4.1%
Government Services	$ 792,704.5	$ 825,410.0	$ 32,706	4.1%
Total	**$ 3,993,419.9**	**$ 4,151,550.7**	**$ 158,130.8**	**4.0%**

Source: Email communication between the Civic Federation and the Governor's Office of Management and Budget, March 26, 2010.

113 Public Act 96-795

114 Agencies not under the Governor include the State Board of Elections, General Assembly agencies, judicial agencies and the offices of the Executive Inspector General, the Attorney General, the Secretary of State, the State Comptroller, and the State Treasurer.

115 Includes members of the General Assembly, but excludes General Assembly staff. Excludes employees of the State's nine public universities and the Illinois Math and Science Academy. Data in the FY2011 Government Services category is not congruent with appropriations data in this report for agencies not under the Governor. The cost data for agencies not under the Governor reflect the amount these agencies requested that the Governor include in the FY2011 budget recommendation, rather than an amount based on the Governor's recommended appropriations. The salary cost data and the headcount data do not completely correspond because the cost data include personnel costs for some employees that are not included in the headcount and the headcount data include some employees that are not in the cost data.

The increase in salary costs for human services for FY2011 is primarily due to a $65.6 million increase for the Department of Human Services in order to reduce overtime costs by hiring additional staff. Despite losing 463.0 FTEs, public safety salary costs increase by $4.4 million or 0.4%. The $24.6 million savings in the Department of State Police is offset by a $30.5 million increase for salary costs in the Department of Corrections. The Department of Corrections budget recommendation includes increased institutional staffing in order to reduce overtime costs in the future. Salary costs for employees dedicated to economic development and infrastructure increase by $24.8 million or 4.1%. This increase consists of an additional $11.9 million for additional Department of Transportation employees funded by the Road Fund and $14.1 million in Federal Funds for the Department of Employment Security. Salary costs for government services increase by $32.7 million or 4.1% largely due to an additional $10.9 million for the Supreme Court and $17.2 million for the Secretary of State. However, as mentioned above, the increase in salary costs for agencies not under the Governor, such as the Supreme Court and the Secretary of State, do not reflect the Governor's FY2011 recommended appropriations.

In FY2010, 68.5% of the total salary cost appropriations were from General Funds. The Governor recommends that General Funds expenditures for salary costs increase from $2.7 billion in FY2010 to $2.9 billion in FY2011. Salary expenditures account for 9.2% of total General Funds expenditures in FY2011.[116] This $209.9 million or 7.7% increase in General Funds salary costs is primarily a result of a funding shift from the Road Fund to General Funds for the Secretary of State. The Governor's recommendation reduces Road Fund support to the Secretary of State by $130.5 million, $86.2 million of which was used for salary costs in FY2010. The next chart compares salary costs by purpose for General Funds for FY2010 and FY2011.[117]

State of Illinois Salary Costs for General Funds: FY2010-FY2011
(in $ thousands)

	FY2010 Enacted	FY2011 Recommended	$ Change	% Change
Education	$ 21,483.4	$ 21,878.9	$ 396	1.8%
Human Services	$ 1,119,367.3	$ 1,210,808.6	$ 91,441	8.2%
Public Safety	$ 982,533.9	$ 986,705.1	$ 4,171	0.4%
Environment and Business Regulations	$ 44,882.0	$ 39,002.9	$ (5,879)	-13.1%
Economic Development and Infrastructure	$ 40,151.5	$ 37,124.3	$ (3,027)	-7.5%
Government Services	$ 528,260.1	$ 651,051.3	$ 122,791	23.2%
Total	**$ 2,736,678.2**	**$ 2,946,571.1**	**$ 209,893.0**	**7.7%**

Source: Email communication between the Civic Federation and the Governor's Office of Management and Budget, March 26, 2010.

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[116] Total General Funds expenditures including transfers out totaled $32.1 billion in the FY2011 Governor's recommendation.

[117] Includes members of the General Assembly, but excludes General Assembly staff. Excludes employees of the State's nine public universities and the Illinois Math and Science Academy. Data in the FY2011 Government Services category is not congruent with appropriations data in this report for agencies not under the Governor. The cost data for agencies not under the Governor reflects the amount these agencies requested that the Governor include in the FY2011 budget recommendation, rather than an amount based on the Governor's recommended appropriations. The salary cost data and the headcount data do not completely correspond because the cost data include personnel costs for some employees that are not included in the headcount and the headcount data include some employees that are not in the cost data.

Personnel costs for human services from General Funds increases by $91.4 million or 8.2% under the Governor's FY2011 budget recommendation. The majority of the General Funds increase totaling $61.6 million is in the Department of Human Services. Salary costs for employees dedicated to environment and business regulations decrease by $5.9 million or 13.1% primarily due to a $5.2 million reduction in Department of Natural Resources (DNR) salary costs. This reduction is partially offset by a $1.2 million increase in Other State Funds support for DNR salary costs. The Governor recommends reducing economic development and infrastructure General Funds salary costs by $3.0 million or 7.5%. This reduction includes a $1.9 million reduction for the Illinois Historic Preservation Agency.

FY2007 Actual and FY2011 Recommended Payroll

The Governor's FY2011 budget recommendation includes a headcount of 64,236.4 FTEs, an increase of 118.5 FTEs or 0.2% over the FY2007 headcount of 64,117.9 FTEs. While the total headcount remained flat over the five-year period, various departments have experienced increases and decreases. The FY2011 headcount includes the Governor's headcount recommendation for agencies under the Governor. However, for agencies not under the Governor,[118] the headcount does not reflect the Governor's recommendation; rather it reflects the appropriations these agencies requested from the Governor. The following chart compares the actual headcount in FY2007 with the headcount recommended by the Governor for FY2011.[119]

State of Illinois FTE Headcount: FY2007-FY2011				
	FY2007 Actual	FY2011 Recommended	# Change	% Change
Education	1,023.0	918.0	(105.0)	-10.3%
Human Services	23,372.5	23,691.5	319.0	1.4%
Public Safety	16,022.0	15,071.5	(950.5)	-5.9%
Environment and Business Regulations	4,142.4	3,969.4	(173.0)	-4.2%
Economic Development and Infrastructure	8,166.0	8,831.0	665.0	8.1%
Government Services	11,392.0	11,755.0	363.0	3.2%
Total	**64,117.9**	**64,236.4**	**118.5**	**0.2%**

Source: Illinois State FY2009 Budget; Illinois State FY2011 Budget .

Employees dedicated to public safety experienced the largest drop since FY2007. The reduction of 950.5 FTEs or 5.9% came from 733.5 FTE reduction for the Department of State Police and a 246.5 FTE reduction for the Department of Corrections. The largest headcount increase since FY2007 affects employees dedicated to economic development and infrastructure. This increase of 665.0 FTEs or 8.1% consists of a 335.0 FTE increase in the Department of Transportation, a

[118] Agencies not under the Governor include the State Board of Elections, General Assembly agencies, judicial agencies and the offices of the Executive Inspector General, the Attorney General, the Secretary of State, the State Comptroller, and the State Treasurer.

[119] Includes members of the General Assembly, but excludes General Assembly staff. Excludes employees of the State's nine public universities and the Illinois Math and Science Academy. Data in the FY2011 Government Services category is not congruent with appropriations data in this report for agencies not under the Governor. The headcount for agencies not under the Governor reflects the amount these agencies requested that the Governor include in the FY2011 budget recommendation, rather than an amount based on the Governor's recommended appropriations. The salary cost data and the headcount data do not completely correspond because the cost data include personnel costs for some employees that are not included in the headcount and the headcount data include some employees that are not in the cost data.

248.0 FTE increase for the Department of Employment Security and a 130.0 FTE increase for the Department of Commerce and Economic Opportunity.

The headcount of employees dedicated to human services increases by 319.0 FTEs or 1.4% primarily due to headcount increases for the Department of Veterans' Affairs totaling 238.0 FTEs or 21.8% more than the 1,090.5 FTEs authorized in FY2007.

In FY2007, the State of Illinois spent $3.7 billion on salary costs, $2.5 billion or 66.8% of which was from General Funds.[120] The FY2011 Governor's recommendation includes $4.2 billion for salary costs, an increase of $450.8 million or 12.2% from FY2007. Since FY2007, General Funds salary costs rose $474.0 million or 19.2% to $2.9 billion in FY2011. The 12.2% increase in total salary costs is primarily attributable to pay increases. The 19.2% increase in General Funds support for salaries resulted partially from salary increases, and also may have resulted from other factors, such as changes in the mix of employees whose salaries are provided through General Funds changing or greater state reliance on General Funds for salary costs than Other State Funds or Federal Funds.

State Employee and Retiree Health Insurance

Governor Quinn's FY2011 budget includes $324.5 million in savings from the State Employees' Group Insurance Program. These savings consist of $254.5 million in increased health insurance contributions from retirees and $70.0 million in health insurance savings related to current employees.[121] This section provides a brief overview of the State Employees' Group Insurance Program and examines the changes in retiree contributions proposed by the Governor. No details are available on the savings related to current employees, which will be negotiated with Council 31 of the American Federation of State, County and Municipal Employees (AFSCME).[122]

Health insurance costs for employees and retirees have been a rapidly growing part of the state budget, increasing by $393.9 million, or 22.0% in the last five years, from $1.8 billion in FY2007 to $2.2 billion in FY2010, according to a recent report by the legislature's Commission on Government Forecasting and Accountability (COGFA).[123] Costs are projected to rise by $59.9 million, or 2.7%, to $2.24 billion in FY2011.[124]

The group insurance program provides relatively generous health coverage for retirees. Under state law, retirees with at least 20 years of service and their survivors are not required to pay any

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[120] State of Illinois Office of the Comptroller, *Illinois Detailed Annual Report of Revenues and Expenditures 2007*, January 8, 2008, http://www.apps.ioc.state.il.us/ioc-pdf/DetAnn07.pdf (last visited on April 5, 2010).
[121] Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 10, 2010, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).
[122] Communication between the Civic Federation and officials of the Illinois Department of Healthcare and Family Services, April 1, 2010.
[123] Commission on Government Forecasting and Accountability, *State Employees Group Insurance Program Projected FY2011 Liabilities Report*, March 16, 2010, Executive Summary, p .i, at http://www.ilga.gov/commission/cgfa2006/Upload/fy2011stateemployees'groupinsurance.pdf (last visited on April 8, 2010).
[124] Ibid, Executive Summary, p.i. This is an estimate by the Illinois Department of Healthcare and Family Services; the estimate by the Commission on Government Forecasting and Accountability is slightly higher, at $2.3 billion in FY2011.

portion of their health insurance premiums.[125] Currently 90% of retirees pay no premiums, according to the Department of Healthcare and Family Services (HFS).[126]

Participants—including employees, retirees and dependents of the state government, state universities, the General Assembly and the judiciary—can choose from three major kinds of health care plans: an indemnity plan, a modified preferred provider plan (PPO) and various health maintenance organizations (HMOs). An indemnity plan offers traditional fee-for-service coverage, in which participants are permitted to choose any physician or hospital. PPOs and HMOs are forms of managed care, in which patients' choices of healthcare providers are restricted to control costs.

The State's indemnity plan, the Quality Care Health Plan (QCHP), is a self-insured plan. Although participants may choose any medical services provider, they receive enhanced benefits for using doctors and hospital who are members of a network. Indemnity plans also typically have higher participant out-of-pocket costs than managed care plans.

The Open Access Plan (OAP) is a modified PPO, a plan that uses significant monetary incentives to encourage the use of network providers. The Open Access Plan has different tiers offering different levels of freedom of choice and participant cost-sharing.

HMOs are typically the most restrictive but lowest cost health insurance programs. HMO plan coverage is restricted to network providers only and referrals for specialized services or hospitalization must be directed by the patient's primary care physician. Participant plan costs are low, with no deductibles and limited co-payments.

The State Employees' Group Health Insurance Program had an estimated 347,935 participants in FY2010, of which 34.7% were in the QCHP and 65.3% were in managed care plans, according to COGFA.[127] Membership in the QCHP has been declining since FY2005, while membership in managed care plans has been increasing since FY2004.

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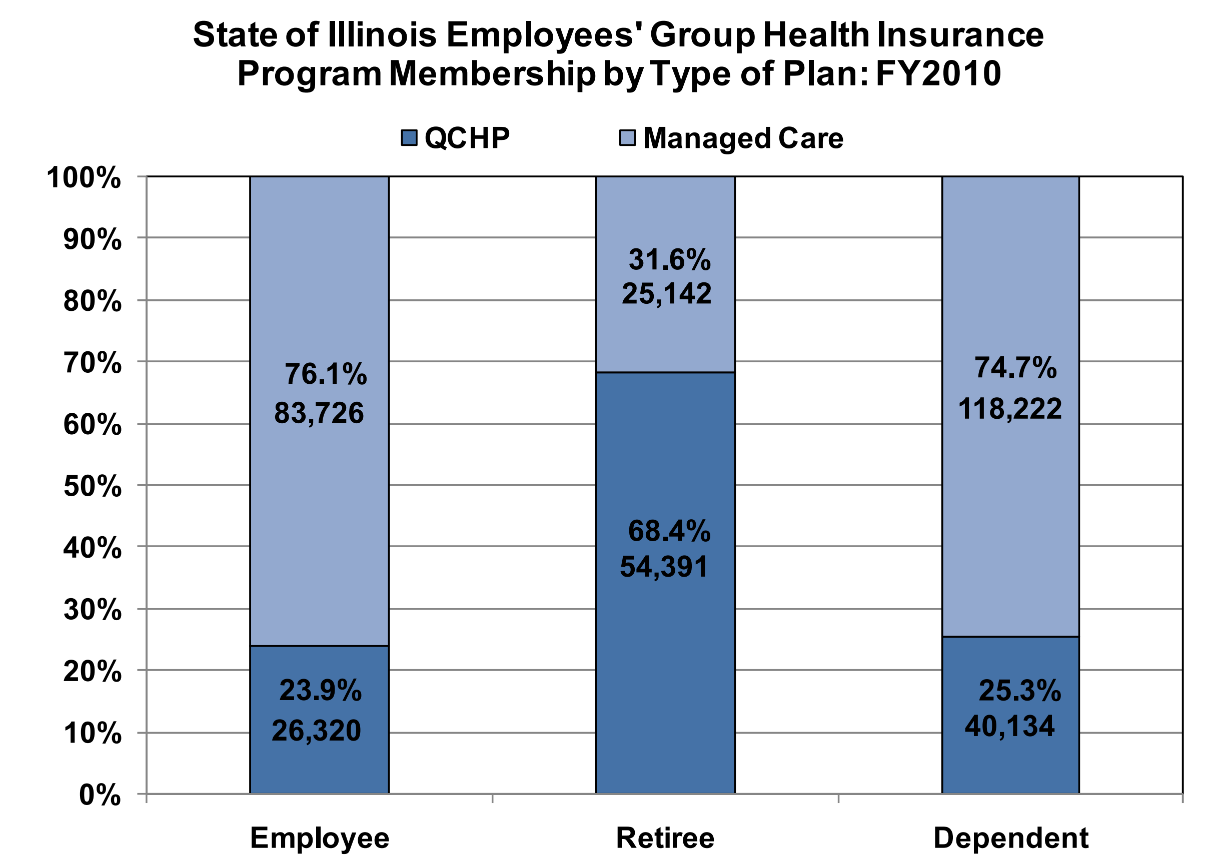
[125] State Employee Group Insurance Act of 1971, 5 ILCS 375/10.
[126] Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 10, 2010, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).

[127] Commission on Government Forecasting and Accountability, *State Employees Group Insurance Program Project FY2011 Liabilities Report*, March 16, 2010, p. 6, at http://www.ilga.gov/commission/cgfa2006/Upload/fy2011stateemployees'groupinsurance.pdf (last visited on April 8, 2010).

The following chart shows the breakdown of program membership in the QCHP and managed care plans. In FY2010, 68.4% of retirees chose QCHP, compared with 23.9% of employees and 25.3% of dependents. Employees and dependents overwhelmingly favored the less expensive managed care plans.[128]



Source: Commission on Government Forecasting and Accountability, email communication with Civic Federation, April 8, 2010.

[128] Email communication between the Civic Federation and the Commission on Government Forecasting and Accountability, April 8, 2010.

In FY2010, the average annual cost per participant (including both contributions by the State and by participants) was $6,486 for the QCHP, 28.5% higher than the $5,047 average annual cost for the managed care plans.[129] The State's average share of the annual cost was $5,685 per participant for the QCHP and $4,394 per participant in managed care.[130] On average, plan participants paid 12% to 13% of the premium bill, while the State paid the remaining 87% to 88%.

State of Illinois Employees' Group Health Insurance Average Annual Cost by Type of Plan: FY2010 (in $ per participant)			
	Member Contribution per Year	State Cost per Year (Minus Member Contribution)	Total Cost per Year
QCHP	$ 801	$ 5,685	$ 6,486
Managed Care	$ 653	$ 4,394	$ 5,047

Source: Commission on Government Forecasting and Accountability, *State Employees Group Insurance Program Projected FY2011 Liabilities Report*, March 16, 2010, p.10.

In his FY2011 budget, Governor Quinn proposes that the State limit its share of retiree health insurance premiums to $300 per month.[131] The change would mean that Medicare-eligible retirees, for whom the state plan serves as supplemental insurance, would pay between $4 per month and $50 per month, depending on which insurance plan they chose. For retirees not yet on Medicare, the cost would be between $290 per month and $500 per month.[132]

The proposal follows the premium-sharing practices of the federal government and most private businesses that offer retiree health benefits.[133] Over the past two decades, many employers have stopped offering retiree health benefits. Only 29% of large employers that provided health benefits to active workers in 2009 also offered retiree health benefits, down from 66% in 1988, according to a survey by the Kaiser Family Foundation and the Health Research & Educational Trust.[134] However, 81% of state and local governments in the survey offered retiree health benefits.

Implementing the Governor's proposal would require a change in state law but would not require labor negotiations, according to HFS officials.[135] Council 31 of the American Federation of

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[129] Ibid, p.10.
[130] Ibid, p.10.
[131] Illinois State FY2011 Budget, p. 6-16.
[132] Illinois Department of Healthcare and Family Services, Fiscal Year 2011 Budget Overview, March 10, 2010, at http://www.hfs.illinois.gov/assets/fy2011.pdf (last visited on April 7, 2010).
[133] U.S. Office of Personnel Management, *Insurance Programs/Retirees/Health* ,at http://www.opm.gov/insure/retirees/index.asp?ProgramId=1 (last visited on April 19, 2010); Kaiser Family Foundation and Hewitt Associates, Retiree Health Benefits Examined: Findings from the Kaiser/Hewitt 2006 Survey on Retiree Health Benefits, December 2006, p. 16, at http://www.kff.org/medicare/upload/7587.pdf (last visited on April 19, 2010). In 2009, only 29% of large firms offering health benefits to active workers offered retiree health benefits, according to Kaiser's 2009 *Employer Health Benefits Survey*.
[134] Kaiser Family Foundation and Health Research & Educational Trust, *Employer Health Benefits: 2009 Annual Survey*, September 15, 2009, p.165 at http://ehbs.kff.org/pdf/2009/7936.pdf (last visited on April 19, 2010).
[135] Civic Federation conversations with officials at the Illinois Department of Healthcare and Family Services, April 1, 2010, and April 9, 2010.

State, County and Municipal Employees (AFSCME), which represents many of the affected state workers, has said the Governor's proposal cannot be put into effect without negotiations.[136]

In his FY2010 budget, the Governor proposed increased premiums for both employees and retirees who participated in QCHP. The proposal faced considerable opposition from AFSCME Council 31.[137] No action was taken on the proposal by the General Assembly.

In October of 2009, the State began charging retirees a monthly premium for dental insurance. This action did not require a change in state law, because dental insurance is not part of basic health coverage. AFSCME Council 31 filed a grievance against the State, arguing that it had historically bargained with the union over the terms of retiree healthcare and that the State could not unilaterally make a change. An arbitrator ruled against the union, and in March of 2010 the union filed a lawsuit against the State in Cook County Court over the issue.[138]

State Retirement Systems

Illinois' retirement systems are in the worst shape of any state retirement systems in the country[139] and represent a growing burden on the State's operating budget. On April 14, 2010, Governor Quinn signed into law pension legislation that would substantially reduce Illinois' pension costs in the long run by reducing benefits for new workers.[140] This section reviews the financial condition of the retirement systems and examines the new pension reforms.

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[136] Dean Olsen, "State Retiree Health Premiums 'Totally Unaffordable,' AFSCME Says," *The State Journal-Register*, March 13, 2010, at http://www.behealthyspringfield.com/sections/local-news/state-retiree-health-premiums-totally-unaffordable-afscme-says (last visited on April 12, 2010).
[137] Kurt Erickson, "State Workers Could See Health Insurance Increases," *The Pantagraph*, April 22, 2009.
[138] Council 31 AFSCME, AFSCME Sues State Over Change to Retiree Insurance, March 9, 2010, at http://www.afscme31.org/news?id=0035 (last visited on April 8, 2010).
[139] The Pew Center on the States, *The Trillion Dollar Gap*, February 2010, p.3, at http://downloads.pewcenteronthestates.org/The_Trillion_Dollar_Gap_final.pdf (last visited on April 9, 2010).
[140] Public Act 96-0889, approved on March 24, 2010.

The State of Illinois funds five state retirement systems: the Teachers' Retirement System (TRS), the State Employees' Retirement System (SERS), the State Universities Retirement System (SURS), the Judges' Retirement System (JRS) and the General Assembly Retirement System (GARS). Employees also contribute to the systems, with contributions ranging from 4% to 12.5% of salary depending on the system and whether or not the employee participates in the federal Social Security program.[141] As of June 30, 2009, there were a total of 722,914 participants in the systems.

Members of Illinois Retirement Systems: Enrollment as of June 30, 2009			
Pension Fund	**Members**	**Annuitants**	**Total**
Teachers	273,890	94,419	368,309
Universities	161,325	46,810	208,135
State Employees	86,738	57,099	143,837
Judges	991	982	1,973
General Assembly	259	401	660
Total	**523,203**	**199,711**	**722,914**

Source: Illinois State FY2011 Budget, p. 3-1.

The financial health of retirement systems is measured by the extent to which their assets cover their estimated liabilities, as determined by actuarial calculations. Estimated pension liabilities are the total benefits earned by employees on the date of the estimate. Unfunded liabilities are liabilities that are not covered by assets held by the systems' investment funds. A funded ratio shows the percentage of liabilities that are covered by assets.

As shown in the table below, Illinois' retirement systems had total unfunded liabilities estimated at $62.4 billion and a combined funded ratio of 50.6% as of June 30, 2009.

State of Illinois Retirement Systems Funded Ratios and Unfunded Liabilities: FY2009* (in $ millions)				
Pension Fund	**Accrued Liability**	**Net Assets**	**Unfunded Liability**	**Funded Ratio**
Teachers	$ 73,027.5	$ 38,026.0	$ 35,001.2	52.1%
Universities	$ 26,316.2	$ 14,282.0	$ 12,034.2	54.3%
State Employees	$ 25,298.3	$ 11,000.0	$ 14,298.3	43.5%
Judges	$ 1,548.5	$ 616.8	$ 931.7	39.8%
General Assembly	$ 245.2	$ 71.6	$ 173.6	29.2%
Total	**$ 126,435.4**	**$ 63,996.4**	**$ 62,439.0**	**50.6%**

*Based on June 30, 2009 assets with asset smoothing
Source: Commission on Government Forecasting and Accountability, Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009, March 2010, p.18.

The figures in the table above reflect legislation passed by the General Assembly in July of 2009 that requires the retirement systems to account for unexpected investment gains or losses over a five-year period. This method, known as asset smoothing, replaced the market value approach,

[141] State of Illinois, $400,000,000 General Obligation Bonds Series A of September 2009, *Preliminary Official Statemen*t, September 9, 2009, p 42.

under which unexpected gains or losses are recognized immediately in the current year.[142] Asset smoothing is used by major Chicago area local pension funds and by most other states.[143] Because of the substantial decline in the stock market during much of FY2009, the use of asset smoothing will result in lower reported unfunded liability levels and higher funded ratios in the short term.

Under the previous method of calculating asset values, the retirement systems had total unfunded liabilities of $77.8 billion and a combined funded ratio of 38.5% as of June 30, 2009, according to a recent report by the legislature's Commission on Government Forecasting and Accountability (COGFA).[144] The Pew Center study that ranked Illinois' retirement systems as the least well funded of any state was based on funded ratios as of June 30, 2008. At that time, using the market value method, the Illinois retirement systems had a combined funded ratio of 54.3%.[145]

Although Illinois' pension funding problems have been exacerbated by recent market conditions, the State has skimped on contributions to its pension funds for decades.[146] To help deal with chronic underfunding, lawmakers enacted a pension funding reform law that took effect in 1995 and established a 50-year schedule of funding requirements.[147] After a phase-in period of 15 years, the law required state contributions at a level percentage of payroll beginning in FY2010 sufficient to achieve a 90% funded ratio by 2045. The retirement systems calculate and certify the amounts needed each year to meet the requirements of this funding schedule. Each retirement system must certify the contribution for the following fiscal year by November 15.

The pension reform law imposed specific requirements for state funding, but it did not require the State to make adequate contributions to keep unfunded liabilities from growing until approximately 2034. The contribution amount that is adequate to keep unfunded liabilities from growing consists of the normal cost, which is the amount needed to cover the present value of benefits earned by system members in each fiscal year, plus interest on the unfunded liability. This contribution, while adequate to prevent growth in unfunded liabilities, is not enough to pay down unfunded liabilities.

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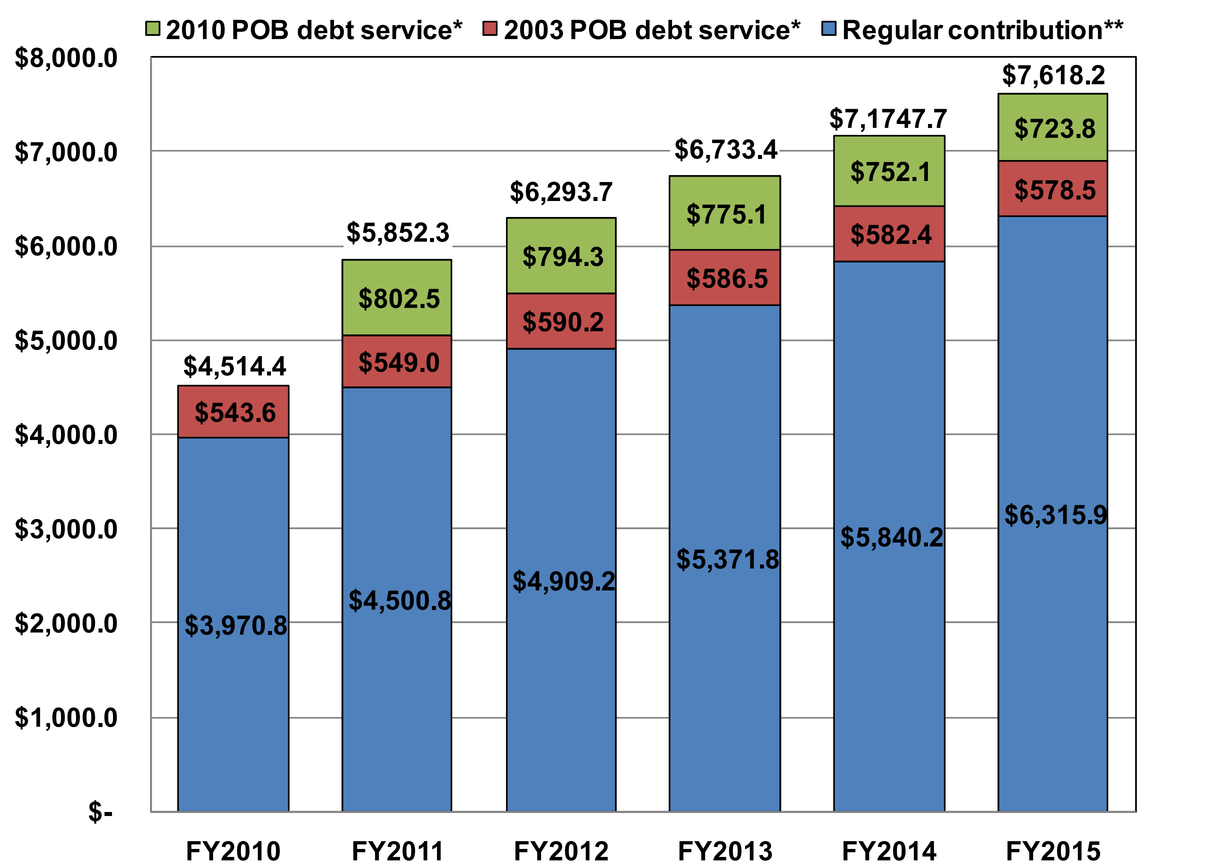
[142] Public Act 96-0043.
[143] Pew Center on the States, *The Trillion Dollar Gap*, February 2010, p. 5, http://downloads.pewcenteronthestates.org/The_Trillion_Dollar_Gap_final.pdf (last visited on April 13, 2010); Civic Federation, *Status of Local Pension Funding Fiscal Year 2008: An Evaluation of Ten Local Government Employee Pension Funds in Cook County*, March 8, 2010, p. 8, at http://civicfed.org/sites/default/files/StatusofLocalPensionsFY2008.pdf (last visited on April 13, 2010).
[144] Commission on Government Forecasting and Accountability, *Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009*, March 2010, p. 19 at http://www.ilga.gov/commission/cgfa2006/Upload/FinCondILStateRetirementSysMar2010.pdf (last visited on April 9, 2010).
[145] Pew Center on the States, *The Trillion Dollar Gap*, February 2010, p. 4, http://downloads.pewcenteronthestates.org/The_Trillion_Dollar_Gap_final.pdf (last visited on April 13, 2010).
[146] For a more comprehensive look at the history of Illinois pension funding, see The Civic Federation, *State of Illinois Retirement Systems: Funding History and Reform Proposals*, September 30, 2008 at http://civicfed.org/sites/default/files/civicfed_279.pdf (last visited on January 14, 2010).
[147] Public Act 88-593.

In FY2010, the State's total pension contribution was $4.0 billion.[148] The General Funds portion of the contribution was paid for through the issuance of $3.5 billion in five-year Pension Obligation Bonds.[149] The State will be paying debt service on these notes through FY2015 and on a previous $10 billion issue of Pension Obligation Bonds through FY2033. Debt service on the two bond issues totals $22.7 billion.[150] In FY2011, the State's total pension contribution has been certified at $4.6 billion.[151] The General Funds portion of the contribution is $4.2 billion.[152]

The following chart shows how pension funding pressures on the operating budget will increase in the next five years.

State of Illinois Retirement Systems Projected Total State Pension Cost: FY2010-FY2015 (in $ millions)



Source: Commission on Government Forecasting and Accountability, Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009, March 2010, p. 23.
*Pension Obligation Bond.
**Small portion of SERS contribution includes POB debt service; this is subtracted from required contribution to get regular contribution.

148 Commission on Government Forecasting and Accountability, *Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009*, March 2010, p. 87.
149 Ibid, p. 13.
150 Illinois State FY2011 Budget, p. 11-10.
151 Commission on Government Forecasting and Accountability, *Report on the Financial Condition of the Illinois State Retirement Systems as of June 30, 2009*, March 2010, p.87.
152 Illinois State FY2011 Budget, p. 2-10.

The costs above include state pension contributions as well as debt service costs. It should be noted that contributions may be changed by statute, but debt payments are guaranteed by the full faith and credit of the State.[153] More information on pension borrowing costs is contained in the Debt Trends section on page 66.

In his FY2010 budget, the Governor proposed several changes to the pension structure for newly hired state workers. The changes included adjustments to the retirement age, benefit formula and cost of living payment increases. The proposal maintained the pension benefit structure for existing state employees but increased their contributions.[154] No action on the proposal was taken by the General Assembly.

The pension reform legislation signed into law by the Governor on April 14, 2010 contains major reductions in pension benefits for newly hired state employees, while maintaining the current pension structure for existing employees.[155] The legislation raises the retirement age, limits the maximum pensionable salary and reduces cost of living adjustments. It also eliminates double-dipping by suspending the pension of any retiree who goes to work for a government that participates in another pension system until that employment ends. The legislation does not include changes in employee contributions.

The following chart compares current pension benefits in the largest state retirement systems—TRS, SERS and SURS—to benefits for new hires in these systems under the reform legislation.

State of Illinois FY2011 Budget:
Comparison of SELECTED Current Pension Benefits and Pension Benefits in Reform Legislation

	Current Plan for Current Employees and New Hires	Changes for New Hires under Reform Legislation
Retirement Age - Unreduced Benefits	SERS: age 60 & 8 years; 35 years; Rule of 85 SURS: age 60 &8; age 62 &5; 30 years TRS: age 60 &10; age 62 & 5; 35 years	Age 67 & 10 years
Retirement Age - Reduced Benefits	SERS: age 55 & 25 years SURS: age 55 & 8 years TRS: age 55 & 20 years Reduction = 6% per early year	Age 62 & 10 years Reduction = 6% per early year
COLA	3% & Compound Interest	Lesser of 3% or ½ of CPI & Simple Interest
Maximum Pensionable Salary	245,000*	$106,800 & Increase with ½ of CPI
Final Average Salary	Averaged over 4 highest consecutive years during final 10 years	Averaged over 8 highest consecutive years during final 10 years

Source: Governor's Office of Management and Budget, State of Illinois; Senate Bill 1946.
*40 ILCS 5/1-117. Applies to employees hired on or after January 1, 1996; no limit for employees hired before that date.

[153] Illinois State Constitution, Article IX, Sec. 9(a).
[154] Illinois State FY2010 Budget, p. 4-2.
[155] In addition to the five state retirement systems, Public Act 96-0889 affects all local and state retirement systems under the Illinois Pension Code except systems covering firefighters and police officers. The legislation also allows the Chicago Public Schools to take a partial pension holiday totaling more than a billion dollars over the next three years and extends the agency's 50-year funding schedule to 2060.

The pension reforms, which take effect on January 1, 2011, will reduce the growth of the State's pension liabilities as new employees are added to the payroll. The reforms will lower required state contributions, which are based on actuarial calculations of payroll costs through 2045. The Governor's Office said the measure will reduce the State's pension liabilities by $220 billion, from $537.2 billion to $312.7 billion, in 2045, and save the State $67 billion on pension contributions through 2045.[156]

The Governor's budget recommends reducing the State's FY2011 contribution to the retirement systems from the amounts certified under the 1995 pension law. The budget includes a $267.0 million reduction in required pension contributions due to unspecified pension stabilization measures. The change would reduce the required General Funds contribution in FY2011 from $4.2 billion to $3.9 billion.[157] The budget does not explain how the pension savings would be achieved. The Governor's budget was released on March 10, 2010, two weeks before March 24, when the pension legislation was introduced and passed by the General Assembly in one day. The Governor's Office currently estimates that the pension legislation will save the State $382 million on retirement systems contributions in FY2011.[158]

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[156] State of Illinois, Governor's Office, "Governor Quinn Signs Historic Illinois Public Pension Reform Law," news release, April 14, 2010, at http://www.illinois.gov/gov/ with http://www.illinois.gov/publicincludes/statehome/gov/documents/Pension%20Reform%20Background.pdf (last visited on April 15, 2010)
[157] Illinois State FY2011 Budget, p. 2-10.
[158] Email communication between the Civic Federation and the Governor's Office of Management and Budget, April 15, 2010.

DEBT TRENDS

In FY2011, the Governor proposes both an operating budget that depends heavily on borrowing and a capital budget that is primarily debt funded. The State passed several new revenue sources in FY2010 to support the debt service for the increase in capital borrowing. However, debt issued for operations, including making the required annual payment to the pension system in FY2010, has contributed to the growing state deficit.

The following section examines trends in existing long-term and short-term debt issued by the State of Illinois and the amount of debt service owed by the State on an annual basis. It shows that Illinois' outstanding long-term debt nearly tripled between FY2002 and FY2011. The growing debt service associated with this level of indebtedness has become a much larger drain on the State's financial resources over this period. The State in recent years has also depended on larger and more frequent short-term loans to buttress the operating budget and carry forward deficits from one year to the next.

Voucher Payment Notes

The Governor's recommended operating budget begins with an estimated $12.9 billion budget deficit going into FY2011. Through reduction of expenditures and some anticipated increases in revenue from moderate financial recovery, the Governor's budget reduces this deficit to $10.6 billion. Of the remaining deficit, $4.7 billion is attributed to FY2011 operations and the rest is a carry forward deficit from FY2010 totaling $5.9 billion. The State's deficit is described in further detail in the General Funds Budget Deficit section, which begins on page 76.

The Governor proposes borrowing $4.7 billion to pay for the operating shortfall in FY2011 through "voucher payment notes."[159] There is currently no provision in the Illinois Bond Authorization Act to provide for this type of borrowing.[160] No details are provided in the budget regarding the term of the debt, cost of the issuance or type of authorization the State would need to enact to issue this new debt to fund operations. The FY2011 budget book simply defines the voucher payment notes as "a series of notes to pay specific vouchers during the fiscal year."[161]

On April 20, 2010, the Governor's Office of Management and Budget provided further information on a budget based on a possible income tax increase as a suggested alternative plan to the recommended budget.[162] The new plan also included details about a different borrowing strategy for FY2011.

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[159] Illinois State FY2011 Budget, p. 2-10.
[160] 30 ILCS 305
[161] Illinois State FY2011 Budget, p. 2-10.
[162] Email communication between Civic Federation and Governor's Office of Management and Budget, April 20, 2010.

The Governor's suggested alternative plan calls for "low-cost refinancing" that increases total borrowing for operations in FY2011 by $1 billion, for a total of $5.7 billion. The new plan specifies three types of debt including:

- Private placement pension notes totaling $3.7 billion;
- Borrowing $1.0 billion from "rainy day funds;" and
- Securitizing part of the State's Tobacco Settlement revenue to borrow $1.0 billion.

Similar to the Governor's recommended budget document, the alternative plan does not provide information regarding the cost, repayment or authorization needed to issue these bonds. Because the Governor has not provided details of the proposed "voucher payment note" borrowing plan or the "low-cost refinancing" alternative, the additional indebtedness and cost of repayment of the debt is not included with the data in the following section.

General Obligation and Revenue Bonds

Under the General Obligation Bond Act,[163] the State is authorized to issue General Obligation Bonds (G.O. Bonds) to fund a variety of capital investments including roads, schools, mass transit, environmental projects and other facilities. G.O. Bonds are guaranteed by a pledge of the full faith and credit of the State, which is a legally binding pledge to pay both principal and interest on these loans as required by the bond agreements prior to any other use of state funds.

The G.O. Bond Act was amended in recent years to allow for debt-funded payments to the State's retirement systems. In 2003, the State approved $10 billion in Pension Obligation Bonds (POB) to pay for unfunded liabilities of the State's retirement systems. The amount was increased in FY2010 by $3.5 billion to make the annual contributions that would have come from the State's General Funds. The 2003 POB issuances were used to justify reducing the annual contribution to the pension system. In FY2010, the pension borrowing was used to fund nearly the entire annual pension contribution. This action allowed the General Assembly to use more General Funds for other expenditures. The FY2010 POBs will be paid back over the next five years. The original FY2003 POBs were financed over 30 years and the last bonds will be retired in FY2033. The State's current pension liabilities are discussed in detail in the State Retirement Systems section, which begins on page 60.

The State appropriated a total of $17.1 billion in capital projects to be funded by borrowing in FY2010, of which $13.5 billion were new appropriations.[164] The FY2011 capital budget increases the debt-funded appropriations for capital by an additional $1.6 billion. As part of the capital budget approved by the Governor and General Assembly in FY2010, the State approved the sale of $5.8 billion in new G.O. Bonds to support capital projects. The Governor's budget estimates that the total G.O. debt sold in FY2010 will total $2.5 billion and proposes selling an additional $3.7 billion in G.O. Bonds for capital proposes in FY2011.[165] In order to continue funding the capital plan as proposed for FY2011 the General Assembly will need to approve additional borrowing authority of at least an additional $1.0 billion. Between FY2010 and

[163] 30 ILCS 330/1 (2001).
[164] Commission on Government Forecasting and Accountability, *2011 Capital Plan*, April 2010, p. 5.
[165] State of Illinois FY2011 Budget, p. 11-3.

FY2016, the State estimates it will issue $19.0 billion in total capital debt to support the capital program.[166] Details of the Governor's recommended FY2011 capital budget are included in the Capital Budget section, which begins on page 81.

In March 2010, the State also approved the sale of $250 million in special purpose G.O. debt to fund Medicaid payments through the Healthcare Provider Relief Fund.[167] This new borrowing authority is used to leverage enhanced federal matching funds due to expire on December 31, 2010 and decrease the payment cycle of outstanding Medicaid bills. The debt was issued on April 1, 2010 and must be repaid by March 31, 2011. More information about the State's healthcare costs and funding are included in the Medicaid section on page 47.

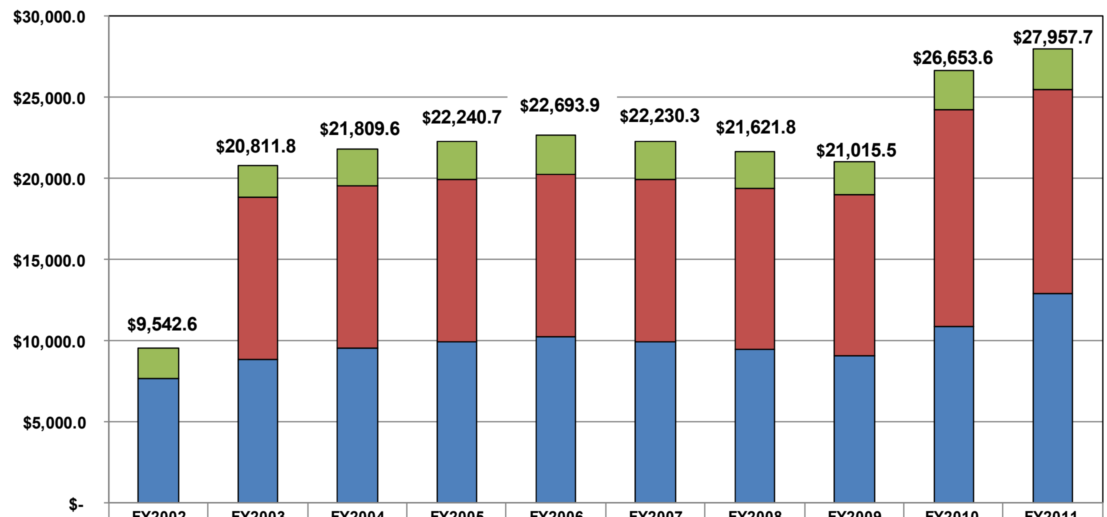
Illinois has also issued several types of revenue bonds to fund capital projects. Unlike G.O. Bonds, revenue bonds are not guaranteed by the full faith and credit of the State but rather pledge a portion of specific state revenues. The State currently pays directly for two types of revenue bonds. The Metropolitan Exposition and Auditorium Authorities bond program was supported by the issuance of Civic Center Bonds, the last of which were sold in 1992. The FY2011 budget shows $82.3 million in Civic Center Bonds outstanding and the State will make its final payment on this debt in FY2021. Although originally financed in part by horse racing taxes, these bonds are now fully repaid by General Funds and are treated more like G.O. bonds.[168]

Build Illinois Bonds were first issued in 1985 and are backed by 3.8% of the State's sales tax receipts. The total bond authorization has been increased by the General Assembly on several occasions since Governor James Thompson's inaugural program in the late 1980s. The Governor's proposed FY2011 budget estimates the State will issue $530 million in new Build Illinois debt in FY2010 and proposes selling an additional $250 million to support capital projects in FY2011.[169] At the end of fiscal year 2011, the State will have $2.4 billion worth of outstanding Build Illinois bonds.[170]

[166] Ibid., p. 11-9.
[167] Public Act 96-885
[168] 30 ILCS 355, Metropolitan Civic Center Support Act, 1987.
[169] Illinois State FY2011 Budget, p. 11-6.
[170] Illinois State FY2010 Budget, p. 61.

The Governor's budget shows the State of Illinois in FY2011 will increase the total G.O. Debt to $28.0 billion. This is an $18.4 billion increase, or 193.0%, over FY2002 prior to the State's first issuance of pension bonds. The existing debt includes $12.6 billion from the State's two issuances of POBs in FY2003 and FY2010. Capital purpose G.O. debt will total $12.9 billion and the State will have $2.5 billion in revenue bonds outstanding. The following graph shows the increase in total long-term state debt between FY2002 and FY2011.

State of Illinois Total General Obligation and Capital Debt
FY2001-FY2011 (in $ millions)



	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011
Build Illinois/Civic Center	$1,912.7	$1,999.2	$2,253.3	$2,347.7	$2,442.5	$2,304.6	$2,208.9	$2,063.7	$2,443.6	$2,519.7
Pension Bonds	$-	$10,000.0	$10,000.0	$10,000.0	$10,000.0	$10,000.0	$9,950.0	$9,900.0	$13,316.0	$12,572.8
GO Debt	$7,629.9	$8,812.6	$9,556.3	$9,893.0	$10,251.4	$9,925.7	$9,462.9	$9,051.8	$10,894.0	$12,865.2

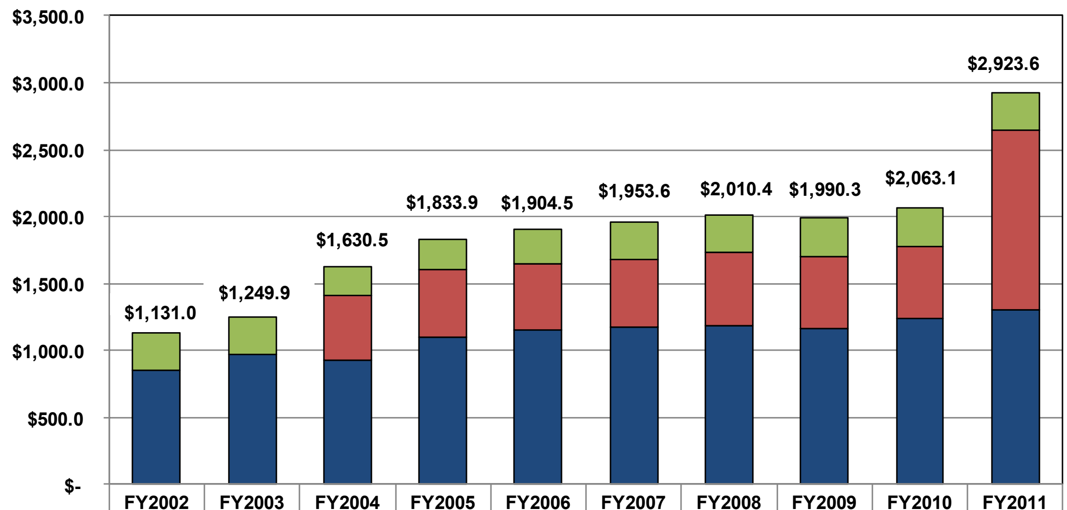
Source: Illinois State Budgets FY2005-FY2011.

Illinois' total G.O. debt increased dramatically in FY2003 due to the issuance of $10 billion in Pension Obligation bonds in 2003. Likewise, the new capital borrowing and pension borrowing approved in FY2010 have contributed to another significant increase in outstanding state debt of $4.8 billion or 21.8% from FY2010 to FY2011.

Debt Service

The State's debt service schedule sets forth the principal and interest amounts due for outstanding bonds on an annual basis. In FY2011, the State estimates its required debt payment will total \$2.9 billion for all outstanding G.O. Bonds, POBs and revenue bonds for which it directly appropriates funds.[171] This is a 158.5% increase in annual debt service cost owed by the State since FY2002, or \$1,792.7 million. The largest increases to annual debt service came in FY2004 and FY2011, the years immediately following the sale of new POBs. The following chart shows the total debt service for existing Pension Obligation bonds, G.O. capital bonds and other capital bonds.

State of Illinois Capital Purpose and Pension Bonds Total Debt Service (Principal + Interest) FY2002-FY2011 (in \$ millions)

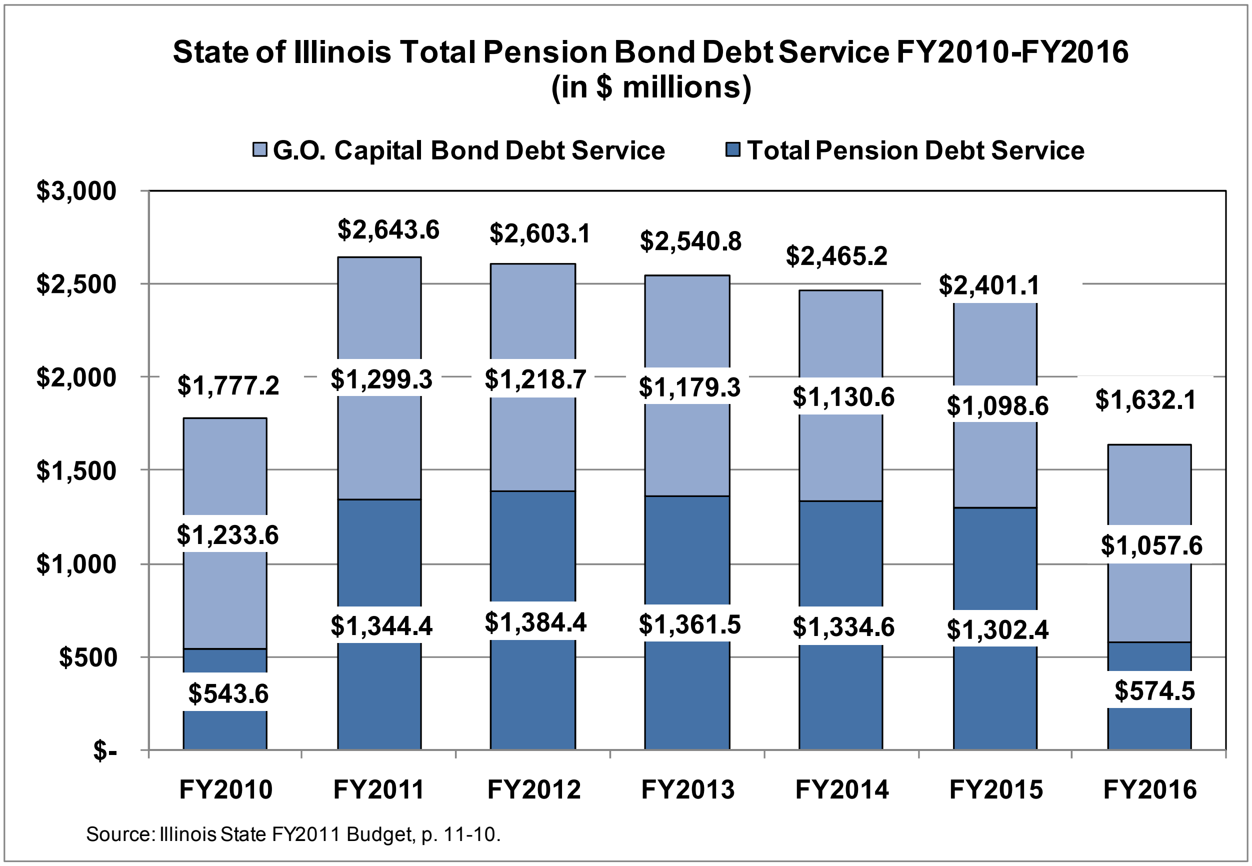


	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011
Build Illinois/Civic Center	$279.0	$275.9	$218.5	$234.5	$255.0	$278.0	$280.0	$286.0	$286.0	$280.0
Pension Bonds	$-	$-	$481.0	$496.2	$496.0	$496.0	$546.0	$544.0	$543.6	$1,344.4
GO Bonds	$852.0	$974.0	$931.0	$1,103.2	$1,153.5	$1,179.6	$1,184.4	$1,160.3	$1,233.6	$1,299.3

Source: Illinois State Budgets FY2005-FY2011.

[171] State of Illinois General Obligation Bonds, Taxable Build America Bonds, Series 2010-1, *Official Statement*, p. 36, 41.

Prior to enacting the FY2010 capital and operating budget, total debt service payments for principal and interest were projected to decline from FY2009 through FY2033, from $1.9 billion to $1.2 billion, falling to $89 million in 2034 and retiring all debt by FY2035.[172] However, because of the new capital borrowing and pension borrowing approved in FY2010, the State will pay dramatically higher debt service in FY2011 and over the next five years. Debt service will grow by $860.5 million from FY2010 to FY2011, an increase of 41.7%. The following chart compares G.O. Bonds debt service for capital projects to POB debt service between FY2010 and FY2016.



Although the capital budget was accompanied by a series of new fees and taxes to pay for the increase in capital purpose debt service, no new revenues were passed to pay for the increase in debt service for the pension bonds. The State will owe an annual payment of $802.5 million in FY2011 to repay the FY2010 pension bonds. This amount decreases slightly each year until the last payment of $723.8 is made in FY2016 on the $3.5 billion pension bond sale.[173]

Between FY2010 and FY2033, the State of Illinois will pay a total of $22.7 billion in debt service, of which $9.4 billion is interest and $13.4 billion is principal for all POBs combined. It will also pay $18.1 billion in total debt service for the total outstanding G.O. bonds for capital

[172] State of Illinois Budget FY2010, p. 12-10.
[173] State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement*, January 7, 2010.

purposes.[174] The capital G.O. debt service is made up of $6.6 billion in interest due on $11.5 billion of principal spread over the next 24 years. The State will also continue to expend 3.8% of its sales tax receipts annually through FY2034 to pay a total debt service of $3.7 billion on $2.5 billion in total outstanding Build Illinois revenue bonds.[175]

As the State continues to issue more G.O. debt than it retires on an annual basis, the amount of General Funds committed to debt service payments will continue to rise. To make these payments the State pledges its full faith and credit to its bondholders and legally commits itself to transfer the debt service payment into the General Obligation Bond Retirement and Interest Fund (GOBRI) prior to paying any other bills or transferring funds for any other appropriations.[176] The monthly transfers to the GOBRI fund needed to make the State's debt service payments in FY2011 will average between $230 million and $250 million. Compared to the estimated monthly General Fund receipts and transfers in ranging from $2.3 billion and $1.4 billion projected for the next 12 months, the State is in no danger of defaulting on its G.O. debt service payments.[177] However, as the State continues to struggle to keep up with its backlog of outstanding bills, increased monthly transfers to the GOBRI fund further increase delays in payments to state service providers for current operations.

Short-Term Debt

Short-term debt is a financial obligation that must be satisfied within one year. An increasing trend in short-term debt may be a warning sign of future financial difficulties. The amount of short-term debt issued is a good measure of budgetary solvency, or a government's ability to generate enough revenue over the course of a normal budgetary period to meet its expenditures and prevent deficits. The State of Illinois Short Term Borrowing Act governs the State's ability to access short-term capital.[178]

Under the Short Term Borrowing Act, the State may issue short-term debt certificates based upon revenue anticipation or shortfall. The act provides for two qualifications for short-term borrowing. If the State experiences significant timing variations between disbursement of appropriations and receipt of revenues it may borrow up to 5% of the State's total appropriations for that fiscal year that must be repaid entirely within the same budget cycle.[179] The second scenario, which applies to the $1 billion in short-term notes that were issued at the close of the FY2009 budget, allows the State to borrow up to 15% of the total appropriations for any year if there is a failure in revenue.[180] This type of short-term borrowing must be paid back within 12 months of issuance.

When the State issues failure of revenue borrowing and does not repay the debt until the following fiscal year, it effectively transfers current liabilities into future fiscal years. This is an indicator of deficit spending in the year the debt is issued.

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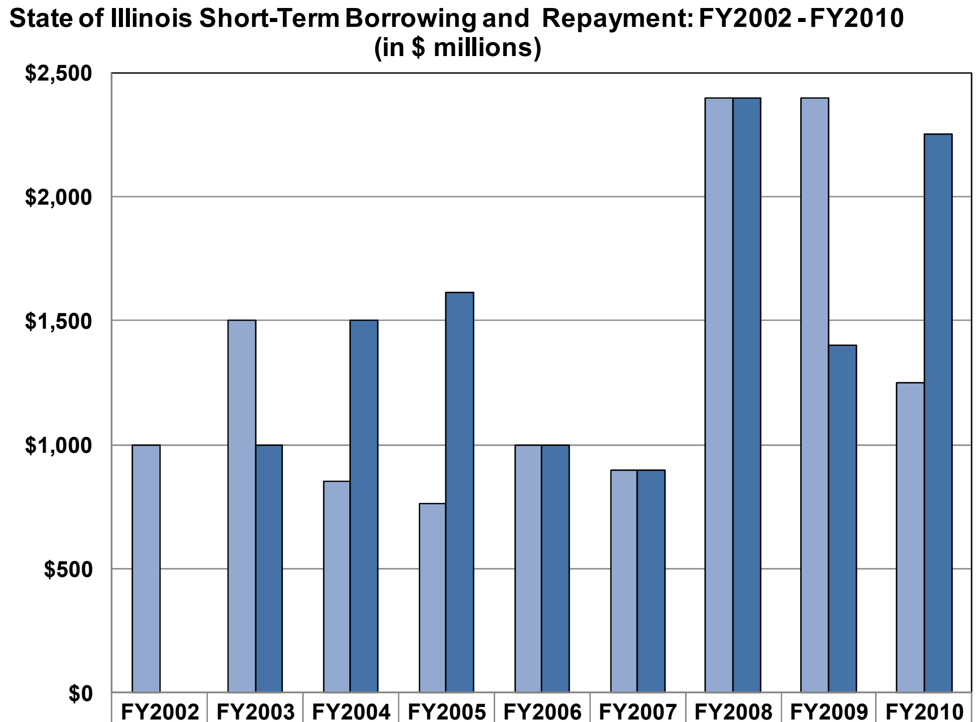
[174] Illinois State FY2011 Budget, p. 11-10.
[175] Ibid., 11-11.
[176] 30 ILCS 330/17
[177] State of Illinois, General Obligation Bonds, *Series of April 2010, $250 million*, p. 4.
[178] 30 ILCS 340 (2004).
[179] 30 ILCS 340/1 (2004).
[180] 30 ILCS 340/1.1 (2004).

The State will most likely continue to rely on short-term borrowing to finance part of the State's anticipated $12.9 billion deficit. However, the recommended budget does not include any information on the type or amount of short-term debt that the State may issue at the end of FY2010 or throughout FY2011. The following exhibit shows the upward trend in frequency and total amount of short-term certificates issued and repaid from FY2002 through FY2010.



	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010
Short-Term Debt Issued	$1,000.0	$1,500.0	$850.0	$765.0	$1,000.0	$900.0	$2,400.0	$2,400.0	$1,250.0
Short-Term Debt Repaid	$-	$1,000.0	$1,500.0	$1,615.0	$1,000.0	$900.0	$2,400.0	$1,400.0	$2,250.0

Source: Illinois State FY2011 Budget, p. 11-5.

Prior to FY2002, the State had never issued more than $900 million in short term certificates in any given fiscal year and never authorized short-term borrowing in more than three consecutive fiscal years. Since 2002, the State has increased both the frequency and volume of its issuance of short-term debt. On average, the State has had $1.8 billion in short-term notes outstanding at any given time since FY2003. In both FY2003 and FY2009, the State borrowed under the State's revenue failure provisions to carry forward portions of the State's deficits from one year to the next.

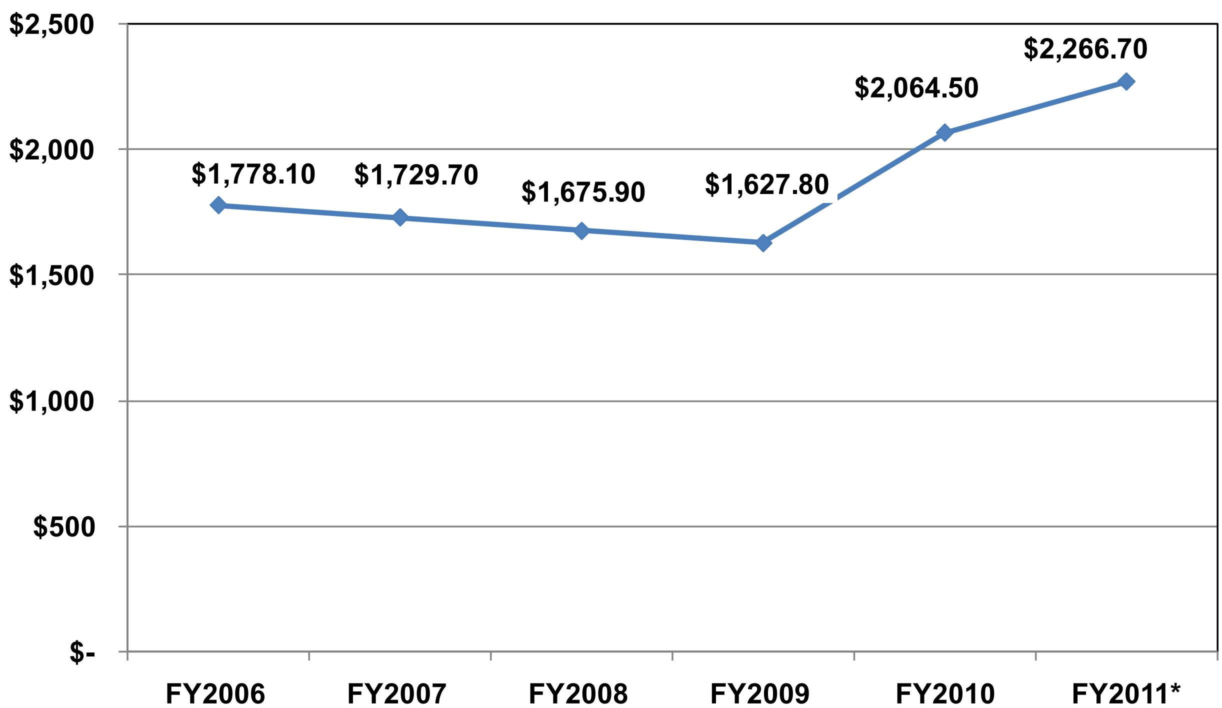
Halfway through FY2009, in December of 2008, the State issued $1.4 billion in short-term debt to pay down some of the State's outstanding liabilities. These notes were due to be repaid by the end of FY2009. However, the State declared a failure of revenue for FY2009 as part of the FY2010 budget and sold $1 billion of new short-term notes shortly after repaying the December notes to carry forward the deficit to the new fiscal year. As part of the FY2010 budget, the State sold an additional $1.25 billion in short-term debt in August 2009. The combined total of $2.3 billion in outstanding short-term borrowing will be repaid before the end of FY2010.

As mentioned in the debt is not included with the data in the following section.
General Obligation and Revenue Bonds section, the State sold $250 million of special purpose bonds that will be repaid within one year. Although this debt was issued under the G.O. Bond Act and not the Short Term Borrowing Act, the bonds will be treated like a short-term issuance for failure of revenues, passing on liabilities from FY2010 to FY2011.

Debt Per Capita

One of the most common measures used to analyze a state's debt burden is the ratio of total outstanding debt to the state's estimated population. Between FY2006 and FY2011, existing debt per capita for all capital purpose and pension debt increased by $488.60, or 27.5%. The majority of the increase in debt per capita can be attributed to the sales of POBs in FY2010 and the authorization of the debt-funded capital plan. The Governor's proposed budget for FY2011 shows the total debt per capita increasing by 9.8% from FY2010 to FY2011, a total increase of $202.20.[181] The following exhibit shows total Illinois' debt per capita including capital purposes and pension debt from FY2006 to FY2011 .

State of Illinois Debt Per Capita FY2006-FY2011



Source: Illinois State FY2011 Budget, p. 11-9.

[181] Illinois State FY2011 Capital Budget, p. 11-9.

Bond Ratings

The State of Illinois' G.O. bond ratings have been lowered by each of the three major rating agencies in FY2010. The State's debt has been the second lowest rated among all states for two years, just one level above California. All three agencies also characterize the outlook for Illinois' ratings as "negative." The following chart shows the reduction in rating since FY2010.

	Moody's Investors Services	Standard & Poor's	Fitch Ratings
FY2010	Aa3	AA-	AA-
FY2011	A2	A+	A

Source: Illinois State FY2010 Budget, p. 12-2; State of Illinois, $250 million General Obligation Bonds, Series of April 2010, *Official Statement* , p. 53.

Debt ratings are one of the factors that weigh heavily in determining the interest rate the State must pay to issue debt. Consequently, the decline in the State's rating will lead to an overall increase in debt service costs for Illinois. However, the State does not provide current interest rate estimates or estimated increases in debt service cost due to this change.

In downgrading the State's rating and future financial outlook, each agency has pointed to several of the same financial problems facing Illinois. The agencies look negatively on the State's poor cash position, or the lack of available revenue pay its bills, the FY2010 budget's reliance on one-time revenue sources to pay for ongoing operational expenses, the growing imbalance in the operating budget and the State's unfunded pension liabilities. The agencies' reports also explain that the long-term challenge of properly funding the retirement systems has placed an increasing burden on the State's current finances, as the required annual contribution increases to make up for past underfunding and losses in the pension funds due to the recession.

GENERAL FUNDS BUDGET DEFICIT

Under the Illinois Constitution, the Governor must propose a balanced budget in which expenditures do not exceed revenues estimated to be available for the year.[182] Similarly, the General Assembly is required to pass a balanced budget.[183] A balanced General Funds budget requires enough revenue to meet expenditures and transfers out. In addition, if the State issued short-term debt in the previous year because of a revenue shortfall, there must be enough revenue available for repayment.

The Governor's recommended budget projects that the State of Illinois faces a $12.9 billion General Funds budget deficit in FY2011. The budget gap is comprised of a $7.0 billion operating gap in the FY2011 budget and a $5.9 billion shortfall carried forward from FY2010. This section will provide an overview of the budget deficit and the Governor's recommended measures to reduce the deficit.

[182] Constitution of the State of Illinois, Article VIII, Section 2(a).
[183] Ibid, Section 2(b).

Budget Deficit in FY2010 and FY2011

The State began FY2010 with a $3.7 billion deficit from the previous fiscal year. This deficit was carried forward by deferring $4.0 billion in unpaid bills to FY2010. As enacted, the FY2010 budget would have used an operating surplus of $279 million to pay down a portion of the backlog of bills to end the year with a $3.4 billion deficit. However, the Governor's FY2011 budget estimates that FY2010 General Funds revenues and expenditures will result in the deficit increasing by $2.2 billion and FY2010 will end with a deficit of $5.9 billion that will carry forward into FY2011. The following chart provides an overview of the FY2010 budget deficit.

State of Illinois General Funds Budget Surplus (Deficit): FY2010 (in $ millions)		
Revenues		
State Sources	$	19,085
Federal Sources	$	6,743
Statutory Transfers-In	$	2,117
Total Revenues	**$**	**27,945**
Expenditures		
Appropriations	$	(26,309)
Unspent Appropriations	$	400
Subtotal Expenditures	**$**	**(25,909)**
Statutory Transfers Out		
Legislatively Required Transfers to Other Funds	$	(2,002)
Pension Obligation Bond Debt Service	$	(564)
Debt Service Transfers for Capital Projects	$	(670)
Subtotal Statutory Transfers Out	**$**	**(3,236)**
Total Expenditures and Transfers Out	**$**	**(29,145)**
Budget Operating Surplus (Deficit)	**$**	**(1,200)**
Short-term Borrowing Proceeds, net of Repayment	**$**	**(1,045)**
Budget Basis Surplus (Deficit) for FY2010	**$**	**(2,245)**
Carry Forward of FY2009 Year-end Deficit	**$**	**(3,673)**
Total Year-end Deficit FY2010	**$**	**(5,918)**

Source: Illinois State FY2011 Budget, p. 2-10 and 4-16. Statutory Transfers-In were adjusted by the Civic Federation to reflect the $50 million loss in Riverboat Gaming Taxes discussed in the text on 4-16.

The Governor estimates that expenditures will outpace revenues by $1.2 billion in FY2010. In addition to this operating deficit, the State is required to pay $2.3 billion in debt service on the short-term debt issued in May 2009 and August 2009. However, this debt service only increases the deficit by $1.0 billion because the State also realized $1.3 billion in proceeds from the August 2009 issuance in the FY2010 budget. The $1.2 billion operating deficit, the $1.0 billion short-term debt repayment net of proceeds and the $3.7 billion deficit carried forward from FY2009 results in a $5.9 billion deficit for FY2010.

In order to maintain a year-end positive cash balance, the State will end FY2010 with $6.2 billion in unpaid bills. This represents 21.3% of total estimated General Funds expenditures of $29.2 billion in FY2010. At the end of March of 2010, the backlog of unpaid bills at the Illinois Office of the Comptroller stood at $4.5 billion up from $3.4 billion at the same time a year earlier.[184] The Commission on Government Forecasting and Accountability estimates that there are currently $692 million of unpaid employees and retiree group health insurance bills.[185]

The FY2011 General Funds budget deficit starts with the $5.9 billion gap projected to be carried forward from FY2010. The State also begins FY2011 with a baseline operating deficit of $1.2 billion, which is the budgetary imbalance before any changes to revenues and expenditures in the coming fiscal year. The State must then fill a budget hole resulting from the loss of one-time revenues. These revenues include the loss of $947 million in federal recovery funds,[186] $352 million from sweeps of Other State Funds and $3.5 billion from the proceeds from the sale of the five-year pension bonds. Additional required expenditures also contribute to the deficit, including $803 million in debt service on the pension bonds, $345 million for a statutory transfer of pension bond debt service and a $691 million increase in the statutory contribution to the State's retirement systems. General Funds revenue growth reduces the deficit by $798 million. The following chart outlines the FY2011 budget gap of $12.9 billion.

State of Illinois General Funds Budget Gap: FY2011 (in $ millions)	
Carry-forward of FY2010 Deficit	$ (5,918)
FY2011 Baseline Deficit	$ (1,200)
Loss of Federal Recovery Funds	$ (947)
Fund Sweeps Included in FY2010 Revenue	$ (352)
Borrowing FY2010 Contributions to Retirement Systems	$ (3,466)
Increase in Statutory Contributions to Retirement Systems	$ (691)
Pension Bond Repayment	$ (803)
Statutory Transfer of Pension Bond Debt Service	$ (345)
FY2011 Revenue Growth	$ 798
FY2011 Total Budget Gap	**$ (12,923)**

Source: Illinois State FY2011 Budget, p. 2-10, 4-16, 4-17.

184 Illinois Office of the Comptroller, "Cash Position Deteriorates as State Begins to Repay Short-Term Borrowing," Comptroller's Quarterly, April 2010, p. 1, at http://www.apps.ioc.state.il.us/ioc-pdf/CQ_35.pdf (last visited on April 12, 2010).

185 Commission on Government Forecasting and Accountability, *State Employees Group Insurance Program Project FY2011 Liabilities Report*, March 16, 2010, p. i, at http://www.ilga.gov/commission/cgfa2006/Upload/fy2011stateemployees'groupinsurance.pdf (last visited on April 12, 2010).

186 This assumes an extension of the enhanced Medicaid match beyond the currently scheduled expiration date of December 31, 2010.

Measures to Reduce the Deficit

To reduce the deficit, the Governor proposes a net appropriations reduction of $1.5 billion, reducing contributions to the retirement systems by $267 million and other General Funds expenditure[187] reductions totaling $534 million. After these measures, a $10.6 billion deficit consisting of a $4.7 billion operating deficit in FY2011 and the $5.9 billion carry-forward from FY2010 remains. A reasonable financial analysis would indicate that the budget is unbalanced if expenditures outpace revenues by $4.7 billion.[188] The Governor proposes to borrow $4.7 billion to finance the operating deficit. In addition, these measures do not address the $5.9 billion deficit carried forward from FY2010. The following chart summarizes the Governor's recommendations to reduce the General Funds budget deficit.

Governor's Recommended Measures to Reduce the General Funds Deficit: FY2011 (in $ millions)	
FY2011 Budget Gap	**$ (12,923)**
Net Appropriations Reduction	$ 1,532
Reduction in Contributions to Retirement Systems	$ 267
Reduction in Transfer to Local Governments	$ 308
Other Expenditure Reductions	$ 226
Subtotal Deficit Reduction Measures	**$ 2,333**
FY2011 Deficit After Measures	**$ (10,590)**
Voucher Payment Notes (Borrowing for Operations)	**$ 4,672**
Year-end FY2011 Deficit	**$ (5,918)**

Appropriations Reductions - $1.5 billion

The Governor recommends reducing General Funds appropriations by $1.5 billion. Total cuts to departments total $2.2 billion but are partially offset by $636.8 million in budget increases to other departments. Program reductions include a $70.0 million reduction to Illinois Cares Rx, $150.0 million reduction to the Department of Human Services and a $613.1 million cut to General State Aid to elementary and secondary education. More information on appropriations reductions is contained in the Appropriations section.

The cuts also include a $254.5 million reduction to the State's contributions for retiree health care and a $70.0 million reduction in state employee health insurance. The State would achieve savings by limiting its share of retiree health insurance premiums to $300 per month. However, no details are available on the $70.0 million savings related to current employees, which will be negotiated with Council 31 of the American Federation of State, County and Municipal Employees (AFSCME).[189] Additional information on group insurance is contained in the State Employee and Retiree Health Insurance subsection.

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[187] In addition to expenditures authorized through annual appropriations, the State also makes transfers out of General Funds pursuant to statute.
[188] At a press conference on March 9, 2010, officials of the Governor's Officer said they believe the FY2011 recommended operating budget is balanced and meets constitutional requirements.
[189] Civic Federation conversation with officials of the Illinois Department of Healthcare and Family Services, April 1, 2010.

Reduction in Contributions to the State's Retirement Systems - $267 million

The Governor recommends reducing the FY2011 contributions to the retirement systems from the amounts certified under the 1995 pension funding reform law.[190] The recommendation states that the $267 million savings would be achieved through enacting unspecified pension stabilization measures. However, the recommendation does not provide specific details regarding how the proposed pension stabilization would achieve savings in FY2011. After the Governor released the FY2011 budget recommendation, the General Assembly passed and the Governor signed Public Act 96-0889, which would create a second tier of reduced pension benefits for new employees hired after January 1, 2011.

Reduction in Transfer to Local Governments - $308 million

The State Revenue Sharing Act requires that 10% of personal and corporate income tax proceeds be transferred from General Funds to the Local Government Distributive Fund, for distribution to units of local government based on population. Local governments may use these funds for any purpose. The Governor recommends reducing the local share of the income tax revenue to 7% in order to reduce the budget deficit by $308 million.

Other Expenditure Reductions - $226 million

The General Funds budget deficit is reduced by a net $226 million due to a projected increase in unspent appropriations[191] of $96 million and less statutory transfers out of the General Funds, including debt service transfers, totaling $130 million.

Voucher Payment Notes - $4.7 billion

A $10.6 billion deficit remains after the Governor's proposed spending reductions. This deficit consists of the $5.9 billion carry-forward from FY2010 and a $4.7 billion operating deficit in FY2011. To cover the remaining operating deficit of $4.7 billion, the Governor recommends issuing a series of notes to pay specific vouchers during the fiscal year. The State would issue a "combination of short-, intermediate- and long-term borrowing" in order to pay for operations and not increase the backlog of unpaid bills.[192] The budget does not include details on the term or costs of the proposed voucher payment notes.

Under the Governor's recommendation, the State's General Funds would end FY2011 in the same budgetary position as the end of FY2010: with a budget deficit of $5.9 billion and a backlog of bills totaling $6.2 billion. While the backlog of bills would remain level, the Department of Healthcare and Family Services estimates that this backlog of bills would include approximately $900 million in unpaid employee and retiree group health insurance claims, above the current claim backlog of $692 million.[193]

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[190] Under Public Act 88-0593, each retirement system must certify the contribution for the following fiscal year by November 15.
[191] Several hundred million in General Funds appropriations typically remain unspent at the end of each fiscal year because expenses do not reach budgeted levels and checks issued by the State have not been cashed by the payee.
[192] Illinois State FY2011 Budget, p. 2-3.
[193] Phone communication between the Civic Federation and officials of the Illinois Department of Healthcare and Family Services, April 1, 2010.

CAPITAL BUDGET

Since FY2005, the Governor's annual recommendations for the capital budget and the operating budget have been submitted as separate documents. The budgets are primarily different insomuch as the appropriations in the operating budget are intended to be spent in the year they are approved, while appropriations in the capital budget are to fund large infrastructure investments that often take several years to complete construction and must be reappropriated each year as a project moves forward. The capital budget is also primarily funded by long-term debt to pay for major projects over 20 to 30 years.

The following section examines the Governor's recommended capital budget for FY2011, which includes reauthorizing unspent appropriations from the *Illinois Jobs Now!* capital budget approved in FY2010[194] and the new appropriations proposed for FY2011. The recommended appropriations total $30.5 billion. The capital budget includes appropriations for maintenance on state-owned assets such as roads and bridges, transit facilities, schools, economic development projects, environmental infrastructure, energy programs and state facilities. It also includes building new assets that the State will have to maintain and operate in future years.

Capital Planning

The State of Illinois does not have an established and publicly available capital improvement plan (CIP) to explain the prioritization of projects in the capital budget or the overall needs assessment for all state-owned assets. Although a list of nearly 9,000 appropriations accompanies the capital budget document, no planning documents are available to explain the prioritization of projects or estimates of total capital needs for the State. The capital budget book describes a process coordinated by the Capital Development Board and the Governor's Office of Management and Budget to assemble and prioritize the projects in the capital program, but no documentation of the process or final ranking of projects was included with the budget.[195] Some of the important elements of a CIP that are missing from the Governor's proposed capital budget include:[196]

- A comprehensive inventory of all state-owned assets, with description of useful life and current condition;
- A five-year summary list of all projects and expenditures per project as well as funding sources per project;
- Criteria for projects to earn funding in the capital budget including a description of an objective and needs-based prioritization process;
- Information about the impact of capital spending on the annual operating budget of each project;
- Brief narrative descriptions of individual projects, including the purpose, need, history, and current status of each project; and

[194] Public Acts 96-0004, 96-0035, 96-0039, 96-0819.
[195] Illinois State FY2011 Capital Budget, pg. 5.
[196] Vogt, A. John, *Capital Budgeting and Finance: A Guide for Local Governments* (International City/County Management Association, 2004) p. 62.

- An expected timeframe for completing each project and a plan for fulfilling overall capital priorities.

A well-organized and annually updated CIP helps ensure efficient and predictable execution of capital projects and helps prevent the waste of scarce funding resources.

The Governor's proposed budget includes some elements of a CIP such as a brief description of how some completed projects will affect the State's operating expenses. The Governor estimates in the FY2011 capital budget that over the next five years, the State will save $1.6 billion in operating expense for reduced repair, maintenance and utility savings through the proposed investment in state owned assets and infrastructure. However, these savings are offset by an estimated increase of $2.0 billion in operating expenses for new personnel and increased utilities expense associated with new facilities.[197] The five-year net operating increase of $317 million may be underestimated because it only includes increased costs associated with the completion of two relatively small projects out of 8,774 appropriations included in the budget. The purchase of the Tinley Dry Goods Store for the Illinois Historic Preservation Department is estimated to cost $43,000 annually to operate, and construction of a new State Police forensic lab in the city of Belleville will cost the State $350,000 annually. The impact of the State's capital expansion included in the capital budget on the already stressed operating budget is unclear.

It is also important that the capital budget prioritize and fund the State's most critical infrastructure needs before funding new facilities or initiatives. The American Society of Civil Engineers recently released a study on the condition of Illinois' infrastructure. The report compared the State's infrastructure needs to its funding and plans to address those needs, including the projects approved in FY2010. The report concluded that the overall condition and investment in the Illinois' infrastructure was "poor." Specifically, the report showed the State's aviation facilities, dams and bridges were in "mediocre" condition and the State's infrastructure for drinking water, navigable waterways, rail, roads, transit and wastewater were in "poor" condition.[198]

Three of the largest areas of capital expense for the State are surface transportation, public transit and education. In 2007, the Regional Transit Authority, which manages public transit for the State's population center in Northeastern Illinois, estimated it would need $7.3 billion over the next five years to bring the CTA, Metra and Pace systems into a state of good repair.[199] The Illinois State Board of Education reports a need of $7.6 billion for statewide maintenance for elementary and high school facilities.[200] However, the survey only represents the needs of 456 school districts that responded to the survey and the State has 870 total school districts. The Illinois Department of Transportation reports that it needs an annual budget of at least $6.1 billion to keep pace with maintenance and replacement of the State's road and bridge

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[197] Illinois State FY2011 Capital Budget, p. 96.
[198] American Society of Civil Engineers, *Illinois Infrastructure 2010 Report Card*, http://www.isasce.org/web/2010InfrastructureReport.htm (last visited April 15, 2010).
[199] Regional Transit Authority, Moving Beyond Congestion, June 2007, http://www.movingbeyondcongestion.org/downloads/10_Billion_new.pdf (last visited April 15, 2010).
[200] Illinois State Board of Education, *Capital Needs Assessment Survey Results 2009*, http://www.isbe.state.il.us/finance/pdf/cnas_FY09.pdf (last visited April 15, 2010).

inventory.[201] Illinois' wastewater infrastructure reportedly needs $13.4 billion in maintenance funding.[202]

The examples above are just a few of the known critical areas of infrastructure maintained by the State of Illinois. These funding requests illustrate how the State's capital funding needs far outpace even the resources proposed in State's $30.5 billion capital budget. An annually updated CIP would provide for a strategic, transparent and comprehensive approach to infrastructure investment and would make clear to what extent the Governor's proposed capital budget will address these needs.

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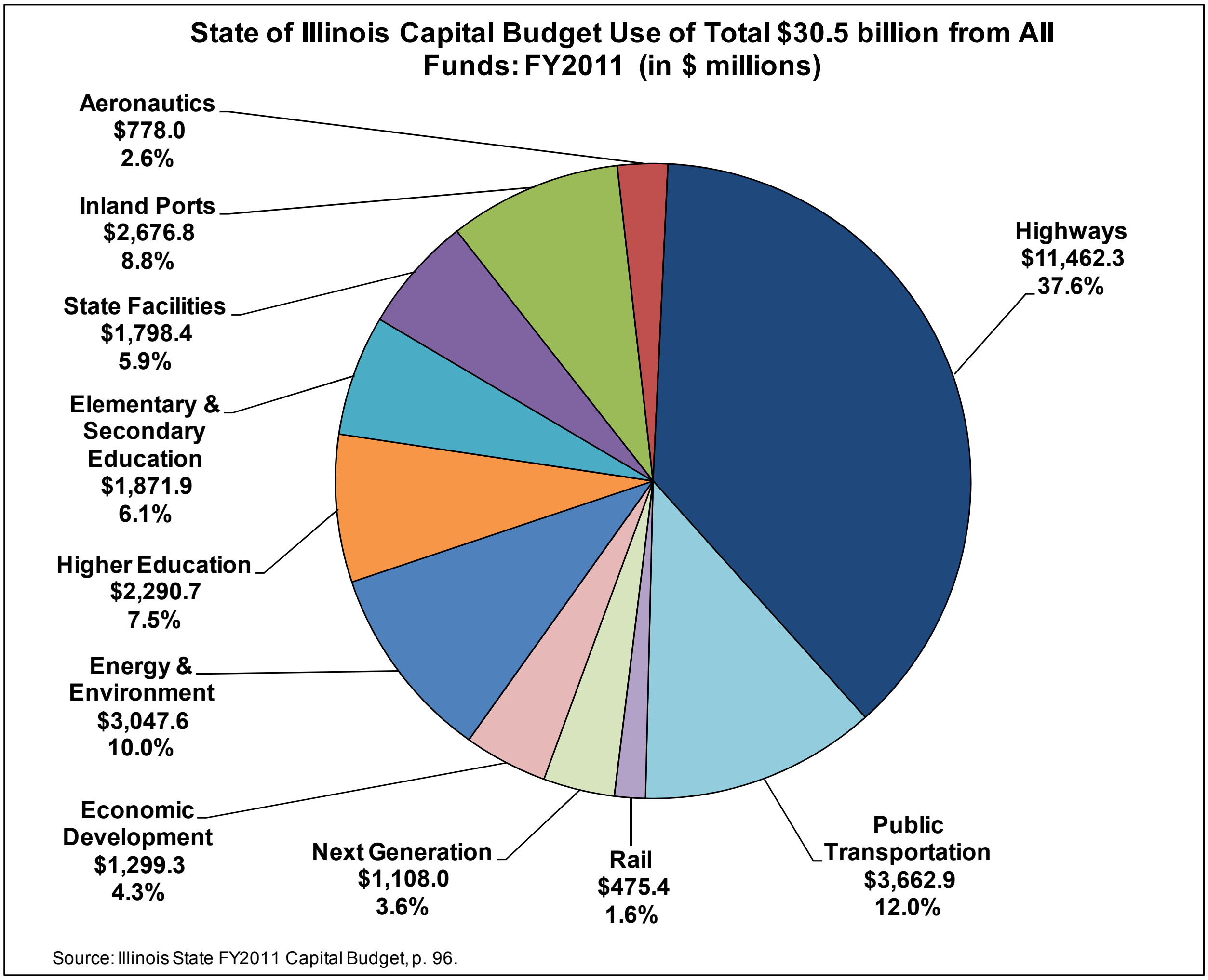
[201] Illinois Department of Transportation, *Illinois State Transportation Plan, Special Report: Transportation Funding*, June 2007, p. 19.
[202] American Society of Civil Engineers, *Illinois Infrastructure 2010 Report Card*, http://www.isasce.org/web/2010InfrastructureReport.htm (last visited April 15, 2010).

Total Appropriations

The FY2011 capital budget recommends the reauthorization of $26.2 billion and new spending totaling $4.3 billion, or a 14.1% increase, bringing the total for capital appropriations back up to $30.5 billion in FY2011. The following graph shows the use of all capital funds by type of project.



The Governor proposes allocating $11.4 billion, or 36.7%, of the total capital appropriations for state highways. This is more than triple the next largest category, public transit, which is allocated $3.7 billion or 12.0 % of the appropriations. Both of these areas of funding are managed by the Illinois Department of Transportation (IDOT), as are the rail and airport investments.

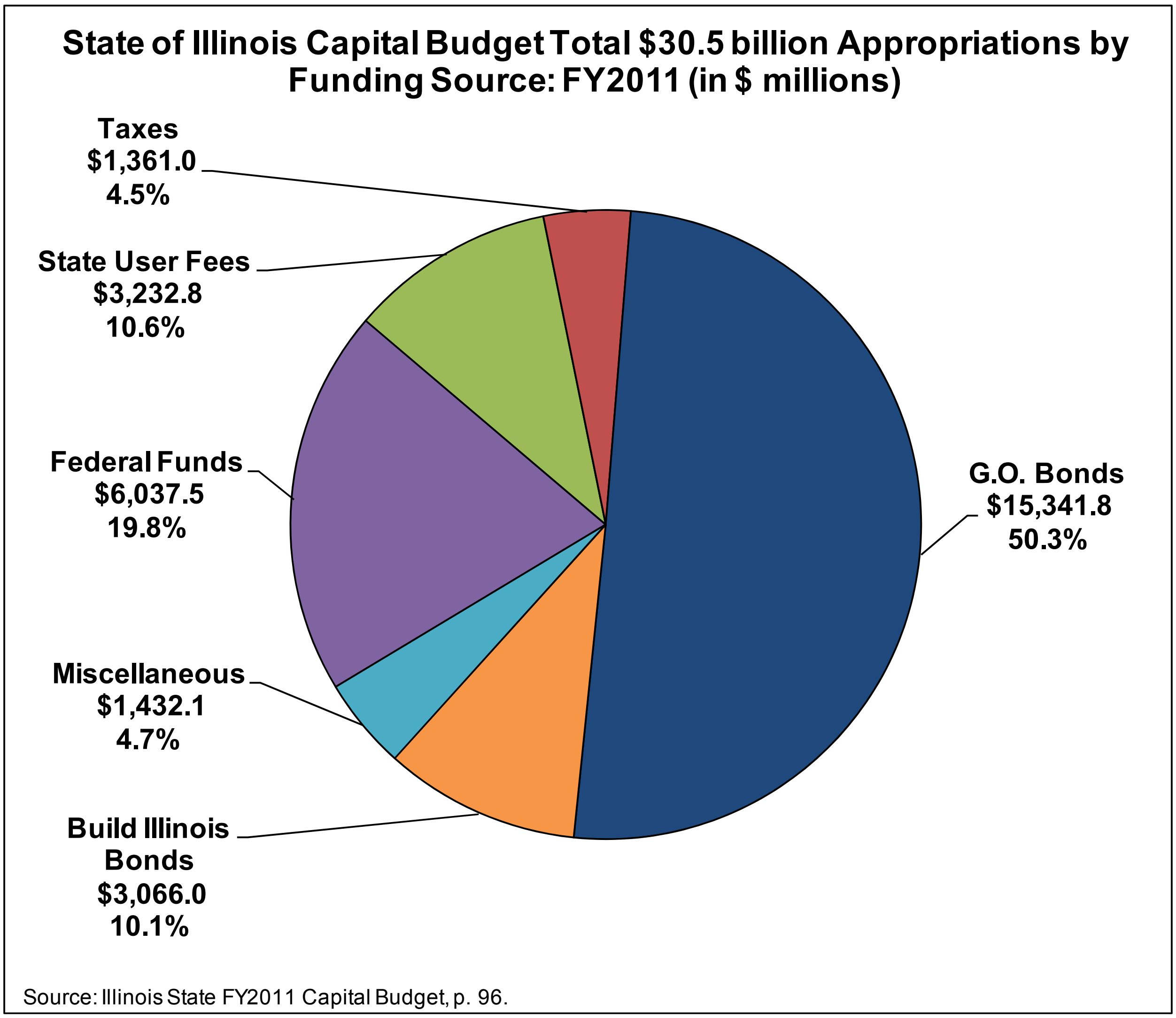
The largest 31 appropriations included in the capital budget, ranging in size from $250 million to $2.9 billion, make up $20.6 billion or 67% of the total budget.[203] All of these largest spending areas are for general departmental spending and not specific projects. The largest appropriation

[203] Illinois State FY2011 Capital Budget, Capital Projects List, http://www.state.il.us/budget/FY2010/FY2010_Capital_Projects_List.xls (last visited April 15, 2010).

for a specific project in the capital project list released with the budget is the reappropriation of $250 million for upgrades to the Capitol Complex in Springfield.[204]

The Governor's proposed budget also includes a new category of appropriations called Next Generation. The $1.1 billion in Next Generation projects mostly is made up of reappropriations for technology expansion projects and includes some grants for environmental abatement and weatherization projects.

Multiple funding sources will be needed to pay for the $30.5 billion capital appropriations. The largest source of funding for the capital budget is state-issued debt through the General Obligation Bond and Build Illinois Bond programs. The Debt Trends section, which begins on page 66, discusses the history and current total indebtedness associated with the capital budget. Debt-funded projects total $18.4 billion or 60.4% of the total capital budget. The following graph shows the funding for the FY2011 capital budget by source of funding.



[204] Illinois State FY2011 Capital Budget, Capital Projects List, http://www.state.il.us/budget/FY2010/FY2010_Capital_Projects_List.xls (last visited April 15, 2010).

To fund all the appropriations included in the capital budget, the General Assembly will need to approve additional bond authorization by a three-fifths vote. The State only enacted authorization for $5.8 billion in new bond sales as part of the FY2010 *Illinois Jobs Now!* capital bills. The remaining pay-as-you-go funding comes from federal funds, tax revenue, user fees and other miscellaneous sources.[205]

Federal funds for capital focus primarily on transportation projects including highways, aeronautics, rail and public transportation provided through the federal transportation bill called the Safe, Accountable, Flexible and Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) and the American Recovery and Reinvestment Act of 2009.[206] Federal funds also include some grants for environmental projects and appropriations for the State's inland ports. Federal funding for capital totals $6.0 billion or 19.8% of the total capital budget.

Tax funds are generated from the motor fuel tax charged by state, county and local governments. User fees are primarily generated through vehicle licensing, registration and title fees.[207]

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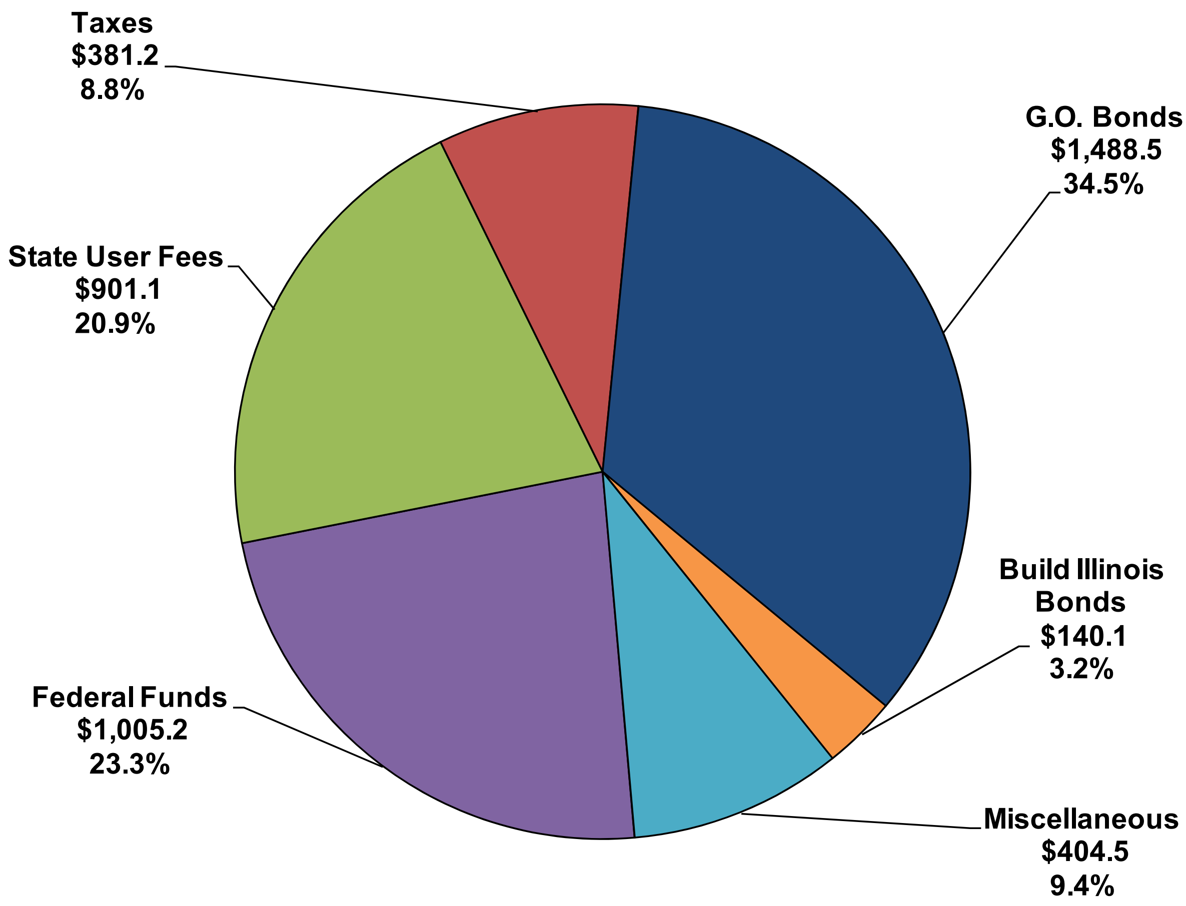
[205] Miscellaneous includes loan repayments, investment income and settlements. Illinois State FY2011 Capital Budget, p. 96.
[206] Illinois State FY2011 Capital Budget, p. 39.
[207] Illinois State FY2011 Capital Budget, p. 99.

FY2011 New Appropriations

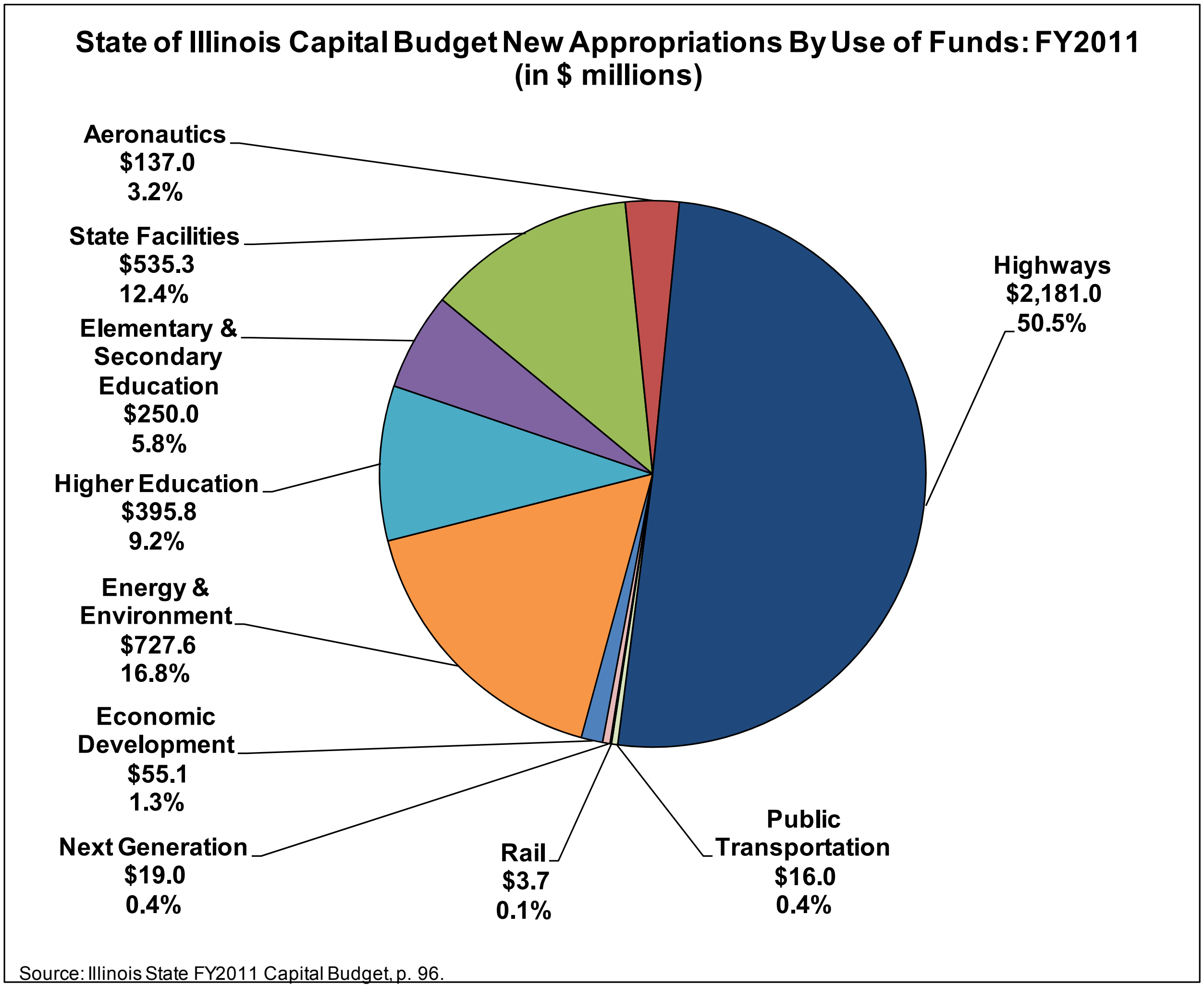
The proposed increase of $4.3 billion in new capital spending in FY2011 will be funded primarily through additional bond funds. Combined G.O. Bonds and Build Illinois Bonds fund 37.7% of the FY2011 new appropriations or $1.6 billion.

State of Illinois Capital Budget New Appropriations by Funding Source: FY2011 (in $ millions)



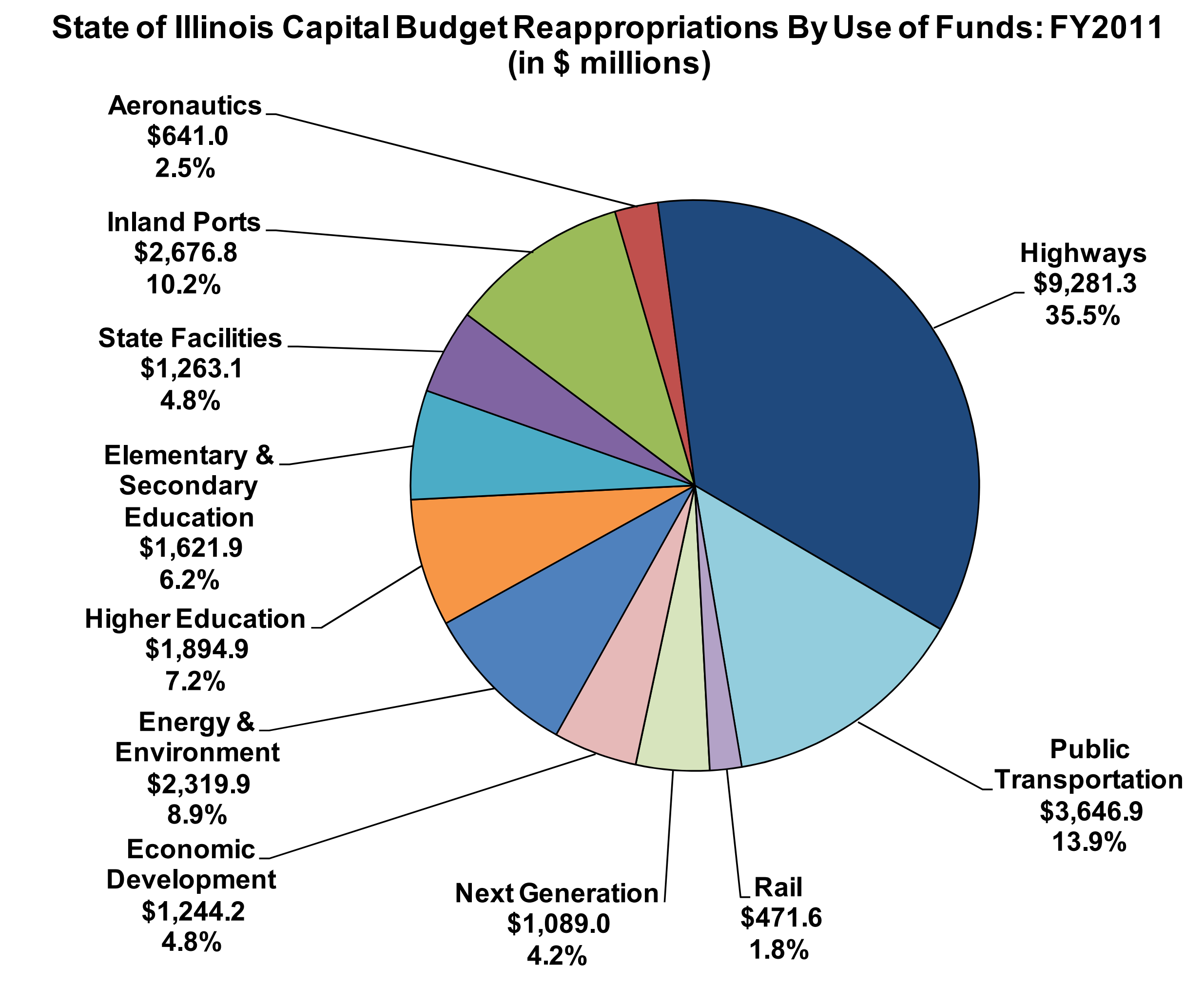
Source: Illinois State FY2011 Capital Budget, p. 96.

The largest new appropriation proposed in the FY2011 capital budget is a new School Consolidation grant program totaling $250 million. The Illinois Community College Board also received a significant amount of new funding totaling $127.7 million for both new construction and facility renewal. The following graph shows the proposed new appropriations by purpose.



FY2011 Reappropriations

On July 13, 2009, the Governor signed the $30.5 billion *Illinois Jobs Now!* program as enacted by the General Assembly. This was the first statewide transportation bill enacted in Illinois since the *Illinois FIRST* capital program in 1999. As part of the FY2011 capital budget, the Governor proposes reauthorizing $26.2 billion of unspent appropriations from the FY2010 capital budget. The following chart shows the proposed reappropriations in FY2011 capital budget by type of project.



Source: Illinois State FY2011 Capital Budget, p. 96.

The total $9.3 billion for highway projects also includes portions of the State's multiyear road plan for FY2010 through FY2015. However, the Governor's office announced on April 15, 2010, a new multi-year program for FY2011 through FY2016 totaling $12.8 billion.[208] The total funding and sources of funding do not match the Governor's proposed capital budget and it is unclear how this changes the total appropriations and reappropriations proposed for FY2011.

[208] FY2011-FY2016 *Proposed Highway Improvement Program*. http://www.dot.state.il.us/hip1116/hwyimprov.htm (last visited April 20, 2010).

Of the $3.6 billion allocated for public transit funding, only $900 million will be spent on maintenance to the Chicago Transit Authority, the largest provider of mass transit in the State. The CTA has identified a need of more than $6 billion in capital funding to maintain its bus and rail system.

The reappropriations also include $400 million within the inland ports budget to fund high-speed rail. Illinois was awarded $1.2 billion in additional funding for high speed rail from the federal government that is not included in the capital budget.[209] The inland ports appropriations also include $300 million for the Chicago Environmental and Transportation Efficiency Program (C.R.E.A.T.E.) and $110 million to build a third Chicago regional airport south of the city.

The capital budget also includes $1.5 billion reappropriated for the statewide school construction program and $1.4 billion for projects at public universities.

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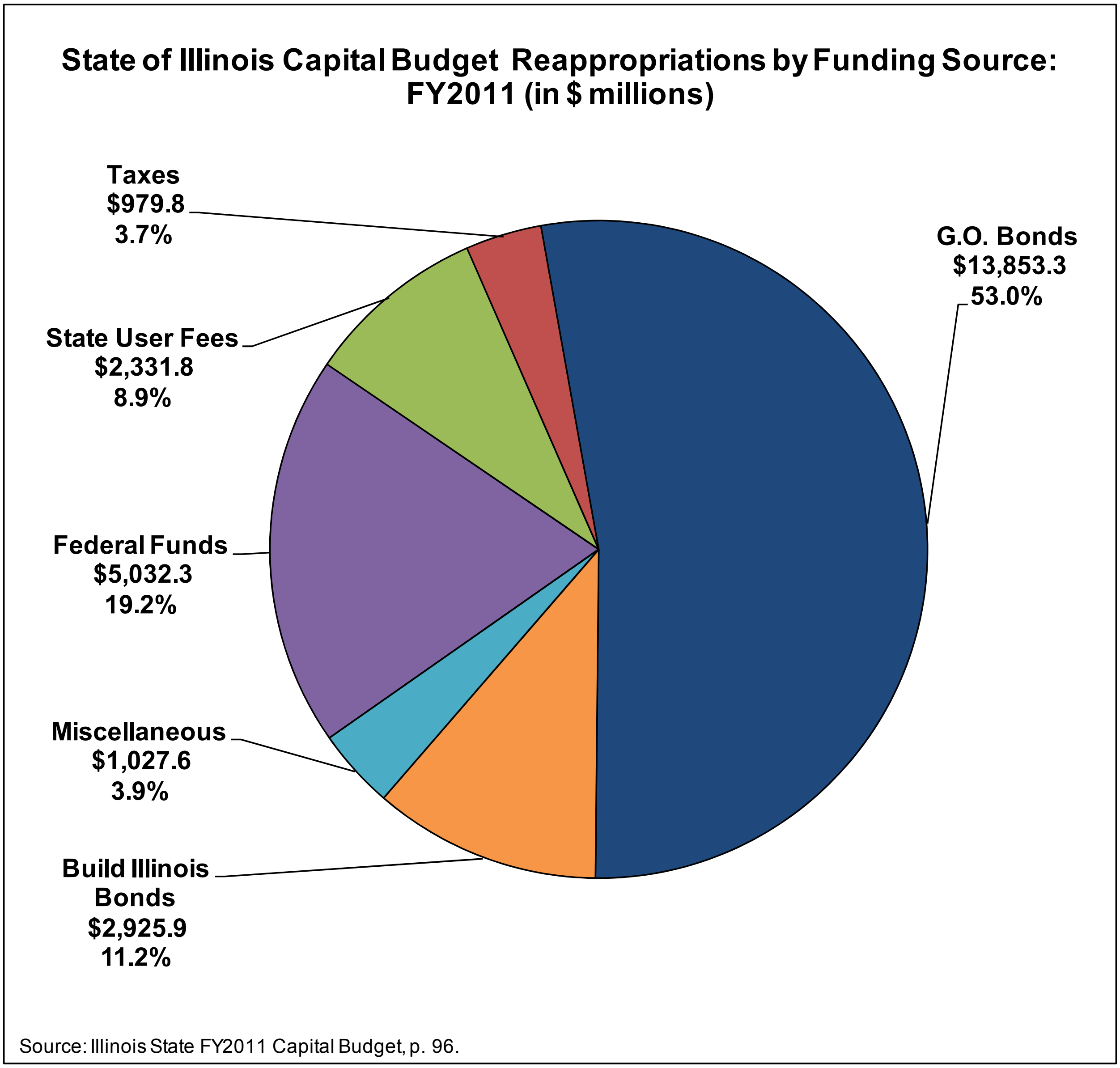
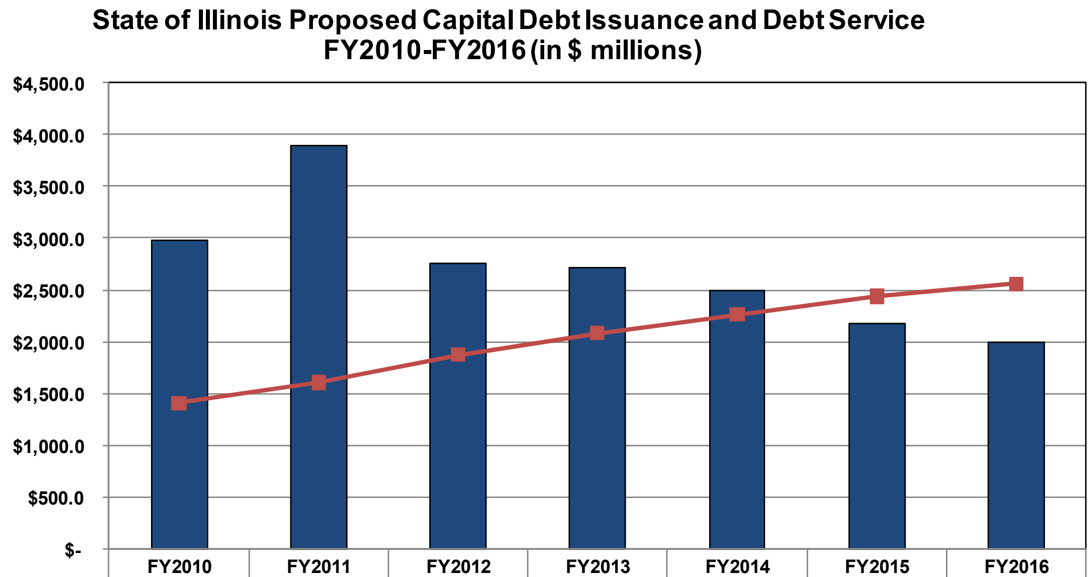
[209] Illinois State FY2011 Capital Budget, p. 34.

The capital projects proposed for reauthorization in the capital budget are mostly debt-funded projects. Build Illinois and G.O. Bonds make up 64.2% of the funding totaling $16.8 billion. As mentioned above, the General Assembly only authorized a $5.8 billion increase in new bond authorization and will need to vote to approve more bond funding as the spending continues in FY2011. The following graph shows total reappropriated capital by type of funding.



Capital Debt

The State originally estimated it would need to borrow $12 billion to $14 billion to complete all the new state-funded projects in the *Illinois Jobs Now!* capital budget. However, the capital budget now estimates the State will sell a total of $19.0 billion in capital purpose bonds between FY2010 and FY2016, while retiring only $1.9 billion of existing capital debt in the same years. The following chart shows the estimated annual debt issuance for capital, including General Obligation Bonds and Build Illinois Bonds compared to the total capital debt service.



	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016
New Capital Debt Issuance	$2,986.0	$3,900.0	$2,760.0	$2,711.0	$2,492.0	$2,180.0	$1,997.0
Total Capital Debt Service	$1,408.0	$1,605.0	$1,875.0	$2,080.0	$2,264.0	$2,437.0	$2,559.0

Source: Illinois State FY2011 Capital Budget, p. 87.
Note: Includes both General Obligation Debt for capital purposes and Build Illinois Bonds.

Illinois' total capital indebtedness and other state debt issues are discussed in detail in the Debt Trends section beginning on page 66 of this report.

In 2009, the State approved a package of revenues[210] expected to total $943 million to $1.2 billion annually to support the new capital borrowing, which included:

- Statewide legalization and taxation of video poker – $288 to $534 million;
- Expanded sales tax on candy, sweetened beverages and some hygiene products – $65 million;
- Leasing a portion of state lottery operations – $150 million;
- Increased per gallon tax on beer, wine and liquor – $108 million; and
- Increased license and vehicle fees – $332 million.

[210] Public Act 096-0034.

The FY2011 capital budget does not include any additional funding to support the increase of $1.6 billion in new borrowing for the FY2011 capital budget, and the latest revenue estimates show only roughly $269 million total from these sources in FY2010.[211] Since the enactment of legalized video poker, more than 50 communities have taken advantage of an opt-out clause in the legislation and the City of Chicago already has a prohibition on video gaming in the city. Without the participation of these governments, the revenue from video poker is expected to drop by between $102.2 million and $189.7 million.[212] The Illinois Gaming Board also has stated it does not expect to be ready to monitor and issue licenses until after January 2012.

The lease of the marketing operations of the lottery has been delayed until at least September 2010. In the meantime, increased lottery sales have generated only $25 million for capital debt service. The increased tax on alcoholic beverages has generated $45.1 million since taking affect September 1, 2009. However, $34.5 million of the new revenue has been deposited in a protest fund due to litigation opposing the increase and only $10.6 million has been allocated for capital funding.[213]

If the State issues the proposed $19 billion in new capital debt over the next five years, any shortfall in the revenues passed to pay for the debt service will lead to additional stress on the State's operating budget. The State of Illinois pledges its full faith and credit in support of these debts, which means the funds for monthly debt service payments are transferred to the bond repayment account before any other state appropriations can be paid.

[211] Commission on Government Forecasting and Accountability, *2011 Capital Plan*, April 2010, p. 10.
[212] Commission on Government Forecasting and Accountability, 2011 *Capital Plan*, April 2010, p. 10.
[213] Ibid.

CONCLUSION

The Civic Federation **opposes** Governor Pat Quinn's FY2011 recommended $52.0 billion operating budget for the State of Illinois because it is unbalanced and does too little to address the State's fiscal crisis. The Governor's recommended budget will make the State's financial condition worse, because it calls for borrowing billions to pay for operations while continuing to ignore a massive backlog of unpaid bills.

Although the Civic Federation is **encouraged** that Governor Pat Quinn has signed significant pension reform legislation and recommends reductions in spending, we cannot support his FY2011 State of Illinois operating budget because it does not effectively stabilize state finances or significantly reduce the State's $12.9 billion deficit going into FY2011.

The Civic Federation supports the first steps by the Governor and General Assembly toward comprehensive public pension reform and urges state leaders to implement further reforms. To address its substantial unfunded pension liabilities, the State needs to reduce the pension benefits of current employees. The Civic Federation recommends that the State contribute to its retirement systems in accordance with the amount certified by the systems' boards, pursuant to statute.

The Civic Federation supports efforts to reduce state spending such as the $254.5 million cut to the State's contributions for retiree health care and $70.0 million reduction to Illinois Cares Rx, and encourages the State to make additional reductions. We are concerned that the recommended reductions include a $613.1 million cut to General State Aid to elementary and secondary education and a $308 million reduction in the county and municipality share of state income tax revenue. These reductions pass expenses from one government to another, put added pressure on local property taxes, and do not necessarily cut taxpayer-supported spending.

The Civic Federation **opposes** the Governor's alternative budget plan issued six weeks after his budget address because it relies even more heavily on borrowing than the Governor's original recommendation and proposes to raise taxes primarily to avert spending cuts rather than to pay down the deficit or reduce the State's other growing liabilities.

The Civic Federation **opposes** the Governor's recommended increase and reauthorization of new debt-funded capital spending because the program is not based on a comprehensive capital improvement plan and the revenues approved are not enough to support the estimated $19 billion in borrowing over the next five years.