The Institute for Illinois' Fiscal Sustainability

AT THE CIVIC FEDERATION

State of Illinois Enacted FY2010 Budget:

A Review of the Operating and Capital Budgets Enacted for the Current Fiscal Year

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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.

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EXECUTIVE SUMMARY

This report examines the $54.3 billion FY2010 operating budget for the State of Illinois that was approved by the General Assembly and signed by Governor Pat Quinn on July 15, 2009—two weeks after the start of the State's fiscal year on July 1. The report compares this enacted budget with both the FY2010 budget recommended by Governor Quinn in March of 2009 and the estimated year-end budget for FY2009. Although the Civic Federation has typically focused on comparing proposed budgets from one fiscal year to the next, this report looks at the actual FY2009 budget in order to analyze spending and revenue trends that have led to the State's current fiscal crisis. Because the state has updated certain revenue and appropriation projections since the budget was enacted, this report also examines those revisions. In addition to examining the enacted FY2010 operating budget, the report also reviews the $31 billion enacted FY2010 capital budget, passed on July 13, 2009.

The key findings of the Civic Federation's review of the State of Illinois FY2010 enacted budget include the following:

Deficit

- The State began FY2010 with a $3.7 billion deficit carried over from the prior fiscal year. As enacted in July of 2009, the budget would have paid down the deficit by $279 million;
- Subsequent revisions in revenue and expenditure projections increased the deficit by $2.0 billion to $5.7 billion at the end of FY2010;
- The anticipated two-year deficit is expected to total at least $12.8 billion in FY2011, based on the loss of one-time revenues and the addition of newly required expenditures.

Revenues

- The enacted FY2010 General Funds budget relies on borrowing and one-time sources of revenue, including $1.3 billion from the proceeds of short-term borrowing, $2.0 billion from federal recovery funds and $352 million from one-time transfers into General Funds from other funds;
- State revenue projections in support of the enacted FY2010 General Funds budget were reduced in the second quarter of the fiscal year. Projections of personal income tax collections have declined by 8.3% since the FY2010 budget was enacted;
- The enacted FY2010 budget projected $29.3 billion in General Funds revenue, a $3.8 billion or 11.4% reduction from Governor Pat Quinn's proposed budget of $33.1 billion in General Funds revenue;
- None of the Governor's proposed General Funds revenue increases, including $3.2 billion from a proposed 50% income tax increase, were passed by the General Assembly;

- The $29.3 billion in General Funds revenue in the enacted FY2010 budget represents an increase of $155 million or 0.5% from General Funds revenue of $29.1 billion in the year-end estimated FY2009 budget;

- The State now projects $28.8 billion in General Funds revenue for FY2010, which represents a decrease of $500 million or 1.7% from General Funds revenues of $29.3 billion in the enacted FY2010 budget.

Appropriations

- Appropriations from General Funds totaled $26.1 billion in the enacted FY2010 budget and do not include state pension contributions. The FY2010 number is not comparable with FY2009 General Funds appropriations of $30.3 billion, which do include state pension fund contributions;

- Instead of making $3.5 billion of pension contributions from General Funds in FY2010, the State will use proceeds from the recent sale of pension obligation notes to finance its annual contribution in FY2010;

- The appropriations approved by the General Assembly in the enacted budget were unusual because they consisted mostly of lump sum departmental appropriations rather than direct, line-item funding of specific programs within departments;

- The $54.3 billion total enacted operating budget includes an increase of $1.4 billion or 2.7% from Governor Quinn's recommended budget of $52.9 billion;

- After the FY2010 budget was enacted, General Funds appropriations were revised to $26.3 billion, an increase of 0.9% or $228 million.

Capital

- The General Assembly enacted capital budget that totals roughly $31 billion that was a 19.2% larger than the original capital spending proposal from the Governor;

- The capital spending plan relies on revenue from expansion of gaming to all corners of the State through legalized video poker and other sources that, due to delays in implementation, will not be available to pay for debt service on the necessary capital borrowing for up to one year or longer including a lease of the State's lottery operations;

- The FY2010 enacted capital budget was not based on a comprehensive capital improvement plan (CIP) that effectively manages and prioritizes critical investment in state infrastructure through a transparent, needs-based planning process. As a result, the urgency of the appropriated projects cannot be easily determined.

BUDGET TIMELINE

The State of Illinois, like the rest of the country in early 2009, was in the midst of a severe recession that was driving down economically sensitive revenues, such as income taxes and sales taxes. The nationwide economic problems were compounded in Illinois by many years of fiscal mismanagement.[1] The State faced a longstanding structural deficit; a situation in which a government's expense growth consistently outpaces its revenue growth. Illinois allowed bills to pile up because it did not have the cash on hand to pay them. When the mountain of bills grew too high, the State borrowed money to reduce the backlog. Illinois also put off making contributions to its employee retirement systems or borrowed to pay for contributions. As of December 31, 2008, the pension systems were underfunded by an estimated $73.4 billion and had a combined funded ratio of 40.0%.[2]

Going into FY2010, the State faced a two-year budget gap of $11.6 billion. Of that total, $4.3 billion was due to a projected FY2009 deficit caused by lower than expected revenues and higher expenditures, including a supplemental Medicaid appropriation that allowed the State to collect federal stimulus funds. The remaining $7.3 billion was the estimated FY2010 deficit that would result from not making any changes in revenues or expenditures. The two-year deficit would have amounted to $12.4 billion if the $835 million year-end shortfall from FY2008 were added to the total.[3]

Governor's FY2010 Operating Budget Recommendation

On March 18, 2009, Governor Pat Quinn proposed a $52.9 billion operating budget for FY2010.[4] The Governor's FY2010 operating budget consisted of $28.4 billion in General Funds and $24.5 billion in Other State Funds and Federal Funds.[5] To help finance his proposal, Governor Quinn recommended an increase in income tax rates from 3% to 4.5% for personal taxes and 4.8% to 7.2% for corporate taxes. The standard personal exemption from the income tax would have tripled from $2,000 to $6,000. The Governor's plan included $1.3 billion in spending cuts and $4.8 billion in federal stimulus funds under the American Recovery and Reinvestment Act of 2009 (ARRA). Governor Quinn also recommended increased employee and retiree contributions for health insurance and major reforms to the state employee pension systems, including a two-tier plan providing reduced benefits for new hires. Overall, the two-tier system was projected to reduce pension liabilities by $162 billion over 35 years. In light of these expected savings, the Governor proposed partial pension holidays for FY2009 and FY2010.

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[1] The Pew Center on the States, *Beyond California: States in Fiscal Peril,* November 2009, at http://downloads.pewcenteronthestates.org/BeyondCalifornia.pdf (last visited on December 1, 2009).
[2] Commission on Government Forecasting and Accountability, "Monthly Briefing," (February 2009), p.8.
[3] Illinois General Assembly, Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2010,* November 2009, p. 26 at http://www.ilga.gov/commission/cgfa2006/Upload/FY2010budgetsummary.pdf (last visited on December 2, 2009).
[4] State of Illinois FY2010 Budget at http://www2.illinois.gov/budget/Documents/FY2010OperatingBudget.pdf (last visited on December 1, 2009).
[5] General Funds are used for general operations such as education, public safety and health and human services and are the funds over which the state has the most control and discretion. Other State Funds consist mainly of Special State Funds: accounts for activities funded by earmarked revenue sources that may only be used for special purposes. Federal Funds support a variety of state programs financed with federal revenues.

The Civic Federation, in a report on May 11, 2009, rejected the Governor's proposal because it raised taxes without focusing on eliminating the State's structural deficit.[6] The Federation proposed an income tax increase in FY2010 from 3% to 4% for personal taxes and 4.8% to 6.4% for corporate taxes. Unlike the Governor, the Federation recommended no increase in the personal exemption and said that the new revenue should be used to pay for the State's outstanding liabilities, including its underfunded pension systems, and must be linked to deeper spending cuts and substantive reforms. As an alternative or complement to deep budget cuts, the Federation said that the State could consider new taxes, such as a tax on retirement income and reinstating the State sales tax on food and drugs. The Federation supported the Governor's proposed pension and health insurance reforms and called for more changes, including a moratorium on new pension benefits.

General Assembly Action on Operating Budget

On May 30, 2009, the Illinois Senate approved an alternative to the Governor's budget proposal that increased both personal and corporate income tax rates to 5% and broadened the sales tax to include 39 services such as dry cleaning, cable television and video rental.[7] In FY2010, $1.5 billion of the new tax revenue would have been set aside for education funding.[8] After being passed by the Senate, the proposal did not make it to a floor vote in the Illinois House.

A separate budget proposal was approved by the General Assembly on May 31, 2009. The plan appropriated funding for services at 50% percent of the level recommended by Governor Quinn, resulting in a $7 billion cut. On July 1, 2009, the first day of the new fiscal year, the Governor vetoed Senate Bill 1197, one of the key FY2010 budget bills, and subsequently vetoed a series of other budget measures. A Special Session was called for July 14 by the Senate President and House Speaker to consider budget-related legislation.

Enacted FY2010 Operating Budget

On July 15—two weeks after the start of the fiscal year—a $54.3 billion operating budget was passed by the General Assembly and signed by the Governor.[9] The budget was composed of $26.1 billion in General Funds and $28.2 billion in Other State Funds and Federal Funds. Instead of the line items historically included in appropriations bills, the FY2010 bill allocated roughly half of the total spending in lump sums to agencies. The unusual lump sum approach meant that the Governor, rather than the Legislature, was responsible for deciding which programs to cut or eliminate. The new budget also authorized the issuance of $3.5 billion in five-year pension notes to finance the required General Funds pension contribution.[10]

After the budget was passed, Governor Quinn announced a plan to allocate the lump sums that had been appropriated for various grants and programs. The Governor concluded that the

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[6] The Civic Federation, *State of Illinois FY2010 Recommended Operating & Capital Budgets*, May 11, 2009, at http://civicfed.org/sites/default/files/civicfed_294.pdf (last visited on December 1, 2009).
[7] HB 174, 96th General Assembly.
[8] Rick Pearson and Ray Long, "Senate OKs Tax Hike on Income, Many Services," *Chicago Tribune*, May 31, 2009.
[9] Public Acts 96-0042, 96-0044, 96-0045 and 96-0046.
[10] 30 ILCS 330/7.2 (2009).

FY2010 budget was "deeply underfunded."[11] He stated that the General Funds appropriations of $26.1 billion left $1.4 billion in "unmet needs" and $3.9 billion in unpaid bills from FY2009. Governor Quinn said he would try again later in the year for a tax increase to fund the unmet needs, which included $600 million for Medicaid, $600 million for employee health insurance and $225 million for college scholarships.

The Governor has said he intends to fund the increase and pay off mounting bills through short-term borrowing by issuing new debt or borrowing from the State's special funds.[12] The State's unpaid bills stood at $5.1 billion at the end of December of 2009, according to the Comptroller's Office.[13] Reports are proliferating about social-service agencies and other vendors that have been forced to lay off staff and cut services because they depend on the State for much of their funding and have not been paid. AARP Illinois recently said that the State owes $200 million to 175 social service agencies that provide critical home and community-based services to 60,000 seniors, many of whom might be forced to go into nursing homes if the agencies have to lay off workers or close their doors.[14]

FY2010 Budget Revisions

Following the budget's enactment, lawmakers appropriated $205 million for college scholarships for low-income students under the Monetary Award Program (MAP).[15] Additionally, expenditure estimates were revised[16] to reflect a decline in appropriations that will not be spent during the fiscal year as well as a decline in savings associated with bond refinancing. FY2010 revenue estimates also declined, resulting in a $1.1 billion reduction in General Funds revenue projections since the budget was enacted.

Governor's Recommended FY2010 Capital Budget

Along with the operating budget, Governor Quinn on March 18, 2009 recommended a $26 billion capital budget for FY2010. A preliminary capital bill, signed on April 3, 2009, funded $3 billion in new transportation projects funded with General Obligation debt.[17] The bill also included proposed stimulus projects that had already received federal recovery funds totaling $1.5 billion.

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[11] State of Illinois, *Governor's Allocation Plan,* July 31, 2009 at http://www2.illinois.gov/budget/Documents/FY10%20Allocation%20Plan.pdf (last viewed December 4, 2009).
[12] Rick Pearson, "Illinois Borrows to Stay Afloat," Chicago Tribune, November 2, 2009, at http://www.chicagotribune.com/news/elections/chi-quinn-borrowing-091102,0,4962653,print.story (last visited on December 11, 2009).
[13] Illinois Office of the Comptroller, Comptroller's Quarterly, January 2010, p.1, at http://www.ioc.state.il.us/ioc-pdf/CQJanuary10.pdf (last visited on January 19, 2010).
[14] AARP Illinois, "State $200 Million Behind in Payments to Agencies Providing Care to Thousands of Older Illinoisans, December 10, 2009, at http://www.aarp.org/community/AARPIL/journals/State_Owes_200_Million_to/2300102 (last visited on December 15, 2009).
[15] Public Act 96-0792, signed on October 19, 2009, amends Public Act 96-0042 to provide an additional $205 million for MAP.
[16] State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement*, January 7, 2010.
[17] Public Acts 96-0004 and 96-0005.

The Civic Federation opposed the Governor's recommended $26 billion capital plan because it was unaffordable over time and was not based on a comprehensive capital improvement plan and a transparent assessment of the State's actual infrastructure needs. In its May 11 report on the recommended FY2010 budget, the Federation said that the massive spending proposal failed to provide an adequate revenue stream to pay the debt service on the capital program after the third year.[18] The report also criticized the plan for extending the State's existing capital debt and back loading the debt service payments to reduce current costs.

General Assembly Action on Capital Budget

On July 13, 2009—two days before the operating budget was approved—the General Assembly passed and the Governor signed a multi-year, $31 billion capital plan.[19] This was the State's first public works program in a decade and called for new spending on a variety of infrastructure projects, including statewide improvements in roads, schools and mass transit systems. The program was funded by federal, state and local sources, with the State's share of roughly $13 billion financed through the sale of General Obligation and Build Illinois Bonds. To pay the increased annual debt service on the new borrowing, the General Assembly also approved a revenue bill to legalize and tax video poker, increase auto-related fees, expand liquor taxes and impose new taxes on candy, tea drinks and various other products.[20] It was estimated that these new revenue sources will generate roughly $1.1 billion a year.

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[18] The Civic Federation, *State of Illinois FY2010 Recommended Operating & Capital Budgets*, May 11, 2009, at http://civicfed.org/sites/default/files/civicfed_294.pdf , pp. 85-91 (last visited on December 1, 2009).
[19] The capital package consisted of Public Acts 96-0034 to 96-0038 and 96-0040. The $31 billion plan reappropriated the $1.6 billion of the capital funding approved in April that had been appropriated by the General Assembly.
[20] Public Act 096-0034.

APPROPRIATIONS

Illinois' $54.3 billion total enacted FY2010 operating budget is larger than Governor Pat Quinn's recommended budget, with an increase in Federal Funds and Other State Funds offsetting a decline in General Funds appropriations.[21] General Funds appropriations in the FY2010 budget are also below those in the year-end estimated FY2009 budget. However, comparisons are complicated by differences in how the State's pension contributions are handled in the various budgets, as explained below.

Total Appropriations

The $54.3 billion enacted FY2010 operating budget approved by the General Assembly and signed by Governor Quinn represents an increase of $1.4 billion or 2.7% from the Governor's recommended budget of $52.9 billion.[22] Total appropriations are expected to be $54.5 billion after including mid-year adjustments to the budget, which is a $1.7 billion or 3.1% increase from the Governor's recommended budget. The next table shows that the rise in the total budget was driven by increases of $629.4 million or 7.1% in Federal Funds and $3.1 billion or 19.9% in Other State Funds. At the same time, estimated General Funds appropriations declined by $2.1 billion or 7.4% from the budget proposal. The following chart shows the change in total appropriations from Governor's recommended budget proposal for FY2010 to the most current estimates of the budget.

Appropriations: FY2010 Recommended, Enacted and Estimated (in $ billions)

	Recommended	Enacted	Estimated	$ change	% change
General Funds	$ 28.4	$ 26.1	$ 26.3	$ (2.1)	-7.4%
Other State Funds	$ 15.6	$ 18.8	$ 18.8	$ 3.1	19.9%
Federal Funds	$ 8.8	$ 9.5	$ 9.5	$ 0.6	7.1%
Total	**$ 52.9**	**$ 54.3**	**$ 54.5**	**$ 1.7**	**3.1%**

Sources: Illinois State Budget FY2010, 2-30; Commission on Government Forecasting and Accountability, State of Illinois Budget Summary Fiscal Year 2010, 191; State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, Official Statement, January 7, 2010.

General Funds Appropriations

General Funds appropriations make up 48.0% of the total spending in the enacted FY2010 operating budget. General Funds appropriations declined by 8.1% or $2.3 billion to $26.1 billion from the Governor's recommended budget of $28.4 billion. After including mid-year appropriations adjustments, the FY2010 budget totals $26.3 billion, a 7.3% or $2.1 billion decrease from the Governor's recommended budget. However, the recommended budget included General Funds appropriations for a portion of the State's required contribution to its retirement systems. In contrast, the FY2010 budget includes no General Funds contribution to

[21] General Funds are used for general operations such as education, public safety and health and human services and are the funds over which the State has the most control and discretion. Other State Funds consist mainly of Special State Funds: accounts for activities funded by earmarked revenue sources that may only be used for special purposes. Federal Funds support a variety of state programs financed with federal revenues.

[22] Because of a lack of data, this report does not compare total appropriations in the enacted FY2010 budget with total appropriations in the estimated year-end FY2009 budget.

the pension funds. Instead, the contribution is financed from the proceeds of the sale of $3.5 billion in pension notes.[23]

The following table compares the FY2010 appropriations from General Funds by agency proposed by the Governor with the FY2010 enacted appropriations and mid-year estimates of appropriations from General Funds.

General Funds Appropriations by Agency: FY2010 Recommended, Enacted, and Estimated (in $ millions)					
	Recommended	Enacted	Estimated	$ Change	% Change
Elementary and Secondary Education	$ 7,626.5	$ 7,307.9	$ 7,316.9	$ (309.6)	-4.1%
Higher Education	$ 2,372.6	$ 2,001.8	$ 2,206.8	$ (165.8)	-7.0%
Healthcare and Family Services	$ 8,794.1	$ 7,808.6	$ 7,808.6	$ (985.5)	-11.2%
Revenue	$ 153.8	$ 142.5	$ 142.5	$ (11.3)	-7.3%
Human Services	$ 4,163.5	$ 3,992.5	$ 3,992.5	$ (171.0)	-4.1%
Corrections	$ 1,244.2	$ 1,151.3	$ 1,151.3	$ (92.9)	-7.5%
Children and Family Services	$ 899.3	$ 865.0	$ 865.0	$ (34.3)	-3.8%
Central Management Services	$ 75.0	$ 90.0	$ 90.0	$ 15.0	19.9%
State Police	$ 214.5	$ 287.4	$ 287.4	$ 72.9	34.0%
Other Agencies	$ 2,847.0	$ 2,437.8	$ 2,451.8	$ (395.2)	-13.9%
Total	**$ 28,390.5**	**$ 26,084.8**	**$ 26,312.8**	**$ (2,077.7)**	**-7.3%**

Note: Includes the Governor's allocation of a $2.2 billion lump sum appropriation for human services and an undesignated lump sum appropriation of $1.2 billion.

Sources: Illinois State Budget FY2010, 2-21 to 2-30, March 2009; State of Illinois $400 million General Obligation Bonds Series A of September 2009, *Preliminary Official Statement*, September 9, 2009; Governor's Office of Management and Budget, http://www.state.il.us/budget/; Governor's Office of Management and Budget, Supplemental Notice of Delegation, September 16, 2009; State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement*, January 7, 2010; State of Illinois Office of the Comptroller, Expenditures Control Panel, http://www.ioc.state.il.us (last visited January 19, 2010).

The Department of Healthcare and Family Services (HFS) experienced the largest share of the reductions, receiving $7.8 billion, which is $985.5 million less than the Governor's $8.8 billion proposal. This reduction accounts for more than 40% of the change from the Governor's proposed General Funds budget.

In the enacted budget, the Board of Higher Education received the largest percentage reduction from the Governor's recommendation, a decline of 15.6% or $370.8 million. This reduction resulted in cuts to MAP grants, which fund need-based college scholarships. Following the enactment of the FY2010 budget, the Governor signed Public Act 96-0792, which provided $205.0 million for these college scholarships. With these additional appropriations, the higher education budget is $165.8 million below the Governor's recommendation. General Funds appropriations for elementary and secondary education were reduced by $318.6 million or 4.2% from the recommended budget. However, the enacted budget included an additional $473.5 million from federal ARRA funds, which offset the decrease in General Funds support for elementary and secondary education.

The $26.1 billion enacted General Funds appropriation for FY2010 is $4.2 billion or 13.9% below the year-end estimated FY2009 General Funds appropriation of $30.3 billion. The $26.3 billion estimated FY2010 appropriations are 13.1% or $4.0 billion less than the year-end estimated FY2009 General Funds appropriations. While the FY2009 amount included pension

[23] 30 ILCS 330/7.2 (2009).

contributions, the FY2010 enacted and estimated amounts do not include them because the contribution is to be financed through the sale of $3.5 billion in pension notes. In FY2009, the State contributed $2.2 billion to the retirement systems from General Funds. With pension contributions excluded from FY2009 and estimated FY2010, the General Funds budget reduction drops to $1.8 billion, which is a 6.3% reduction in appropriations from General Funds.

The next table compares General Funds appropriations by agency from the FY2009 year-end estimated budget and the FY2010 enacted budget and the FY2010 budget as estimated in December of 2009. Appropriations to judicial, legislative, and smaller executive agencies were cut by $1.3 billion from FY2009, or 35.0%.[24] HFS appropriations were reduced by $1.8 billion, a 19.0% cut from FY2009. In the enacted appropriations, higher education declined by $464.0 million, resulting in an 18.8% reduction from FY2009. MAP grants incurred nearly half of the Board of Higher Education's reduction in the enacted budget. After including $205.0 million that was provided through supplemental appropriations for this program, higher education incurred an estimated $259 million or 10.5% appropriations reduction from FY2009. The following chart show the change in General Fund appropriations by agency from FY2009 year-end estimates to the most recently available FY2010 estimates.

General Funds Appropriations by Agency: FY2009 Year-End Estimate, FY2010 Enacted, and FY2010 Estimate (in $ millions)

	FY2009 Year-End Estimate	FY2010 Enacted	FY2010 Estimate	$ Change	% Change
Elementary and Secondary Education	$ 7,445	$ 7,308	$ 7,317	$ (128)	-1.7%
Higher Education	$ 2,466	$ 2,002	$ 2,207	$ (259)	-10.5%
Healthcare and Family Services	$ 9,642	$ 7,809	$ 7,809	$ (1,833)	-19.0%
Revenue	$ 164	$ 143	$ 143	$ (22)	-13.1%
Human Services	$ 4,228	$ 3,993	$ 3,993	$ (236)	-5.6%
Corrections	$ 1,351	$ 1,151	$ 1,151	$ (200)	-14.8%
Children and Family Services	$ 914	$ 865	$ 865	$ (49)	-5.4%
Central Management Services	$ 76	$ 90	$ 90	$ 14	18.4%
State Police	$ 228	$ 287	$ 287	$ 59	26.1%
Other Agencies	$ 3,770	$ 2,438	$ 2,452	$ (1,318)	-35.0%
Total	**$ 30,283**	**$ 26,085**	**$ 26,313**	**$ (3,970)**	**-13.1%**

Note: FY2009 appropriations include state pension contributions of $2.2 in billion general funds; FY2010 appropriation amounts do not include state pension contributions. The general funds portion of the FY2010 required state pension contribution to be funded by $3.5 billion General Obligation Pension Notes. FY2010 includes the Governor's allocation of a $2.2 billion lump sum appropriation for human services and an undesignated lump sum appropriation of $1.2 billion.

Sources: State of Illinois $400 million General Obligation Bonds Series A of September 2009, *Preliminary Official Statement,* September 9, 2009; Governor's Office of Management and Budget, Supplemental Notice of Delegation, September 16, 2009; State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement,* January 7, 2010; State of Illinois Office of the Comptroller, Expenditures Control Panel, http://www.ioc.state.il.us (last visited January 19, 2010).

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[24] Other Agencies include: Office of the Governor, Office of the Lt. Governor, Attorney General, Secretary of State, State Comptroller, Treasurer, State Board of Elections, Aging, Agriculture, Commerce and Economic Opportunity, Employment Security, Human Rights, Juvenile Justice, Labor, Military Affairs, Natural Resources, CHIP, Public Health, Transportation, Veterans' Affairs, Arts Council, Office of Management & Budget, Executive Ethics Commission, Executive Inspector General, Civil Service Commission, Criminal Justice Information Authority, Deaf and Hard of Hearing Commission, East St. Louis Financial Advisory Authority, Guardian Advocacy Commission, Historic Preservation Agency, Illinois Emergency Management Agency, Illinois Emergency Management Agency, Illinois Labor Relations Board, Prisoner Review Board, Procurement Policy Board, Southwestern Illinois Development Auth., State Employees' Retirement System, State Police Merit Board, Upper Illinois River Valley Development, Violence Prevention Authority, all Judicial agencies, and all Legislative agencies.

“Lump Sum” Appropriations

The FY2010 enacted budget was distinctive in Illinois’ modern financial history because instead of directly funding specific programs within departments, it provided the majority of the year’s funding through lump sum departmental appropriations for personnel, operations and grants.[25] In addition, the legislation authorizing $3.5 billion in pension obligation notes required that if $2.23 billion from the net proceeds of the notes were used for the retirement contribution an equivalent amount be appropriated from General Funds for human services.[26] The FY2010 spending bill includes this lump sum appropriation for human services and also includes $1.2 billion (the equivalent of the total pension note proceeds minus the human services lump sum) as an undesignated lump sum appropriation.[27] The next three exhibits display how the Governor allocated the $2.2 billion appropriation to be used for human services and the $1.2 billion appropriation that could be used for any purpose. The following table summarizes the Governor’s allocation of the lump sum appropriations by state agency.

Governor's Allocation of "Lump Sum" Appropriations by Agency FY2010 (in $ thousands)		
Elementary and Secondary Education	$	150,670.6
Higher Education	$	26,723.1
Healthcare and Family Services	$	1,000,000.0
Human Services	$	1,399,375.0
Corrections	$	4,000.0
Children and Family Services	$	272,007.4
Other Agencies	$	453,771.0
Total	**$**	**3,306,547.1**

Sources: Governor's Office of Management and Budget, "Allocations and Departmental Budgets by Agency" http://budget.illinois.gov (last visited on November 24, 2009); Supplemental Notice of Delegation, September 16, 2009.

The next table details the Governor’s allocation of the lump sum appropriations for human services by program. More than half of the human services allocation, $1.4 billion, funded Department of Human Services (DHS) grants. The allocation for all DHS grants totals $3.0 billion after the $1.4 billion from the human services lump sum is included. This represents an $81.2 million or 2.6% reduction from FY2009. DHS primarily reduced appropriations for mental health and developmental disability grants. While the Department of Children and Family Services received $272.0 million of the lump sum appropriation, the department’s final allocation is $49.0 million or 5.4% less than it received in FY2009. The following chart shows the Governor’s “Lump Sum” appropriations by program.

[25] Public Act 96-0042.
[26] Public Act 96-0043, Section 1.
[27] Public Act 096-0042, Article 77, Sections 5 and 10.

Governor's Allocation of Human Services "Lump Sum" Appropriations by Program FY2010 (in $ thousands)	
Children and Family Services	$ 272,007.4
Human Services	$ 1,399,375.0
Transportation	
RTA Reduced Fares	$ 18,435.0
Aging	
Community Care Program	$ 342,000.0
Higher Education	
Adult Education Grants	$ 16,227.2
CTE Grants	$ 10,495.9
Illinois Violence Prevention Authority	$ 1,200.0
Supreme Court	$ 16,000.0
Corrections	$ 4,000.0
Veterans' Affairs	$ 1,000.0
Total	**$ 2,080,740.5**
Human Services "Lump Sum" Appropriation	**$ 2,230,000.0**
Unallocated Appropriation	**$ 149,259.5**

Sources: Governor's Office of Management and Budget, "Allocations and Departmental Budgets by Agency" http://budget.illinois.gov (last visited on November 24, 2009).; Supplemental Notice of Delegation, September 16, 2009.

The next exhibit lists the Governor's allocation of the $1.2 billion lump sum appropriation that could be used for any purpose. The Governor allocated $700.0 million of the $1.2 billion undesignated lump sum for State employee group insurance, as well as $300.0 million for Medicaid. Elementary and secondary education programs also received $150.7 million from the undesignated lump sum appropriation.

Governor's Allocation of Undesignated "Lump Sum" Appropriations by Program FY2010 (in $ thousands)	
Agriculture	
Cook County Extension	$ 1,269.4
Grants to Soil and Water Conservation	$ 2,933.8
Commerce and Economic Opportunity	
Community Programs	$ 3,375.0
Healthcare and Family Services	
Group Insurance	$ 700,000.0
Medicaid	$ 300,000.0
Public Health	$ 39,642.1
Transportation	
State Share of Operating Deficit for AMTRAK	$ 12,865.0
Veterans' Affairs	
PTSD Outpatient Counseling	$ 50.0
Illinois Warrior Assistance Program	$ 250.0
Bonus Payments	$ 47.8
Educational Opportunities	$ 23.7
Cartage & Erection of Headstones	$ 48.7
Elementary and Secondary Education	
Grow Your Own Teachers	$ 1,400.0
Early Childhood Education	$ 85,307.3
Tax-Equivalent Grants	$ 222.6
Re-Enrollment Student Program	$ 1,600.0
Truant Alternative & Optional Education Program	$ 8,031.3
Children's Mental Health Partnership	$ 690.0
Agricultural Education Program	$ 1,352.5
Alternative Ed/Regional Safe Schools	$ 4,263.2
Bilingual Education	$ 11,347.8
Reading Improvement Block Grant	$ 30,455.9
Afterschool Matters	$ 5,000.0
Classroom Cubed	$ 1,000.0
Comprehensive Health Insurance Plan	$ 14,630.5
Total	**$ 1,225,806.6**
Undesignated "Lump Sum" Appropriation	**$ 1,236,000.0**
Unallocated Appropriation	**$ 10,193.4**

Source: Governor's Office of Management and Budget, "Allocations and Departmental Budgets by Agency" http://budget.illinois.gov (last visited on November 24, 2009).

Programs Identified by the Governor as Unmet Needs

The Governor has stated that vital programs remain underfunded in the $26.1 billion General Funds budget. The Governor's estimated funding shortfalls total $1.6 billion, which would be reduced to $1.4 billion if $180.0 million is utilized from contingency reserve funds. The estimated shortfall for both Medicaid and state employee and retiree group insurance was $600.0 million. The Governor estimated that elementary and secondary education funding falls short by $145.0 million. Since the Governor identified these programs, he has signed legislation amending the spending bill to provide an additional $205.0 million for need-based college scholarships, which would cover the majority of his original estimate of the college scholarship shortfall. Additionally, $300.0 million in Medicaid appropriations was shifted from General Funds to Federal Funds mid-year, freeing up funds that the Governor intends to use for group insurance. After adjusting for mid-year appropriations changes, the shortfall estimate drops to $885 million. The following chart shows programs for which the Governor is expected to seek additional funding from the General Assembly before the end of the fiscal year.

Programs Identified by the Governor as Vital and Underfunded
FY2010 (in $ millions)

	Governor's Revised Budget Recommendation	Governor's Allocation of Enacted Appropriations	Governor's Shortfall Estimate
Medicaid	$ 7,533.9	$ 6,914.9	$ 600.0
Group health coverage for state employees, retirees & dependents	$ 1,312.0	$ 700.0	$ 600.0
Pre K-12 education	$ 7,452.7	$ 7,307.9	$ 145.0
College scholarships	$ 440.6	$ 220.0	$ 225.0
Subtotal			**$ 1,570.0**
Use of contingency reserve funds			$ (180.0)
Additional college scholarship funding			$ (205.0)
Funding shift to group health coverage			$ (300.0)
Total Unmet Needs			**$ 885.0**

Note: The Governor signed Public Act 96-0792 on October 19, 2009. The legislation amends the FY2010 spending bill, Public Act 96-0042, to provide an additional $205.0 million for college scholarships.

Source: Governor's Office of Management and Budget, "Governor's Allocation Plan," July 31, 2009, http://www.illinois.gov/publicincludes/statehome/gov/documents/FY10%20Allocation%20Plan.pdf (last visited on November 24, 2009); State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, Official Statement, January 7, 2010.

REVENUES

State revenue projections for the FY2010 budget have proven to be overestimated and have already been reduced by the Governor's Office of Management and Budget.[28] Personal income tax collections, the State's largest revenue source, have been particularly hard hit by the economic slump. Projected personal income tax revenue for FY2010 has declined by 8.3% since the budget was enacted.

General Funds Revenues

The FY2010 enacted budget includes $29.3 billion General Funds revenue, which is $3.8 billion or 11.4% less than Governor Pat Quinn's recommended budget. The following exhibit details General Funds revenue sources for the FY2010 recommended budget, the enacted FY2010 budget and current General Funds revenue estimates. The Governor recommended increasing revenues by $4.0 billion, which included $3.2 billion from income tax rate increases. However, these revenue enhancements were not passed by the General Assembly.

The enacted budget also includes $233 million in additional transfers from other funds into the General Funds not included in the Governor's recommended budget, as well as an increase in income tax projections. The enacted FY2010 budget assumes $9.2 billion from personal income taxes, which is a 3.1% increase from the estimated total presented by the Governor. Although the General Assembly passed the FY2010 budget based on a 3.1% increase in personal income tax revenue estimates, lawmakers did not pass the income tax rate increase recommended by the Governor. Mid-year revenue projections indicate that the State will collect $8.4 billion in personal income tax revenue, which represents a 5.5% or $487 million decrease from the Governor's recommended budget. Corporate income taxes are expected to provide $1.1 billion in the enacted budget, which is 8.5% more than the estimates in the recommended budget, despite the Legislature's rejection of the Governor's proposed corporate tax rate increase. The following table compares the revenues from General Funds in the Governor's recommended FY2010 budget with the FY2010 enacted budget and the most recently available estimates of the current fiscal year budget.

[28] Christopher Wills, "Governor Warns of Growing Problems in Ill. Budget," Chicago Tribune, October 14, 2009.

State of Illinois Revenues for General Funds: FY2010 (in $ millions)					
	Recommended	Enacted	Estimated	$ change	% change
Base Revenues					
State Sources					
Income Taxes (Net)	$ 9,968	$ 10,337	$ 9,570	$ (398)	-4.0%
Personal	$ 8,925	$ 9,205	$ 8,438	$ (487)	-5.5%
Corporate	$ 1,043	$ 1,132	$ 1,132	$ 89	8.5%
Sales Taxes	$ 6,394	$ 6,394	$ 6,394	$ -	0.0%
Public Utility Taxes	$ 1,150	$ 1,150	$ 1,150	$ -	0.0%
Cigarette Taxes	$ 350	$ 350	$ 350	$ -	0.0%
Liquor Taxes	$ 161	$ 161	$ 161	$ -	0.0%
Inheritance Taxes	$ 275	$ 275	$ 275	$ -	0.0%
Insurance Taxes & Fees	$ 325	$ 325	$ 325	$ -	0.0%
Corporate Franchise Fees & Taxes	$ 205	$ 205	$ 205	$ -	0.0%
Interest on State Funds and Investments	$ 80	$ 80	$ 80	$ -	0.0%
Cook County Intergov. Transfer	$ 240	$ 240	$ 240	$ -	0.0%
Other State Sources	$ 430	$ 430	$ 330	$ (100)	-23.3%
Transfers-In					
Lottery	$ 645	$ 645	$ 645	$ -	0.0%
Riverboat Gaming Taxes	$ 478	$ 470	$ 420	$ (58)	-12.1%
Other Transfers	$ 480	$ 459	$ 1,056	$ 576	120.0%
10th Riverboat License	$ 50	$ 50	$ 50	$ -	0.0%
Subtotal State Sources	**$ 21,231**	**$ 21,571**	**$ 21,251**	**$ 20**	**0.1%**
Federal Sources	$ 5,555	$ 5,165	$ 4,985	$ (570)	-10.3%
Total Base Revenues	**$ 26,786**	**$ 26,736**	**$ 26,236**	**$ (550)**	**-2.1%**
Increases to Base Revenues					
One-Time Revenues					
Federal Recovery	$ 1,882	$ 1,966	$ 1,966	$ 84	4.5%
Transfer In	$ 364	$ 597	$ 597	$ 233	64.0%
Subtotal One-Time Revenues	**$ 2,246**	**$ 2,563**	**$ 2,563**	**$ 317**	**14.1%**
Recurring Revenues					
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 Recurring Revenues	**$ 4,044**	**$ -**	**$ -**	**$ (4,044)**	**-100.0%**
Total Adjusting Sources	**$ 6,290**	**$ 2,563**	**$ 2,563**	**$ (3,727)**	**-59.3%**
Total Revenues for General Funds	**$ 33,076**	**$ 29,299**	**$ 28,799**	**$ (4,277)**	**-12.9%**

Note: Enacted Increases to Base Revenues, Transfer In includes the following transfers to the general funds: $245.2 from Capital Projects Fund and $351.7 million from Fund Sweeps

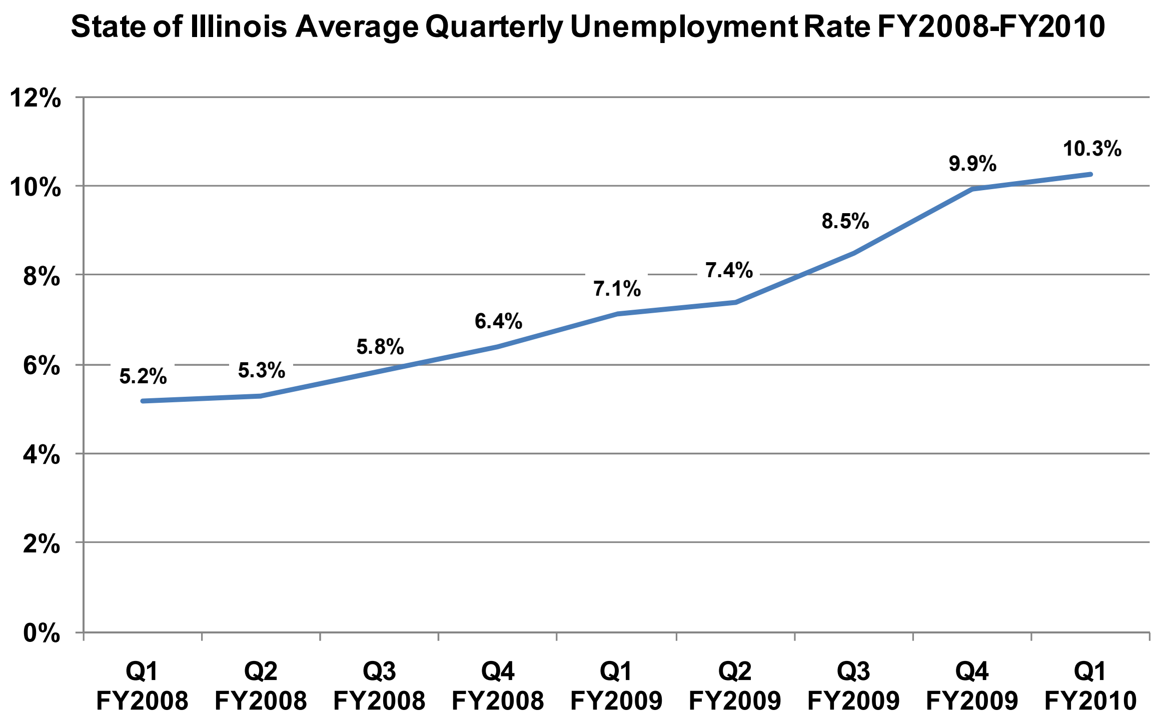
Sources: Illinois State Budget FY2010, 2-33; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2010,* 18, 29, 136; 30 ILCS 105/6z-77 (2009); State of Illinois, $1.25 billion General Obligation Certificates of August 2009, *Official Statement,* August 20, 2009; State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement,* January 7, 2010.

The FY2010 enacted General Funds revenue of $29.3 billion is $155 million or 0.5% higher than FY2009 year-end estimated General Funds revenue of $29.1 billion. However, excluding one-time fund sweeps,[29] General Fund revenues from state sources are expected to decrease by $1.0 billion in the FY2010 enacted budget. This 4.5% decrease is primarily a result of a $578 million decrease in corporate income tax collections and a $379 million reduction in sales tax collections. The FY2010 budget assumes an $18 million drop in personal income tax revenue, which is a reduction of 0.2%. However, since the budget was enacted, personal income tax

[29] Fund sweeps refer to statutory transfers of surplus monies from other funds to General Funds.

estimates have dropped from $9.2 billion to $8.4 billion due in part to the impact of a continuing increase in unemployment rates that began in the second quarter of FY2009.[30]

The State's unemployment rate has nearly doubled since the start of FY2008. The following chart shows state unemployment rates climbing from 7.1% during the first quarter of FY2009 to 10.3% during the first quarter of FY2010. Illinois' personal income has declined due to the increasing unemployment rate as well as other effects of the economic recession. As a result, personal income tax receipts fell 11.7% in this year's fiscal first quarter to $2.1 billion from $2.4 billion in the first quarter of FY2009. The recession that induced rising unemployment rates and declining personal income tax revenue in Illinois has also affected tax collections for the rest of the country. According to the Rockefeller Institute, states collected 27.5% less in personal income taxes between April and June of 2009 than in the same period in 2008.[31]



Source: Commission on Government Forecasting and Accountability, Monthly Briefings: July 2008 - October 2010.

Increases in funds from the federal government and fund transfers offset the reductions in state revenue. Federal funding increases included $164 million in additional revenues from Federal sources, and utilizing $400 million more in federal recovery funds than in FY2009. The federal recovery funds were provided to states through ARRA for the purpose of maintaining state programs and providing fiscal stabilization to state budgets. Since the budget was enacted, an adjustment to Medicaid appropriations resulted in a $180 million reduction in Federal sources.

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[30] State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement,* January 7, 2010.
[31] Rockefeller Institute of Government, "State Revenue Report", October 2009, No. 77.

General Funds revenues also increased due to a transfer of $245.2 million from the Capital Projects Fund and $351.7 million through fund sweeps.[32]

Additionally, riverboat gaming taxes were expected to increase from $430 million to $470 million when the budget was enacted. This increase of 9.3% was the largest percentage change from FY2009 for any of the General Funds' state revenue sources. However, this projected increase came after the enacted FY2009 budget assumed that these revenues would be $287 million more than actual FY2009 collections.[33] Since the FY2010 budget was enacted, riverboat gaming tax revenue projections dropped to $420 million, a 2.3% or $10 million decline from FY2009. The FY2010 budget also includes $50 million from the sale of the tenth riverboat license. After adjusting for mid-year revenue projections, General Funds revenues are expected to total $28.8 billion in FY2010, a $345 million or 1.2% reduction from FY2009. The following table compares the year-end estimated FY2009 revenues with the enacted FY2010 General Funds revenues and current estimates of FY2010 General Funds revenues.

[32] 30 ILCS 105/6z-77 (2009); 30 ILCS 105/8.49 (2009).
[33] Institute for Illinois' Fiscal Sustainability at the Civic Federation, "State of Illinois FY2010 Recommended Operating and Capital Budgets," May 11, 2009.

State of Illinois Revenues for General Funds: Year-End Estimated FY2009, Enacted FY2010 and Estimated FY2010 (in $ millions)					
	Year-end Estimate FY2009	Enacted FY2010	Estimate FY2010	$ change	% change
Base Revenues					
State Sources					
Income Taxes (Net)	$ 10,933	$ 10,337	$ 9,570	$ (1,363)	-12.5%
Personal	$ 9,223	$ 9,205	$ 8,438	$ (785)	-8.5%
Corporate	$ 1,710	$ 1,132	$ 1,132	$ (578)	-33.8%
Sales Taxes	$ 6,773	$ 6,394	$ 6,394	$ (379)	-5.6%
Public Utility Taxes	$ 1,168	$ 1,150	$ 1,150	$ (18)	-1.5%
Cigarette Taxes	$ 350	$ 350	$ 350	$ -	0.0%
Liquor Taxes	$ 158	$ 161	$ 161	$ 3	1.9%
Inheritance Taxes	$ 288	$ 275	$ 275	$ (13)	-4.5%
Insurance Taxes & Fees	$ 334	$ 325	$ 325	$ (9)	-2.7%
Corporate Franchise Fees & Taxes	$ 201	$ 205	$ 205	$ 4	2.0%
Interest on State Funds and Investments	$ 81	$ 80	$ 80	$ (1)	-1.2%
Cook County Intergov. Transfer	$ 253	$ 240	$ 240	$ (13)	-5.1%
Other State Sources	$ 445	$ 430	$ 330	$ (115)	-25.8%
Transfers-In				$ -	
Lottery	$ 625	$ 645	$ 645	$ 20	3.2%
Riverboat Gaming Taxes	$ 430	$ 470	$ 420	$ (10)	-2.3%
Other Transfers	$ 538	$ 459	$ 1,056	$ 518	96.3%
10th Riverboat License	$ -	$ 50	$ 50	$ 50	N/A
Subtotal State Sources	**$ 22,577**	**$ 21,571**	**$ 21,251**	**$ (1,326)**	**-5.9%**
Federal Sources	$ 5,001	$ 5,165	$ 4,985	$ (16)	-0.3%
Total Base Revenues	**$ 27,578**	**$ 26,736**	**$ 26,236**	**$ (1,342)**	**-4.9%**
Increases to Base Revenues					
One-Time Revenues					
Federal Recovery	$ 1,566	$ 1,966	$ 1,966	$ 400	25.5%
Transfer In	$ -	$ 597	$ 597	$ 597	N/A
Subtotal One-Time Revenues	**$ 1,566**	**$ 2,563**	**$ 2,563**	**$ 997**	**63.7%**
Recurring Revenues					
Income Taxes	$ -	$ -	$ -	$ -	N/A
Cigarette Taxes	$ -	$ -	$ -	$ -	N/A
Equity Charges	$ -	$ -	$ -	$ -	N/A
Titles and Fees	$ -	$ -	$ -	$ -	N/A
Subtotal Recurring Revenues	**$ -**	**$ -**	**$ -**	**$ -**	**N/A**
Total Adjusting Sources	**$ 1,566**	**$ 2,563**	**$ 2,563**	**$ 997**	**63.7%**
Total Revenues for General Funds	**$ 29,144**	**$ 29,299**	**$ 28,799**	**$ (345)**	**-1.2%**

Note: Enacted Increases to Base Revenues, Transfer In includes the following transfers to the general funds: $245.2 from Capital Projects Fund and $351.7 million from Fund Sweeps

Sources: State of Illinois $400 million General Obligation Bonds Series A of September 2009, *Preliminary Official Statement,* September 9, 2009; State of Illinois, $1.25 billion General Obligation Certificates of August 2009, *Official Statement,* August 20, 2009; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2010,* 18, 28, 29, 136; 30 ILCS 105/6z-77 (2009); State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement,* January 7, 2010.

One-time Revenue Sources and Borrowing

The FY2010 budget relies heavily on one-time sources of revenue, including the proceeds of short-term borrowing and borrowing for the contribution to the state pension systems.[34] Federal recovery funds and fund sweeps[35] added $2.3 billion to General Funds, which is equal to 8.0% of the total estimated FY2010 General Funds revenue of $28.8 billion. In addition to these revenue sources, $3.5 billion in proceeds of the pension notes will also be a one-time source of revenue. These one-time revenue sources totaling $5.8 billion are equivalent to 20.1% of estimated General Funds. The following table lists one-time revenue sources used to balance the budget that will not be available in future fiscal years.

One-Time Revenue Sources FY2010 (in $ millions)	
Federal Recovery	$ 1,966.0
Fund Sweeps	$ 351.7
Pension Obligation Note Proceeds	$ 3,466.0
Total	**$ 5,783.7**

Sources: Preliminary Official Statement, State of Illinois General Obligation Certificates, $1.25 billion, August 20, 2009, 23; Commission on Government Forecasting and Accountability, State of Illinois Budget Summary Fiscal Year 2010, 136; 30 ILCS 330/7.2 (2009).

The State issued $1.25 billion in General Obligation bond certificates in August of 2009. These bonds are short-term debt, which must be satisfied within one year or less. Additionally, the State borrowed $1.0 billion in May of 2009, which must be repaid during FY2010. The following table shows the revenue generated for FY2010 from short-term borrowing and the cost of short-term bond repayment in FY2010.

Revenue Net of Repayment From Short Term Borrowing FY2010 (in $ millions)		
Short Term Borrowing Proceeds	$	1,250.0
Repayment of Short Term Borrowing	$	(2,295.0)
Total	**$**	**(1,045.0)**

Source: Preliminary Official Statement, State of Illinois General Obligation Bonds, $400 million, September 9, 2009.

Under the State of Illinois Short Term Borrowing Act,[36] the State may issue short-term debt certificates for two reasons: cash flow pressures and failure of revenues. The $1.0 billion May 2009 certificates and the $1.25 billion August 2009 certificates were issued as a result of revenue failure. The State is allowed to borrow up to 15% of the total appropriations for any year if there is a failure of revenues. Before incurring this type of debt, the Governor is required to give written notice to the General Assembly and to the Secretary of State, explaining the reasons for the borrowing and the measures proposed to restore the State's fiscal soundness. The Governor

[34]The Pension Obligation Notes are authorized in 30 ILCS 330/7.2 (2009).
[35] The Civic Federation supports of the concept of transferring surplus monies from special purpose funds to General Funds.
[36] 30 ILCS 340.

filed written notice for the May 2009 and August 2009 certificates on March 27, 2009.[37] The notice stated that the following corrective actions have been taken to restore the State's fiscal soundness:

- Reducing General Funds spending by increasing contingency reserves, placing restrictions on large procurements, consolidating agencies, increasing State employee health benefit contributions, and implementing four furlough days;
- Enhancing revenues by increasing individual and corporate income tax rates, and implementing changes to the corporate income tax code; and
- Reducing General Funds pension spending through pension system reform and/or issuing Pension Obligation Bonds.

Several of these corrective actions require statutory changes to be approved by the General Assembly. The General Assembly has not passed an increase for state employee health benefit contributions, revenue enhancements or pension system reforms. While the General Assembly passed legislation authorizing the pension notes on July 15, 2009, the bonds were not issued until January 15, 2010.

Pension Borrowing

The State's statutorily required FY2010 contribution of $4.0 billion to the five State retirement systems will be made from the proceeds of $3.5 billion in pension obligation notes and Other State Funds. The new pension borrowing will free up an equal amount of General Funds for operations that would have been otherwise needed to fund the pension payment.

The following table provides a comparison between the FY2009 contribution and the FY2010 contribution. In addition to the $1.8 billion appropriated from General Funds for retirement contributions in FY2009, expenditures through a continuing appropriation were made in order to fully fund the required $2.7 billion statutory contribution.[38] If the FY2010 contribution had been made from General Funds, it would have been $1.3 billion more than the full FY2009 contribution of $2.2 billion from General Funds. The total FY2011 contribution is projected to be $4.5 billion, of which $4.1 billion is expected to come from General Funds.[39]

[37] Governor Pat Quinn. Notice of Proposed Short Term Borrowing. March 27, 2009.
[38] If appropriations by the General Assembly are below those required by Public Act 88-593, the legislation provides for continuing appropriations.
[39] State of Illinois, *Report of the Pension Modernization Task Force,* November 2009, p.51, at http://www.ilga.gov/commission/cgfa2006/Upload/112009PensionTaskForceReport.pdf (last visited on January 7, 2010). The projections reflect Public Act 96-0043, which requires that unexpected investment gains or losses be accounted for over a five-year period rather than all at once. General Funds portion of contribution is a Civic Federation calculation based on communication with Dan Hankiewicz, Pension Manager, Commission on Government Forecasting and Accountability.

State Retirement System Contributions: FY2009 and FY2010 (in $ millions)		
	FY2009	FY2010
General Funds Appropriations	$ 1,812.4	$ -
General Funds Continuing Appropriation	$ 419.8	$ -
Other Funds Appropriations	$ 490.1	$ 488.1
Other Funds Continuing Appropriation	$ 23.3	$ -
Pension Obligation Notes	$ -	$ 3,466.0
Total	**$ 2,745.5**	**$ 3,954.1**

Note: FY2009 numbers include expenditures. FY2010 numbers are appropriations.
Sources: Communication between the Civic Federation and the Governor's Office of Management and Budget, December 1, 2009; Illinois State Comptroller, Expenditures Control Panel, http://www.ioc.state.il.us (last visited on December 1, 2009); 30 ILCS 330/7.2 (2009).

In addition to the FY2010 retirement system contributions, the State will make debt service payments on the short-term pension notes that will be used to make the FY2010 contribution, as well as debt service payments on outstanding Pension Obligation Bonds. The debt service payments for the short-term pension notes will begin in FY2011 and total $802.5 million that year.[40] The Pension Obligation Bonds issued in 2003 require debt service payments of $544 million in FY2010 and $542 million in FY2011.[41]

GENERAL FUNDS 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.[42] Similarly, the General Assembly is required to pass a balanced budget.[43] In practice, there are various ways to make sure the requirement is technically met on paper without actually balancing expenditures and revenues. One technique is to adjust projected revenues to match expenditures. Another method is to relieve pressure on General Funds by passing legislation to reduce state pension contributions or by borrowing to make pension contributions. The Governor may declare a shortfall in revenues, which permits the State to issue short-term debt that does not have to be repaid until the following fiscal year. The State also may defer some unpaid bills on to the next fiscal year. Ultimately, these measures enable the State to end the year with a positive cash balance, even when expenditures and obligations outpace revenues.

As shown in the chart below, the State began FY2010 with a $3.7 billion deficit from the previous fiscal year, which was financed though deferring $3.95 billion in unpaid bills to FY2010. The deficit could increase by at least $2.0 billion to $5.7 billion at the end of FY2010.

[40] State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement*, January 7, 2010, p. 3.
[41] Illinois State Budget, FY2009, 12-11.
[42] Constitution of the State of Illinois, Article VIII, Section 2(a).
[43] Ibid, Section 2(b).

FY2010 General Funds Budget Surplus (Deficit) (in $ millions)				
	Enacted July 2009		Revised December 2009	
Revenues				
State Sources	$	19,947	$	19,081
Federal Sources	$	7,131	$	6,951
Statutory Transfers-In	$	2,221	$	2,171
Total Revenues	**$**	**29,299**	**$**	**28,203**
Expenditures				
Appropriations	$	26,085	$	26,310
Unspent Appropriations	$	(951)	$	(400)
Subtotal Expenditures	**$**	**25,133**	**$**	**25,910**
Statutory Transfers Out				
Legislatively Required Transfers to Other Funds	$	2,321	$	2,724
Pension Obligation Bond Debt Service	$	520	$	520
Subtotal Statutory Transfers Out	**$**	**2,842**	**$**	**3,244**
Total Expenditures and Transfers Out	**$**	**27,975**	**$**	**29,154**
Budget Operating Surplus (Deficit)	**$**	**1,324**	**$**	**(951)**
Short-term Borrowing Proceeds, net of Repayment	**$**	**(1,045)**	**$**	**(1,045)**
Budget Basis Surplus (Deficit) for FY2010	**$**	**279**	**$**	**(1,996)**
Carry Forward of FY2009 Year-end Deficit	**$**	**(3,673)**	**$**	**(3,673)**
Total Year-end Deficit FY2010	**$**	**(3,394)**	**$**	**(5,669)**

Source: State of Illinois, $3.466 Billion General Obligation Bonds Taxable Series of January 2010, *Official Statement,* January 7, 2010, page 22.

As enacted in July of 2009, the budget would have used a surplus of $279 million to pay down the backlog of bills. In December of 2009, this FY2010 budget surplus was revised to reflect new revenue and expenditure projections and other adjustments. FY2010 is now projected to have a $2.0 billion budget deficit, resulting in a total year-end deficit of $5.7 billion. The resulting $5.7 billion year-end deficit is equivalent to 20.1% of total General Funds revenues projected for FY2010.

The new projections include several adjustments to revenues and expenditures that worsen the State's budget position by $2.3 billion. Revenue projections dropped by $1.1 billion because of a $767 million decline in General Funds personal income tax revenues, a $50 million decline in gaming tax collections and a change in Medicaid appropriations resulting in a $180 million drop in federal revenues. In addition, the General Assembly appropriated an additional $205 million for MAP scholarships and the estimated appropriations that will not be spent during the fiscal year declined, resulting in a $777 million increase in expenditures. Debt service savings of approximately $561 million that was incorporated in the enacted budget will only be partially realized due to a delay in refinancing bonds. This delay, as well as other adjustments affecting transfers out of General Funds, will increase this year's deficit by an additional $502 million. As a result these adjustments, instead of paying down bills by the end of FY2010 by $279 million, the State is now likely to increase its backlog of bills by at least $2.0 billion, ending the year with $5.9 billion in unpaid bills in order to finance the $5.7 billion deficit.

The two-year budget deficit going into FY2011 starts with the $5.7 billion gap projected to be carried over from the current fiscal year. The State must then fill a budget hole resulting from the loss of one-time revenues, assuming that these revenues are not reinstated in FY2011. These one-time revenue sources consist of the proceeds from the sale of the five-year pension notes, reduced federal recovery funds and sweeps from Other State Funds. The deficit would also be increased by additional required expenditures, including debt service on the pension notes and an increase in the State's required pension contribution. The chart below shows that the anticipated two-year budget gap totals $12.8 billion.

Total Two-Year Budget Deficit FY2010-FY2011 (in $ millions)		
Carry-forward of FY2010 Deficit	$	5,669
Borrowing for Pension System Contribution	$	3,466
Reduction in Federal Recovery	$	1,966
Pension Bond Repayment	$	800
Increase in Statutory Pension Payment	$	593
Fund Sweeps Included in Revenue	$	352
FY2011 Total Budget Gap	**$**	**12,846**

The $12.8 billion FY2011 budget gap is primarily a result of the $5.7 billion FY2010 carry-forward as well as a statutory retirement system contribution of $4.1 billion that would be made from General Funds instead of pension obligation note proceeds. In addition to the retirement system contribution, approximately $800 million must be paid in FY2011 for the pension obligation notes issued in FY2010.

POLICY AND FISCAL RECOMMENDATIONS

In March of 2009, Governor Pat Quinn recommended several revenue enhancements, spending cuts and policy changes to balance the FY2010 operating budget. While the majority of his revenue enhancement proposals were ultimately rejected by the General Assembly, several of the proposed revenues were approved to support the Capital Projects Fund. The following chart shows the policies and fiscal proposals recommended by the Governor, the Civic Federation's reaction and any final action taken by the General Assembly in the enacted budget.

Policy and Fiscal Proposals FY2010		
Governor's Recommendation	**Civic Federation Position**	**Enacted Budget FY2010**
Increase personal income tax rate from 3% to 4.5% and **corporate income tax rate** from 4.8% to 7.2% with an increase in the personal exemption from $2,000 to $6,000. The State would use 10% of the increase to fund part of the $26 billion capital program.	The Civic Federation **opposed** the Governor's tax increase and suggested a more modest tax increase, of 3% to 4%, with no increase in the personal exemption and only if it was used to make the full pension contribution and pay down other liabilities. The Federation also suggested the potential of taxing retirement income and expanding the sales tax.	The state Senate approved HB 174 to increase the personal and corporate income tax to 5% but the House did not take up the bill. **No action** was taken by the General Assembly.
Two-Tiered Pension system that reduces benefits for new employees with long-term savings estimated to total $162 billion over 35 years and a partial pension payment holiday in FY2009 and FY2010.	The Civic Federation **supported** the proposed two-tier pension system but **opposed** taking a pension holiday in FY2009 and FY2010.	The General Assembly **rejected** the two-tiered pension proposal and the proposed pension holiday. The enacted budget makes the full pension contribution for FY2010 but funded it with the proceeds of **$3.5 billion in five-year pension notes**.
Increase employee healthcare contribution by $200 million annually to lower the State's cost.	The Civic Federation **supported** the increase in employee contributions for state workers' health care coverage.	**No action** was taken by the General Assembly.
Increase **tax on cigarettes** from 98 cents per pack to $1.48 per pack in FY2010 and to $1.98 per pack in FY2011 to generated $175.0 million annually.	The Civic Federation **supported** the increase in the cigarette tax to pay for Medicaid costs.	**No action** was taken by the General Assembly.
Expanding the full sales tax rate of 6.25% to sweetened tea and coffee drinks, grooming and hygiene products to fund State operations.	The Civic Federation **supported** this proposal and also recommended reinstating the state sales tax on food and drugs.	The General Assembly **enacted the expanded sales tax** on candy, sweetened drinks and hygiene products as part of the funding for the capital program.
Eleven business tax changes that would have provided $478.0 million in new revenue.	The Civic Federation **supported some** of the business taxes but opposed 5 of the proposed changes.	HB 174 passed by the state Senate included a sales tax on 39 services but was not taken up in the House. **No action was taken** by the General Assembly.
Ten-day sales tax holiday on certain clothing, footwear and school supplies to benefit families with schoolchildren.	The Civic Federation **opposed** the sales tax holiday which would have cost the state $57.0 million.	**No action was taken** by the General Assembly.

The Civic Federation also recommended the following policies, which were not included in the Governor's recommended budget or the enacted budget for FY2010:

- **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.[44] 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.

- **Improve the State's Existing Performance Measurement System**
  The FY2010 Illinois State 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, such as 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 even have such targets. Given the administration's continued focus on improving management efficiency, the Civic Federation urges the State 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. The Emergency Budget Implementation Act of Fiscal Year 2010, passed on July 15, 2009, included the possibility that departments "may" institute many of these rigorous performance management initiatives but were not required to do so.[45]

CAPITAL BUDGET

On July 13, 2009, prior to enacting the State's FY2010 operating budget, Governor Pat Quinn signed into law a $31 billion statewide capital spending program. The capital budget approved by the General Assembly increased by $5 billion, or 19.2%, from the $26 billion *Illinois Jobs Now!* capital budget proposed by Governor Quinn as part of his state budget recommendation on March 18, 2009. The last capital bill approved by the State was the *Illinois FIRST* program in FY1999 under Governor George Ryan.

The Civic Federation opposed the *Illinois Jobs Now!* capital program proposed by the Governor because it was not based on a comprehensive capital improvement plan (CIP) that would effectively manage the State's investment in critical infrastructure through a transparent and needs-based planning process. The proposal also included approximately $12 billion in new debt-funded capital projects, but the proposed revenue to fund the new borrowing did not adequately cover the increase in debt service cost over time.[46] 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 was included with the budget or made public. [47]

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[44] See National Advisory Council on State and Local Budgeting and Government Finance Officers Association.
[45] Public Act 096-0045, Public Accountability and Performance System Act, sec. 3-1 through 3-20.
[46] Institute for Illinois' Fiscal Sustainability at the Civic Federation, "State of Illinois FY2010 Recommended Operating and Capital Budgets," May 11, 2009.
[47] State of Illinois Capital Budget FY2010, pg. 3.

Capital Appropriations

Prior to the end of FY2009, the Governor and General Assembly approved $3 billion in new State funded capital spending and appropriated $1.5 billion in federal stimulus grants for shovel-ready infrastructure investments funded by the ARRA.[48] Of the total $4.5 billion in capital spending approved on April 18, 2009, $1.6 billion was reappropriated in the full FY2010 capital bill approved in July. The total capital appropriations enacted in FY2010 totaled $28.6 billion. The following table shows the new and reappropriated funding included in the FY2010 enacted capital budget.

[48] Public Act 096-0005

State of Illinois Enacted Capital Budget FY2010 (in $ millions)				
Department	**New**	**Reapprop.**	**Total**	**%**
Transportation	$ 8,711.4	$ 9,283.3	$ 17,994.8	63.0%
Commerce and Economic Opportunity	$ 1,600.6	$ 633.6	$ 2,234.2	7.8%
Capital Development Board	$ 1,724.8	$ 393.6	$ 2,118.4	7.4%
Environmental Protection Agency	$ 757.1	$ 1,199.5	$ 1,956.6	6.8%
Higher Education	$ 1,045.9	$ -	$ 1,045.9	3.7%
Natural Resources	$ 467.0	$ 371.3	$ 838.3	2.9%
Community College Board	$ 399.7	$ 115.2	$ 514.9	1.8%
Secretary of State	$ 306.8	$ 11.1	$ 317.9	1.1%
Corrections	$ 20.8	$ 280.4	$ 301.2	1.1%
State Board of Education	$ 185.0	$ -	$ 185.0	0.6%
Public Health	$ 155.0	$ -	$ 155.0	0.5%
Revenue	$ 132.9	$ 8.4	$ 141.3	0.5%
Architect of the Capitol	$ 99.8	$ 3.3	$ 103.1	0.4%
University of Illinois	$ -	$ 99.6	$ 99.6	0.3%
Veteran's Affairs	$ 72.9	$ 6.9	$ 79.7	0.3%
Human Services	$ 27.4	$ 50.0	$ 77.4	0.3%
Central Management Services	$ 51.1	$ 24.0	$ 75.1	0.3%
Military Affairs	$ 44.8	$ 10.1	$ 54.9	0.2%
State Police	$ 43.3	$ 3.6	$ 46.9	0.2%
Chicago State	$ -	$ 28.0	$ 28.0	0.1%
Emergency Management	$ 25.0	$ 0.3	$ 25.3	0.1%
Finance Authority	$ 10.0	$ 14.6	$ 24.6	0.1%
Southern Illinois University	$ 17.6	$ 3.3	$ 20.9	0.1%
Courts	$ 14.4	$ 1.8	$ 16.2	0.1%
Governors State University	$ -	$ 14.8	$ 14.8	0.1%
Agriculture	$ 12.7	$ 0.7	$ 13.4	0.05%
Juvenile Justice	$ 13.2	$ -	$ 13.2	0.05%
Illinois State University	$ -	$ 13.1	$ 13.1	0.05%
Western Illinois University	$ -	$ 12.7	$ 12.7	0.04%
Historic Preservation	$ 0.3	$ 11.8	$ 12.0	0.04%
Northeastern Illinois University	$ -	$ 11.5	$ 11.5	0.04%
Northern Illinois University	$ -	$ 10.1	$ 10.1	0.04%
Eastern Illinois University	$ 1.7	$ 7.3	$ 9.0	0.03%
Attorney General	$ 1.5	$ 0.1	$ 1.6	0.01%
Medical District Commission	$ -	$ 0.9	$ 0.9	0.003%
University Center of Lake County	$ -	$ 0.7	$ 0.7	0.002%
Commerce Commission	$ -	$ 0.6	$ 0.6	0.002%
Math and Science Academy	$ -	$ 0.1	$ 0.1	0.0004%
Total	**$ 15,942.6**	**$ 12,626.3**	**$ 28,568.9**	**100.0%**

Source: Commission on Government Forecasting and Accountability, State of Illinois Budget Summary FY2010, p. A1-B24.

The Governor's office provided a list of projects to be funded and departments to receive discretionary funding from the capital bill. However, documentation showing how projects were prioritized and the criteria for deciding which projects receive funding were not included in the capital budget.

Transportation was the largest spending area totaling $18.0 billion or 63.0% of the total capital appropriations. However, the Transportation allocation included the federally funded multi-year road program for the next five years and the ongoing State road program for highways and bridges funded through the Road Fund. Together these programs total an estimated $14.1 billion over the next five years, according to the Governor's proposed capital budget.[49] In all, the Transportation budget included $2.5 billion for mass transit, or 8.6% of the total FY2010 appropriation, not including aviation projects statewide. The largest provider of mass transit in the state, the Chicago Transit Authority, has identified a capital need of more than $6 billion to bring its system up to a state of good repair but will only receive $900 million over the next five years.

Many of the secondary education institutions, which appear only to receive reappropriated funding for ongoing projects, will receive new funding from the $514.9 million allocated to the Community Colleges Board and the $1.0 billion to the Board of Higher Education.

Capital Revenue

The Governor proposed a capital budget funded by increased license and vehicle fees and 10% of the proposed state income tax increase that was included to fund the proposed operating budget. However, this revenue source appeared insufficient to pay for the debt service on the $12 billion in new borrowing and the increase in debt service associated with a plan to refinance all outstanding capital debt.[50] The General Assembly rejected the income tax proposal but did include the vehicle fees as part of the funding bill for the enacted capital budget.

The $15.9 billion in new state-funded capital spending in the enacted budget will be almost entirely debt funded. The capital budget also includes an estimated $1.19 billion in new revenues to pay for the annual debt service costs. The following chart describes the new revenues passed.

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[49] State of Illinois Capital Budget FY2010, p. 9.
[50] For more details on the Civic Federation/IIFS analysis of the FY2010 proposed Capital Budget see: Institute for Illinois' Fiscal Sustainability at the Civic Federation, "State of Illinois FY2010 Recommended Operating and Capital Budgets," May 11, 2009, p. 79.

New Revenue Sources Passed To Fund FY2010 Capital Budget	
Source	**Description**
Video Gaming	Impose a 30% tax on the operation of between 45,000 and 60,000 video gaming machines statewide. Net daily operating income per machine estimated between $70 and $90 would reap a total of $3.15 million to $5.85 million in new total gaming reciepts per day.
Lottery	Lease the lottery operations to a third party that will offer online lottery and market new lottery games to increase the state's per capita lottery revenue from $161.08 per year to the national average of $236.21 per capita per year.
Sales Tax	Eliminate the state sales tax exemptions for candy, soft drinks, grooming and hygiene products.
Liquor Tax	Increase tax on beer from $.185 per gallon to $.231 per gallon; on wine from $.73 per gallon to $1.39 per gallon; on distilled liquor from $4.50 per gallon to $8.55 per gallon.
Vehicle Fees	Increase registration for motor vehicles by $20; title fee $30; registration transfer fee $10; driver's license $20.

Source: Commission on Government Forecasting and Accountability, "Revenue Bill Analysis, HB255" May 20, 2009.

The following table shows the projections of total annual revenue from these new sources.

Enacted Capital Budget Annual Revenues (in $ millions)	
Source	**COGFA (est.)**
Video Gaming	$287 to $534
Beer & Liquor Tax	$108
Vehicle Fees	$332
Sales Taxes	$65
Online Lottery & Operations Lease	$150
Total	**$942 to $1189**

Source: Commission on Government Forecasting and Accountability, "Revenue Bill Analysis, HB255" May 20, 2009.

However, the estimated revenue capacity of the Video Gaming portion may end up lower than originally projected. Numerous cities and counties statewide have begun taking advantage of a provision in the revenue bill that allows local governments to opt out of legalized Video Gaming within their jurisdiction. The Illinois Gaming Board has also advised the General Assembly and Governor's office that the licensing and regulation will take at least a year to roll out, preventing the state from collecting any revenue from the new gambling taxes until at least FY2011.[51]

The increase in vehicle fees begins on January 1, 2010. The increase in the beer and liquor tax went into effect September 1, 2009 but has been challenged in court. The State has not provided a timeline for receiving the revenues from the potential lease of the State's lottery operations. The expanded sales tax on some candy, sweetened beverages and hygiene products took effect September 1, 2009.

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[51] Testimony of Mark Ostrowski, Illinois Gaming Board Administrator, Commission on Government Forecasting and Accountability, Hearing on Video Poker, December 1, 2009.

Despite the delay in much of the capital revenue needed to fund the new borrowing, the State has begun selling bonds to support the capital spending, issuing the first $400 million of debt on September 23, 2009 out of a new bonding authority totaling $5.8 billion approved for the capital program. In all, the State will need to sell $12 billion to $14 billion to fund all of the capital spending approved in the enacted capital budget. According to the official statement[52] accompanying the bonds, the proceeds will be used for the following areas:

- $25.5 million general capital projects;
- $337 million roads and bridges,
- $15 million mass transit;
- $ 2.5 million antipollution projects and
- $20 million coal and energy development.

[52] Preliminary Official Statement, State of Illinois General Obligation Bonds, $400 million, September 9, 2009, p. 1.