The Institute for Illinois' Fiscal Sustainability

AT THE CIVIC FEDERATION

State of Illinois Enacted FY2014 Budget:

A Review of the Operating and Capital Budgets 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 State of Illinois' operating and capital budgets as enacted for fiscal year 2014, which began on July 1, 2013 and ends on June 30, 2014. Fiscal year 2014 is the last full year before the State faces dramatic reductions in revenues due to the scheduled partial rollback of income tax rate increases in January 2015. While still precarious, the State's financial condition in FY2014 may end up as a high-water mark, based on the near-term outlook under current law.

Unfortunately, the FY2014 budget process also represented a lost opportunity, as it did not result in a plan that addressed the State's major financial problems. The Governor and General Assembly did not deal with unsustainable pension costs and unpaid bills prior to the looming revenue shortfall. Although the budget is roughly balanced on an operating basis, the State remains burdened with an accumulated backlog of bills projected to total $5.8 billion at the end of FY2014.

The FY2014 budget does not show the fiscal discipline required by the State's perilous financial condition. Rather than reining in spending and using any surplus to further reduce the backlog of bills, the budget includes expenditures for current-year services that exceed the amount recommended by Governor Pat Quinn by more than $350 million.

Despite these shortcomings, the FY2014 budget benefits from a decision to set aside revenues in FY2013 and FY2014 to pay down outstanding bills. These efforts were aided by unexpectedly high income tax collections in FY2013, a one-time event related to taxpayer avoidance of higher federal tax rates. While past budgets have masked costs by deferring them to future years, officials maintain that the FY2014 budget presents an accurate picture of annual costs—with the notable exception of pension costs.

The General Assembly's failure to approve comprehensive pension changes during its spring 2013 session triggered further reductions in the State's bond ratings. With the State's unfunded pension liability of $96.8 billion and funded ratio of 39.0% at the end of FY2012, Illinois is currently the lowest rated state by all three major credit ratings firms—only one downgrade away from falling out of the "A" category. Although it is rare for any state to be rated "BBB" or lower, the ratings agencies have indicated that further downgrades are likely without pension changes.

The main findings of the analysis are the following:

- The backlog of unpaid bills and other General Funds liabilities is projected to total approximately $5.8 billion at the end of FY2014. That is down from $8.8 billion at year-end FY2012 and $6.3 billion at year-end FY2013 but still represents more than 16% of total General Funds revenues;
- The decline in unpaid bills is due to the State's decision to allocate funds to reduce the backlog and to an unexpected nationwide surge in income tax revenues in April 2013. Illinois collected $19.7 billion in income taxes in FY2013, $2.1 billion more than initially projected;
- Income tax revenues in FY2013 were $9.8 billion higher than in FY2010, the last full budget year before income tax rates were increased. In FY2014, the last full year prior to the partial roll back of the higher income tax rates in January 2015, income tax revenues are expected to total $9.1 billion more than in FY2010;
- General Funds expenditures are expected to increase by $2.5 billion from $33.3 billion in FY2010 to an estimated $35.7 billion in FY2014, largely due to rising pension costs;

- In FY2014 General Funds pension costs total $7.65 billion, including contributions of $5.99 billion and payments on pension bonds of $1.66 billion. Pension costs consume 24.3% of State-source General Funds revenues in FY2014;
- General Funds expenditures of $35.7 billion in FY2014 represent an increase of $155 million from FY2013 expenditures and $92 million from the level recommended in the Governor's budget proposal. Excluding funds set aside for the payment of outstanding bills, expenditures increase by $354 million from the Governor's proposal.
  - The $354 million includes an increase of $212 million in General Funds agency appropriations for current services (excluding payment of prior year bills). In addition to more funding for education, the enacted budget includes increases for the Secretary of State and Department of Commerce and Economic Opportunity;
- The FY2014 budget is assumed to fully fund State costs (excluding pension costs), with no growth in bills due to inadequate appropriations;
  - The Medicaid program faces significant uncertainties relating to the federal Affordable Care Act expansion and to implementation of a restructuring plan enacted in FY2013. However, the ability to push Medicaid bills into the future has been curtailed, meaning that higher than expected costs must be offset by either increased revenues or reduced spending;
  - General Funds costs for group insurance are projected to decline by $104 million in FY2014 to $1.3 billion. The savings depend on the realization of projected savings from a new union contract. If the savings are achieved, group health insurance bills would remain unchanged from FY2013 at $1.5 billion;
- Wage increases of approximately $140 million in FY2014 were agreed to by the Governor's Office as part of a new contract with the American Federation of State, County and Municipal Employees (AFSCME).
- Net agency appropriations spent decline by $993 million from $24.3 billion in FY2010 to an estimated $23.3 billion in FY2014. However, legislatively required transfers out of General Funds increase by $871 million to $2.9 billion in FY2014 from $2.0 billion in FY2010;
- State debt has increased by $9.2 billion to $31.0 billion in outstanding principal in FY2014, compared with $21.8 billion in FY2010. It will cost the State $47.7 billion in total debt service to repay all outstanding bonds through FY2039; and
- Revenue sources enacted to support the capital budget total only $627.3 million in FY2013, compared with a legislative projection of between $934 million and $1.2 billion, due to delays in the statewide implementation of video gaming.

BUDGET TIMELINE

The State of Illinois' budget for fiscal year 2014 was developed amid growing concern about the State's apparent inability to fix its severe pension problems. Illinois' bond ratings were downgraded both at the beginning of the spring legislative session in January 2013 and after the session ended in May, with ratings firms citing the General Assembly's inaction on the State's dramatically underfunded pension obligations.

In response to the latest downgrades, Governor Pat Quinn called the General Assembly back to Springfield for a special session in June. When it appeared that the special session would not produce results, the Governor proposed the creation of a conference committee to deal with the pension problems. Although the conference committee continues to work on a pension plan, the Governor vetoed lawmakers' pay for FY2014 when the panel failed to meet a July 19 deadline. The veto was overturned in September by a Cook County judge.

The pension crisis largely overshadowed other budget-related activity, including a significant reduction in the State's backlog of outstanding bills. Additional State revenues became available to pay down bills in FY2013 after an unexpected surge in income tax collections in April 2013. As a result, funds originally designated by Governor Quinn to pay down bills in the FY2014 budget were used instead to avert cuts to education funding.

During the last days of the spring session, the General Assembly agreed to a major expansion of Illinois' Medicaid program under the federal Affordable Care Act. The expansion legislation was supported by Governor Quinn and passed by the Senate in February 2013. The measure was not approved by the House until late May, after it was amended to aid nursing homes for the mentally ill and hospitals.

Governor's FY2014 Budget Recommendation—March 6, 2013

On March 6, 2013, Governor Quinn presented his recommended operating budget for FY2014, which began on July 1, 2013 and ends on June 30, 2014.[1] The $62.4 billion proposed budget included General Funds spending of $35.6 billion, up from $34.4 billion in the FY2013 enacted budget.[2] The increase was largely caused by a jump of nearly $1 billion in statutorily required pension contributions.

The Governor's budget address, like his budget speech the year before, emphasized the urgency of reducing State pension costs.[3] Nevertheless, the legislature had completed its spring 2012 session, a special session called by the Governor in August 2012, a fall veto session and the closing session of

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[1] Illinois State FY2014 Budget, March 6, 2013, http://www2.illinois.gov/gov/budget/Documents/Budget%20Book/FY%202014/FY2014IllinoisOperatingBudgetBook.pdf (last visited on August 2, 2013). For more information, see the Institute for Illinois' Fiscal Sustainability at the Civic Federation, *State of Illinois FY2014 Recommended Operating and Capital Budgets: Analysis and Recommendations*, May 13, 2013, http://www.civicfed.org/iifs/publications/fy2014recommended.

[2] General Funds are accounts that support the regular operating and administrative expenses of most State agencies and over which the State has the most discretion and control. The operating budget also includes Other State Funds, accounts for activities funded by specific revenue sources that may only be used for specific purposes, and Federal Funds, which use federal revenues (other than those designated for General Funds) to support a variety of state programs.

[3] Illinois Government News Network, "Governor Quinn Delivers Fiscal Year 2014 Budget Address," *news release*, March 6, 2013, http://www3.illinois.gov/PressReleases/ShowPressRelease.cfm?SubjectID=2&RecNum=10980 (last visited on August 5, 2013).

the 97th General Assembly in January 2013 without approving major pension changes. The inaction led Standard & Poor's to reduce the State's bond ratings on January 25, 2013.[4] Illinois subsequently delayed a bond sale scheduled for January 30, citing indications that investors would demand higher interest rates as a result of the downgrade.[5]

By March 2013, several major pension proposals were pending in the 98th General Assembly, including bills sponsored by Senate President John Cullerton and Representative Tom Cross, Minority Leader in the House of Representatives.[6] In his budget speech, Governor Quinn pledged to sign any comprehensive pension legislation that reached his desk.

The Governor's FY2014 recommended budget made the State's statutorily required pension contributions from General Funds without borrowing.[7] The State issued a total of $7.2 billion in bonds to pay the pension contributions in FY2010 and FY2011 but used General Funds to make the pension payments in FY2012 and FY2013.[8] General Funds pension-related costs in FY2014, including State contributions and debt service on pension bonds, were estimated at $7.7 billion, or 24.5% of State-source General Funds revenues.

The FY2014 General Funds budget proposal included a $246 million increase in State group insurance appropriations from FY2013. Due to delays in labor negotiations, budgeted savings on group insurance were not achieved in FY2013.

Agency appropriations, excluding pension contributions and group insurance payments, increased by $439 million from FY2013. Reductions in education funding were offset by increases for healthcare and human services. Approximately $312 million of the proposed increase for the Department of Human Services and Department on Aging were used to pay outstanding bills.[9] Agency appropriations in FY2013 included $264 million to the Office of the Comptroller to pay down bills not related to Medicaid.[10] The General Funds budget for FY2013 also included a transfer out of $500 million to pay $1 billion of Medicaid bills through a cycle of State spending and federal reimbursements.[11]

The Governor proposed an increase of 914 full-time equivalent positions (FTEs), or 1.7%, at the agencies under his control to 53,172 FTEs at the end of FY2014 from an estimated 52,258 at the end of FY2013. A new three-year contract with the State's largest union, Council 31 of the American Federation of State, County and Municipal Employees (AFSCME), called for a 2% cost of living adjustment on July 1, 2013 and other changes expected to cost $140 million in FY2014.[12]

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[4] Standard & Poor's Ratings Services, "Illinois General Obligation Debt Rating Lowered to 'A-' from 'A'," *news release*, January 25, 2013.

[5] Monique Garcia, "Quinn delays $500 million borrowing in wake of state's bad credit rating; Planned sale of construction bonds halted because of fears of higher interest rates," *Chicago Tribune*, January 30, 2013. The State returned to market with an $800 million bond sale in April 2013.

[6] 98th Illinois General Assembly, Senate Bill 1 (filed on January 9, 2013 by Senator John Cullerton) and House Bill 3411 (filed on February 26, 2013 by Representative Tom Cross).

[7] Approximately 89% of the State's annual pension contributions are from General Funds.

[8] Illinois also issued $10.0 billion in pension bonds in FY2003, which were used to pay down $7.3 billion of unfunded liability and pay for part of the FY2003 pension contributions and all of the FY2004 contributions.

[9] State of Illinois, General Obligation bonds, Series A of April 2013 and Taxable Series B of April 2013, *Official Statement*, April 2, 2013, p. 29.

[10] Under Public Acts 97-0685 and 97-0732, the funds were deposited into a newly created FY13 Backlog Payment Fund and then transferred back into General Funds. Pursuant to Public Act 98-0017, the deposit in FY2014 was $50 million.

[11] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 29.

[12] Illinois Department of Central Management Services, Submission to General Assembly's Commission on Government Forecasting and Accountability, April 16, 2013.

The Governor's budget proposal did not include funding for back wages owed to union members under a contract that ended in June 2012, but the administration pledged to seek a supplemental appropriation to pay the back wages.[13] Governor Quinn had cancelled the wage increases, citing inadequate appropriations by the General Assembly. AFSCME went to court, and a Cook County Circuit Court judge ruled that the State was obligated to pay the raises when it was able to do so. The Governor's Office had agreed to drop an appeal of the ruling as part of the AFSCME negotiations, but the Illinois Attorney General's Office is continuing to pursue the appeal.[14]

The following table summarizes the Governor's recommended FY2014 budget and compares it with the revised FY2013 budget as of March 2013. In the Governor's proposal for FY2014, operating revenues exceeded operating expenditures by $7 million. That amount was used to make a small dent in the accumulated deficit from prior years, resulting in a slight reduction in the total deficit.

State of Illinois General Funds Budget Plan: FY2013-FY2014 as of March 6, 2013 (in $ millions)

	FY2013 Revised*	FY2014 Rec.	$ Change	% Change
Operating Revenues	$ 34,924	$ 35,628	$ 704	2.0%
Operating Expenditures	$ 34,429	$ 35,621	$ 1,192	3.5%
Operating Surplus (Deficit)	$ 495	$ 7	$ (488)	-98.6%
Accumulated Surplus (Deficit)	$ (4,986)	$ (4,491)	$ 495	-9.9%
Total Surplus (Deficit)	**$ (4,491)**	**$ (4,484)**	**$ 7**	**-0.2%**

*As of March 2013.

Source: Illinois State FY2014 Budget, p. 2-16.

The State has dealt with its General Funds deficits by delaying payments owed to vendors, social service agencies, pension funds, school districts and other units of government and making those payments from the next year's revenues. The payments must be made by December 31—six months after the end of the fiscal year.[15]

Certain General Funds liabilities have piled up outside of the budget. These costs, generally relating to Medicaid and group health insurance, may be incurred in a given fiscal year but paid from future appropriations.[16] The proposed FY2014 budget would have reduced the backlog of these Medicaid-related bills by $825 million.[17]

[13] John O'Connor, "Quinn wants attorney general to drop back-pay lawsuit," *State Journal-Register*, April 26, 2013.
[14] Communication between the Civic Federation and the Illinois Attorney General's Office, September 27, 2013.
[15] 30 ILCS 105/25(m).
[16] 30 ILCS 105/25(b-1) – (l).
[17] Legislation enacted in 2012 significantly curtailed the State's ability to defer Medicaid bills relating to the Illinois Department of Healthcare and Family Services beginning at the end of FY2013.

The next table shows General Funds accounts payable and other liabilities for FY2013 and FY2014, as projected in the FY2014 budget. As discussed above, $764 million in General Funds revenues were allocated to pay down bills in FY2013: $264 million for non-Medicaid bills and $500 million for Medicaid bills, which provided $1 billion in total resources after federal reimbursements.

State of Illinois Unpaid Bill Backlog on June 30: 2013-2014 (in $ millions)				
	2013 Est.*	2014 Rec.	$ Change	% Change
General Funds Accounts Payable	**$ (4,724)**	**$ (4,724)**	$ -	0.0%
Other General Funds Liabilities				
Medicaid-Related	$ (966)	$ (141)	$ 825	-85.4%
Group Health Insurance	$ (1,894)	$ (1,894)	$ -	0.0%
Income Tax Refunds	$ -	$ -	$ -	na
Total Other General Funds Liabilities	**$ (2,860)**	**$ (2,035)**	$ 825	-28.8%
Total	**$ (7,584)**	**$ (6,759)**	**$ 825**	**-10.9%**

*As of March 2013.

Source: Civic Federation calculations based on: Illinois State FY2014 Budget, pp. 2-16 to 2-17; Communication between Civic Federation and Governor's Office of Management and Budget, April 12, 2013.

General Assembly Budget Process—March 2013 through May 2013

On March 5, 2013, a day before the Governor's budget address, the House adopted its own estimate of General Funds revenues.[18] The House's estimate of $35.081 million was $549 million below the Governor's revenue projection of $35.630 million.

The General Funds revenue projection has recently played a key role in the legislature's budget process. Since 2011 the General Assembly has begun its work on the budget by adopting a revenue projection that establishes a spending limit for the next fiscal year.

This was the first year that a legislative revenue estimate was approved prior to the release of the Governor's budget. During the discussion of House Resolution 83 on the House floor, it was noted that the Governor's revenue number was expected to be above the House projection and that approval of the measure would put the House at odds with the Governor's spending plan.

The General Funds revenue projection approved by the House matched the revenue analysis presented to the General Assembly by the staff of the legislature's Commission on Government Forecasting and Accountability (COGFA) and published on February 5, 2013.[19] The Governor's estimate was based on a projection by the Illinois Department of Revenue in consultation with the Governor's Council of Economic Advisors.

The difference in revenue estimates related mainly to policy issues rather than economic assumptions.[20] For example, the Governor's budget proposed a reduction in the amount of income tax

[18] 98th Illinois General Assembly, House Resolution 83, adopted March 5, 2013. See Appendix A for a listing of major budget-related resolutions and legislation for FY2014.
[19] Commission on Government Forecasting and Accountability, *House Revenue Committee, Economic Outlook*, February 5, 2013, p. 24.
[20] Commission on Government Forecasting and Accountability, *FY2014 Economic Forecast and Revenue Estimate and FY2013 Revenue Update*, March 12, 2013, p. 26.

revenues diverted from General Funds to the Income Tax Refund Fund to pay refunds owed to individuals and businesses. This reduction required legislative action. In addition, the Governor assumed that a surplus of $155 million in the Income Tax Refund Fund would be transferred to General Funds. Illinois law requires that any surplus in the Income Tax Refund Fund at the end of a fiscal year be transferred into General Funds in the next fiscal year.[21]

On May 31, 2013, the last day of the spring session, the House increased its FY2014 General Funds revenue estimate by $365 million to $35.446 billion.[22] The increase took into account a projected surplus of $300 million in the Income Tax Refund Fund. The change also reflected a reduction in the amount of income tax revenues diverted to the fund, although the diversion rate remained higher than the Governor's proposal.[23] The revised revenue estimate was still below the Governor's projection of $35.630 million, largely due to differing estimates of federally reimbursable Medicaid expenditures by the end of FY2014.

Changes in revenue projections for FY2013 also had a significant impact on the FY2014 budget. When the FY2013 budget was enacted in June 2012, State income tax revenues for FY2013 were projected to total $17.6 billion.[24] Due to a surge in income tax collections in April 2013, however, actual FY2013 income tax revenues were $2.1 billion higher than expected at $19.7 billion.[25] The influx of revenues, known as the "April Surprise," occurred because wealthy taxpayers shifted income into 2012 to avoid higher federal tax rates.[26]

The additional revenues in FY2013 were used to pay down outstanding bills and supplement inadequate annual appropriations for healthcare, human services and State group health insurance. This freed up funds designated for paying down bills in the Governor's proposed FY2014 budget. The General Assembly used the money to avert cuts to education funding in its FY2014 budget, passed on May 31, 2013, the last day of the regular spring session. The additional tax revenues in FY2013 were also applied to $130 million in transfers out of General Funds to be used for FY2014 appropriations.[27]

In the legislature's budget, operational appropriations for many large agencies were lower than the amounts recommended by the Governor and were passed as lump sums.[28] Lump sum appropriations do not identify specific funding purposes, such as employee salaries, by line item. Because the new union contract negotiated by the Governor included wage increases in FY2014, agencies were expected to stay within their budgets by reducing headcount, possibly through attrition.[29] The General Assembly did not pass a bill providing supplemental appropriations to cover back wages for union employees.[30]

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[21] 35 ILCS 5/901(d)(4.5).
[22] 98th Illinois General Assembly, House Resolution 389, adopted May 31, 2013.
[23] In FY2013 diversion rates were 9.75% for individual income taxes and 14.0% for business income taxes. The Governor proposed FY2014 rates of 9.0% and 12.0%, but the General Assembly approved rates of 9.5% and 13.4%.
[24] House Joint Resolution 68, adopted by the House on March 1, 2013 and by the Senate on March 7, 2013. The income tax revenues are net General Funds receipts, after deducting deposits to the Income Tax Refund Fund.
[25] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 1, 2013, p. 50.
[26] Commission on Government Forecasting and Accountability, "Revenue: April Surprise—Revenues Skyrocket But Are They One-Time?" *Monthly Briefing for the Month Ended: April 2013*, p. 1.
[27] 98th Illinois General Assembly, House Bill 206 (Public Act 98-0017, signed on June 5, 2013).
[28] Operational spending covers the cost of running State government on a day-to-day basis and includes payments for salaries, office supplies and equipment and travel expenses.
[29] Council 31 AFSCME, "Where things stand in Springfield," July 19, 2013, http://www.afscme31.org/news/where-things-stand-in-springfield (last visited on August 13, 2013).
[30] 98th Illinois General Assembly, House Bill 212, House Amendment 2, filed on May 2, 2013.

General Funds pension contributions in the General Assembly's budget were reduced by $48 million from the Governor's proposal. Instead of using $150 million in resources provided by the Unclaimed Property Trust Fund to make the statutorily funded payment to the State Universities Retirement System, the legislature's budget used $198 million.[31] In addition, the budget passed by the General Assembly did not include $27.8 million of the $90.4 million statutorily required contribution to the Teachers' Retirement Insurance Program (TRIP).[32] The total amount will be covered by continuing appropriation.

A law allowing the State to expand its Medicaid program under the federal Affordable Care Act to cover low-income adults was strongly supported by Governor Quinn's administration and was passed by the Senate in February.[33] The federal government is scheduled to pay 100% of the cost for the newly eligible population for the first three years of the program; 95% in 2017; 94% in 2018; 93% in 2019; and 90% thereafter. The measure did not win approval from the House until May 27, after it was amended to authorize a new role for nursing homes for the mentally ill and a new kind of hospital-based managed care network.

The General Assembly also approved several bills designed to increase publicly available information about the State's finances. One of the measures requires that the enacted budget be posted in downloadable format on GOMB's website within 60 days after the budget is signed by the Governor.[34] Previously only the Governor's recommended budget was published. Other legislation requires the Governor's annual budget proposal to include additional information about budget deficits and General Funds liabilities[35]and mandates that the amount of bills on hand at State agencies at the end of the fiscal year be reported to the Comptroller's Office and posted on the Comptroller's website.[36]

The State's Budgeting for Results Commission was charged with developing a plan by January 1, 2015 to make the budgeting process "the most transparent, publicly accessible budgeting process in the nation."[37] The Commission oversees an initiative that seeks to make better use of State resources by allocating funds according to program results rather than based on the prior year's appropriations.[38]

The General Assembly created a new panel called the Illinois Single Audit Commission to help improve the administration of State grants.[39] In the past two years, federal prosecutors have filed criminal charges against 13 people in connection with fraud schemes involving State grants and contracts.[40] The new Commission is required to submit a report to the General Assembly by January 1, 2014, recommending uniform standards for grant administration.

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[31] 98th Illinois General Assembly, House Bill 206 (Public Act 98-0017, signed on June 5, 2013).
[32] The General Assembly appropriated $62.6 million for TRIP, which provides health insurance for retired public school teachers outside of Chicago. Under State law, the remainder of the required amount will be paid under continuing appropriation, statutory authority that allows the Comptroller and Treasurer to spend funds if the legislature appropriates an insufficient amount for a specified purpose.
[33] 98th Illinois General Assembly, Senate Bill 26 (Public Act 98-0104, signed on July 22, 2013).
[34] 98th Illinois General Assembly, House Bill 2955 (Public Act 98-0461, signed on August 16, 2013).
[35] 98th Illinois General Assembly, House Bill 2947 (Public Act 98-0460, signed on August 16, 2013).
[36] 98th Illinois General Assembly, House Bill 1682 (Public Act 98-0228, signed on August 9, 2013).
[37] 98th Illinois General Assembly, Senate Bill 2106 (Public Act 98-0580, signed on August 27, 2013).
[38] Public Act 96-1529, enacted on February 16, 2011.
[39] 98th Illinois General Assembly, House Bill 2 (Public Act 98-0047, signed on July 1, 2013).
[40] Chris Fusco, "Watchdogs: Tally in Illinois grant-fraud probe so far: 13 charged, $16 million embezzled," *Chicago Sun-Times*, September 9, 2013.

The legislature approved an estimated $22.2 billion capital budget for FY2014. The capital spending bill included $18.8 billion in reappropriations of previously approved projects from the *IllinoisJobsNow!* program and $3.4 billion in new appropriations.[41]

Despite the introduction of several major pension bills and numerous legislative hearings, the spring session ended on May 31 without passage of comprehensive pension changes. A bill sponsored by Speaker of the House Michael Madigan and supported by Minority Leader Cross was passed by the House but rejected by the Senate.[42] A union-backed bill sponsored by Senate President Cullerton was passed by the Senate but not called for a vote in the House.[43]

Enacted Budget and Subsequent Developments—June 2013 to the Present

After the end of the regular legislative session, two ratings firms lowered the State's bond ratings, citing inaction on pension costs.[44] In response to the downgrades, Governor Quinn called the General Assembly back to Springfield for a special session on June 19 to deal with pensions.[45] When it appeared that the two chambers would not take action on pensions on June 19, the Governor proposed the creation of a conference committee and set a deadline of July 9 for committee action.[46]

The 10-member bipartisan committee held three public meetings and heard testimony from a variety of interested parties. Panel members said they would not meet the July 9 deadline set by the Governor because they were waiting to receive actuarial reviews that would show projected savings from various pension proposals.

At a press conference on July 10, Governor Quinn announced that he had vetoed lawmakers' pay totaling $13.9 million for FY2014 due to the General Assembly's failure to pass pension reform.[47] The line-item veto applied to the only appropriation bill for FY2014 not yet signed into law.[48] The Governor also said that he would not accept a paycheck himself until significant pension changes were approved. The Governor's salary is $177,500 a year; lawmakers receive base salaries of $67,836 and additional stipends for leadership positions.

On July 25, Illinois Comptroller Judy Baar Topinka said that her office would not issue paychecks to General Assembly members without an appropriation.[49] The Comptroller said the matter could be resolved in court or by a vote of the legislature to override the Governor's veto. Overriding a line-item veto requires a three-fifths vote of each chamber.[50]

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41 98th Illinois General Assembly, House Bill 215 (Public Act 98-0050, signed on July 2, 2013).
42 98th Illinois General Assembly, Senate Bill 1, House Amendments 1 and 3, passed by the House on May 30, 2013 and failed in the Senate on May 30, 2013.
43 98th Illinois General Assembly, Senate Bill 2404, Senate Amendments 2, 4 and 5, passed by the Senate on May 9, 2013.
44 Reuters, "Another ratings agency downgrades Illinois credit; Moody's cuts Illinois general obligation rating on pension issues," *Chicago Tribune*, June 6, 2013.
45 Illinois Government News Network, "Governor Quinn Statement on Moody's Downgrade: Legislators to Return to Springfield on June 19th," *news release*, June 6, 2013.
46 Illinois Government News Network, "Gov. Pat Quinn Sets July 19 for General Assembly to Act on Comprehensive Pension Reform; Conference Committee Convened," *news release*, June 19, 2013.
47 Illinois Government News Network, "Governor Quinn Suspends Pay to Illinois Representatives and Senators; General Assembly Fails Yet Again to Pass Comprehensive Pension Reform, Governor Vetoes Out Legislative Salaries and Stipends," *news release*, July 10, 2013.
48 Public Act 98-0064, signed on July 10, 2013 with a line-item veto. The Governor also issued a line-item veto of $2.6 million in Public Act 98-0050, which did not affect General Funds.
49 Natasha Korecki, "Topinka: 'I'm not paying any legislators,'" *Chicago Sun-Times*, July 25, 2013.
50 Illinois Constitution, Article IV, Section 9(d).

On July 29, House Speaker Madigan and Senate President Cullerton filed a lawsuit against Governor Quinn in Cook County Circuit Court. The General Assembly leaders argued that withholding lawmakers' pay undermined the separation of powers between the executive and legislative branches.[51]

Lawmakers had missed two paychecks by September 26, when a Cook County judge issued a decision on the lawsuit. Judge Neil Cohen ruled that the veto violated a provision of the Illinois Constitution that prohibits changes in legislators' salaries during their term of office.[52] The Governor said he would appeal the ruling.[53]

The next table summarizes the FY2014 enacted General Funds budget plan and compares it with the Governor's recommended FY2014 budget and the revised FY2013 budget. Operating expenditures are projected to approximately equal operating revenues, resulting in a roughly flat total deficit of $4.2 billion.

State of Illinois General Funds Budget Plan: FY2013-FY2014 as of July 2013 (in $ millions)

	FY2013 Revised*	FY2014 Rec.	FY2014 Enacted**
Operating Revenues	$ 36,328	$ 35,628	$ 35,707
Operating Expenditures	$ 35,558	$ 35,621	$ 35,713
Operating Surplus (Deficit)	$ 770	$ 7	$ (6)
Accumulated Surplus (Deficit)	$ (4,984)	$ (4,491)	$ (4,214)
Total Surplus (Deficit)	**$ (4,214)**	**$ (4,484)**	**$ (4,220)**

*As of June 2013. Includes revised legislatively required transfers out as of August 1, 2013.

**FY2014 revenues include a transfer in of a $397 million surplus in the Income Tax Refund Fund. FY2014 expenditures include a $27.8 million continuing appropriation for Teachers' Retirement Insurance Program and a $1 million appropriation to the Illinois Department of Public Health relating to the legalization of medical marijuana pursuant to Public Act 98-0122.

Source: Illinois State FY2014 Budget, p. 2-16; State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, pp. 16-17; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014* , August 2013, p. 25; Communications between Civic Federation and Governor's Office of Management and Budget, July 25 and August 1, 2013.

The enacted FY2014 budget figures represent estimates by the Governor's Office of Management and Budget (GOMB) based on the budget passed by the General Assembly and signed by the Governor. General Funds operating revenues of $35.707 billion in the table exceed the legislature's projection of $35.446 billion, largely due to a higher estimate of federal revenues by GOMB. In addition, the actual

[51] Monique Garcia, Rick Pearson and Ray Long, "Madigan, Cullerton sue Quinn over blocked lawmaker paychecks," *Chicago Tribune*, July 30, 2013.
[52] Dave McKinney and Jon Seidel, "In blow to Gov. Quinn, judge rules state lawmakers must be paid," Chicago Sun-Times.com, September 26, 2013. The provision is Article IV, Section 11.
[53] Illinois Government News Network, "Governor Pat Quinn Statement on Judge Ruling Against Suspension of Legislative Pay," *news release,* September 26, 2013.

year-end FY2013 surplus in the Income Tax Refund Fund that was transferred into General Funds totaled $397 million, up from a previous estimate of $300 million.[54]

General Funds operating expenditures of $35.713 million also exceed the General Assembly's budget of $35.446 billion. The difference stems mainly from the General Assembly's assumption that $650 million in appropriations would not be spent; GOMB assumed $500 million in unspent appropriations. In addition, the Civic Federation's projections increased FY2014 expenditures by $27.8 million to account for a continuing appropriation to TRIP and by $1 million to account for an appropriation relating to the legalization of medical marijuana.[55]

The following table shows revised estimates of accounts payable and other General Funds liabilities at the end of FY2013 and FY2014.

State of Illinois Unpaid Bill Backlog on June 30: 2013-2014 (in $ millions)

	2013 Est.*	2013 Est.**	2014 Rec.	2014 Enacted
General Funds Accounts Payable	**$ (4,724)**	**$ (4,254)**	**$ (4,724)**	**$ (4,260)**
Other General Funds Liabilities				
Medicaid-Related	$ (966)	$ (500)	$ (141)	$ -
Group Health Insurance	$ (1,894)	$ (1,540)	$ (1,894)	$ (1,540)
Income Tax Refunds	$ -	$ (45)	$ -	na
Total Other General Funds Liabilities	**$ (2,860)**	**$ (2,085)**	**$ (2,035)**	**$ (1,540)**
Total	**$ (7,584)**	**$ (6,339)**	**$ (6,759)**	**$ (5,800)**

*As of March 2013.
**As of July 2013.
Source: Illinois State FY2014 Budget, pp. 2-16 to 2-17; State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, pp. 16-17;Communications between Civic Federation and Governor's Office of Management and Budget, July 25 and July 26, 2013.

Due to the April Surprise, the total bill backlog at the end of FY2013 declined to $6.3 billion from a previous estimate of $7.6 billion. At the end of FY2014, accounts payable and other General Funds liabilities are projected at approximately $5.8 billion, down from a previous estimate of $6.8 billion.

[54] Illinois Office of the Comptroller, *Online Expenditure Query By Fund: Income Tax Refund Fund*, http://www.ioc.state.il.us/ (last visited on August 29, 2013).
[55] The Illinois Department of Public Health received a General Funds appropriation of $1 million related to the regulation of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.

GENERAL FUNDS REVENUES

Current projections for FY2014 show General Funds revenues totaling $35.7 billion. This amount is down slightly from FY2013, when year-end revenues totaled $36.1 billion.[56] The year-to-year decline is due to a one-time surge in income tax revenues in FY2013, which totaled more than $2.0 billion but is not expected to reoccur in FY2014.

General Funds revenues are the source of funding over which the Governor and General Assembly have the most discretion during the annual appropriation process. The remaining revenues are designated for Other State Funds or Federal Funds and are earmarked for specific purposes outside of the General Funds budget. The Governor's recommended FY2014 budget estimated that revenues for all appropriated funds would total $59.6 billion; an updated estimate is not currently available.[57]

The largest portion of General Funds resources comes from individual and corporate income taxes. FY2014 represents the final full fiscal year of the State's increased income tax rates that were passed in FY2011. On January 1, 2015, halfway through FY2015, the State's individual income tax rate will partially roll back to 3.75% from 5.0% and the corporate rate will decline from 7.0% to 5.0%.[58] Prior to the increase halfway through FY2011, the individual rate was 3.0% and the corporate rate was 4.8%.[59]

The second largest source of General Funds revenues are sales taxes. The State collects sales taxes at a rate of 6.25%, of which the State keeps the part equal to 5% of the purchase price and transfers the remaining 1.25% to local governments.

General Funds revenues also include federal revenues, which primarily represent reimbursements for Medicaid spending by the State. The federal government generally reimburses State Medicaid spending at a rate of 50%.[60]

Among other sources, General Funds revenues also include public utility taxes, vehicle taxes, cigarette taxes and transfers from the lottery and gaming sources.

Fiscal Year 2013 Preliminary Results

Total General Funds revenues collected by the State in FY2013 exceeded the projections used by the General Assembly when developing the FY2013 budget by $2.3 billion, totaling $36.1 billion compared to estimates of $33.7 billion.

House Joint Resolution 68 was adopted on March 7, 2012 as the consensus revenue estimate among the chambers of the General Assembly for developing its spending plan. At the time it was enacted,

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[56] State of Illinois, General Obligation Bonds, Series June of 2013, *Official Statement*, June 26, 3013, p. 16; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p. 25.
[57] Illinois State FY2014 Budget, p. 2-64.
[58] The State also collects the Personal Property Replacement Tax on behalf of local governments at a rate of 2.5% on corporate income, making the current effective corporate income tax rate 9.5%.
[59] Public Act 96-1496.
[60] State costs associated with newly eligible Medicaid recipients under the Affordable Care Act are reimbursed by the federal government in FY2014 at a rate of 100% but these costs and revenues are accounted for outside of the General Funds.

the estimate was $221 million more than the amount included in the Governor's recommended FY2013 budget.[61]

The majority of the increase in FY2013 operating revenues is attributable to gains in income taxes, which totaled $19.7 billion, or $2.1 billion more than originally included in the General Assembly's projections. Personal income taxes totaled $16.5 billion net of refunds, or $1.4 billion more than the legislative estimate of $15.1 billion. Net corporate income tax collected by the State totaled $3.2 billion, exceeding expectations of $2.5 billion by $673 million.

A surge in income tax revenues occurred in April 2013 due to federal tax changes that motivated taxpayers to avoid higher tax rates in 2013 by shifting taxable income to the 2012 calendar year. April is the month when most of the final income tax payments are due for the prior year, leading to an increase of $1.6 billion in combined income tax revenues over the projections for that month alone. This has been widely referred to as the "April Surprise."[62]

The biggest contributor to this behavior on the part of taxpayers was the increase in the top federal tax rate on capital gains to 20.0% from 15.0% and on ordinary income to 39.6% from 35.0%.[63] Capital gains are the easiest forms of income for individuals and business to move from one fiscal year to another but were not the only contributors. Taxpayers also advance bonus and other income that would have been realized after income tax rates went up. Illinois was not alone in this revenue surge; at least 26 other states reported double-digit percentage increases in income tax revenues collected in April 2013 over previous months.[64]

This jump in revenues is considered a one-time phenomenon and also may lead to reduced collections in FY2014 and beyond, when the revenue would have been realized under normal circumstances. However, the Illinois Department of Revenue and the Commission on Government Forecasting and Accountability have not modified forecasts for FY2014 or published an analysis of the future effects of the surge.

Sales taxes in FY2013 slightly exceeded the projection of $7.3 billion from the General Assembly, only beating expectations by $20 million. Due to additional resources available to fund Medicaid costs, federal revenues increased by $219 million to $4.2 billion in FY2013 compared to projections of $3.9 billion.

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[61] Illinois State FY2013 Budget, p. 2-63.
[62] Illinois Department of Revenue, *Monthly Revenue Report: April Fiscal Year 2013*, May 2013, p. 2.
[63] Don Boyd and Lucy Dadayan, "Time Bandits? State Income Taxes Surge in April," The Nelson A. Rockefeller Institute of Government, May 8, 2013.
[64] Elizabeth McNichol, "States Should React Cautiously to Recent Income Tax Growth:
April Surge Provides Opportunity to Invest in Infrastructure, Boost Reserves," Center on Budget Policy Priorities, September 5, 2013.

The following chart compares the preliminary year-end results for FY2013 General Funds revenues to the General Assembly's estimates included in HR89, which was used as the basis of the FY2013 budget.

Projections Compared to Actual Results (in $ millions)				
	FY2013 (Enacted)	FY2013 (Actual)	$ Change	% Change
State Taxes				
Income Tax	$ 17,644	$ 19,715	$ 2,071.0	11.7%
Personal Income Tax (net)	$ 15,140	$ 16,538	$ 1,398.0	9.2%
Corporate Income Tax (net)	$ 2,504	$ 3,177	$ 673.0	26.9%
Sales Taxes	$ 7,335	$ 7,355	$ 20.0	0.3%
Public Utility Taxes	$ 1,085	$ 1,033	$ (52.0)	-4.8%
Cigarette Tax	$ 355	$ 353	$ (2.0)	-0.6%
Liquor Gallonage Taxes	$ 162	$ 165	$ 3.0	1.9%
Vehicle Use Tax	$ 29	$ 27	$ (2.0)	-6.9%
Inheritance Tax	$ 230	$ 293	$ 63.0	27.4%
Insurance Taxes & Fees	$ 285	$ 334	$ 49.0	17.2%
Corporate Franchise Tax & Fees	$ 195	$ 205	$ 10.0	5.1%
Interest on State Funds & Investments	$ 20	$ 20	$ -	0.0%
Cook County Intergovernmental Transfer	$ 244	$ 244	$ -	0.0%
Other Sources	$ 400	$ 462	$ 62.0	15.5%
Total State Taxes	**$ 27,984**	**$ 30,206**	**$ 2,222.0**	**7.9%**
Transfers				
Lottery	$ 649	$ 656	$ 7.0	1.1%
Riverboat Transfers & Receipts	$ 340	$ 345	$ 5.0	1.5%
Proceeds From 10th Gaming License	$ 10	$ 15	$ 5.0	50.0%
Other	$ 801	$ 688	$ (113.0)	-14.1%
Total Transfers	**$ 1,800**	**$ 1,704**	**$ (96.0)**	**-5.3%**
Total State-Source Revenue	**$ 29,784**	**$ 31,910**	**$ 2,126.0**	**7.1%**
Federal Sources	**$ 3,935**	**$ 4,154**	**$ 219.0**	**5.6%**
Total Revenue	**$ 33,719**	**$ 36,064**	**$ 2,345**	**7.0%**

Source: 97th Illinois General Assembly, House Joint Resolution 68; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014* , August 2013, p. 50.

Fiscal Year 2014 Projections

On May 31, 2013, the legislature increased its General Funds revenue estimate for FY2014 by $365 million to $35.4 billion from an earlier projection of $35.1 billion. The original estimate was adopted by the House of Representative on March 5, 2013 and was used as the basis of the General Assembly's FY2014 budget deliberations until the last week of their spring legislative session. House Resolution 389 was passed in the final days of the budget negotiations to account for a larger than originally expected surplus in the Income Tax Refund Fund in FY2013. By law the surplus must be transferred to the General Funds at the beginning of the next fiscal year. The projections also took into account the reduction of the diversion rates used to set aside income tax receipts to pay for refunds in the coming year.[65]

The General Assembly's original General Funds revenue projection was passed in House Resolution 83, totaling $35.1 billion. This totaled $549 million less the total included in the Governor's recommended FY2014 budget. HR389 was passed to incorporate an increase of $300 million in revenue for FY2014 to be transferred from the Income Tax Refund Fund. It also increased income tax

[65] For more information about the Income Tax Refund Fund and diversion rates see page 20 of this report.

estimates by $65.0 million to account for lowering the Refund Fund rates. After the revisions in HR389, the General Assembly's projections were only $184.0 million less than the Governor's for FY2014. The remaining difference was almost entirely accounted for in the estimate of federal revenues. The General Assembly included a total of $4.0 billion in federal revenues, which were $178.0 million less than the Governor's projection.

The following chart shows the three different revenue estimates for FY2014 and compares the final legislative amounts to the Governor's proposed budget.

State of Illinois FY2014 General Funds Revenue Estimates: Governor's Recommendation Compared to House Resolutions 83 and 389 (in $ millions)					
Sources	**HR83**	**Governor's Rec.**	**HR389**	**$ Gov/HR389**	**% Gov/HR389**
Income Taxes	$ 18,902.0	$ 18,970.0	$ 18,967.0	$ (3.0)	0.0%
Personal Income Tax	$ 15,986.0	$ 16,073.0	$ 16,030.0	$ (43.0)	-0.3%
Corporate Income Tax	$ 2,916.0	$ 2,897.0	$ 2,937.0	$ 40.0	1.4%
Sales Taxes	$ 7,348.0	$ 7,385.0	$ 7,348.0	$ (37.0)	-0.5%
Public Utility	$ 1,032.0	$ 1,079.0	$ 1,032.0	$ (47.0)	-4.6%
Cigarette Tax	$ 355.0	$ 355.0	$ 355.0	$ -	0.0%
Liquor Gallonage Tax	$ 165.0	$ 168.0	$ 165.0	$ (3.0)	-1.8%
Inheritance Tax & Fees	$ 210.0	$ 169.0	$ 210.0	$ 41.0	19.5%
Insurance Taxes & Fees	$ 350.0	$ 325.0	$ 350.0	$ 25.0	7.1%
Corporate Franchise Tax & Fees	$ 203.0	$ 203.0	$ 203.0	$ -	0.0%
Interest	$ 20.0	$ 15.0	$ 20.0	$ 5.0	25.0%
Cook County Transfer	$ 244.0	$ 244.0	$ 244.0	$ -	0.0%
Other	$ 437.0	$ 611.0	$ 437.0	$ (174.0)	-39.8%
State-Source Taxes & Fees	**$ 29,266.0**	**$ 29,524.0**	**$ 29,331.0**	$ (193.0)	-0.7%
Transfers					
Lottery	$ 669.0	$ 669.0	$ 669.0	$ -	0.0%
Riverboat Transfers & Fees	$ 366.0	$ 366.0	$ 366.0	$ -	0.0%
Other	$ 780.0	$ 893.0	$ 1,080.0	$ 187.0	17.3%
Total Transfers	**$ 1,815.0**	**$ 1,928.0**	**$ 2,115.0**	**$ 187.0**	**8.8%**
Total State-Sources	**$ 31,081.0**	**$ 31,452.0**	**$ 31,446.0**	**$ (6.0)**	**0.0%**
Federal Revenue	**$ 4,000.0**	**$ 4,178.0**	**$ 4,000.0**	**$ (178.0)**	**-4.5%**
Total	**$ 35,081.0**	**$ 35,630.0**	**$ 35,446.0**	**$ (184.0)**	**-0.5%**

Source: 98th Illinois General Assembly, House Resolutions 83 and 389; Illinois State FY2014 Budget, p. 2-65.

In recent years, the General Assembly has relied on the revenue forecasts originating in the House for the annual budget passed by the legislature. The change in estimate for FY2014 was the first time in the past several years that an update was issued by the General Assembly during its budget deliberations.

After the close of the fiscal year on July 1, 2013, the Illinois Department of Revenue reported the actual surplus in the Income Tax Refund Fund totaled $397 million. The Governor's Office of Management and Budget also issued updated FY2014 General Funds revenue projections as part of the disclosures accompanying its General Obligation Bond sale on June 26, 2013.[66]

[66] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 16.

The new estimates from the Governor's office combined with the actual transfer amount result in an updated FY2014 revenue estimate of $35.7 billion, or a decline of $407 million from the FY2013 preliminary estimate of $36.1 billion.

The loss of one-time income tax revenues from the April 2013 revenue surge make up the majority of the year-to-year decline from FY2013 to FY2014. Total income taxes are down by $748.0 million, of which $508.0 million is attributable to the individual income tax and $240.0 million to the corporate income tax.

In all, State taxes decline by $875.0 million, totaling $29.3 billion in FY2014 compared to $30.2 billion in FY2013. However, the decrease is partially offset by an increase in transfers of $444.0 million, which total $2.1 billion in FY2014 compared to $1.7 billion in FY2013.

State-source General Funds revenue declines by $431.0 million to $31.5 billion in FY2014 from a total of $31.9 billion in FY2013.

Combined with federal revenues, which only increase by $24.0 million from year to year, total General Funds revenues decline by $407.0 million in FY2014 to $35.7 billion from $36.1 billion in FY2013.

The following table shows the updated FY2014 General Funds revenue projections by source of funds compared to the preliminary year-end results for FY2013.

State of Illinois General Funds Revenue: FY2013 Year-End Results Compared to Updated FY2014 Projections (in $ millions)

	FY2013	FY2014	$ Change	% Change
State Taxes				
Income Tax	$ 19,715	$ 18,967	$ (748.0)	-3.8%
Individual Income Tax (net)	$ 16,538	$ 16,030	$ (508.0)	-3.1%
Corporate Income Tax (net)	$ 3,177	$ 2,937	$ (240.0)	-7.6%
Sales Taxes	$ 7,355	$ 7,348	$ (7.0)	-0.1%
Public Utility Taxes	$ 1,033	$ 1,032	$ (1.0)	-0.1%
Cigarette Tax	$ 353	$ 355	$ 2.0	0.6%
Liquor Gallonage Taxes	$ 165	$ 165	$ -	0.0%
Vehicle Use Tax	$ 27	$ 27	$ -	0.0%
Inheritance Tax	$ 293	$ 210	$ (83.0)	-28.3%
Insurance Taxes & Fees	$ 334	$ 350	$ 16.0	4.8%
Corporate Franchise Tax & Fees	$ 205	$ 203	$ (2.0)	-1.0%
Interest on State Funds & Investments	$ 20	$ 20	$ -	0.0%
Cook County Intergovernmental Transfer	$ 244	$ 244	$ -	0.0%
Other Sources	$ 462	$ 410	$ (52.0)	-11.3%
Total State Taxes	**$ 30,206**	**$ 29,331**	**$ (875.0)**	**-2.9%**
Transfers In*	**$ 1,704**	**$ 2,148**	**$ 444.0**	**26.1%**
Total State-Source Revenue	**$ 31,910**	**$ 31,479**	**$ (431.0)**	**-1.4%**
Federal Sources	**$ 4,154**	**$ 4,178**	**$ 24.0**	**0.6%**
Total Revenue	**$ 36,064**	**$ 35,657**	**$ (407.0)**	**-1.1%**

*Excludes transfers from Backlog Payment Fund of $264 million in FY2013 and $50 million in FY2014. Includes actual Income Tax Refund Fund transfer in FY2014 of $397 million.

Source: State of Illinois, General Obligation Bonds, Series of June of 2013, *Official Statement* , June 26, 3013, p. 16; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014* , August 2013, p. 25.

Five-Year Comparison

Both the income tax and sales tax, on which the State relies most heavily for General Funds revenues, are economically sensitive and declined dramatically during the recession that began in December 2007 and lasted until June 2009.[67]

Revenues did not stabilize and continued to decline from FY2010 to FY2011, with overall revenue projections $500 million less in FY2011 than FY2010 when the Governor proposed the FY2011 budget.[68] After the State increased income tax rates halfway through FY2011 to 5.0% from 3.0% for individuals and to 7.0% from 4.8% for corporations, final revenues for the year increased by $2.6 billion in FY2011 from FY2010.[69] In FY2012, the first full year of the increased income tax rates, General Funds revenues increased by an additional $3.3 billion to $33.8 billion from $30.5 billion in FY2011.

Buttressed by the surge in April revenues, FY2013 represents the high-water mark for General Funds revenues prior to the partial sunset of the income tax increases in FY2015. Income taxes nearly doubled, increasing by $9.8 billion to $19.7 billion in FY2013 from $9.9 billion in FY2010. Total General Funds revenues were $9.0 billion more in FY2013 than FY2010 after accounting for losses of federal revenues totaling $1.7 billion and sales tax increases totaling $1.0 billion.

The FY2014 enacted budget is the final full year of increased income taxes prior to the scheduled partial sunset halfway through FY2015. Although State-source revenues will have increased by $10.3 billion in the five years since FY2010, after accounting for federal revenue losses of $1.7 billion, total General Funds revenues increase by a net $8.6 billion in FY2014 from FY2010.

[67] National Bureau of Economic Research, "US Business Cycle Expansions and Contractions," September 20, 2010.
[68] Illinois State FY2011 Budget, p. 2-10.
[69] Illinois State FY2012 Budget, p. 2-13.

The following chart shows General Funds revenues from FY2010 through FY2014.

State of Illinois General Funds Revenue: Five-Year Comparison FY2010-FY2014 (in $ millions)							
	FY2010	FY2011	FY2012	FY2013	FY2014	$ Change	% Change
State Taxes							
Income Tax	$ 9,871	$ 13,076	$ 17,973	$ 19,715	$ 18,967	$ 9,096.0	92.1%
Individual Income Tax (net)	$ 8,511	$ 11,225	$ 15,512	$ 16,538	$ 16,030	$ 7,519.0	88.3%
Corporate Income Tax (net)	$ 1,360	$ 1,851	$ 2,461	$ 3,177	$ 2,937	$ 1,577.0	116.0%
Sales Taxes	$ 6,308	$ 6,833	$ 7,226	$ 7,355	$ 7,348	$ 1,040.0	16.5%
Public Utility Taxes	$ 1,089	$ 1,147	$ 995	$ 1,033	$ 1,032	$ (57.0)	-5.2%
Cigarette Tax	$ 355	$ 355	$ 354	$ 353	$ 355	$ -	0.0%
Liquor Gallonage Taxes	$ 159	$ 157	$ 164	$ 165	$ 165	$ 6.0	3.8%
Vehicle Use Tax	$ 30	$ 30	$ 29	$ 27	$ 27	$ (3.0)	-10.0%
Inheritance Tax	$ 243	$ 122	$ 235	$ 293	$ 210	$ (33.0)	-13.6%
Insurance Taxes & Fees	$ 322	$ 317	$ 345	$ 334	$ 350	$ 28.0	8.7%
Corporate Franchise Tax & Fees	$ 208	$ 207	$ 192	$ 205	$ 203	$ (5.0)	-2.4%
Interest on State Funds & Investments	$ 26	$ 28	$ 21	$ 20	$ 20	$ (6.0)	-23.1%
Cook County Intergovernmental Transfer	$ 244	$ 244	$ 244	$ 244	$ 244	$ -	0.0%
Other Sources	$ 431	$ 404	$ 399	$ 462	$ 410	$ (21.0)	-4.9%
Total State Taxes	**$ 19,286**	**$ 22,920**	**$ 28,177**	**$ 30,206**	**$ 29,331**	**$ 10,045.0**	**52.1%**
Transfers In*	**$ 1,884**	**$ 2,182**	**$ 1,938**	**$ 1,704**	**$ 2,148**	**$ 264.0**	**14.0%**
Total State-Source Revenue	**$ 21,170**	**$ 25,102**	**$ 30,115**	**$ 31,910**	**$ 31,479**	**$ 10,309.0**	**48.7%**
Federal Sources	**$ 5,920**	**$ 5,386**	**$ 3,682**	**$ 4,154**	**$ 4,178**	**$ (1,742.0)**	**-29.4%**
Total Revenue	**$ 27,090**	**$ 30,488**	**$ 33,797**	**$ 36,064**	**$ 35,657**	**$ 8,567**	**31.6%**

*Excludes transfers from Backlog Payment Fund of $264 million in FY2013 and $50 million in FY2014. Includes actual Income Tax Refund Fund transfer of $397 million in FY2014.

Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, p. 16. Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014* , August 2013, p. 50.

Income Tax Refund Fund

The corporate and personal income tax revenue estimates discussed in this section are net of amounts diverted to the Income Tax Refund Fund to pay for anticipated refunds. Each year diversion rates, known as Refund Fund rates, are determined in order to repay expected overpayment of taxes by individuals and businesses.[70]

All refunds, both personal and business, are paid out of the Income Tax Refund Fund. The Illinois Department of Revenue makes it a priority to pay personal income tax refunds to individuals, so when there is a shortfall in the fund, unpaid business refunds rise. Unlike unpaid bills to vendors and local governments, unpaid tax refunds are not reflected in the State's operating budget.

The higher the Refund Fund rate, the more money is deposited into the Refund Fund and the less revenue is available for the State's general operations. Higher rates also reduce the share of income taxes transferred to local governments. Under State law, a specific share of state income tax proceeds is deposited in the Local Government Distributive Fund for distribution to local governments.[71] The share had been 10% but was lowered after the State increased income tax rates in January 2011 to allow the State to receive the full benefit of the tax increase.[72] The deposit into the Local Government Distributive Fund is made after income tax revenues are diverted into the Refund Fund.[73]

The Refund Fund rates are set by the Illinois General Assembly or can be set through a statutory formula that takes into account refunds paid and refunds approved but unpaid from the prior year as well as income tax revenues from the prior year.[74] The last time the rates were set using the formula was FY1998. Since then it has been specifically designated in budget legislation passed by the General Assembly and signed by the Governor.[75]

Despite experiencing a large increase in unpaid refunds in FY2009 and FY2010, the State set its individual Refund Fund rate lower by one percentage point to 8.75% from 9.75% in FY2011 and FY2012. The rate was increased in FY2013 for individuals to 9.75% and lowered for corporations to 14.0% from 17.5%. The enacted budget for FY2014 includes an individual Refund Fund rate of 9.5% and a business Refund Fund rate of 13.4%.

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[70] Business refunds and refund rates discussed in this section include both the corporate income tax, the Personal Property Replacement Tax (PPRT) on corporations and the PPRT on subchapter S corporations, partnerships and estates. Replacement taxes are revenues collected by the State and paid to local governments to replace money that was lost by local governments when their power to impose personal property taxes on corporations, partnerships and other business entities was rescinded pursuant to the 1970 Illinois Constitution.

[71] 35 ILCS 5/901(b).

[72] Public Act 96-1496.

[73] A higher business refund rate would also decrease the amount of Personal Property Replacement Tax transferred to local governments.

[74] 35 ILCS 5/901.

[75] Communication between the Civic Federation and the Department of Revenue, April 25, 2011.

The following chart shows the Refund Fund rates and backlog of unpaid refunds from FY2008 through FY2014.

State of Illinois Income Tax Refund Rates and Unpaid Tax Refunds: FY2008-FY2014 (in $ millions)				
	Personal Refund Rate	Unpaid Personal Refunds*	Business Refund Rate	Unpaid Business Refunds*
FY2008	7.75%	$ -	15.50%	$ 3.5
FY2009	9.75%	$ 5.0	17.50%	$ 214.0
FY2010	9.75%	$ 44.0	17.50%	$ 691.0
FY2011	8.75%	$ 19.0	17.50%	$ 627.0
FY2012	8.75%	$ 3.0	17.50%	$ 69.0
FY2013	9.75%	$ 5.0	14.00%	$ 40.0
FY2014	9.50%	na	13.40%	na

*As of June 30, reported on a cash basis.

Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, p. 58; Communication between the Civic Federation and Governor's Office of Management and Budget, September 12, 2013.

The Revenue Department is required to report refunds owed at the end of the fiscal year on a cash basis, so the table above includes amounts that were approved but unpaid at the end of the last business day of the month. There is an expected lag between approval of refunds and when they are paid even if there is adequate funding in the Refund Fund. However, due to the requirement that the $397 million Refund Fund surplus be transferred into General Funds based on the year-end cash balance, the $45 million in unpaid FY2013 refunds will be paid using resources from FY2014 diversions to the fund.

Due to the anticipated surplus, the Governor's recommended budget proposed lowering the Refund Fund rates from 9.75% in FY2013 to 9.0% in FY2014 for individual income taxes and from 14.0% to 12.0% for business income taxes.[76] The General Assembly enacted rates of 9.5% and 13.4%.[77] According to data from the Revenue Department, the rates would have been set at 8.4% and 14.5% under the statutory formula.[78]

Although the enacted Refund Fund rate for individual income taxes is much higher than the statutory rate, officials from the Revenue Department say the enacted rate is reasonable. According to the Department, the FY2014 formula is skewed by abnormally high gross receipts in April 2013. The revenue surge in April did not greatly increase the demand for refunds but inflated the denominator in the statutory formula.[79]

[76] Illinois State FY2014 Budget pp. 3-11, 3-12.
[77] Public Act 98-0024.
[78] Communication between the Civic Federation and Illinois Department of Revenue, August 29, 2013.
[79] Communication between the Civic Federation and Illinois Department of Revenue, September 5, 2013.

APPROPRIATIONS AND EXPENDITURES

The State of Illinois' enacted budget for FY2014 includes total appropriations of $64.4 billion, of which $31.1 billion are from General Funds. An appropriation is spending authority from a specific fund for a specific amount, purpose and time period.[80]

General Funds expenditures in FY2014 are estimated at $35.7 billion. General Funds expenditures include both spending from appropriations and transfers out of General Funds to make debt payments, provide funding for local governments and for other purposes.

General Funds represent the largest component of the State budget and are the funds over which the State has the most control.[81] They support the regular operating and administrative expenses of most agencies. General Funds resources include State income taxes and sales taxes as well as certain federal revenues, mainly related to federal reimbursements for State Medicaid spending.

Another broad category of State accounts is Other State Funds, which are funded by designated revenue sources that may only be used for specific purposes. The last category of State accounts is Federal Funds, which use federal revenues outside of the General Funds to support a variety of programs.

Appropriations by Fund

Total FY2014 appropriations of $64.4 billion are up 4.4% from $61.7 billion in FY2013 and 11.9% from $57.6 billion in FY2010. The following table shows the State's increasing reliance on appropriations from Other State Funds, although as explained below appropriations from these funds are typically in excess of actual spending.

State of Illinois Appropriations by Fund: FY2010-FY2014 (in $ millions)

	FY2010	FY2013 Revised	FY2014 Enacted	2-Year $ Change	2-Year % Change	5-Year $ Change	5-Year % Change
General Funds	$ 29,820	$ 30,812	$ 31,125	$ 313	1.0%	$ 1,305	4.4%
Other State Funds*	$ 17,533	$ 22,952	$ 25,250	$ 2,298	10.0%	$ 7,717	44.0%
Federal Funds	$ 10,208	$ 7,911	$ 8,042	$ 131	1.7%	$ (2,166)	-21.2%
Total	**$ 57,561**	**$ 61,675**	**$ 64,417**	**$ 2,742**	**4.4%**	**$ 6,856**	**11.9%**

*Other State Funds Appropriations are reduced to avoid double counting of appropriations spent for services provided by revolving funds.

Source: Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013; Illinois State FY2012 Budget, p. 2-32.

General Funds appropriations increase by 1.0% to $31.1 billion over the two-year period and by 4.4% over the five-year period. Much of the increase from FY2010 relates to growth in statutorily required pension contributions. Pension contributions are included in General Funds appropriations in FY2010 for purposes of comparability even though the State sold bonds to make the payments for that fiscal year.

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[80] Illinois State FY2014 Budget, p. 9-1.

[81] Illinois' General Funds consist of four funds: the General Revenue Fund, the Education Assistance Fund, the Common School Fund and the General Revenue-Common School Special Account Fund.

Appropriations from Other State Funds have shown the largest increase, accounting for 39.2% of total appropriations in FY2014, compared with 30.5% in FY2010. The increase has been particularly marked in the area of Medicaid, where General Funds appropriations have remained relatively flat while funding from Other State Funds has increased.[82] Federal Funds appropriations increase by 1.7% in the two-year period and decline by 21.2% in the five-year period.

It should be noted that spending from Other State Funds and Federal Funds is often significantly below appropriated amounts. In FY2010, for example, expenditures from Other State Funds totaled $14.5 billion, compared with appropriations of $17.5 billion, and Federal Funds spending was $5.5 billion, compared with appropriations of $10.2 billion.[83] Budget officials typically seek additional spending authority for Other State Funds and Federal Funds in case additional resources become available during the year. Appropriations for these funds do not affect the operating deficit and are less politically sensitive than General Funds appropriations.

Other State Funds appropriations are also inflated in FY2014 due to an apparent budgeting error by the General Assembly that affected the Illinois Department of Healthcare and Family Services (HFS), which administers the State's Medicaid program. In the legislature's budget, HFS received a $1.2 billion Other State Funds appropriation that duplicated spending authority already covered in the HFS budget.[84]

The State also spends somewhat less than the appropriated amount of General Funds. General Funds spending authority remains unused at the end of the year because insufficient resources are available or expenses do not reach budgeted levels. In FY2010, with economically sensitive State tax revenues depressed due to the national economic recession, an unusually large $896 million of General Funds appropriations was left unspent.[85]

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[82] Resources for these appropriations come from transfers out of General Funds and from non-General Funds sources, such as an increase in the cigarette tax in FY2013 that is deposited into Other State Funds that support Medicaid. For more information on Medicaid, see p. 37 of this report.

[83] Illinois State FY2012 Budget, p. 2-32.

[84] Communication between the Civic Federation and the Governor's Office of Management and Budget, August 27, 2013. The duplicative $1.2 billion is appropriated in Public Act 98-0017, signed on June 5, 2013. See also Illinois Senate Republicans, *2013 at a Glance: An Overview of the 2013 Spring Session*, p. 6, http://www.senategop.state.il.us/Portals/0/Senate-Action/At%20a%20Glance-Web_Budget-2.pdf (last visited on September 10, 2013).

[85] State of Illinois, General Obligation Bonds. Series of September 2012, *Official Statement*, September 13, 2012, p. 8.

The following table compares Governor Quinn's recommended appropriations for FY2014 with enacted FY2014 appropriations. Appropriations for General Funds and Federal Funds are roughly similar, while Other State Funds appropriations increase by $2.1 billion, or 8.8%, in the enacted budget. In addition to the $1.2 billion budgeting mistake involving HFS discussed above, the enacted budget includes increased Other State Funds appropriations for Medicaid, human services and pension contributions.

State of Illinois Total Appropriations by Fund: FY2014 Recommended-FY2014 Enacted (in $ millions)

	FY2014 Rec.	FY2014 Enacted	$ Change	% Change
General Funds	$ 31,223	$ 31,125	$ (98)	-0.3%
Other State Funds*	$ 23,200	$ 25,250	$ 2,050	8.8%
Federal Funds	$ 7,993	$ 8,042	$ 49	0.6%
Total	**$ 62,416**	**$ 64,417**	**$ 2,001**	**3.2%**

*Other State Funds appropriations are reduced to avoid double counting of appropriations spent for services provided by revolving funds.

Source: Illinois State FY2014 Budget, p. 2-35; Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013.

General Funds Appropriations by Category

General Funds appropriations can be divided into four components: agency appropriations for current services, agency appropriations to pay down prior year bills, pension contributions and group insurance. The major increase from FY2010 to FY2014 involves appropriations for statutorily required pension contributions. Pension contributions increase to $6.0 billion in FY2014, up by $2.5 billion from $3.5 billion in FY2010 and by $881 million from $5.1 billion in FY2013.[86]

Agency appropriations for current services are $23.7 billion in FY2014. That represents a decrease of $1.5 billion from $25.2 billion in FY2010 and an increase of $129 million from $23.6 billion in FY2013. It should be noted that General Funds agency appropriations understate General Funds resources used for current services because current services are also funded by transfers out of General Funds.

In FY2013 General Funds appropriations of $643 million were used to pay down accumulated bills from prior years. The total included a $264 million appropriation to the Comptroller's Office to be deposited into the newly created Backlog Payment Fund and transferred back into General Funds for payment of outstanding bills not related to Medicaid.[87] The remaining $379 million was part of a supplemental appropriation resulting from an unexpected surge in State income tax collections in April 2013.[88] In the FY2014 enacted budget, the appropriation for deposit into the Backlog Payment Fund was reduced to $50 million.[89]

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[86] For more information on the State Retirement Systems, see p. 32 of this report.
[87] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 29.
[88] Public Act 98-0011, signed on May 10, 2013 and Public Act 98-0017, signed on June 5, 2013.
[89] Public Act 98-0017, signed on June 5, 2013.

The General Funds appropriation for group insurance declines by $104 million from $1.45 billion in FY2013 to $1.35 billion in FY2014.[90] The FY2013 appropriation for group insurance included a supplemental appropriation of $350 million enacted in June 2013.[91] The original FY2013 appropriation was inadequate because protracted labor negotiations delayed State savings on health insurance costs that were expected to be realized in that fiscal year. Despite the additional appropriation, the backlog of unpaid health insurance bills grew by an estimated $358 million by the end of FY2013 to roughly $1.5 billion.[92] The FY2014 appropriation reflects projected State health insurance savings due to a new union contract.[93] The Governor's Office of Management and Budget expects the appropriation to fully fund the program in FY2014 with no growth in outstanding bills.[94]

The next table shows General Funds appropriations by category from FY2010 to FY2014.

State of Illinois General Funds Appropriations by Category: FY2010-FY2014 (in $ millions)

	FY2010	FY2013 Revised[1]	FY2014 Enacted	2-Year $ Change	2-Year % Change	5-Year $ Change	5-Year % Change
Agency Appropriations[2]	$ 25,208	$ 23,612	$ 23,741	$ 129	0.5%	$ (1,467)	-5.8%
Agency Appropriations for Payment of Prior Year Bills	$ -	$ 643	$ 50	$ (593)	-92.2%	$ 50	na
Pension Contributions[3]	$ 3,466	$ 5,107	$ 5,988	$ 881	17.3%	$ 2,522	72.8%
Group Insurance	$ 1,146	$ 1,450	$ 1,346	$ (104)	-7.2%	$ 200	17.5%
Total	**$ 29,820**	**$ 30,812**	**$ 31,125**	**$ 313**	**1.0%**	**$ 1,305**	**4.4%**

[1]As of June 2013.

[2]FY2014 agency appropriations include $1 million appropriation to the Illinois Department of Public Health relating to regulation of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.

[3]Pension contributions in FY2010 were made by issuance of pension obligation bonds and are included as appropriations for purposes of comparability.

Source: State of Illinois, General Obligation Bonds, Series of September 2012, *Official Statement*, September 13, 2012, pp. 8-9; State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, pp. 16-17; Illinois State FY2012 Budget, p. 2-26; Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013; Public Act 98-0017, pp. 2 and 90.

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90 Appropriations in the table, as in the budget, include both health insurance and life insurance. General Funds health insurance appropriations in FY2014 are $1.33 billion. For more information on group insurance, see p. 43 of this report.

91 Public Act 98-0017, signed on June 5, 2013.

92 Communication between the Civic Federation and the Governor's Office of Management and Budget, July 26, 2013.

93 Illinois Department of Central Management Services, Submission to General Assembly's Commission on Government Forecasting and Accountability, April 16, 2013.

94 Communication between the Civic Federation and the Governor's Office of Management and Budget, July 26, 2013.

The Governor's budget proposal in March 2013 devoted more funding to paying off accumulated bills. Unexpectedly large State income tax collections in April permitted these bills to be discharged through supplemental appropriations in FY2013. The enacted budget also uses $48 million less in General Funds to make required pension contributions, shifting this portion of funding to the State Pensions Fund, which receives revenue from the sale of abandoned property.[95]

The following table compares the Governor's proposed FY2014 General Funds appropriations by category with enacted FY2014 appropriations by category.

State of Illinois General Funds Appropriations by Category: FY2014 Recommended-FY2014 Enacted (in $ millions)

	FY2014 Rec.	FY2014 Enacted	$ Change	% Change
Agency Appropriations*	$ 23,529	$ 23,741	$ 212	0.9%
Agency Appropriations for Payment of Prior Year Bills	$ 312	$ 50	$ (262)	-84.0%
Pension Contributions	$ 6,036	$ 5,988	$ (48)	-0.8%
Group Insurance	$ 1,346	$ 1,346	$ -	0.0%
Total	**$ 31,223**	**$ 31,125**	**$ (98)**	**-0.3%**

*FY2014 agency appropriations include $1 million appropriation to the Illinois Department of Public Health relating to regulation of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.

Source: Illinois State FY2014 Budget, pp. 2-16 to 2-17 and p. 2-29; Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013; Public Act 98-0017, pp. 2 and 90.

Appropriations by Agency

The table on page 29 shows appropriations from FY2010 to FY2014 for the 10 largest agencies, ranked by total FY2014 appropriations. In this table, agency appropriations include appropriations for payment of prior year bills. Agency appropriations do not include pension contributions or group insurance, which are appropriated separately.

The largest agency is HFS, which administers the State's Medicaid program. Total FY2014 appropriations of $19.6 billion are up 8.3% from $18.1 billion in FY2013 and 28.6% from $15.2 billion in FY2010.

State spending on Medicaid is reimbursed by the federal government, generally at a rate of 50%, and additional funding is provided by local governments and healthcare providers. As a result, State appropriations for Medicaid significantly overstate net State funding for the program. In addition, as previously explained, Other State Funds appropriations in the budget are typically in excess of Other State Funds spending. Appropriations from Other State Funds represent 62.0% of total HFS appropriations for FY2014 and reflect a budgeting error of $1.2 billion. An analysis of trends in HFS' annual budget is further complicated by the State's traditional practice of deferring Medicaid costs and paying them out of future appropriations. As discussed below, the best way to analyze the cost of the Medicaid program is by examining program liabilities rather than appropriations.

[95] Public Act 98-0017, signed on June 5, 2013.

Total appropriations for elementary and secondary education increase by 1.9% to $9.8 billion in FY2014 from $9.6 billion in FY2013. Since FY2010 appropriations for elementary and secondary education have declined by $1.2 billion, or 11.2%, with a decrease in funding from General Funds compounded by a reduction in federal funding due to the expiration of the federal American Recovery and Reinvestment Act of 2009.

General State Aid, the main State spending program for elementary and secondary education, increases by $155.4 million to $4.44 billion in FY2014 from $4.29 billion in FY2013.[96] General State Aid payments are based on a Foundation Level of funding, which is established by statute and represents the minimum per child amount of financial support that should be available to provide for the basic education of each student.[97] 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. The Foundation Level has been unchanged from FY2010 at a per pupil amount of $6,119.[98] General State Aid funding for FY2014 represents 89% of the amount that would have been required to fully fund the Foundation Level, or an estimated $5,720 per pupil.[99]

Total FY2014 appropriations for higher education of $2.4 billion are approximately unchanged from FY2013 levels. Since FY2010 total appropriations for higher education have declined by $229.9 million, or 8.6%. Higher education includes nine public universities, the Illinois Board of Higher Education, the Illinois Community College Board, the Illinois Student Assistance Commission, the Illinois Mathematics and Science Academy and the State Universities Civil Service System.

The Illinois Department of Human Services (DHS) has total FY2014 appropriations of $6.1 billion. That represents an increase of $30.0 million from FY2013 and a decrease of $258.5 million from FY2010. Over the five-year period, an increase in Other State Funds appropriations is more than offset by a reduction in funding from General Funds.

DHS and several other agencies received appropriations for day-to-day operations in the form of lump sums. [100] Lump sum appropriations do not identify specific funding purposes, such as employee salaries, by line item. Because a new union contract negotiated by the Governor's Office included wage increases in FY2014, agencies were expected to stay within their budgets by reducing headcount, possibly through attrition.[101]

Total lottery appropriations increase by 18.0% to $1.2 billion in FY2014 from $1.0 billion in FY2013 based on a projected increase in ticket sales and payment of additional prizes. The Lottery Department,

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[96] Illinois State Board of Education, *FY2014 Operating Budget: Public Acts 98-0033 & 98-0034*, June 27, 2013, http://www.isbe.state.il.us/budget/FY14/fy14-budget.pdf (last visited on September 9, 2013).
[97] 105 ILCS 5/18-8.05(B).
[98] Illinois State Board of Education, *GSA Overview*, January 20, 2013, http://www.isbe.state.il.us/funding/pdf/gsa_overview.pdf (last visited on September 9, 2010).
[99] Illinois Association of School Boards, "Legislature Close to Wrapping Up," *Alliance Legislative Report 98-19*, May 31, 2013.
[100] Other agencies with lump sum appropriations for operations include the State Board of Education, the Department on Aging, the Department of Veterans' Affairs, the Department of Central Management Services, the Department of Commerce and Economic Opportunity, the Department of Employment Security, the Department of Natural Resources, the Illinois Supreme Court and the Department of State Police. For more information, see Illinois Senate Republicans, *2013 at a Glance: An Overview of the 2013 Spring Session*, http://www.senategop.state.il.us/Portals/0/Senate-Action/At%20a%20Glance-Web_Budget-2.pdf (last visited on September 10, 2013).
[101] Council 31 AFSCME, "Where things stand in Springfield," July 19, 2013, http://www.afscme31.org/news/where-things-stand-in-springfield (last visited on August 13, 2013).

which receives no General Funds revenues, was established as a separate agency in 2011 to supervise the private manager selected to run the State's lottery.[102]

State of Illinois All Funds Appropriations for Ten Largest Agencies: FY2010-FY2014 (in $ millions)[1]							
Agency	FY2010	FY2013 Revised[2]	FY2014 Enacted	2-Year $ Change	2-Year % Change	5-Year $ Change	5-Year % Change
Healthcare and Family Services	**$ 15,203.5**	**$ 18,051.6**	**$ 19,557.5**	**$ 1,505.9**	**8.3%**	**$ 4,354.0**	**28.6%**
General Funds	$ 6,733.1	$ 7,042.8	$ 7,038.6	$ (4.2)	-0.1%	$ 305.5	4.5%
Other State Funds	$ 8,270.4	$ 10,593.8	$ 12,118.9	$ 1,525.1	14.4%	$ 3,848.5	46.5%
Federal Funds	$ 200.0	$ 415.0	$ 400.0	$ (15.0)	-3.6%	$ 200.0	100.0%
State Board of Education	**$ 11,003.9**	**$ 9,587.5**	**$ 9,771.3**	**$ 183.8**	**1.9%**	**$ (1,232.6)**	**-11.2%**
General Funds	$ 7,332.2	$ 6,549.8	$ 6,687.0	$ 137.2	2.1%	$ (645.2)	-8.8%
Other State Funds	$ 44.3	$ 61.1	$ 76.9	$ 15.8	25.9%	$ 32.6	73.6%
Federal Funds	$ 3,637.5	$ 2,976.7	$ 3,007.4	$ 30.7	1.0%	$ (630.1)	-17.3%
Human Services	**$ 6,345.1**	**$ 6,056.6**	**$ 6,086.6**	**$ 30.0**	**0.5%**	**$ (258.5)**	**-4.1%**
General Funds	$ 3,976.9	$ 3,495.7	$ 3,179.3	$ (316.4)	-9.1%	$ (797.6)	-20.1%
Other State Funds	$ 750.0	$ 865.8	$ 1,163.7	$ 297.9	34.4%	$ 413.7	55.2%
Federal Funds	$ 1,618.2	$ 1,695.1	$ 1,743.5	$ 48.4	2.9%	$ 125.3	7.7%
Transportation	**$ 2,512.2**	**$ 2,688.6**	**$ 2,720.2**	**$ 31.6**	**1.2%**	**$ 208.0**	**8.3%**
General Funds	$ 78.0	$ 22.2	$ 5.7	$ (16.5)	-74.3%	$ (72.3)	-92.7%
Other State Funds	$ 2,430.3	$ 2,661.4	$ 2,709.8	$ 48.4	1.8%	$ 279.5	11.5%
Federal Funds	$ 3.9	$ 5.0	$ 4.7	$ (0.3)	-6.0%	$ 0.8	20.5%
Higher Education[3]	**$ 2,672.1**	**$ 2,440.6**	**$ 2,442.2**	**$ 1.6**	**0.1%**	**$ (229.9)**	**-8.6%**
General Funds	$ 2,220.4	$ 1,979.8	$ 1,991.3	$ 11.5	0.6%	$ (229.1)	-10.3%
Other State Funds	$ 70.8	$ 86.4	$ 73.3	$ (13.1)	-15.2%	$ 2.5	3.5%
Federal Funds	$ 380.9	$ 374.4	$ 377.6	$ 3.2	0.9%	$ (3.3)	-0.9%
DCEO[4]	**$ 2,668.7**	**$ 1,754.9**	**$ 1,857.0**	**$ 102.1**	**5.8%**	**$ (811.7)**	**-30.4%**
General Funds	$ 51.7	$ 31.3	$ 44.1	$ 12.8	40.9%	$ (7.6)	-14.7%
Other State Funds	$ 272.6	$ 421.3	$ 443.1	$ 21.8	5.2%	$ 170.5	62.5%
Federal Funds	$ 2,344.5	$ 1,302.3	$ 1,370.2	$ 67.9	5.2%	$ (974.3)	-41.6%
Corrections	**$ 1,304.8**	**$ 1,260.3**	**$ 1,309.9**	**$ 49.6**	**3.9%**	**$ 5.1**	**0.4%**
General Funds	$ 1,176.8	$ 1,173.3	$ 1,218.2	$ 44.9	3.8%	$ 41.4	3.5%
Other State Funds	$ 128.1	$ 87.0	$ 91.7	$ 4.7	5.4%	$ (36.4)	-28.4%
Federal Funds	$ -	$ -	$ -	$ -	na	$ -	na
Lottery[5]	**na**	**$ 1,042.0**	**$ 1,229.9**	**$ 187.9**	**18.0%**	**na**	**na**
General Funds	na	$ -	$ -	$ -	na	na	na
Other State Funds	na	$ 1,042.0	$ 1,229.9	$ 187.9	18.0%	na	na
Federal Funds	na	$ -	$ -	$ -	na	na	na
Children and Family Services	**$ 1,297.4**	**$ 1,199.6**	**$ 1,181.6**	**$ (18.0)**	**-1.5%**	**$ (115.8)**	**-8.9%**
General Funds	$ 868.6	$ 732.0	$ 696.0	$ (36.0)	-4.9%	$ (172.6)	-19.9%
Other State Funds	$ 420.7	$ 459.9	$ 475.2	$ 15.3	3.3%	$ 54.5	13.0%
Federal Funds	$ 8.1	$ 7.7	$ 10.4	$ 2.7	35.1%	$ 2.3	28.4%
Aging	**$ 745.2**	**$ 1,201.2**	**$ 1,121.4**	**$ (79.8)**	**-6.6%**	**$ 376.2**	**50.5%**
General Funds	$ 656.2	$ 1,100.1	$ 1,030.9	$ (69.2)	-6.3%	$ 374.7	57.1%
Other State Funds	$ 8.4	$ 12.9	$ 4.9	$ (8.0)	-62.0%	$ (3.5)	-41.7%
Federal Funds	$ 80.5	$ 88.1	$ 85.6	$ (2.5)	-2.8%	$ 5.1	6.3%

[1]Does not include pension contributions, State group insurance or debt service.
[2]As of July 2013.
[3]Includes nine public universities, Board of Higher Education, Community College Board, Student Assistance Commission, Mathematics and Science Academy and State Universities Civil Service System.
[4]Department of Commerce and Economic Opportunity.
[5]Created in 2011, after a private firm began managing lottery operations.
Source: Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013; Illinois State FY2012 Budget, pp. 2-24 to 2-32.

Although not shown in the table, the Illinois Supreme Court has General Funds appropriations of $301.8 million in FY2014, an increase of $20.7 million from $281.1 million in FY2013. The increase is related to the costs of county probation officers, which are reimbursed by the State. In seeking

[102] Public Act 97-0464, signed on August 19, 2011.

additional funding, the Supreme Court cited a sharp decline in appropriations since FY2002 and argued that probation saves taxpayers money because court supervision costs less than detention.[103]

It is also of interest to compare enacted FY2014 agency appropriations with the Governor's proposed agency appropriations for FY2014. The largest shifts involve funding for human services and education.

Total appropriations for DHS decline by $221.7 million from the Governor's proposal, while total appropriations for the Department on Aging decline by $153.4 million. The Governor's FY2014 budget proposal in March 2013 included appropriations of approximately $170 million for the payment of outstanding bills at DHS and $142 million for the payment of outstanding bills at the Department on Aging.[104] Due to the unexpected increase in State income tax collections in April 2013, those outstanding bills were actually paid in FY2013, along with an additional $59 million in DHS bills. As a result, all outstanding DHS and Aging bills were paid as of the end of FY2013.[105] In the enacted FY2014 budget, the reduction in total appropriations for DHS and Aging more than offsets the amounts designated for bill payment in the Governor's proposal, meaning that the two agencies have less to spend on current services than recommended by the Governor. The decrease for DHS is about $52 million, while the decrease for Aging is approximately $12 million.

Appropriations for the Department of Corrections and the Department of Children and Family Services (DCFS) also decline in FY2014 from the Governor's recommended budget. General Funds appropriations for the Department of Corrections decline by $24.9 million, or 2.0%, to $1.2 billion, while General Funds appropriations for DCFS decline by $20.1 million, or 2.8%, to $696.0 million.

In contrast, appropriations for education increase in FY2014 from the Governor's proposal. The enacted total appropriation for elementary and secondary education of $9.8 billion is up $462.0 from the Governor's recommendation. The enacted General Funds appropriation is $6.7 billion, up $445.9 million from the Governor's proposal. The appropriation for General State Aid is $4.4 billion in the enacted FY2014 budget, an increase of $305.8 million from $4.1 billion in the Governor's proposal.[106] The enacted budget funds 89% of the Foundation level, compared with 82% funding in the Governor's recommended budget.[107]

Appropriations for higher education increase by $95.0 million to $2.4 billion in the enacted FY2014 budget from $2.3 billion in the Governor's proposal. The Governor's budget included decreased appropriations for each of the State's nine public universities from FY2013, but the enacted budget has higher appropriations for all except two, Northern Illinois University and Southern Illinois University. Appropriations for Chicago State University increase by $2.1 million, or 5.5%, to $39.2 million.

The Department of Commerce and Economic Opportunity (DCEO) has an increase in total appropriations of $17.4 million from the Governor's proposal to $1.86 billion. General Funds appropriations for DCEO increase by $9.8 million, or 28.6%, to $44.1 million from the Governor's

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[103] Communication between the Civic Federation and the Illinois Supreme Court, September 23, 2013.
[104] State of Illinois, General Obligation bonds, Series A of April 2013 and Taxable Series B of April 2013, *Official Statement*, April 2, 2013, p. 29.
[105] Communication between the Civic Federation and the Governor's Office of Management and Budget, July 26, 2013.
[106] Illinois State Board of Education, *FY2014 Operating Budget: Public Acts 98-0033 & 98-0034*, June 27, 2013, http://www.isbe.state.il.us/budget/FY14/fy14-budget.pdf (last visited on September 9, 2013).
[107] Illinois State Board of Education, *FY2014 Operating Budget: Public Acts 98-0033 & 98-0034*, June 27, 2013, http://www.isbe.state.il.us/budget/FY14/fy14-budget.pdf (last visited on September 9, 2013).

recommendation. The enacted General Funds budget includes numerous grants for job training and tourism bureaus that were not part of the Governor's proposal.[108]

The table on the next page compares the Governor's proposed FY2014 appropriations for the largest ten agencies with enacted FY2014 appropriations for those agencies.

[108] Illinois Senate Republicans, *2013 at a Glance: An Overview of the 2013 Spring Session*, pp. 21-23; http://www.senategop.state.il.us/Portals/0/Senate-Action/At%20a%20Glance-Web_Budget-2.pdf (last visited on September 10, 2013).

State of Illinois All Funds Appropriations for Ten Largest Agencies: Recommended FY2014-Enacted FY2014 (in $ millions)[1]				
Agency	FY2014 Rec.	FY2014 Enacted	$ Change	% Change
Healthcare and Family Services	**$ 17,746.8**	**$ 19,557.5**	**$ 1,810.7**	**10.2%**
General Funds	$ 7,060.2	$ 7,038.6	$ (21.6)	-0.3%
Other State Funds	$ 10,286.6	$ 12,118.9	$ 1,832.3	17.8%
Federal Funds	$ 400.0	$ 400.0	$ -	0.0%
State Board of Education	**$ 9,309.3**	**$ 9,771.3**	**$ 462.0**	**5.0%**
General Funds	$ 6,241.1	$ 6,687.0	$ 445.9	7.1%
Other State Funds	$ 61.1	$ 76.9	$ 15.8	25.9%
Federal Funds	$ 3,007.4	$ 3,007.4	$ -	0.0%
Human Services	**$ 6,308.3**	**$ 6,086.6**	**$ (221.7)**	**-3.5%**
General Funds	$ 3,606.1	$ 3,179.3	$ (426.8)	-11.8%
Other State Funds	$ 972.2	$ 1,163.7	$ 191.5	19.7%
Federal Funds	$ 1,730.0	$ 1,743.5	$ 13.5	0.8%
Transportation	**$ 2,712.7**	**$ 2,720.2**	**$ 7.5**	**0.3%**
General Funds	$ -	$ 5.7	$ 5.7	na
Other State Funds	$ 2,708.1	$ 2,709.8	$ 1.7	0.1%
Federal Funds	$ 4.6	$ 4.7	$ 0.1	2.2%
Higher Education[2]	**$ 2,347.2**	**$ 2,442.2**	**$ 95.0**	**4.0%**
General Funds	$ 1,900.0	$ 1,991.3	$ 91.3	4.8%
Other State Funds	$ 69.7	$ 73.3	$ 3.6	5.2%
Federal Funds	$ 378.0	$ 377.6	$ (0.4)	-0.1%
DCEO[3]	**$ 1,839.6**	**$ 1,857.0**	**$ 17.4**	**0.9%**
General Funds	$ 34.3	$ 44.1	$ 9.8	28.6%
Other State Funds	$ 436.6	$ 443.1	$ 6.5	1.5%
Federal Funds	$ 1,368.7	$ 1,370.2	$ 1.5	0.1%
Corrections	**$ 1,334.8**	**$ 1,309.9**	**$ (24.9)**	**-1.9%**
General Funds	$ 1,243.1	$ 1,218.2	$ (24.9)	-2.0%
Other State Funds	$ 91.7	$ 91.7	$ -	0.0%
Federal Funds	$ -	$ -	$ -	na
Lottery[4]	**$ 1,229.9**	**$ 1,229.9**	**$ -**	**0.0%**
General Funds	$ -	$ -	$ -	na
Other State Funds	$ 1,229.9	$ 1,229.9	$ -	0.0%
Federal Funds	$ -	$ -	$ -	na
Children and Family Services	**$ 1,199.8**	**$ 1,181.6**	**$ (18.2)**	**-1.5%**
General Funds	$ 716.1	$ 696.0	$ (20.1)	-2.8%
Other State Funds	$ 473.2	$ 475.2	$ 2.0	0.4%
Federal Funds	$ 10.4	$ 10.4	$ -	0.0%
Aging	**$ 1,274.8**	**$ 1,121.4**	**$ (153.4)**	**-12.0%**
General Funds	$ 1,184.2	$ 1,030.9	$ (153.3)	-12.9%
Other State Funds	$ 4.9	$ 4.9	$ -	0.0%
Federal Funds	$ 85.6	$ 85.6	$ -	0.0%

[1]Does not include pension contributions, State group insurance or debt service. Totals may not add due to rounding.

[2]Includes nine public universities, Board of Higher Education, Community College Board, Student Assistance Commission, Mathematics and Science Academy and State Universities Civil Service System.

[3]Department of Commerce and Economic Opportunity.

[4]Created in 2011, after a private firm began managing lottery operations.

Source: Illinois State FY2014 Budget, pp. 2-27 to 2-35; Communication between Civic Federation and Governor's Office of Management and Budget, July 25, 2013.

The Secretary of State's Office, which is not shown in the previous table, has an FY2014 General Funds appropriation of $259.3 million, which is $16.8 million above the Governor's recommendation of $242.5 million. The enacted FY2014 General Funds appropriation for the Secretary of State's Office is $4.0 million above the FY2013 amount of $255.3 million.

State Retirement Systems

General Funds contributions to the State's five retirement systems are $5.99 billion in FY2014, or 19.0% of projected State-source General Funds revenues of $31.48 billion.[109] Total General Funds pension costs, including $1.66 billion in pension bond payments, are $7.65 billion, or 24.3% of State-source revenues.

State pension contributions are determined by a 50-year funding plan that began in FY1996.[110] After a phase-in period of 15 years, the law requires State contributions at a level percentage of payroll sufficient to achieve a 90% funded ratio by the end of FY2045.

When the funding plan began, the total unfunded liability of the five systems stood at approximately $19.5 billion.[111] By the end of FY2012, the unfunded liability had grown to $96.8 billion and the combined funded ratio stood at 39.0%.[112] Moody's Investors Service determined in June 2013 that Illinois had the largest pension burden of any state relative to State revenues.[113]

The growth in the unfunded liability is largely attributable to inadequate State contributions. The funding plan and subsequently enacted changes deferred a large portion of the required State contributions to later years. The unfunded liability has also increased because of lower than expected investment returns, enhanced benefits and changes in mortality rates and other factors.[114]

The funding schedule does not require the State to make adequate contributions to keep the unfunded liability from growing until approximately 2031.[115] Statutorily required State contributions have also

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[109] The five systems are the Teachers' Retirement System (TRS), the State Universities Retirement System (SURS), the State Employees' Retirement System (SERS), the Judges' Retirement System (JRS) and the General Assembly Retirement System (GARS). The State is also statutorily required to make contributions to the Public School Teachers' Pension and Retirement Fund of Chicago equal to 0.544% of teacher payroll to offset a portion of the cost of benefit increases enacted under Public Act 90-0582. This contribution is not required if the funded ratio is at least 90%; the funded ratio stood at 54.5% in FY2012. This State contribution is $11.9 million in FY2014.

[110] Public Act 88-0593. Employees also contribute to the systems, with contributions ranging from 4% to 12.5% of salary depending on the plan and whether the member is also covered by Social Security. For more information, see the Institute for Illinois' Fiscal Sustainability at the Civic Federation, *State of Illinois FY2014 Recommended Operating and Capital Budgets: Analysis and Recommendations*, May 13, 2013, pp. 65-75, http://www.civicfed.org/iifs/publications/fy2014recommended.

[111] Commission on Government Forecasting and Accountability, *Report on the 90% Funding Target of Public Act 88-0593*, January 2006, p. i. This statistic is based on the market value of assets. Unfunded liability is the actuarial value of accrued pension benefits that are not covered by pension assets. A pension fund is considered 100% funded when its asset level equals the actuarial accrued liability.

[112] Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012*, February 2013, p. 25. Figures are based on the market value of assets.

[113] Moody's Investors Service, *Adjusted Pension Liability Medians for US States*, June 27, 2013, p. 10. The ranking reflected Moody's recalculation of State pension obligations using a new methodology.

[114] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p. 109.

[115] Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012*, February 2013, p. 97. The contribution amount that is adequate to keep unfunded liabilities from growing consists of the normal cost (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

been less than those required under the reporting standards of the Governmental Accounting Standards Board.[116]

Under the current funding plan, the State's total annual pension contributions are expected to increase to $17.6 billion by FY2045 from $6.8 billion in FY2014.[117] Total pension contributions include payments from General Funds and Other State Funds; approximately 89% of total contributions come from General Funds.

General Funds pension contributions increase by $881 million to $5.988 billion in FY2014 from $5.107 billion in FY2013. The General Funds contributions in the enacted FY2014 budget are $48 million below the Governor's proposed contributions of $6.036 billion, reflecting increased funding from the State Pensions Fund. The State Pensions Fund, which receives revenues from the sale of unclaimed property, will pay for $198 million of required contributions, up from $150 million in the Governor's proposal.[118]

The sharp increase in required contributions in FY2014 is largely due to poor investment returns at all of the systems in FY2012 and to revised actuarial assumptions by the Teachers' Retirement System (TRS). TRS, the largest State fund, decided in September 2012 to reduce the system's assumed investment rate of return to 8.0% from 8.5%, thus increasing the need for other sources of funding. The decision affected required State contributions in FY2014 because the retirement systems calculate and certify the amounts needed in each fiscal year by November of the prior fiscal year.[119]

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prevent growth in the unfunded liability, is not enough to pay down the unfunded liability.

[116] State of Illinois, General Obligation Bonds, Series A of April 2013 and Taxable Series B of April 2013, *Official Statement*, April 2, p. 59. Under Government Accounting Standards Board (GASB) 25, the Annual Required Contribution (ARC) is the amount required to pay the employer's normal cost plus the cost to amortize a pension plan's unfunded liability over a period of no more than 30 years.

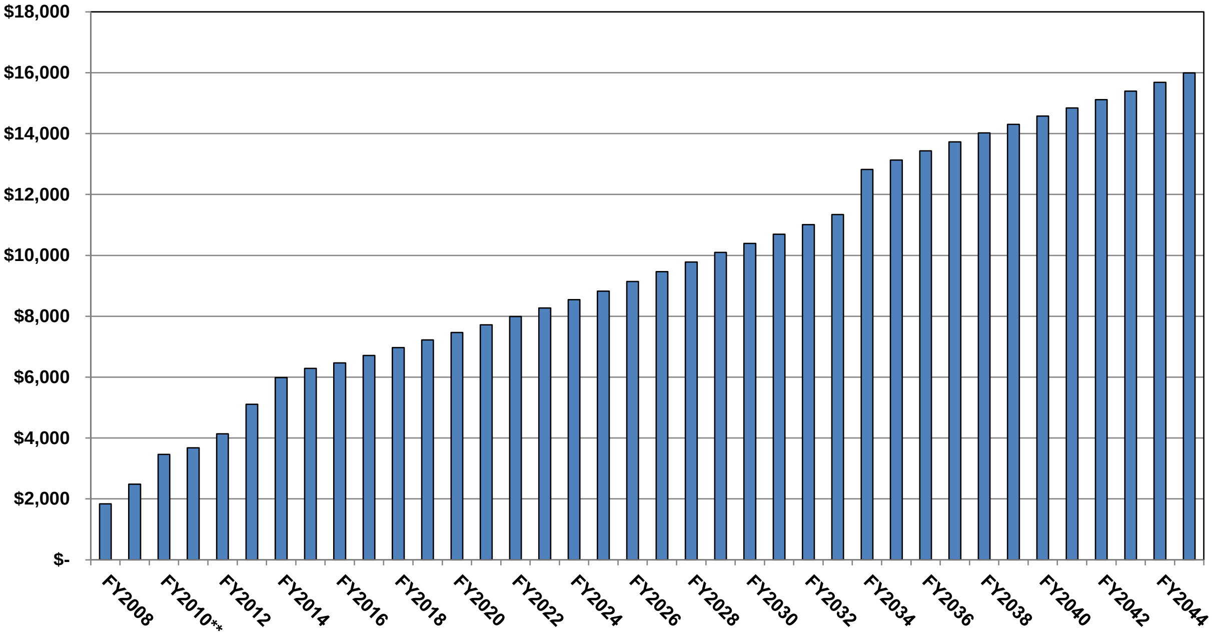
[117] Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012*, February 2013, p. 97.

[118] Public Act 98-0017, signed on June 5, 2013.

[119] 40 ILCS 5/16-158 (a-1).

The following chart shows actual and projected General Funds pension contributions from FY2008 through FY2045 under the State's current funding plan. General Funds contributions were $1.8 billion in FY2008 and are projected to increase to $16.0 billion by FY2045.[120] Contributions increase sharply after FY2033, when the State fully pays off $10 billion in pension bonds sold in 2003. Until the bonds are paid off, pension contributions are reduced by the amount of debt service payments on the bonds.[121]

State of Illinois Actual and Projected General Funds Pension Contributions Under Current State Law: FY2008-FY2045 (in $ millions)*



*FY2008 through FY2014 are actual contributions; FY2015 through FY2045 are Civic Federation projections based on actuarial valuations as of June 30, 2012. See Appendix B for data.
**General Funds contributions in FY2010 and FY2011 were made through the issuance of General Obligation Bonds.
Source: Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012*, February 2013, pp. 97-102; State of Illinois, General Obligation Bonds, Series of June 2013, Official Statement, June 26, 2013, p. 16; Illinois State FY2012 Budget, p. 2-14; Communication between Civic Federation and Governor's Office of Managment and Budget, February 23, 2012.

After analyzing how much of the State's future revenues will have to go toward pension costs under current law, the TRS Board of Trustees approved a resolution on March 30, 2012 stating that it no longer had confidence that the State could meet its funding obligations to TRS.[122] The resolution represented a change of position for TRS, which had previously maintained that the State would adhere to the pension funding law requiring 90% funding by FY2045.

Previous actions to reduce State pension obligations did not have a significant impact on funding requirements in the short term because they did not affect retirees or current employees. In April 2010, the State created a two-tier benefits system with less generous benefits for workers hired on or after January 1, 2011.[123] The new tier of benefits, known as Tier 2, includes higher retirement ages, a maximum pensionable salary and lower automatic annual benefit increases.

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[120] See Appendix B on p. 70 for data and methodology.
[121] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 73.
[122] Teachers' Retirement System of the State of Illinois, *Board of Trustees Resolution*, March 30, 2012.
[123] Public Act 96-0889. This legislation also applies to most non-public safety local government pension funds across the State.

Tier 2 employees receive annual benefit increases of 3% or one-half of the annual increase in the Consumer Price Index (CPI), whichever is less. Current Illinois retirees and those hired before January 1, 2011 receive automatic annual increases of 3%. New workers' benefits grow more slowly over time because the annual increase is based on a simple rate, while the benefits of retirees and existing employees are increased based on a compounded rate.[124]

Savings due to these benefit reductions will increasingly affect the State's budget in future years. As a larger percentage of the workforce is covered by the lower benefits, the accrued pension liability will decline and statutorily required State contributions will be reduced.[125]

Efforts to reduce pension benefits for retirees and current workers are strongly opposed by labor unions and complicated by constitutional protections. The State's largest union, Council 31 of the American Federation of State, County and Municipal Employees (AFSCME), contends that pension changes that significantly reduce State costs would unduly burden employees and threaten their retirement security.[126]

Any major pension changes are expected to be challenged on constitutional grounds. The Illinois Constitution provides that membership in any pension system in the State is an enforceable contractual relationship and that member benefits "shall not be diminished or impaired."[127] However, legal opinions have varied on the interpretation of this provision.[128]

At the end of the General Assembly's spring 2013 session, the legislature reached an impasse over two bills that take different approaches to the constitutional provision.[129] A proposal by House Speaker Michael Madigan, apparently based on the State's general governmental or police powers, maintains that pension benefits must be reduced to prevent further harm to public welfare.[130] A bill sponsored by Senate President John Cullerton and backed by labor unions is based on the idea that cutting pension benefits can only be constitutional if employees and retirees are granted something valuable in exchange for forgone benefits.[131] The House passed Speaker Madigan's plan, while the Senate approved Senate President Cullerton's proposal and rejected the Speaker's bill.

According to actuarial reviews, Speaker Madigan's plan would lower the unfunded liability by $20.0 billion and reduce the State's total pension contributions by $2 billion in FY2015 and $163.2 billion through FY2045.[132] Senate President Cullerton's proposal offers employees and retirees benefit choices centered on keeping or reducing the 3% compounded automatic annual benefit increase; potential State savings would depend on the choices made by participants. Actuarial reviews, based on

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[124] A simple rate increase applies the stated rate only to the initial benefit amount, while a compounded rate increase applies the stated rate to the initial benefit amount plus previously earned increases.
[125] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, pp. 86-87.
[126] Council 31 AFSCME, *Where Things Stand in Springfield*, July 19, 2013, http://www.afscme31.org/news/where-things-stand-in-springfield (last visited on September 13, 2013).
[127] Illinois Constitution, Article XIII, Section 5.
[128] For a collection of legal opinions on the pension clause in the Illinois Constitution, see the Illinois Senate Democrats' website, http://www.senatedem.ilga.gov/index.php/component/content/article/108-public-information-brochures/1517-pension-debate (last visited on September 13, 2013).
[129] See Appendix C for details on the provisions of the two bills.
[130] 98th Illinois General Assembly, Senate Bill 1 as amended by House Amendments 1 and 3, passed by the House on May 2, 2013 and rejected by the Senate on May 30, 2013. The State's general governmental powers are granted in Article II, Section 2 of the Illinois Constitution.
[131] 98th Illinois General Assembly, Senate Bill 2404, passed by the Senate on May 9, 2013.
[132] The projection of State savings through FY2045 was reduced by $24.49 billion after the Teachers' Retirement System revised its estimate in August 2013.

specified scenarios, show that the plan could lower the unfunded liability by $5.3 billion to $9.0 billion. State contributions could be reduced by $420 million to $824 million in FY2015 and by $35.4 billion to $53.7 billion through FY2045.[133]

The legislature's failure to pass pension reform during its spring session led to the downgrading of the State's bond ratings by two ratings firms.[134] In response to the downgrades, Governor Quinn called the General Assembly back to Springfield for a special session on June 19 to deal with pensions. When it appeared that the House and Senate could not agree on either of the two proposals, the Governor proposed the creation of a conference committee and set a deadline of July 9 for committee action.[135]

The 10-member bipartisan committee held three public meetings and heard testimony from a variety of interested parties. Panel members said they would not be able to meet the Governor's deadline because they were waiting for actuarial reviews of proposed pension changes. Senator Kwame Raoul, the committee's chairman, said the panel was considering a proposal based on an idea supported by presidents of the State's public universities.[136]

The Governor responded on July 10 by vetoing lawmakers' pay for FY2014 and stating that he would not accept a paycheck himself until significant pension changes were enacted.[137] The action eliminated line-item appropriations totaling $13.9 million, covering salaries of General Assembly members and stipends for legislative leaders.[138] On July 29, Speaker Madigan and Senate President Cullerton filed a lawsuit against Governor Quinn in Cook County Circuit Court.[139] The General Assembly leaders argued that withholding lawmakers' pay undermined the separation of powers between the executive and legislative branches.

Lawmakers had missed two paychecks by September 26, when a Cook County judge issued a decision on the lawsuit. Judge Neil Cohen ruled that the veto violated a provision of the Illinois Constitution that prohibits changes in legislators' salaries during their term of office.[140] The Governor said he plans to appeal the ruling.[141]

The conference committee has not held a public hearing since July 8 but is reportedly working on a pension proposal based on the university plan.[142] The central feature of the university proposal is a compounded annual benefit increase set at half of the percentage increase in the CPI.[143]

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[133] For more information and links to actuarial reviews, see the Institute for Illinois' Fiscal Sustainability at the Civic Federation blog, http://www.civicfed.org/iifs/blog/new-reports-show-financial-impact-proposed-state-pension-changes.
[134] For more information on the State's bond ratings, see p. 63 of this report.
[135] Illinois Government News Network, "Gov. Pat Quinn Sets July 9 for General Assembly to Act on Comprehensive Pension Reform; Conference Committee Convened," *news release*, June 19, 2013.
[136] Doug Finke, "Quinn blasted for missing pension hearing," *State Journal-Register*, July 8, 2013.
[137] Illinois Government News Network, "Governor Quinn Suspends Pay to Illinois Representatives and Senators; After General Assembly Fails Yet Again to Pass Comprehensive Pension Reform, Governor Vetoes Out Legislative Salaries and Stipends," *news release*, July 10, 2013.
[138] 98th Illinois General Assembly, House Bill 214 (Public Act 98-0064, signed with line-item veto on July 10, 2013).
[139] Monique Garcia, Rick Pearson and Ray Long, "Madigan, Cullerton sue Quinn over blocked lawmaker paychecks," *Chicago Tribune*, July 30, 2013.
[140] Dave McKinney and Jon Seidel, "In blow to Gov. Quinn, judge rules state lawmakers must be paid," Chicago Sun-Times.com, September 26, 2013. The provision is Article IV, Section 11.
[141] Illinois Government News Network, "Governor Pat Quinn Statement on Judge Ruling Against Suspension of Legislative Pay," *news release*, September 26, 2013.
[142] Doug Finke, "Progress, but no deal yet on pensions," *State Journal-Register*," July 24, 2013.
[143] Institute of Government and Public Affairs, University of Illinois, *Six Simple Steps: Reforming the Illinois State Universities Retirement System*, March 12, 2013.

The university plan appears to be regarded as a promising framework because it offers the potential for more State savings than Senate President Cullerton's plan while possibly following the legal approach favored by the Senate President. In exchange for giving up automatic annual compounded benefit increases of 3%, participants would receive something of value: protection from inflation. Details have not been publicly released, so it is not clear whether the conference committee is considering a cap on annual benefit increases to protect the State from high inflation rates.

In response to reports about the conference committee's plan, the We Are One Illinois coalition of labor unions issued a statement in August opposing the proposal and urging lawmakers to focus on Senate President Cullerton's bill.[144] The statement said setting the annual benefit adjustment at half of the CPI increase would dramatically reduce pension benefits and harm State retirees.

Medicaid

Illinois' Medicaid program is undergoing major changes, including eligibility expansion under the federal Affordable Care Act, a State-mandated movement to managed care and continuing implementation of program cuts enacted by the General Assembly in 2012. These changes add to the complexity of tracking the finances of a program that involves several agencies and multiple funding sources.

Medicaid is a joint federal-state program that funds medical services for certain categories of low-income people, including children, pregnant women, parents, the elderly and the disabled.[145] Beginning in January 2014, the Affordable Care Act (ACA) gives states the option of providing Medicaid to the major population group that generally has not been covered: non-elderly, non-disabled adults without dependent children.

The ACA extends Medicaid coverage to all adult citizens with annual incomes up to 138% of the federal poverty level ($15,415 for an individual in 2013). The federal government is scheduled to pay 100% of the cost for the newly eligible population for the first three years of the program; 95% in 2017; 94% in 2018; 93% in 2019; and 90% thereafter.

Medicaid has no single programmatic appropriation in the State of Illinois budget. The Illinois Department of Healthcare and Family Services (HFS) administers the program and accounts for most of its spending, but a significant share of Medicaid expenditures are made by other agencies.[146] In the State budget, the best approximation to Medicaid is HFS' Medical Assistance Program, although roughly 10% of that program's appropriations are not part of Medicaid.

State Medicaid expenditures are generally reimbursed by the federal government at a rate known as the Federal Medical Assistance Percentage (FMAP), which varies by state depending on per capita income and is set at 50% for Illinois. Appropriations in the State budget are gross amounts, meaning that they represent total authorized spending funded by both the State and federal governments. In

[144] We Are One Illinois, *Conference Committee Bill Outline Leaked*, August 26, 2013. http://www.weareoneillinois.org/news/statement-on-conference-committee-outline (last visited on September 14, 2013).
[145] For more information on Medicaid, see the Civic Federation's Institute on Illinois' Fiscal Sustainability, *Illinois Medicaid Program: An Issue Brief*, May 22, 2009, http://www.civicfed.org/iifs/publications/illinois-medicaid-program-issue-brief.
[146] Illinois Department of Healthcare and Family Services, *Medical Assistance Program Annual Report: Fiscal Years 2009, 2010 and 2011*, March 30, 2012, p. 18. Other agencies include the Departments of Human Services, Public Health and Children and Family Services and the Department on Aging.

General Funds, for example, a $1 appropriation for Medicaid represents 50 cents in State-funded spending and 50 cents in federally funded spending. Federal reimbursements for State Medicaid spending are a major component of General Funds revenues.

In addition to General Funds, the Illinois Medicaid program receives funding from a number of Other State Funds sources, including rebates paid by prescription drug manufacturers, proceeds from the settlement of tobacco-related litigation and payments by local governments and healthcare providers that are structured to bring in additional federal matching funds.

The following table shows Medical Assistance expenditures from FY2010 through FY2012, appropriations and estimated expenditures in FY2013 and enacted appropriations in FY2014. The table shows relatively flat General Funds spending, generally accompanied by an increase in appropriations from other funding sources.

HFS Medical Assistance Program Expenditures and Appropriations: FY2010-FY2014 (in $ millions)

	FY2010 Exp.	FY2011 Exp.	FY2012 Exp.	FY2013 Approp.	FY2013 Est. Exp.	FY2014 Enacted
General Funds	$ 5,971.9	$ 6,313.2	$ 6,627.4	$ 6,879.3	$ 6,619.7	$ 6,965.8
Other State Funds	$ 7,035.8	$ 6,964.3	$ 5,772.7	$ 10,637.9	$ 8,449.7	$ 12,025.2
Total	$ 13,007.7	$ 13,277.5	$ 12,400.1	$ 17,517.2	$ 15,069.4	$ 18,991.0

Source: Communications between Civic Federation and Illinois Department of Healthcare and Family Services and Governor's Office of Management and Budget, August 29, 2013.

Total appropriations increase by $1.5 billion, or 8.4%, to $19.0 billion in FY2014 from $17.5 billion in FY2013. General Funds appropriations increase by $86.5 million, or 1.3%, to $7.0 billion, while Other State Funds appropriations increase by $1.4 billion, or 13.0%, to $12.0 billion.

Several caveats are in order, however. It should be noted that appropriations from Other State Funds are typically in excess of actual expenditures. Budget officials typically seek additional spending authority from Other State Funds; this prevents the need to request supplemental appropriations from the General Assembly in case additional resources become available during the year. Appropriations from Other State Funds do not affect the operating deficit and are less politically sensitive than General Funds appropriations.

Other State Funds appropriations for HFS are also inflated in FY2014 due to an apparent budgeting error by the General Assembly. In the legislature's budget, HFS received a $1.2 billion Other State Funds appropriation that duplicated spending authority already covered in the HFS budget.[147] The increase in Other State Funds appropriations in FY2014 also reflects a delay in federal approval for a hospital assessment program that was expected to be approved in FY2013. This delay reduced Other State Funds expenditures in FY2013 and added $508 million to Other State Funds appropriations in FY2014.[148]

Although spending from General Funds appropriations is relatively flat, it is important to understand that the Medical Assistance program also receives General Funds resources through transfers out to

[147] Communication between the Civic Federation and the Governor's Office of Management and Budget, August 27, 2013. The duplicative $1.2 billion is appropriated in Public Act 98-0017, signed on June 5, 2013. See also Illinois Senate Republicans, *2013 at a Glance: An Overview of the 2013 Spring Session*, p. 6, http://www.senategop.state.il.us/Portals/0/Senate-Action/At%20a%20Glance-Web_Budget-2.pdf (last visited on September 10, 2013).
[148] Communication between the Civic Federation and the Governor's Office of Management and Budget, July 26, 2013.

other funds. In FY2014, the Healthcare Provider Relief Fund, which is used to pay medical bills, is expected to receive a $601 million transfer from General Funds, up from $500 million in FY2013 and $160 million in FY2012.[149] Through a cycle of State spending and federal reimbursement known as churning, the $601 million can provide roughly $1.2 billion in total resources.[150] This requires an appropriation of $1.2 billion from the Healthcare Provider Relief Fund.

If the funding were budgeted as a General Funds appropriation rather than a transfer, the required General Funds appropriation would be $1.2 billion. The net impact on the General Funds budget would be the same because the $1.2 billion appropriation would be offset by $601 million in federal reimbursements. However, a General Funds appropriation of $1.2 billion might appear less attractive than a transfer of $601 million for political reasons.

The General Assembly also makes appropriations for deposit into Other State Funds. At the end of FY2013, $130 million was appropriated to HFS from General Funds for deposit into the Healthcare Provider Relief Fund.[151] According to HFS officials, the $130 million will be used in FY2014, with $90 million going to the Department of Human Services and $40 million to HFS. With federal matching, the $130 million provides total resources of roughly $260 million.[152]

An analysis of trends in HFS' annual budget is further complicated by the State's traditional practice of deferring Medicaid costs and paying them out of future appropriations. In general, Section 25 of the State Finance Act requires that bills incurred in a given year be paid out of that year's appropriation.[153] However, what is known as the Section 25 exception has allowed the State to pay Medicaid bills out of future years' appropriations. Relying on this provision, the State has appropriated inadequate amounts for Medicaid in order to help balance the budget. In the meantime, Medicaid bills have accumulated outside the budget.

Bills have accumulated because simply reducing Medicaid appropriations will not reduce Medicaid costs. Medicaid is an entitlement program under which certain categories of low-income people who meet eligibility requirements are entitled to specified medical services. Medicaid costs cannot be cut without reductions in program eligibility, benefits or reimbursement rates paid to healthcare providers such as hospitals, nursing homes and pharmacies.

Legislation enacted in 2012 significantly curtails the State's ability to defer HFS Medicaid bills beginning at the end of FY2013.[154] The new law limits these deferred liabilities to $700 million in FY2013 and $100 million thereafter, with certain exceptions.[155] In FY2013 the General Assembly allocated $500 million in General Funds revenues for the payment of outstanding Medicaid bills. These funds were transferred out of General Funds and provided $1 billion in resources after federal reimbursements.

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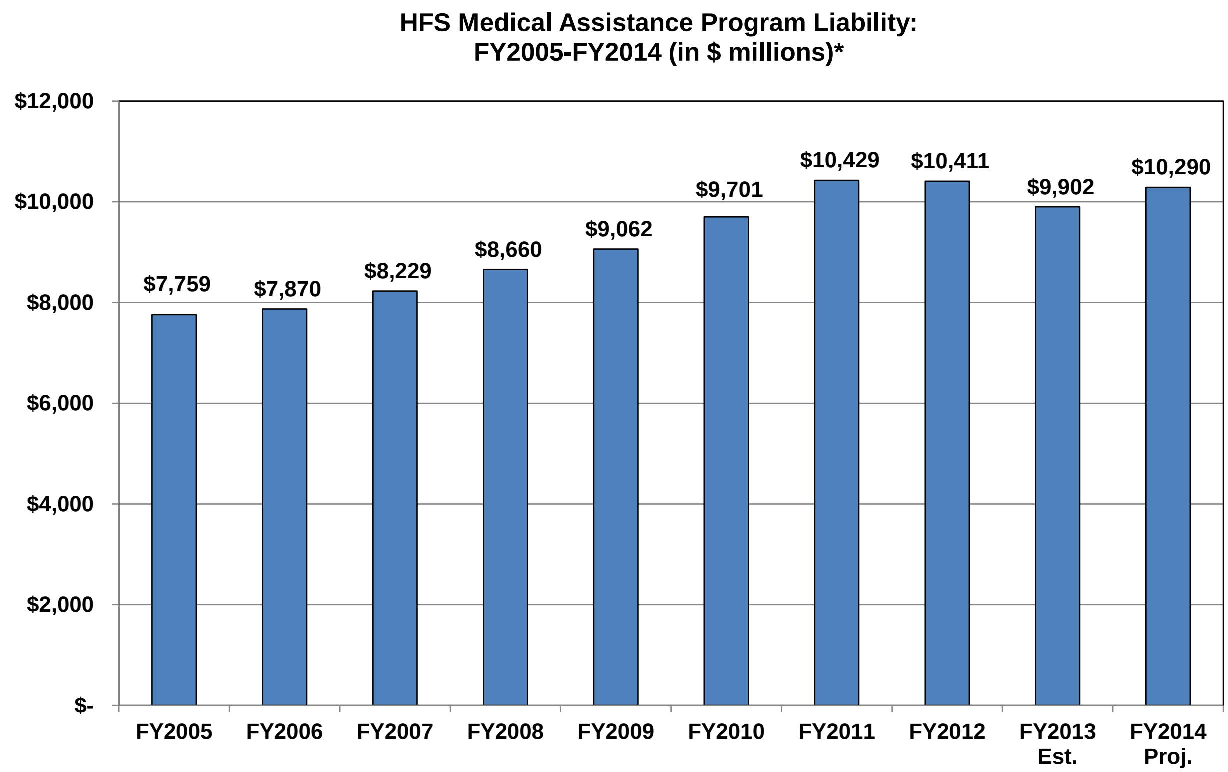
[149] Communication between the Civic Federation and the Governor's Office of Management and Budget, August 1, 2013. For more information on transfers, see p. 49 of this report. In FY2012 the Medicaid program was also supported by a $140 million transfer out to the FY12 Hospital Relief Fund.
[150] For an illustration of how this process works, see the Institute for Illinois' Fiscal Sustainability at the Civic Federation's blog at http://www.civicfed.org/iifs/blog/medicaid-101-how-3375-million-turns-675-million.
[151] Public Act 98-0017, signed on June 5, 2013, p. 49.
[152] Communication between the Civic Federation and the Illinois Department of Healthcare and Family Services, August 28, 2013.
[153] 30 ILCS 105/25.
[154] Public Act 97-0691.
[155] The exceptions relate partly to bills that were incurred before June 30 but not received by that date.

Annual liability—rather than spending—provides the best measure of the Medicaid program's cost trends. The next table shows Medical Assistance liability from FY2005 through FY2014. This table does not include special funding arrangements that are structured to generate federal revenue, such as hospital assessments. Annual liability is expected to increase by $388 million, or 3.9%, to $10.3 billion in FY2014 from $9.9 billion in FY2013.



*Liability includes General Funds and related funds only.
Source: Illinois Department of Healthcare and Family Services, *FY14 Cashflow*, FY14 Final Spring Session Cashflow; *FY13 Cashflow and FY14 Cashflow*, FY13 April Revised; Communication between Civic Federation and Illinois Department of Healthcare and Family Services, April 13, 2012.

This projection of FY2014 costs depends on assumptions about the impact of the ACA expansion and other major changes in Illinois' Medicaid program. The Medicaid expansion was made optional for states by a U.S. Supreme Court opinion in June 2012.[156] The Supreme Court generally upheld the ACA but ruled that the federal government could not withhold matching funds for states' existing Medicaid programs if they chose not to participate in the ACA expansion. The Illinois General Assembly approved the expansion at the end of the spring 2013 session.[157]

Illinois' Medicaid program has an estimated 2.8 million participants, and HFS is expecting 509,000 more people to enroll as a result of the ACA by 2017.[158] Of the 509,000, 342,000 are expected to be newly eligible under the ACA and 167,000 are expected to be previously eligible but not enrolled. Previously eligible individuals are expected to sign up because of publicity surrounding the ACA and policies that steer people to Medicaid if they are not eligible to obtain insurance coverage through a

[156] Kaiser Family Foundation, *A Guide to the Supreme Court's Affordable Care Act Decision*, July 2012, pp. 5-6.
[157] Public Act 98-0104, signed on July 22, 2013.
[158] Illinois Department of Healthcare and Family Services, *Fiscal Year 2014 Budget Overview*, March 6, 2013, pp. 7 and 22.

new ACA-mandated health insurance exchange.[159] Expenses for recipients who were previously eligible but not enrolled will be reimbursed by the federal government at the regular rate of 50%.

ACA-related costs in FY2014 depend on the number of people who sign up and the medical condition of the new enrollees. Since the Governor's budget proposal, HFS has increased its estimate of average medical expenses by approximately 66% for each category of ACA enrollees.[160] The total cost estimate is now $282 million, up from $170 million, and includes $189 million for the newly eligible and $93 million for the previously eligible but not enrolled. These numbers represent total costs; the federal government will cover 100% of the cost for the newly eligible and 50% for the previously eligible.

ACA-related costs account for approximately 73% of the projected annual liability growth of $388 million, or 3.9%, in FY2014. Without the ACA-related costs, the projected liability growth in FY2014 would be $106 million, or 1.1%, based on HFS projections.[161]

The modest growth in non-ACA liabilities is partly related to assumptions about the results of cost-cutting measures under the Saving Medicaid Access and Resources Together (SMART) Act.[162] The SMART Act, signed in June 2012, was part of a restructuring program designed to close a funding gap of $2.7 billion projected for FY2013. The funding crisis was triggered by an underappropriation of $1.5 billion in FY2012.[163] The legislation authorized $1.36 billion in program reductions, $240 in reimbursement rate cuts to healthcare providers and $1.1 billion in additional revenue, including a $1-a-pack increase in the State cigarette tax.[164]

HFS has stated that savings in FY2013 were expected to be approximately $494.5 million short of the target but that the shortfall would be largely offset by $395 million in savings in FY2012.[165] The agency has not updated its savings estimates since March 2013.

The largest projected saving—$350 million—was related to an effort to remove ineligible enrollees from the Medicaid program. HFS initially estimated that the effort could reduce costs by $120 million in FY2013.[166] The Illinois Hospital Association projected savings of between $240 million and $720 million, based on the assumption that 100,000 to 300,000 enrollees could be ineligible and could represent an average of $200 a month of Medicaid spending.[167] The final savings projection—$350

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[159] Kaiser Family Foundation, *The Cost and Coverage Implications of the ACA Medicaid Expansion: National and State-by-State Analysis*, November 2012, p. 29.
[160] Communication between the Civic Federation and the Illinois Department of Healthcare and Family Services, August 29, 2013.
[161] Illinois Department of Healthcare and Family Services, *FY14 Cashflow*, FY14 Final Spring Session Cashflow; Illinois Department of Healthcare and Family Services, *FY13 Cashflow and FY14 Cashflow*, FY13 April Revised.
[162] Public Act 96-0689.
[163] For more information on the Medicaid funding crisis and the restructuring plan, see the Institute for Illinois' Fiscal Sustainability at the Civic Federation, *State of Illinois Enacted Budget FY2013: A Review of the Operating Budget for the Current Fiscal Year*, October 8, 2012, pp. 32-36. http://www.civicfed.org/StateofIllinoisEnactedBudgetFY2013 and *State of Illinois FY2014 Budget Roadmap: State of Illinois Budget Overview, Projections and Recommendations for the Governor and the Illinois General Assembly*, February 25, 2013, pp. 27-29, http://www.civicfed.org/iifs/publications/IllinoisRoadmapFY2014.
[164] In addition to Public Act 96-0689, the legislative package included 97-0688 and 97-0691.
[165] Illinois Department of Healthcare and Family Services, *SMART Act Implementation Status Report*, Senate Appropriations Committee hearing, March 19, 2013; Illinois Department of Healthcare and Family Services, *FY12 Budget Update: FY12 Medicaid Costs Less Than Expected*.
[166] Office of Governor Pat Quinn, *FY13 Medicaid Liability and Spending Reductions: Governor's Proposal to General Assembly*, April 19, 2012, p. 1.
[167] Illinois Hospital Association, *IHA Medicaid Savings* Alternatives, April 17, 2012.

million—was regarded as a victory by the Hospital Association because it averted the potential for additional cuts to reimbursement rates for hospitals and other healthcare providers.[168] In March 2013, HFS projected savings in that year of $150 million.[169]

At a legislative hearing on September 17, HFS officials said actual savings over a 12-month period would likely be in line with the original estimate of $120 million.[170] The screening effort has led to the removal of 128,700 enrollees but is expected to save less than the General Assembly hoped because those removed from the Medicaid program did not use many services, according to HFS. Of the first 105,000 enrollees dropped between April and August, 42,000, or 40%, had no Medicaid claims in the prior six months. Of the remaining 63,000 with claims, the average State savings was $58 per person per month, or a total of $44 million a year.

The pace of cancellations is expected to decline, HFS officials said, because enrollees deemed most likely to be ineligible were reviewed first. In addition, 75% of the cancelled cases involved clients who did not respond to a letter asking for additional information. Enrollees probably do not respond if they know they are not eligible or if they did not receive the letter, according to HFS. So far in calendar year 2013, more than 15% of cases that were cancelled have already applied again, found to be eligible and re-enrolled.

The outcome of the enhanced verification effort was further clouded by an arbitrator's decision in June 2013 that the State must cancel a contract with a private vendor hired to assist in verifying eligibility.[171] The arbitrator ruled that the State violated its labor agreement with AFSCME by failing to negotiate on the decision to use outside workers. The State said it will appeal the ruling, which states that the contract must be cancelled by December 31, 2013.[172]

Over the long term, HFS' strategy to hold down Medicaid costs depends on moving recipients to managed care, which is also called coordinated care. A Medicaid reform law enacted in 2011 requires that half of Medicaid recipients be enrolled in coordinated care by January 1, 2015.[173]

Illinois has historically lagged behind other states in the use of managed care for Medicaid enrollees. Only 213,417 Medicaid recipients in Illinois, or 7.7% of the total, were enrolled in comprehensive managed care in 2011, compared with a nationwide average of 51.0%.[174]

States are increasingly turning to managed care in an effort to control Medicaid costs and improve patient care. Doctors and hospitals have traditionally been paid on a fee-for-service basis, in which payment depends on the volume of services provided. In contrast, managed care is designed to reward

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168 Illinois Hospital Association, *2012 Legislative Report: An Extraordinary Legislative Session*, p. 5.
169 Illinois Department of Healthcare and Family Services, *SMART Act Implementation Status Report*, Senate Appropriations Committee hearing, March 19, 2013, p. 1.
170 Statement by Julie Hamos, Director of the Illinois Department of Healthcare and Family Services, Joint Hearing of the House Human Services Appropriations and Senate Appropriations I Committees, September 17, 2013. For more information, see Institute for Illinois' Fiscal Sustainability at the Civic Federation blog, http://www.civicfed.org/iifs/blog/update-eligibility-screening-medicaid.
171 Dean Olsen, "Future of Medicaid-eligibility contract in doubt," *State Journal Register*, July 29, 2013.
172 Statement by Julie Hamos, Director of the Illinois Department of Healthcare and Family Services, Joint Hearing of the House Human Services Appropriations and Senate Appropriations I Committees, September 17, 2013.
173 Public Act 96-1501.
174 Kaiser Family Foundation, *Medicaid Enrollment in Comprehensive Risk-Based Managed Care*, http://kff.org/medicaid/state-indicator/medicaid-enrollment-in-comprehensive-risk-based-managed-care/#table (last visited on September 15, 2013); Centers for Medicare and Medicaid Services, *2011 Medicaid Managed Care Enrollment Report: Summary Statistics as of July 1, 2011*, p. 1.

healthcare organizations for keeping patients healthy and avoiding unnecessary tests and procedures. Health maintenance organizations (HMOs), for example, receive a fixed monthly fee, known as a capitation rate, for each Medicaid enrollee.

Currently 286,692 Medicaid recipients, roughly 10% of the total, are enrolled in HMO-style managed care.[175] Most of these recipients joined HMOs voluntarily.[176] The State's first experiment with mandatory HMO-style managed care for Medicaid began in May 2011 and currently covers 39,487 elderly and disabled recipients in Northeastern Illinois, excluding Chicago. Seniors and people with disabilities account for 16% of the Medicaid population but incur 55% of Medicaid costs.[177]

HFS has issued a schedule that calls for approximately two million recipients, or two-thirds of total enrollees, to be covered by care coordination by the 2015 deadline.[178] The implementation has been delayed by several factors, including a decision by the General Assembly to give hospitals extra time to form their own networks to compete with HMOs.

The Illinois General Assembly required HFS to solicit proposals for the new networks as part of its approval of Medicaid expansion under the ACA.[179] The Medicaid expansion bill was passed by the Senate in February 2013 but was not approved by the House until May 27, after it was amended to include the new hospital networks and a new role for Institutions for Mental Diseases, nursing homes that specialize in treating the mentally ill.

The new hospital-based networks could serve as many as 1.5 million children and their families covered by Medicaid, as well as adults who are newly eligible under the ACA. HFS had originally intended to enroll those recipients in managed care beginning in January 2014, but the date has been pushed back to July 2014 to accommodate the new networks. In January 2014, the newly eligible recipients will now have a choice between traditional Medicaid and the managed care program CountyCare run by Cook County's public health system.

State Group Health Insurance

General Funds appropriations for the State Employees' Group Insurance Program decline by $104 million to $1.346 billion in FY2014 from $1.450 billion in FY2013. The reduction reflects savings projected by the State due to a new collective bargaining agreement with its largest union.

The State Employees' Group Insurance Program is expected to provide health insurance coverage for an estimated 365,066 participants in FY2014, including employees and retirees and their dependents.[180] The State offers both a traditional health insurance plan, which allows participants to

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[175]Illinois Department of Healthcare and Family Services, *Managed Care Enrollment*, http://www2.illinois.gov/hfs/ManagedCare/Pages/Enrollment.aspx (last visited on September 15, 2013).
[176] Illinois Department of Healthcare and Family Services, *Managed Care Enrollment* http://www2.illinois.gov/hfs/ManagedCare/Pages/Enrollment.aspx (last visited on September 15, 2013).
[177] Illinois Department of Healthcare and Family Services, *Care Coordination Roll-Out Plan: January 2013-January 2015*, November 29, 2012, http://www2.illinois.gov/hfs/SiteCollectionDocuments/CareCoorPlan.pdf (last visited on September 15, 2013).
[178] Illinois Department of Healthcare and Family Services, *Care Coordination Roll-Out Plan, January 2013-January 2015*, November 29, 2012.
[179] Public Act 98-0104, signed on July 22, 2013.
[180] Commission on Government Forecasting and Accountability, *FY2014 Liabilities of the State Employees' Group Health Insurance Program*, May 2013, p. 7. The program also provides life insurance at a relatively small cost to the State.

choose any doctor or hospital, and managed care plans such as HMOs, which generally restrict choices.[181]

The State paid the entire bill for retirees' health insurance premiums prior to 1998, when retirees with less than 20 years of service were required to start paying a portion of the costs.[182] The State continued to cover all premiums for those who had worked at least 20 years.[183]

General Assembly members and constitutional officers could retire with as few as four years of service and not pay any premiums, and judges could retire with as few as six years of service and not pay premiums.[184] Approximately 90% of the more than 80,000 retirees covered by the State's group insurance program did not pay any health insurance premiums as of January 2011.[185]

In June 2012, Illinois enacted legislation that eliminated premium-free health coverage for retirees.[186] The legislation did not specify how retiree health insurance premiums would be determined, leaving that decision to the State's Department of Central Management Services (CMS).

The State negotiated retiree health benefits with its largest union, the American Federation of State, County and Municipal Employees (AFSCME), during the collective bargaining process for a new contract to replace an agreement that expired on June 30, 2012. The new contract was not executed until May 2013, when union members ratified an initial vote taken in March.[187]

Administration officials have said that they are required to negotiate on retiree health insurance because State officials have followed that practice since the early 1990s.[188] The administration has cited a provision of the Illinois Public Labor Relations Act that requires collective bargaining with regard to matters that were previously the subject of labor negotiations.[189]

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[181] For more information on the State's group insurance program, see The Civic Federation, *State of Illinois Employee Health Insurance Plans: Analysis and Recommendations for Cost Containment*, April 16, 2007, http://www.civicfed.org/civic-federation/publications/state-illinois-employee-health-insurance-plans-analysis-and-recommenda.
[182] Public Act 90-065.
[183] Under the law, the State contributed 5% of the premium cost for each full year of service, up to a maximum of 100% for retirees with 20 or more years of service.
[184] General Assembly members elected before January 1, 2011 can retire at age 62 with four years of service; those elected on or after that date must be 67 with eight years of service. Judges elected or appointed before January 1, 2011 can retire at 62 with six years of service; judges elected or appointed on or after that date must be 67 with eight years of service.
[185] Commission on Government Forecasting and Accountability, *Request for Proposals to Provide Consulting Services*, February 17, 2011, p. 2.
[186] Public Act 97-0695.
[187] AFSCME Council 31, *State contract ratification affirmed*, May 17, 2013, http://www.afscme31.org/news/state-contract-ratification-is-affirmed (last visited on September 17, 2013).
[188] Communication between the Civic Federation and the Governor's Office of Management and Budget, March 6, 2013.
[189] 5 ILCS 315/4.

The next table shows health insurance savings expected from the new three-year contract, as summarized by CMS in April 2013. As shown in the table, the State expects savings of $903 million from the contract, including $354 million in FY2014. It should be noted that these savings are expected to be partially offset by wage increases.

State of Illinois Health Projected Health Savings Due to AFSCME Contract: FY2013-FY2015 (in $ millions)				
	FY2013	FY2014	FY2015	All Years
Plan Design	$ -	$ (52)	$ (86)	$ (138)
Employee Contributions	$ -	$ (111)	$ (124)	$ (235)
Retiree Contributions	$ -	$ (64)	$ (64)	$ (128)
Maximum Reimbursable Charge[1]	$ -	$ (10)	$ -	$ (10)
Medicare Advantage[2]	$ -	$ (58)	$ (174)	$ (232)
Medicare Coordination[3]	$ -	$ (34)	$ -	$ (34)
SERS Opt Out[4]	$ -	$ (25)	$ (13)	$ (38)
Wellness	$ -	$ -	$ (53)	$ (53)
Insurance Committee Initiatives	$ -	$ -	$ (35)	$ (35)
Total	**$ -**	**$ (354)**	**$ (549)**	**$ (903)**

[1]Change in methodology for computing reimbursement for out-of-network services.

[2]The FY2015 savings for Medicare Advantage includes $58 milliion in FY2016.

[3]Effective July 1, 2013, the State will no longer pay 100% of the claim balance of medical claims after Medicare pays its portion for a plan participant enrolled in QCHP. Medicare primary participants will be subject to standard benefit deductibles and coinsurance for services after Medicare pays.

[4]Retirees not eligible for Medicare who opt out of the State plan for other coverage receive $500 a month.

Source: Illinois Department of Central Management Services, Submission to General Assembly's Commission on Government Forecasting and Accountability, April 16, 2013.

According to the data presented by CMS, projected State savings due to retiree contributions total $128 million. Under the new contract, retirees who are eligible for Medicare will pay 1% of their pension toward health insurance beginning July 1, 2013 and another 1% beginning July 1, 2014.[190] Retirees not eligible for Medicare, who are more expensive for the State to cover, will contribute 2% of their pensions on July 1, 2013, and another 2% starting on July 1, 2014. Although retirees who are not eligible for Medicare will pay a larger share of their pensions, retiree payments are not based on the cost of the health insurance.

Retirees will also pay $34 million more in deductibles and coinsurance because of Medicare coordination, under which the State will stop paying 100% of the claim balance of medical claims for the State's traditional insurance plan after Medicare pays its portion.[191] The State expects to save $38 million by giving retirees not eligible for Medicare a $500 a month incentive to opt out of the State group health insurance plan and get other coverage.

A substantial portion of the projected savings—$232 million—is expected to come from enrolling Medicare-eligible retirees in a Medicare Advantage plan. Medicare Advantage plans are offered by private companies that contract with the federal government to provide Medicare benefits. In addition to Medicare benefits, the Medicare Advantage plan would provide State retirees with supplemental

[190] Doug Finke, "AFSCME ratifies contract with Quinn administration," *State Journal-Register*, March 20, 2013.
[191] State of Illinois, Department of Central Management Services, *Benefit Choice Options*, State of Illinois, Enrollment Period May 1 – May 31, 2013. p.5.

benefits similar to those offered by the State group insurance plan. CMS expects to have contracts in place for new Medicare plans to begin on January 1, 2014.[192]

The FY2014 budget includes total appropriations of $2.939 billion for State group insurance, including General Funds appropriations of $1.346 billion. In addition to General Funds, resources for the program come from the State's Road Fund, State universities, member contributions and other sources.

The next table shows group health insurance expenditures for FY2010 through FY2012, estimated expenditures for FY2013 and enacted appropriations for FY2014. The FY2014 General Funds appropriation of $1.346 billion represents a decrease of 7.2% from $1.450 billion in FY2013. [193] The FY2013 appropriation was increased by $350 million because savings expected from the new AFSCME contract were delayed until FY2014.[194]

State of Illinois Group Insurance Expenditures and Appropriations: FY2010-FY2014 (in $ millions)*

	FY2010 Actual	FY2011 Actual	FY2012 Actual	FY2013 Est.	FY2014 Enacted
General Funds	$ 1,146	$ 885	$ 1,436	$ 1,450	$ 1,346
Other State Funds**	$ 833	$ 1,084	$ 1,001	$ 1,237	$ 1,593
Total	**$ 1,979**	**$ 1,969**	**$ 2,437**	**$ 2,687**	**$ 2,939**

*Includes health insurance and life insurance.

**Other State Funds appropriations are adjusted to avoid double counting.

Source: Public Act 98-0017; Illinois State FY2013 Budget, p. 2-31 and p. 5-67; Illinois State FY2012 Budget, p. 2-26 and p. 11-72.

Group health insurance bills, like Medicaid bills, are covered by the Section 25 exception to the State Finance Act that allows prior years' bills to be paid from future years' appropriations.[195] Unpaid group health insurance bills rose sharply starting in FY2009, when deferral of Medicaid bills began to be restricted by federal stimulus legislation.[196] A new law that imposes limitations on the deferral of Medicaid bills does not cover health insurance bills.[197] Based on projected savings, the FY2014 budget assumes that the program will be adequately funded in FY2014 and that unpaid bills will not grow.

The FY2014 budget does not provide funding to pay down the $1.5 billion backlog at the end of FY2013. As a result of insufficient funds, healthcare providers for State employees are currently waiting as long as 385 days to be paid, according to COGFA.[198] The payment delay is expected to increase to as much as 413 days in FY2014.

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[192] State of Illinois, Request for Proposal, Illinois Department of Central Management Services, Medicare Plans, #22030665, published on June 27, 2013 and closed on July 19, 2013.

[193] Appropriations in the table, as in the budget, include both health insurance and life insurance. Health insurance appropriations in FY2014 total $2.71 billion, including $1.33 billion in General Funds appropriations and $1.38 billion in net Other State Funds appropriations.

[194] Public Act 98-0017, signed on June 5, 2013.

[195] 30 ILCS 105/25 (b-4).

[196] Illinois State Comptroller, "The State Fiscal Crisis—How Did We Get Here?" *Fiscal Focus*, September 2011, p.7. The American Recovery and Reinvestment Act of 2009 required that many Medicaid healthcare providers be paid within 30 days.

[197] Public Act 97-0691.

[198] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p. 71.

The State also makes General Funds contributions to the Teachers' Retirement Insurance Program (TRIP) and the College Insurance Program (CIP) to cover retired teachers outside Chicago and downstate retired community college employees. Retirees in TRIP and CIP have been required to pay premiums.

The State is required by law to contribute specific annual amounts to TRIP and CIP, as certified by the Teachers' Retirement System and the State Universities Retirement System.[199] Those amounts are $90.4 million and $4.4 million, respectively, in FY2014.

The enacted FY2014 budget includes only $62.6 million for TRIP and has no appropriation for the contribution to CIP.[200] However, these contributions are covered by continuing appropriation, meaning that the full required contribution will continue to be paid.[201]

Personnel

The Governor's FY2014 budget proposed an increase of 914 full-time equivalent positions (FTEs) at agencies under his control. As shown in the next table, that represented a 1.7% increase to 53,172 FTEs at the end of FY2014 from an estimated 52,258 at the end of FY2013.

State of Illinois Full-Time Equivalent Positions at Governor's Agencies
FY2010-FY2014

Agency Group	FY2010 Actual	FY2011 Actual	FY2012 Actual	FY2013 Est.	FY2014 Target	2-Year Change	2-Year % Change
Human Services	21,511	21,682	20,165	20,798	20,990	192	0.9%
Healthcare	2,311	2,241	2,083	2,409	2,466	57	2.4%
Public Safety	22,289	22,580	21,412	21,789	22,118	329	1.5%
Government Services	3,850	3,799	3,545	3,939	4,069	130	3.3%
Environment and Culture	1,454	1,425	1,295	1,356	1,541	185	13.6%
Economic Development	1,220	1,178	1,082	1,119	1,137	18	1.6%
Education*	872	810	788	848	851	3	0.4%
Total	**53,507**	**53,715**	**50,370**	**52,258**	**53,172**	**914**	**1.7%**

*Includes the Illinois State Board of Education, the Illinois Board of Higher Education, the Illinois Community College Board and the Illinois Student Assistance Commission.

Source: Illinois State FY2014 Budget, p. 2-18; Email communication between Civic Federation and Governor's Office of Management and Budget, April 30, 2013.

The proposed increase in headcount appears unlikely because the FY2014 budget passed by the General Assembly reduces the operational appropriations for many agencies from the Governor's recommended levels. At the same time, agencies including the Department of Human Services received appropriations for day-to-day operations in the form of lump sums.[202] Lump sum appropriations do not identify specific funding purposes, such as employee salaries, by line item.

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[199] 5 ILCS 375/6.6(c) and 5 ILCS 375 6.10(c).
[200] Public Act 98-0064, signed on July 10, 2013.
[201] 40 ILCS 15/1.3 and 40 ILCS 15/1.4.
[202] Other agencies with lump sum appropriations for operations include the State Board of Education, the Department on Aging, the Department of Veterans' Affairs, the Department of Central Management Services, the Department of Commerce and Economic Opportunity, the Department of Employment Security, the Department of Natural Resources, the Illinois Supreme Court and the Department of State Police. For more information, see Illinois Senate Republicans, *2013 at a Glance: An Overview of the 2013 Spring Session*, http://www.senategop.state.il.us/Portals/0/Senate-Action/At%20a%20Glance-Web_Budget-2.pdf (last visited on September 10, 2013).

Approximately 90% of State employees are covered by collective bargaining agreements.[203] Because the new AFSCME contract negotiated by the Governor included wage increases of approximately $140 million in FY2014, agencies were expected to stay within their budgets by reducing headcount, possibly through attrition.[204]

The following table shows wage-related provisions of the new three-year contract, as summarized by the Department of Central Management Services. According to the administration's analysis, total wage-related increases of $222 million will be offset by the savings of $903 million on group health insurance discussed previously, resulting in net savings of $681 million.

State of Illinois Budget Impact of Wage Changes in AFSCME Contract: FY2013-FY2015 (in $ millions)				
	FY2013	FY2014	FY2015	Total
COLA*	$ -	$ 49	$ 50	$ 99
Step Increases	$ 22	$ 22	$ 22	$ 66
Sub Steps	$ (2)	$ (10)	$ (10)	$ (22)
Pay Parity	$ -	$ 74	$ -	$ 74
Longevity pay increase**	$ -	$ 5	$ -	$ 5
Total	**$ 20**	**$ 140**	**$ 62**	**$ 222**

*The cost of living adjustment is 0% in FY2013, 2% in FY2014 and 2% in FY2015.

**The longevity pay increase is $25 per month.

Source: Illinois Department of Central Management Services, Submission to General Assembly's Commission on Government Forecasting and Accountability, April 16, 2013.

The major wage-related provisions include 2% cost of living adjustments in FY2014 and FY2015; a "pay parity" adjustment in FY2014 to bring employees up to the wage level they would have reached under the previous contract; and step increases (based on years of experience). The agreement also includes some savings due to lower starting wages for new employees.

The table above does not include the payment of back wages owed from a previous contract. On July 1, 2011, Governor Quinn cancelled all scheduled FY2012 raises for employees in 14 agencies, citing inadequate appropriations by the General Assembly. AFSCME filed a lawsuit in Cook County Circuit Court, challenging the State's failure to pay the negotiated increase, and the court ruled in the union's favor in December 2012.[205]

The State appealed the ruling, but the Governor agreed as part of the contract negotiations to drop the appeal and seek a supplemental appropriation to pay the back wages. A bill to cover the back pay and related federal payroll taxes owed was introduced in the General Assembly but not approved by the legislature.[206] However, the Illinois Attorney General's Office is still pursuing the appeal.[207] According to the Governor's Office, the total amount owed is approximately $111 million.[208]

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[203] State of Illinois, General Obligation Bonds, Series "A of April 2013 and Taxable Series B of April 2013, *Official Statement*, April 2, 2013, p. 12.

[204] Council 31 AFSCME, "Where things stand in Springfield," July 19, 2013, http://www.afscme31.org/news/where-things-stand-in-springfield (last visited on August 13, 2013).

[205] Doug Finke, "Judge orders Quinn to honor state employee raises," *State Journal-Register*, December 7, 2012.

[206] 98th Illinois General Assembly, House Bill 212, House Amendment 2, filed May 2, 2013. The bill includes $154.9 million in back wages and $11.9 million in federal payroll taxes related to the back wages.

[207] Communication between the Civic Federation and the Illinois Attorney General's Office, September 27, 2013.

[208] Communication between the Civic Federation and the Governor's Office of Management and Budget, September 30, 2013.

General Funds Expenditures

Expenditures from General Funds consist of net appropriations spent and statutory transfers out. General Funds are diverted or transferred out to Other State Funds to make debt service payments on bonds and for a wide range of other legislatively required purposes.

The next table shows General Funds expenditures from FY2010 to FY2014. Expenditures in FY2014 are projected at $35.7 billion: net appropriations spent of $30.65 billion and total transfers out of $5.06 billion, including $2.88 billion of legislatively required transfers and $2.18 billion of debt-related transfers. General Funds expenditures increase by $155 million, or 0.4%, from $35.56 billion in FY2013. Over the last five years, expenditures increase by $2.46 billion, or 7.4%, from $33.25 billion in FY2010.

State of Illinois General Funds Expenditures for Current Services: FY2013-FY2014 (in $ millions)

	FY2013 Revised	FY2014 Rec.	FY2014 Enacted	$ Change FY2014 Enacted-FY2013	% Change FY2014 Enacted-FY2013	$ Change FY2014 Enacted-FY2014 Rec.	% Change FY2014 Enacted-FY2014 Rec.
Agency Appropriations*	$ 24,255	$ 23,841	$ 23,819	$ (436)	-1.8%	$ (22)	-0.1%
Less Appropriations for Prior Bills	$ (643)	$ (312)	$ (50)	$ 593	-92.2%	$ 262	-84.0%
Less Unspent Appropriations	$ (300)	$ (500)	$ (500)	$ (200)	66.7%	$ -	0.0%
Net Agency Appropriations Spent for Current Services	$ 23,312	$ 23,029	$ 23,269	$ (43)	-0.2%	$ 240	1.0%
Pension Contributions	$ 5,107	$ 6,036	$ 5,988	$ 881	17.3%	$ (48)	-0.8%
Group Insurance	$ 1,450	$ 1,346	$ 1,346	$ (104)	-7.2%	$ -	0.0%
Total Appropriations Spent for Current Services	**$ 29,869**	**$ 30,411**	**$ 30,603**	**$ 734**	2.5%	$ 192	0.6%
Statutory Transfers Out							
Legislatively Required Transfers	$ 2,840	$ 2,716	$ 2,878	$ 38	1.3%	$ 162	6.0%
Less Transfers for Prior Bills	$ (500)	$ (250)	$ (250)	$ 250	-50.0%	$ -	0.0%
Debt Service on Pension Bonds	$ 1,552	$ 1,655	$ 1,655	$ 103	6.6%	$ -	0.0%
Other Debt Service	$ 654	$ 527	$ 527	$ (127)	-19.4%	$ -	0.0%
Total Transfers Out for Current Services	**$ 4,546**	**$ 4,648**	**$ 4,810**	$ 264	5.8%	$ 162	3.5%
Total	**$ 34,415**	**$ 35,059**	**$ 35,413**	**$ 998**	**2.9%**	**$ 354**	**1.0%**

*FY2014 agency appropriations include a $27.8 million continuing appropriation for Teachers' Retirement Insurance Program and a $1 million appropriation to the Illinois Department of Public Health relating to regulation of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.

Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, pp. 16-17; Illinois State FY2014 Budget, pp. 2-16 to 2-17 and p. 2-29; Communications between Civic Federation and Governor's Office of Management and Budget, July 25 and August 1, 2013; Public Act 98-0017, pp. 2 and 90.

In both periods, increases in pension costs offset declines in agency appropriations spent. Pension contributions increase by $881 million from FY2013 to FY2014, while net agency spending declines by $636 million. Between FY2010 and FY2014, a decrease of $993 million in net agency appropriations is more than offset by an increase of $3.6 billion in pension-related costs, including both pension contributions and payments on pension bonds. Legislatively required transfers increase by $871 million from FY2010 to FY2014.

Debt service payments on pension bonds are transferred out of General Funds along with debt service payments on other borrowings and legislatively required transfers.[209] In FY2003 the State sold $10 billion in General Obligation pension bonds, of which $7.3 billion was used to reduce the retirement systems' unfunded liability and roughly $2.2 billion was used for statutory required contributions in FY2003 and FY2004. The State also issued a total of $7.2 billion of pension bonds in FY2010 and

[209] For more information on pension bond payments, see p. 57 of this report.

FY2011 to pay for required General Funds contributions. Debt service on pension bonds increases by $1.1 billion, or 193.4%, to $1.7 billion in FY2014 from $564 million in FY2010.

Additional debt service transfers are made to pay for bonds backing capital projects and to repay borrowing from Other State Funds. Debt service transfers for capital projects are approximately flat at $527 million in FY2014. The FY2013 budget included $132 million to make the final repayment on interfund borrowing in FY2011.

General Funds are also used for a wide range of legislatively required transfers to Other State Funds—from funding mass transit to supporting the Lincoln Presidential Library in Springfield to promoting thoroughbred racing.

The following table shows legislatively required transfers out of General Funds for FY2011 through FY2014. Legislatively required transfers increase by $38 million from $2.84 million in FY2013 to $2.88 billion in FY2014. The transfers have grown by $886 million, or 44.5%, from $2.4 billion in FY2011, largely due to increased transfers to the Healthcare Provider Relief Fund, which funds Medicaid. A portion of the Medicaid transfers—$500 million in FY2013 and $250 million in FY2014—are for the payment of outstanding bills.

State of Illinois Legislatively Required General Funds Transfers Out by Fund: FY2011-FY2014 (in $ millions)

Fund	FY2011 Actual	FY2012 Actual	FY2013 Actual	FY2014 Rec.	FY2014 Projected
Local Government Distributive	$ 1,013	$ 1,095	$ 1,204	$ 1,095	$ 1,163
Healthcare Provider Relief	$ 365	$ 160	$ 500	$ 601	$ 601
Public Transportation	$ 407	$ 438	$ 483	$ 438	$ 470
Downstate Public Transportation	$ 169	$ 170	$ 209	$ 170	$ 215
FY12 Hospital Relief	$ -	$ 140	$ -	$ -	$ -
Workers' Compensation Revolving	$ 55	$ 100	$ 101	$ 75	$ 81
School Infrastructure	$ 68	$ 65	$ 84	$ 64	$ 64
Tourism Promotion	$ 40	$ 30	$ 42	$ 46	$ 46
University of Illinois Hospital Services	$ 45	$ 45	$ 45	$ 45	$ 45
Metropolitan Exposition, Auditorium and Office Building	$ 38	$ 38	$ 38	$ 38	$ 38
Agricultural Premium	$ 24	$ 24	$ 24	$ 24	$ 24
Live and Learn	$ 21	$ 21	$ 21	$ 21	$ 21
Audit Expense	$ 18	$ 18	$ 16	$ 19	$ 19
DCFS Children's Services	$ 17	$ -	$ -	$ -	$ -
Capital Litigation Trust	$ 15	$ 7	$ -	$ -	$ -
Estate Tax Collection Distributive	$ 9	$ 12	$ 4	$ -	$ -
Metropolitan Pier and Exposition Authority Incentive	$ -	$ -	$ 15	$ 15	$ 15
Presidential Library and Museum	$ 7	$ 8	$ -	$ 10	$ 10
Partners for Conservation	$ 14	$ 12	$ 14	$ -	$ 14
All Others	$ 73	$ 90	$ 40	$ 55	$ 52
Total	**$ 2,398**	**$ 2,473**	**$ 2,840**	**$ 2,716**	**$ 2,878**

Source: Illinois State FY2014 Budget, pp. 2-62 to 2-63; Communication between Civic Federation and Governor's Office of Management and Budget, August 1, 2013.

The Governor had proposed reducing legislatively required transfers to $2.7 billion in FY2014 by capping transfers for local governments and statewide public transportation at the FY2012 levels. State savings were estimated at $143 million, based on the difference between the proposed FY2014 payment and the projected payment under current law.[210] The General Assembly did not approve the statutory changes required to enact the proposed caps.

The Local Government Distributive Fund is projected to receive $1.163 billion in FY2014, or 40.4% of all such transfers. That is an increase of $68 million from the Governor's recommendation of $1.095 billion.

The Local Government Distributive Fund receives the share of State income tax proceeds that is distributed to local governments. The share had been 10% but was lowered in January 2011 after the State temporarily increased income tax rates so that the State could get the full benefit of the tax increase. Local governments currently receive 6% of individual income tax revenues and 6.86% of corporate income tax revenues.

Led by the Illinois Municipal League, local governments strongly opposed the Governor's recommended reduction in revenue.[211] They pointed out that the amount of State income taxes shared with local governments remains below its pre-recession level of $1.208 billion in FY2008.[212]

The Governor had also proposed capping transfers to the Public Transportation and Downstate Public Transportation Funds at the FY2012 level in FY2014. These funds receive money under various State sales tax acts and distribute it to the Regional Transportation Authority (RTA) and to local mass transit districts outside of the boundaries of the RTA. The enacted transfer to the Public Transportation Fund is $470 million, $32 million above the Governor's recommendation. The FY2014 transfer to the Downstate Public Transportation Fund is $215 million, an increase of $45 million from the Governor's proposal.

Excluding funds used to pay outstanding bills, General Funds expenditures for current-year services in the enacted FY2014 budget are $354 million above the amount recommended in the Governor's FY2014 budget proposal. The Governor's proposal included appropriations of approximately $312 million to pay accumulated bills, while the enacted budget includes $50 million for bill payment. Due to the April Surprise, bills to be paid in FY2014 under the Governor's budget were instead paid in FY2013. The enacted budget also includes $162 million more in transfers out than the Governor's proposal. Both the Governor's recommended budget and the enacted budget include transfers out in FY2014 to pay Medicaid bills.

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[210] State of Illinois, General Obligation Bonds, Series A of April 2013 and Taxable Series B of April 2013, *Official Statement*, April 2, 2013, p. 29.

[211] Illinois Municipal League, "LGDF Threat Update," March 8, 2013, http://legislative.iml.org/page.cfm?key=10051 (last visited on April 30, 2013).

[212] Illinois Department of Revenue, Income Tax and Local Use Tax, http://www.revenue.state.il.us/LocalGovernment/Disbursements/IncomeUse/income.htm. (last visited on September 15, 2013).

The next table shows General Funds expenditures for current-year services in the Governor's FY2014 budget proposal and the enacted FY2014 budget. Expenditures for current-year services are calculated by subtracting expenditures for payment of outstanding bills from total expenditures.

State of Illinois General Funds Expenditures for Current Services: Recommended FY2014-Enacted FY2014 (in $ millions)				
	FY2014 Rec.	**FY2014 Enacted**	**$ Change**	**% Change**
Agency Appropriations*	$ 23,841	$ 23,819	$ (22)	-0.1%
Less Appropriations for Prior Bills	$ (312)	$ (50)	$ 262	-84.0%
Less Unspent Appropriations	$ (500)	$ (500)	$ -	0.0%
Net Agency Appropriations Spent for Current Services	$ 23,029	$ 23,269	$ 240	1.0%
Pension Contributions	$ 6,036	$ 5,988	$ (48)	-0.8%
Group Insurance	$ 1,346	$ 1,346	$ -	0.0%
Total Appropriations Spent for Current Services	**$ 30,411**	**$ 30,603**	**$ 192**	**0.6%**
Statutory Transfers Out				
Legislatively Required Transfers	$ 2,716	$ 2,878	$ 162	6.0%
Less Transfers for Prior Bills	$ (250)	$ (250)	$ -	0.0%
Debt Service on Pension Bonds	$ 1,655	$ 1,655	$ -	0.0%
Other Debt Service	$ 527	$ 527	$ -	0.0%
Total Transfers Out for Current Services	**$ 4,648**	**$ 4,810**	$ 162	3.5%
Total	**$ 35,059**	**$ 35,413**	**$ 354**	**1.0%**

*FY2014 agency appropriations include $27.8 million continuing appropriation for Teachers' Retirement Insurance Program and $1 million appropriation to the Illinois Department of Public Health relating to regulation of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.

Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, pp. 16-17; Illinois State FY2014 Budget, pp. 2-16 to 2-17 and p. 2-29; Communications between Civic Federation and Governor's Office of Management and Budget, July 25 and August 1, 2013; Public Act 98-0017, pp. 2 and 90.

BUDGET DEFICIT AND UNPAID BILLS

The FY2014 budget results in a projected total General Funds deficit of $4.2 billion. The total deficit is the sum of the operating deficit and the accumulated deficit from prior years.

The State has recently dealt with deficits by delaying payments to vendors and local governments and paying those bills from next year's revenues. In addition, the State has masked deficits by incurring costs but not appropriating required funds until the next year. Total General Funds payables and other liabilities are roughly estimated at $5.8 billion at the end of FY2014.

It is important to note that the actual budget deficit at the end of FY2014 is likely to vary from the projection due to fluctuations in revenues and supplemental appropriations enacted during the year. Year-end General Funds payables and other liabilities should similarly be regarded as rough estimates, presented to show the approximate magnitude of State obligations and their general trend.

Budget Deficit

The FY2014 budget is approximately balanced, compared with an estimated surplus of $770 million in FY2013. Total operating revenues decline by $621 million from FY2013, while total operating expenditures increase by $155 million. State revenues in FY2014 are not bolstered by an unexpected influx of income tax collections, as they were in April FY2013. Increased FY2014 pension costs offset decreased agency spending.

The total deficit is virtually unchanged at $4.2 billion in FY2014. The State carried over to FY2014 $4.2 billion in unpaid bills accumulated from prior years.

The following table shows the General Funds deficit for FY2010, estimated FY2013 and recommended and enacted FY2014.

State of Illinois Budget: FY2010-FY2014 (in $ millions)	FY2010 Actual	FY2013 Revised[1]	FY2014 Rec.	FY2014 Enacted	2-Year $ Change	2-Year % Change
State Tax Revenues	$ 19,287	$ 30,206	$ 29,524	$ 29,331	$ (875)	-2.9%
State Transfers In	$ 2,159	$ 1,968	$ 1,928	$ 2,198	$ 230	11.7%
Total State Revenues	**$ 21,446**	**$ 32,174**	**$ 31,452**	**$ 31,529**	**$ (645)**	**-2.0%**
Federal Revenues	**$ 5,920**	**$ 4,154**	**$ 4,178**	**$ 4,178**	**$ 24**	**0.6%**
Total Operating Revenues	**$ 27,366**	**$ 36,328**	**$ 35,630**	**$ 35,707**	**$ (621)**	**-1.7%**
Agency Appropriations[2]	$ 25,208	$ 24,255	$ 23,841	$ 23,819	$ (436)	-1.8%
Less Unspent Appropriations	$ (896)	$ (300)	$ (500)	$ (500)	$ (200)	66.7%
Net Agency Appropriations Spent	$ 24,312	$ 23,955	$ 23,341	$ 23,319	$ (636)	-2.7%
Pension Contributions[3]	$ 3,466	$ 5,107	$ 6,036	$ 5,988	$ 881	17.3%
Group Insurance	$ 1,146	$ 1,450	$ 1,346	$ 1,346	$ (104)	-7.2%
Total Appropriations	**$ 28,924**	**$ 30,512**	**$ 30,723**	**$ 30,653**	**$ 141**	**0.5%**
Statutory Transfers Out						
Legislatively Required Transfers	$ 2,007	$ 2,840	$ 2,716	$ 2,878	$ 38	1.3%
Debt Service on Pension Bonds	$ 564	$ 1,552	$ 1,655	$ 1,655	$ 103	6.6%
Other Debt Service and Transfers Out[4]	$ 1,759	$ 654	$ 527	$ 527	$ (127)	-19.4%
Total Transfers Out	**$ 4,330**	**$ 5,046**	**$ 4,898**	**$ 5,060**	**$ 14**	**0.3%**
Total Operating Expenditures	**$ 33,254**	**$ 35,558**	**$ 35,621**	**$ 35,713**	**$ 155**	**0.4%**
Operating Surplus (Deficit)	**$ (5,888)**	**$ 770**	**$ 9**	**$ (6)**	**$ (776)**	**-100.8%**
Borrowing for Operations	$3,466	$ -	$ -	$ -	$ -	na
Operating Surplus (Deficit) After Borrowing	$ (2,422)	$ 770	$ 9	$ (6)	$ (776)	-100.8%
Accumulated Deficit from Prior Years	$ (3,673)	$ (4,984)	$ (4,491)	$ (4,214)	$ 770	-15.4%
Total Deficit	**$ (6,095)**	**$ (4,214)**	**$ (4,482)**	**$ (4,220)**	**$ (6)**	**0.1%**

[1]As of August 2013 for revenues and June 2013 for expenditures.
[2]FY2014 agency appropriations include $27.8 million continuing appropriation for Teachers' Retirement Insurance Program and $1 million appropriation to the Illinois Department of Public Health relating to the legalization of medical marijuana pursuant to Public Act 98-0122, enacted on August 1, 2013.
[3]Pension contributions in FY2010 and FY2011 were made by issuance of pension obligation bonds.
[4]Includes interfund borrowing repayment and Budget Stabilization Fund repayment. Interest on short-term borrowing in FY2010 includes $1.0 billion to repay failure of revenue borrowing in FY2009.
Source: State of Illinois, General Obligation Bonds, Series of September 2012, *Official Statement*, September 13, 2012, pp. 8-9; State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, pp. 16-17; Illinois State FY2014 Budget, pp. 2-16 to 2-17 and p. 2-29; Illinois State FY2013 Budget, p. 2-13; Illinois State FY2012 Budget, p. 2-26; Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2014, p. 25; Communications between Civic Federation and Governor's Office of Management and Budget, July 25, and August 1, 2013; Public Act 98-0017, pp. 2 and 90.

Unpaid Bills

From FY2009 through FY2011, the State relied on borrowing to help close the operating deficit. The borrowing included the sale of pension bonds to pay for General Funds pension contributions in FY2010 and FY2011. The FY2012 and FY2013 budgets and the enacted FY2014 budget do not rely on borrowing for operations.

Illinois has dealt with its General Funds deficit by delaying payments to vendors, social service agencies, school districts and other units of government and paying those bills from the next year's revenue. In general, Section 25 of the State Finance Act requires that bills incurred in a given year be paid out of that year's appropriation.[213]

There is a lapse period, which has typically lasted two months, during which next year's revenues may be used to pay this year's bills. This lapse period was extended to six months—through December 31—in FY2010, FY2011 and FY2012 due to the large amount of outstanding bills on June 30.

[213] 30 ILCS 105/25.

Beginning in FY2013, the law permanently grants the Comptroller's office up to six months to pay bills, although the bills are to be paid as soon as practical after the close of the fiscal year.[214]

The Section 25 deadline for paying bills does not apply to Medicaid bills, State group health insurance claims and certain other State bills. Under exceptions to Section 25, these liabilities can be paid from future years' appropriations. This has allowed the State to mask budget deficits by appropriating an insufficient amount to cover Medicaid and group health insurance costs in one year, knowing that remaining bills could be paid in the next year. The ability to defer Medicaid bills in this way was curtailed by legislation enacted in 2012.[215] The new law limited Section 25 liabilities incurred by the State's principal Medicaid agency, the Illinois Department of Healthcare and Family Services, to $700 million in FY2013 and $100 million thereafter, with certain exceptions.[216] Group health insurance liabilities were not limited by the new law.

Another General Funds liability that does not appear in the budget involves the Community Care Program in the Illinois Department on Aging, which is designed to allow seniors to stay out of nursing homes. Obligations of the Department on Aging have not been Section 25 liabilities, but in recent years the State's annual appropriation bills have allowed the program's prior year costs to be paid for out of the current year's funding. [217] This language has allowed the State to budget expenditures in a given year that are below expected costs in order to help balance the budget. An amendment to Section 25 of the State Finance Act in 2013 authorized the Department on Aging to pay up to $150 million of prior year costs of the Community Care Program from FY2014 appropriations.[218]

In recent years the State has also accumulated unpaid income tax refunds, an additional General Funds liability that is not included in the budget. Unpaid income tax refunds, primarily owed to businesses, peaked at $735 million at the end of FY2010. Only $45 million in approved but unpaid income tax refunds were on hand at the end of FY2013.[219]

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[214] 30 ILCS 105/25(m).
[215] Public Act 97-691.
[216] The exceptions relate to bills incurred by the end of the fiscal year but not received until after June 30.
[217] Public Act 97-0730.
[218] Public Act 98-0008, signed on May 3, 2013.
[219] Communication between the Civic Federation and the Illinois Department of Revenue, September 12, 2013.

The next table shows unpaid bills and other General Funds liabilities from FY2012 to FY2014. The backlog of bills declines by an estimated $2.9 billion from $8.8 billion at the end of FY2012 to $5.8 billion at the end of FY2014.

State of Illinois Unpaid Bills Backlog on June 30: FY2012-FY2014 (in $ millions)*				
	FY2012 Prelim.	**FY2013 Est.***	**FY2013 Revised****	**FY2014 Est.****
General Funds Accounts Payable	**$ (5,024)**	**$ (4,724)**	**$ (4,254)**	**$ (4,260)**
Other General Funds Liabilities				
HFS Medicaid	$ (2,100)	$ (500)	$ (500)	$ -
Department of Human Services	$ (201)	$ (321)	$ -	$ -
Department on Aging	$ (178)	$ (145)	$ -	$ -
Group Health Insurance	$ (1,182)	$ (1,894)	$ (1,540)	$ (1,540)
Income Tax Refunds	$ (72)	$-	$ (45)	na
Total Other General Funds Liabilities	**$ (3,733)**	**$ (2,860)**	**$ (2,085)**	**$ (1,540)**
Total	**$ (8,757)**	**$ (7,584)**	**$ (6,339)**	**$ (5,800)**

*As of March 2013.

**As of July 2013.

Source: Civic Federation calculations based on: Illinois State FY2014 Budget, pp. 2-16 to 2-17; Communications between Civic Federation and Governor's Office of Management and Budget, April 12 and July 26, 2013; Communication between Civic Federation and Illinois Department of Revenue, September 12, 2013.

The decrease in unpaid bills from FY2012 to FY2013 resulted partly from the surge in income tax collections in April 2013. The FY2013 budget also allocated $1.1 billion in General Funds revenues to pay down bills, much of which was related to Medicaid spending and resulted in twice the amount of resources after federal reimbursements.

The Governor's Office projects that Medicaid-related programs will be adequately funded in FY2014 and that there will be no growth in group health insurance bills due to savings from the State's new three-year contract with the American Federation of State, County and Municipal Employees (AFSCME). The FY2014 budget does not provide funding to pay off the backlog of healthcare bills, which is estimated at $1.5 billion.

The table above does not include back wages owed to union employees as a result of a dispute over cancelled wages. Although a judge ordered the State to pay the back wages and the Governor agreed to make the payments as part of contract negotiations with AFSCME, the ruling is being appealed by the Attorney General's Office. The total amount owed is approximately $111 million, according to the Governor's Office.[220]

[220] Communication between the Civic Federation and the Governor's Office of Management and Budget, September 30, 2013. The $111 million includes both back wages and related federal payroll taxes. Legislation pending in the General Assembly (98th Illinois General Assembly, House Bill 212, House Amendment 2, filed May 2, 2013) shows the total owed at $166.8 million, but a portion of that amount has been paid since the bill was filed.

DEBT BURDEN AND RATINGS

In FY2014 the State of Illinois will pay debt service totaling $3.5 billion due on $31.0 billion of outstanding bonded debt as of July 1, 2013.[221] The State currently owes $16.7 billion in interest on these bonds through FY2039 for a total outstanding debt service cost of $47.7 billion.

Although the total debt service represents the entire annual payment due to bond holders during the fiscal year, only a portion of the repayment is made through a transfer from the General Funds. The remaining amounts are paid through transfers from Other State Funds that are funded through separate designated revenue sources. The General Funds transfer for FY2014 totals $2.2 billion, or 7.0% of State-source General Funds resources.

Total outstanding debt and amounts owed to bondholders may change throughout the year as the State continues to make payments, issue new bonds or refinance outstanding debt. The FY2014 amounts discussed in this section are as of July 1, 2013, the beginning of the fiscal year.

Total Debt

The State is authorized under the General Obligation Bond Act to issue bonds to fund a variety of capital investments including roads, schools, mass transit, environmental projects and other facilities.[222] In 2003 the State amended the act to include the authorization to issue Pension Obligation Bonds (POBs), used to increase the assets in its pension funds and make the required annual contributions to the State's five retirement systems. General Obligation (GO) 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 State issued a total of $2.15 billion in capital GO bonds during FY2013.[223] After accounting for payments made in FY2013, total outstanding capital purpose GO bonds increased by $1.4 billion to $13.5 billion going into FY2014 from $12.1 billion at the beginning of FY2013.[224] Total interest due on the State's outstanding capital-purpose GO bonds increased by $1.6 billion to $7.6 billion in FY2014 from $6.0 billion in FY2013. The combined total debt service owed on all outstanding capital GO bonds totals $21.1 billion in FY2014 compared to $18.1 billion in the prior fiscal year.

Under the 2003 pension bond authorization, the State issued $10 billion in POBs that are repaid through FY2033 to pay for unfunded liabilities of the State's retirement systems. A portion of the bond proceeds were also used to make part of the State's required annual contributions to the fund. The pension bond authorization was increased in FY2010 by $3.5 billion to make the annual contributions that otherwise would have come from the State's General Funds. The FY2010 POBs are repaid through FY2015. In FY2011 the State again issued POBs to make its annual contribution to its retirement systems, this time totaling $3.7 billion to be repaid over eight years. The FY2011 POBs will be completely retired in FY2019.

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[221] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 50; State of Illinois, Build Illinois Bonds, Series of May 2012, *Official Statement*, May 21, 2012, p. 16; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement*, June 15, 2013, p. 18.
[222] 30 ILCS 330/1.
[223] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p 185.
[224] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013.

Interest on the $3.5 billion of POBs sold in FY2010 totaled $382 million over five years. The FY2011 bonds, which totaled $3.7 billion, cost the State a total of $1.3 billion of interest over eight years. The FY2011 pension debt included $234 million more principal than FY2010 POBs, or 6.8%, but the interest owed on the bonds was $897.5 million greater, or 234.8%. The significant increase in the borrowing costs is due to the structure of the FY2011 bonds, which backload the principal repayment into the later years of the bonds and pays mostly interest only until the FY2010 bonds are repaid in FY2015.

The FY2003 POBs are also severely back loaded. The State only paid interest on the loan through FY2007. Then annual principal amounts increased to $50 million per year from FY2008 through FY2011 and to $100 million per year from FY2012 through FY2016. Beginning in FY2017, principal repayment increases annually by increments of $25 million, $50 million or $100 million through FY2033, when $1.1 billion is due in the final year of the loan. This structure leads to more than 75% of the principal borrowed to be repaid in the final 10 years of the debt service schedule and a total of $11.9 billion in interest cost over 30 years for the original $10 billion in borrowed funds.

Total principal owed on all outstanding POBs in FY2014 declined to $14.7 billion from $15.5 billion in FY2013.[225] The outstanding interest owed on the pension debt declined by $767.8 million to $8.0 billion in FY2014 from $8.8 billion in FY2013. Total debt service, including principal and interest, on the State's pension bonds totals $22.7 billion in FY2014 compared to $24.2 billion in FY2013. The State has not issued new POBs since FY2011.

Illinois also depends on several types of revenue bonds to fund capital projects. Unlike GO 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 Build Illinois Program began in 1985 and issues bonds backed by a pledge of the State's portion of sales tax receipts.[226] 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 State issued a total of $750 million in new Build Illinois Bonds in FY2012 and $300 million to support capital projects in FY2013.[227]

Beginning in FY2010, the new Build Illinois Bonds sold to support the *IllinoisJobsNow!* capital spending program also receive a transfer from the Capital Projects Fund to pay for the increase in debt service. Although the new Build Illinois Bonds are structured to receive additional funding from the revenue package of taxes and fees approved in 2009 to fund the increased capital appropriations, the bonds are still backed by the State's sales tax revenues.[228] The State is required to transfer the larger of 3.8% of its share of the sales taxes collected each year or the certified annual debt service owed on all outstanding Build Illinois Bonds.

After accounting for new issuances of $300 million, savings from the refinancing of $604.1 million of bonds on June 15, 2013 and debt service payments totaling $342.1 million in FY2013, the State enters FY2014 with a total of $2.8 billion in outstanding Build Illinois Bond principal. This represents a decrease of $97.3 million from the total of $2.9 billion in FY2013.[229] Interest on the loans totals $1.1 billion in FY2014, which is down by $195.2 million from a total of $1.3 billion in FY2013. Total debt

[225] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 50.
[226] Build Illinois Bond Act, 30 ILCS 425.
[227] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p 187.
[228] For more information on the State capital budget see p. 65 of this report.
[229] State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement*, June 15, 2013, p. 18.

service on all outstanding Build Illinois Bonds declines by $292.5 million to $3.9 billion in FY2014 from $4.2 billion in FY2013.

The following chart shows the total principal, interest and debt service in FY2014 compared to FY2013 for all GO bonds and Build Illinois Bonds currently outstanding.

State of Illinois Total Outstanding General Obligation and Build Illinois Bonds FY2013 and FY2014 (in $ millions)*				
	FY2013	**FY2014**	**$ Change**	**% Change**
Principal				
GO Capital	$12,071.4	$13,487.5	$ 1,416.1	11.73%
GO Pension	$15,479.0	$14,686.4	$ (792.6)	-5.12%
Build Illinois	$ 2,896.3	$ 2,798.9	$ (97.3)	-3.36%
Total Principal	**$30,446.7**	**$30,972.9**	**$ 526.2**	**1.73%**
Interest				
GO Capital	$ 6,009.1	$ 7,576.5	$ 1,567.4	26.08%
GO Pension	$ 8,754.1	$ 7,986.3	$ (767.8)	-8.77%
Build Illinois	$ 1,328.7	$ 1,133.6	$ (195.2)	-14.69%
Total Interest	**$16,091.9**	**$16,696.4**	**$ 604.5**	**3.76%**
Debt Service				
GO Capital	**$18,080.5**	**$21,064.1**	**$ 2,983.5**	**16.50%**
GO Pension	**$24,233.1**	**$22,672.7**	**$ (1,560.4)**	**-6.44%**
Build Illinois	**$ 4,225.0**	**$ 3,932.5**	**$ (292.5)**	**-6.92%**
Total	**$46,538.6**	**$47,669.2**	**$ 1,130.7**	**2.43%**

*As of July 1, the beginning of the fiscal year.
Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, p. 50; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement* , June 15, 2013, p. 18; State of Illinois, Build Illinois Bonds, Series of May 2012, *Official Statement* , May, 21, 2012, p. 16.

The State of Illinois has issued more principal than it has repaid over the last five fiscal years due to the ongoing capital program and the issuance of POBs. This has led to an increase of $9.2 billion in principal repayment owed by the State over the last five fiscal years, which totals $31.0 billion in FY2014 compared to $21.8 billion in FY2010.

However, the interest owed on the State's outstanding debt has only increased by $673.5 million over the same period. Interest owed on all outstanding GO bonds and Build Illinois Bonds totals $16.7 billion compared to $16.0 billion in FY2010. This disparity between the increase in principal and interest owed is due to the heavy back-loading of principal in the FY2003 and FY2011 POBs. Interest owed on POBs is $1.5 billion less in FY2014 than FY2010, while principal owed on POBs has grown $4.7 billion over the same period.

The following chart compares the outstanding principal, interest and total debt service on all Build Illinois Bonds, GO capital bonds and POBs from FY2010 to FY2014.

State of Illinois Total Outstanding Debt Service: General Obligation and Build Illinois Bonds Five-Year Comparison FY2010 to FY2014 (in $ millions)*							
	FY2010	**FY2011**	**FY2012**	**FY2013**	**FY2014**	**5-year $ Change**	**5-year % Change**
Principal							
GO Capital	$ 9,612.9	$12,340.1	$11,428.9	$ 12,071.4	$13,487.5	$ 3,874.6	40.3%
GO Pension	$ 9,950.0	$13,316.0	$16,272.8	$ 15,479.0	$14,686.4	$ 4,736.4	47.6%
Build Illinois	$ 2,201.0	$ 2,336.1	$ 2,171.2	$ 2,896.3	$ 2,798.9	$ 597.9	27.2%
Total Principal	**$21,763.9**	**$27,992.1**	**$29,872.9**	**$ 30,446.7**	**$30,972.9**	**$ 9,208.9**	**42.3%**
Interest							
GO Capital	$ 5,448.0	$ 6,559.9	$ 5,917.6	$ 6,009.1	$ 7,576.5	$ 2,128.5	39.1%
GO Pension	$ 9,467.9	$ 8,861.1	$ 9,538.8	$ 8,754.1	$ 7,986.3	$ (1,481.6)	-15.6%
Build Illinois	$ 1,107.0	$ 1,094.3	$ 960.2	$ 1,328.7	$ 1,133.6	$ 26.6	2.4%
Total Interest	**$16,022.9**	**$16,515.3**	**$16,416.6**	**$ 16,091.9**	**$16,696.4**	**$ 673.5**	**4.2%**
Debt Service							
GO Capital	**$15,061.0**	**$18,900.0**	**$17,346.5**	**$ 18,080.5**	**$21,064.1**	**$ 6,003.1**	**39.9%**
GO Pension	**$19,417.9**	**$22,177.1**	**$25,811.6**	**$ 24,233.1**	**$22,672.7**	**$ 3,254.8**	**16.8%**
Build Illinois	**$ 3,308.0**	**$ 3,430.3**	**$ 3,131.4**	**$ 4,225.0**	**$ 3,932.5**	**$ 624.5**	**18.9%**
Total	**$37,786.8**	**$44,507.4**	**$46,289.5**	**$ 46,538.6**	**$47,669.2**	**$ 9,882.4**	**26.2%**

*As of July 1, the beginning of the fiscal year.
Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, p. 50; State of Illinois, General Obligation Bonds, Series of May 2009, *Official Statement* , May, 21, 2009, p. 36; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement* , June 15, 2013, p. 18; Illinois State FY2010 Budget, p. 12-11; State of Illinois, General Obligation Bonds, Taxable Build America Bonds Series 2010-5, *Official Statement* , July 14, 2010, p. 38; State of Illinois, General Obligation Bonds, Taxable Series of February 2011, *Official Statement* , Feb. 23, 2011, p. 43; State of Illinois Build Illinois Bonds, Junior Obligation Series of June 2010, *Official Statement* , June 15, 2010.

Several other smaller debt-funded capital programs are supported by either direct appropriations or pledges in support of repayment but are not included in the total debt service figures above. These debts do not significantly affect the State's General Funds operating expenses and are typically funded through dedicated revenue sources and shared costs with local governments.

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. As of FY2014, outstanding Civic Center Bonds total $72.8 million; the State will make its final payment on this debt in FY2028. Although originally financed in part by horseracing taxes, these bonds are now fully repaid by General Funds and are treated more like GO bonds. The Civic Center bonds were issued using a level debt service structure and the State will pay $13.9 million through FY2016 and $14.4 million thereafter until the remaining bonds are completely retired.[230]

The State has supported bond payments owed by the Metropolitan Pier and Exposition Authority (MPEA), which manages Navy Pier and the McCormick Place Convention Center in Chicago. State funds are used to prefund its debt service and the Authority repays the State from its annual revenues. The MPEA did not completely repay the State between FY2009 and FY2011 and received a direct appropriation of $25.8 million in FY2011 to support its debt service and operations. The MPEA owes the State $57 million, which is expected to be repaid through a share of expected revenue surplus after FY2015.[231] The City of Chicago also pledges revenue from its airport departure tax, automobile renting tax, hotel tax and local restaurant sales tax to support bonds issued by the MPEA for expansion.

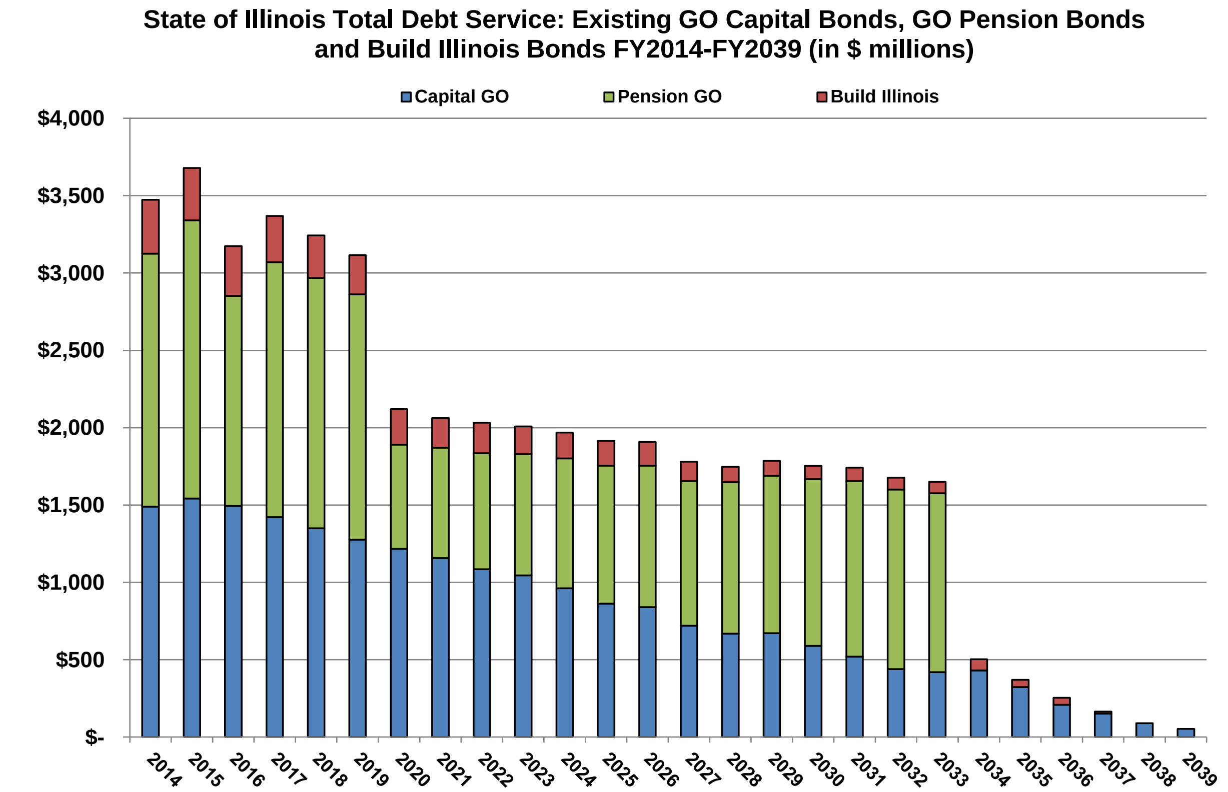
[230] Commission on Government Forecasting and Accountability, *Capital Plan Analysis FY2014*, April 2013, p. 30.
[231] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p. 48.

Debt Service

The State's debt service schedule sets forth the principal and interest amounts due to investors for its outstanding bonds on an annual basis. In FY2014 the State is required to pay a total of $3.5 billion for all outstanding GO Bonds, POBs and Build Illinois Bonds.[232] The largest portion of this payment is due on POBs, totaling $1.6 billion. Debt service in FY2014 totals $1.5 billion for capital-purpose GO bonds and $348.4 million for Build Illinois Bonds.

Based on the State's current bonded indebtedness, debt service payments will peak in FY2015 at $3.7 billion before declining marginally through FY2019 to $3.1 billion. Once the State has paid off the FY2011 POBs, debt service declines by $995 million to $2.1 billion in FY2020.

The following chart shows total debt service for existing Pension Obligation bonds, GO capital bonds and other capital bonds through FY2040.[233]



Source: State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 50; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement*, June 15, 2013, p. 18.

It should be noted that the State does not pay for all debt service out of General Funds. As mentioned above, revenue bonds have specific dedicated sources outside the General Funds. GO capital bonds are also funded through transfers from the Road Fund, Capital Projects Fund, School Infrastructure and State Construction Fund, which have dedicated revenue sources outside the State's General Funds operating budget.

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[232] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 50; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement*, June 15, 2013, p. 18.
[233] For more details on total debt service, see Appendix D on p. 73 of this report.

The enacted FY2014 budget includes General Funds debt service transfers totaling $2.2 billion, an increase of $109.0 million from $2.1 billion in FY2013.[234]

The FY2014 debt service transfer associated with capital GO bonds totals $527 million, up from $521 million in FY2013. Debt service transferred to pay for POBs totals $1.7 billion in FY2014 compared to $1.56 billion in FY2013.

To make payments on the Build Illinois Bonds, the State transfers the certified amount needed for debt service from its portion of the sales tax receipts to the Build Illinois Fund before sales tax revenues are transferred to the General Funds. In FY2014 the transfer will total $348.4 million, up from $342.1 million in FY2013. The Capital Projects Fund also supports Build Illinois Bond debt service and will transfer an estimated $53.4 million in FY2014 compared to $31.9 million in FY2013 to offset the cost of new bonds issued to support the *IllinoisJobsNow!* capital expenditures.

Short-Term Debt

Short-term debt is a financial obligation that must be satisfied within one year. 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.[235]

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, which must be repaid entirely within the same budget cycle.[236] The State may also borrow up to 15% of the total appropriations for any year if there is a declared failure in revenue.[237] Failure of revenue 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.

The State has not issued short-term debt since FY2011 and does not include any short-term borrowing as part of the FY2014 enacted budget. Rather than relying on short-term debt to finance its deficits, the State has extended its lapse period spending, the time available to use subsequent year resources to pay current year expenses, from 60 days to six months.[238] Beginning in FY2010, the State took action in each budget year to extend the lapse period deadline to pay all of its prior year bills from August 30 to December 31. This change was made permanant in FY2013.[239]

[234] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 16.
[235] 30 ILCS 340 (2004).
[236] 30 ILCS 340/1 (2004).
[237] 30 ILCS 340/1.1 (2004).
[238] Public Act 97-0732.
[239] Public Act 97-0932.

Bond Ratings

Bond ratings are one of the factors that weigh heavily in determining the interest rates the State must pay to issue debt. The State of Illinois' ratings have been lowered by all three ratings agencies multiple times over the last several years, which has led to an overall increase in debt service costs above better rated governments.

After the Illinois General Assembly enacted its regular spring session without approving reform of the State's underfunded retirement systems, two of the three major ratings agencies downgraded the State's bond ratings.[240] Both Fitch Ratings and Moody's Investors Service cut the State's rating one level, while Standard and Poor's affirmed its existing A- rating.[241]

Specifically citing the inaction on pension reform, Fitch Ratings lowered Illinois' General Obligation (GO) bond rating to A- from A on June 3, 2013, the first business day following the end of the General Assembly's regular session.[242] On June 6, 2013, Moody's Investors Service followed suit, reducing the State's rating to A3 from A2, due to the State's unresolved pension crisis.[243] S&P downgraded the State's rating on January 25, 2013 to A- from A and affirmed that rating as part of its review of the State's $1.3 billion GO bond issuance.[244]

Moody's report accompanying the downgrade stated that its analysis of the State's financial condition not only took into account the legislature's failure to act on pension reform but also assumed that the General Assembly would not take action to resolve the problem anytime soon. The agency blamed the "legislature's political paralysis" regarding pension reform on the magnitude of the State's unfunded liabilities as well as the legal and political hurdles any comprehensive reform measure would face.

The following table compares the State's GO bond ratings from all three agencies in FY2014 to the ratings at the beginning of each fiscal year since FY2008, which is the last time the State was rated 'AA' by all three agencies.

State of Illinois General Obligation Bond Ratings FY2008-FY2013			
	Moody's Investors Service	**Standard & Poor's**	**Fitch Ratings**
FY2008	Aa3	AA	AA
FY2009	A1	AA-	A
FY2010	A1, Aa3*	A+	A-, A+*
FY2011	A1	A+	A
FY2012	A2	A+	A
FY2013	A2	A	A
FY2014	A3	A-	A-

*Moody's and Fitch increased Illinois' bond ratings in March 2010 due to recalibrations of their entire rating scales but this was not considered an upgrade.

Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014* , August 2013, pp. 193-195.

[240] For more information on the State retirement systems, see p. 32 of this report.
[241] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p. 193.
[242] Fitch Ratings, "Fitch Downgrades Illinois' GO Rating to 'A-'; Outlook Negative," June 3, 2013.
[243] Moody's Investors Service, "Moody's downgrades State of Illinois' $27 billion of General Obligation Bonds to A3 from A," June 6, 2013.
[244] State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement*, June 26, 2013, p. 99.

Illinois' bond ratings are the lowest of all 50 states, leading to dramatically higher borrowing costs than better-rated governments. The latest downgrades put Illinois on the final step of the 'A' ratings for all three agencies before entering 'BBB" status. Fitch and S&P have downgraded Illinois' rating six steps in the past five years, while Moody's has reduced its level four times. All three agencies maintain a negative outlook on the State's finances, indicating the possibility for further downgrades.

Despite the low ratings compared to other states, Illinois' bonds are still considered investment grade. This means that investors can be assured of the government's good credit and face little or no risk of default, according to the agencies' rating definitions. The State would need to be downgraded at least five more levels to be considered at risk of default by the issuer or a speculative grade credit. Speculative grade bonds are sometimes referred to as junk bonds and typically pay much higher rates of interest to investors due to the additional risk of defaulting on the loans.

The chart below shows the letter ratings and definitions for each level of bond as described by each ratings agency. Within each letter rating, the agencies have three grades of credit. Both Fitch and S&P use a plus sign, no sign and minus sign to delineate where within a letter grade the credit stands. Moody's system is slightly different and includes the numbers 1, 2 and 3 to show a credit's stratification within a particular letter grade (1 being the highest quality and 3 the lowest).

Major Credit Ratings Agencies: Ratings Scales and Definitions

	Moody's	Definition	S&P	Definition	Fitch	Definition
Investment Grade	**Aaa**	Highest quality, subject to the lowest level of credit risk	**AAA**	Extremely strong capacity to meet financial commitments, highest rating	**AAA**	Lowest default risk, exceptionally strong capacity for payment of financial commitments and highly unlikely to be adversely affected by foreseeable events
Investment Grade	**Aa**	High quality and are subject to very low credit risk	**AA**	Very strong capacity to meet financial commitments	**AA**	Very low default risk, very strong capacity for payment of financial commitments and not significantly vulnerable to foreseeable events
Investment Grade	**A**	Upper-medium grade and are subject to low credit risk	**A**	Strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances	**A**	Low default risk, strong capacity for payment of financial commitments but more vulnerable to adverse business or economic conditions
Investment Grade	**Baa**	Medium-grade and subject to moderate credit risk and may possess certain speculative characteristics	**BBB**	Adequate capacity to meet financial commitments, but more subject to adverse economic conditions	**BBB**	Low default risk, adequate capacity for payment of financial commitments but adverse business or economic conditions are more likely to impair this capacity
Above Investment Grade, Below Speculative						
Speculative Grade	**Ba**	Speculative and are subject to substantial credit risk	**BB**	Considered highest speculative grade by market participants	**BB**	Elevated vulnerability to default risk, particularly in the event of adverse changes in business or economic conditions over time; however, business or financial flexibility exists which supports the servicing of financial commitments
Speculative Grade	**B**	Speculative and are subject to high credit risk	**B**	More vulnerable to adverse business, financial and economic conditions but currently has the capacity to meet financial commitments	**B**	Material default risk is present, but a limited margin of safety remains; financial commitments are currently being met but capacity for continued payment is vulnerable to deterioration in the business and economic environment
Speculative Grade	**Caa**	Speculative of poor standing and are subject to very high credit risk	**CCC**	Currently vulnerable and dependent on favorable business, financial and economic conditions to meet financial commitments	**CCC**	Default is a real possibility
Speculative Grade	**Ca**	Speculative and are likely in, or very near, default, with some prospect of recovery of principal and interest	**CC**	Currently highly vulnerable	**CC**	Default of some kind appears probable.
Speculative Grade	**C**	Lowest rated and are typically in default, with little prospect for recovery of principal or interest	**C**	Currently highly vulnerable obligations and other defined circumstances	**C**	Default is imminent or inevitable, or the issuer is in standstill.

Source: Fitch Ratings, *Definitions of Ratings and Other Forms of Opinion* , August 2012, http://www.fitchratings.com/web_content/ratings/fitch_ratings_definitions_and_scales.pdf; Moody's Investors Service, *Ratings Symbols and Definitions* , June 2012, http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004; Standard & Poor's, *Standard & Poor's Ratings Definitions* , June 2012, http://www.standardandpoors.com/ratings/articles/en/us/?articleType=HTML&assetID=1245335682757.

CAPITAL BUDGET

The FY2014 capital budget marks the fifth year of the State's $31 billion *Illinois Jobs Now!* capital program. The capital budget includes reauthorization of $18.8 billion in previously approved projects and $3.4 billion in new appropriations, bringing the total to $22.2 billion in spending authority.[245]

Unlike the State's operating budget, which requires that all appropriated funds be spent in the same year they are approved, capital appropriations must be reauthorized over multiple years as planning, engineering and construction of capital investments commences. The total spending approved in the FY2014 capital budget includes funding from the State, as well as grants from the federal government and local matching funds to pay for projects.

The State's annual capital budget is presented separately from the operating budget and is not part of the annual General Funds expenditures.

The capital budget approved for FY2014 is $856.2 million more than the total $21.3 billion in the Governor's recommended FY2014 capital budget, which proposed $3.3 billion in new appropriations and $18.0 billion in reappropriations. The larger reappropriation in the enacted budget represents the difference between the amount the State expected to spend on projects in March when the Governor's proposed budget was published and the actual year-end amounts.

The following table compares the capital budget proposed by the Governor for FY2014 to the enacted capital budget.

State of Illinois FY2014 Capital Spending Authorization (in $ millions)				
	FY2014 Rec.	FY2014 Enacted	$ Change	% Change
Reappropriation	$ 17,997.0	$ 18,783.0	$ 786.0	4.4%
New	$ 3,339.5	$ 3,409.6	$ 70.1	2.1%
Total	**$ 21,336.4**	**$ 22,192.6**	**$ 856.2**	**4.0%**

Source: Illinois State FY2014 Capital Budget p.70; Email communication between Civic Federation staff and Governor's Office of Management and Budget, August 12, 2013.

The new spending in the enacted capital budget is almost entirely dedicated to additional transportation spending on roads, bridges, airports, rail and mass transit. Transportation spending largely consists of broad grants given to the Illinois Department of Transportation that are later assigned to specific projects. New capital appropriations for transportation in FY2014 include $1.4 billion in statewide transportation grants, $500 million in federal funding for high speed rail and $120 million in federal and local funding for airport projects. The capital budget also includes $62.2 million in new State funding for the planned South Suburban Airport in Peotone, Illinois.

The General Assembly also approved a State-funded appropriation of $350 million for the State's wastewater loan program. The largest new State-funded project not related to transportation specifically included in the enacted FY2014 capital budget is $10 million to fund the construction of a "Chicago Film Studio." There are 424 lines of new appropriations ranging in cost from $10,000 to

[245] Public Act 98-0050. Email communication between the Civic Federation and the Governor's Office of Management and Budget, August 12, 2013.

$10.0 million that make up $133.1 million of the FY2014 capital budget as approved in Public Act 98-0050.

Compared to FY2013, total approved spending in the FY2014 capital budget declines by $513.7 million. In FY2014 reappropriations decrease by $1.9 billion and new capital spending increases by $1.4 billion. The following table compares the total spending enacted in the FY2014 capital budget to the totals for FY2013.

State of Illinois FY2014 Capital Spending Authorization (in $ millions)				
	FY2013 Enacted	FY2014 Enacted	$ Change	% Change
Reappropriation	$ 20,719.2	$ 18,783.0	$ (1,936.2)	-9.3%
New	$ 1,987.1	$ 3,409.6	$ 1,422.5	71.6%
Total	**$ 22,706.3**	**$ 22,192.6**	**$ (513.7)**	**-2.3%**

Source: Illinois State FY2012 Capital Budget p.104; Email communication between Civic Federation staff and Governor's Office of Management and Budget , August 13, 2012 and August 12, 2013.

The State relies heavily on the sale of bonds to fund the capital budget but also receives federal funding and some pay-as-you go funding from user fees, taxes and local government funds. Updated estimates of the funding for the enacted FY2013 budget are not yet available, but the Governor's recommended FY2014 capital budget estimated that $10.9 billion, or 51.2% of total spending remaining in the capital budget, will be paid for with General Obligation (GO) bonds issued by the State.[246]

As of July 1, 2013, the State has issued $8.7 billion in bonds to pay for capital projects since the capital program began in FY2010.[247] The package of new revenue sources authorized in FY2010 to pay for the additional debt related to spending on *Illinois Jobs Now!* consists of the following:[248]

- Statewide legalization and taxation of video poker;
- Expanded sales tax on candy, sweetened beverages and some hygiene products;
- Leasing a portion of state lottery operations;
- Increased per gallon tax on beer, wine and liquor; and
- Increased license and vehicle fees.

The proceeds from these sources are deposited in the Capital Projects Fund and used to pay for debt service on new capital bonds and some ongoing capital expenses. However, the taxes and fees have yet to produce the funding levels projected when *Illinois Jobs Now!* originally was approved. Online records from the Illinois Comptroller's Office show a total of $627.3 million in capital revenues in FY2013. This is up from $532.5 million in FY2012 but still well short of the legislative projections of between $943 million and $1.2 billion made available when the original spending was approved in FY2010.

The following table shows the revenues deposited into the Capital Projects Fund from FY2010 through FY2013 compared to the original projections for each revenue source.

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[246] Illinois State FY2014 Capital Budget, p. 75.
[247] Commission on Government Forecasting and Accountability, *State of Illinois Budget Summary Fiscal Year 2014*, August 2013, p.185.
[248] Public Acts 96-0034, 96-0037, 96-0038.

Capital Projects Fund: Revenues by Source (in $ millions)					
Source	Original Projections	FY2010	FY2011	FY2012	FY2013
Video Poker Tax*	$288 - $534	$ -	$ -	$ -	$ 58.0
Lottery Fund	$ 150	$ 32.9	$ 54.1	$ 65.2	$ 135.0
Sales Tax	$ 65	$ 39.0	$ 52.0	$ 52.7	$ 54.0
Liquor Tax	$ 108	$ 77.6	$ 105.2	$ 114.8	$ 115.1
Vehicle Related	$ 332	$ 117.7	$ 294.6	$ 299.7	$ 264.9
Investment Income and Other	$ -	$ 0.3	$ -	$ 0.1	$ 0.4
Total	**$943 - $1,189**	**$ 267.5**	**$ 505.9**	**$ 532.5**	**$ 627.3**

*FY2013 includes one-time video poker operator fees totaling $33.5 million.

Source: Commission on Government Forecasting and Accountability, *Capital Plan Analysis FY2014* , April 2013, pp.10-12; Illinois Comptroller, *Online Revenue Query by Fund: Capital Projects Fund,* www.ioc.state.il.us (last visited on July 31, 2013).

The largest shortfall in revenues is related to the delay in implementing and taxing the newly legalized video gaming, which was the largest single source of revenues in the approved funding package. Due to administrative delays, the first machines were not put into service until October 2012. Fiscal year 2013 marks the first year that the capital budget received revenue from the 30% tax on video gaming in the State, of which five-sixths is used for capital project funding and the remainder given to local governments to pay for adverse social effects of gaming.[249]

The total of $58.0 million in FY2013 video gaming revenues is well below the projections of $288 million to $534 million annually. The FY2013 revenues also include one-time operator fees totaling $33.5 million, making the total recurring revenue only $24.5 million.[250] Even after video gaming is fully implemented, total revenues generated for the State construction program will likely only reach between $106 million and $196 million annually, according to a report on the capital program by the Commission on Government Forecasting and Accountability (COGFA).[251]

The COGFA report states that 63.3% of the Illinois population lives in communities where video gaming is illegal. This includes communities like Chicago, which represents 21.0% of the State population, where existing bans would have to be lifted to allow video gaming, as well as other communities that passed resolutions preventing expansion of video gaming after the law was passed.[252]

Although video gaming revenue accounts for the largest shortfall in capital funding, all other sources of capital revenue except liquor taxes also continue to fall short.

In FY2013 the Capital Projects Fund received $627.3 million in revenue and paid for $397.7 million in debt service. The debt service paid from the Capital Projects Fund will jump to $564.3 million in FY2014 due to debt service owed on the $2.15 billion in new debt to support the capital expenditures.

[249] Public Act 96-0034.
[250] Illinois Comptroller, *Online Revenue Query by Fund: Capital Projects Fund*, www.ioc.state.il.us (last visited on July 1, 2013).
[251] Commission on Government Forecasting and Accountability, *Capital Plan Analysis FY2014*, April 2013, p. 10.
[252] Commission on Government Forecasting and Accountability, *Capital Plan Analysis FY2014*, April 2013, p. 10.

The following chart shows debt service due from the Capital Projects Fund from FY2013 through FY2018 based on current outstanding debt.

State of Illinois Capital Projects Fund: Debt Service Transfers FY2013 to FY2018 (in $ millions)						
Issuance	**FY2013**	**FY2014**	**FY2015**	**FY2016**	**FY2017**	**FY2018**
Previously Sold Bonds	$ 397.7	$ 376.1	$ 369.9	$ 363.0	$ 355.7	$ 348.0
FY2013 Bonds	$ -	$ 188.2	$ 186.9	$ 183.6	$ 180.5	$ 177.2
Total	**$ 397.7**	**$ 564.3**	**$ 556.8**	**$ 546.7**	**$ 536.2**	**$ 525.2**

Source: Communication between Civic Federation and Governor's Office of Management and Budget, September 3, 2013.

The State has sold slightly more than half of the debt needed to pay for the $16 billion in debt-funded capital projects originally approved by the General Assembly in FY2010. Although there is some capacity for additional debt supported by the Capital Projects Fund, the available resources may fall short of the amount that would be needed to pay for the remaining approved but unfunded projects.

The State also pays capital debt service for funding annual transportation improvements on roads, bridges and mass transit from the Road Fund and State Constructions Fund. The School Infrastructure Fund contributes to debt service for annual school maintenance and improvements. If the Capital Projects Fund does not have sufficient funds to cover the debt service owed on the new projects included in *Illinois Jobs Now!*, the remainder is covered by the Road Fund, which must then be repaid out of future Capital Projects Fund revenues.

The State's General Funds revenues are used to pay for capital bonds approved prior to the authorization of *Illinois Jobs Now!* and pension bonds sold by the State in FY2003, FY2010 and FY2011. Typically the Build Illinois Bonds are paid from a portion of the State's sales tax receipts. However, any Build Illinois Bonds sold based on the increased authorization included in *Illinois Jobs No*w! are paid for out of the Capital Projects Fund.

APPENDIX A: MAJOR BUDGET-RELATED RESOLUTIONS AND LEGISLATION

State of Illinois FY2014 Budget Resolutions		
Resolution	**Description**	**Date Adopted**
House Resolution 83	General Funds revenue estimate	March 5, 2013
House Resolution 389	Updated General Funds revenue estimate	May 31, 2013

Source: Illinois General Assembly website at http://www.ilga.gov/legislation/.

State of Illinois FY2014 Budget-Related Legislation				
Bill*	**Description**	**Public Act**	**Date Signed (2013)**	**Governor's Vetoes**
SB26	Medicaid expansion	98-0104	July 22	
SB1515	Group health insurance opt-out incentives and procurement exemptions	98-0019	June 10	
SB1329	Budget implementation bill	98-0024	June 19	
SB1621	Reduction of State mandates	98-0044	June 28	
SB2106	Budget transparency working group	98-0580	August 27	
SB2555	Elementary and secondary education appropriations	98-0034	June 27	
SB2556	Higher education appropriations	98-0035	June 27	
HB2	Single audit commission	98-0047	July 1	
HB156	Delay of Governor's budget address	98-0002	February 19	
HB190	Supplemental appropriations for FY2013	98-0001	February 7	
HB206	Non-discretionary appropriations and supplemental appropriations for FY2013	98-0017	June 5	
HB207	Supplemental appropriations for FY2013	98-0011	May 10	
HB208	Education-related appropriations	98-0033	June 27	
HB213	Human services appropriations	98-0027	June 21	
HB214	General services appropriations	98-0064	July 10	Line item
HB215	Public safety and capital appropriations	98-0050	July 2	Line item
HB1544	State strategic economic development plan	98-0397	August 16	
HB1682	Agency reports on unpaid bills	98-0228	August 9	
HB2275	Community Care Program reforms	98-0008	May 3	
HB2947	Enhanced budget disclosure	98-0460	August 16	
HB2955	Enacted budget publication	98-0461	August 16	

*SB stands for Senate Bill; HB stands for House Bill.

Source: Illinois General Assembly website at http://www.ilga.gov/legislation/.

APPENDIX B: GENERAL FUNDS PENSION CONTRIBUTIONS

The table below shows the data used in the State Retirement Systems section, which begins on page 32 of this report. In the table, figures for FY2008 through FY2014 are actual General Funds pension contributions. Figures for FY2015 through FY2045 are Civic Federation calculations based on a report by the General Assembly's Commission on Government Forecasting and Accountability (COGFA).[253] The numbers in the COGFA report come from actuarial valuations of the five State retirement systems as of June 30, 2012.

The State's five retirement systems are required to calculate and certify statutorily required State contributions for the next fiscal year by November of the current fiscal year. The systems certify total contributions without specifying the amounts from General Funds. Three of the systems receive all of their contributions from General Funds, but the other two systems receive a portion of their contributions from Other State Funds.

In the table, it is assumed that the State Employees' Retirement System will receive about 66% of its total State contributions from General Funds. This reflects the share of State employees who are paid from General Funds resources. It is assumed that the State Universities Retirement System will receive $150 million a year from the State Pensions Fund, which is funded by the sale of unclaimed property. It should be noted that this amount was increased to $198 million in FY2014.

State of Illinois Actual and Projected General Funds Pension Contributions Under Current State Law FY2008-FY2045 (in $ millions)*

FY2008	$	1,838	FY2021	$	7,721	FY2034	$	12,823
FY2009	$	2,486	FY2022	$	7,989	FY2035	$	13,134
FY2010**	$	3,466	FY2023	$	8,272	FY2036	$	13,437
FY2011**	$	3,680	FY2024	$	8,545	FY2037	$	13,732
FY2012	$	4,135	FY2025	$	8,825	FY2038	$	14,022
FY2013	$	5,107	FY2026	$	9,141	FY2039	$	14,302
FY2014	$	5,988	FY2027	$	9,468	FY2040	$	14,575
FY2015	$	6,288	FY2028	$	9,781	FY2041	$	14,846
FY2016	$	6,470	FY2029	$	10,098	FY2042	$	15,117
FY2017	$	6,712	FY2030	$	10,395	FY2043	$	15,399
FY2018	$	6,974	FY2031	$	10,693	FY2044	$	15,686
FY2019	$	7,222	FY2032	$	11,011	FY2045	$	15,996
FY2020	$	7,465	FY2033	$	11,340			

*FY2008 through FY2014 are actual contributions; FY2015 through FY2045 are Civic Federation projections.

**Pension contributions in FY2010 and FY2011 were made through the issuance of General Obligation Bonds and are shown here for purposes of comparability.

Source: Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012* , February 2013, pp. 97-102; State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , June 26, 2013, p. 16; Illinois State FY2012 Budget, p. 2-14; Communication between Civic Federation and Governor's Office of Management and Budget, February 23, 2012.

[253] Commission on Government Forecasting and Accountability, *Illinois State Retirement Systems: Financial Condition as of June 30, 2012*, February 2013, pp. 97-102.

APPENDIX C: PROVISIONS OF MAJOR PENSION PROPOSALS

The main pension proposals considered by the Illinois General Assembly during its spring 2013 session were Senate Bill 1, as amended by the House, and Senate Bill 2404. SB1, as amended, was introduced by House Speaker Michael Madigan and passed by the House on May 2. House Bill 2404 was sponsored by Senate President John Cullerton and passed the Senate on May 2. The amended Senate Bill 1 was rejected by the Senate on May 30.

Both bills apply to four of the State's five retirement systems: the Teachers' Retirement System, the State Employees' Retirement System, the State Universities Retirement System and the General Assembly Retirement System. The fifth system, the Judges' Retirement System, is not affected by the bills.

Senate Bill 1, as Amended[254]

Speaker Madigan's plan includes the following major changes:

- Limit automatic annual benefit increases to the lesser of 1) 3% of the pension benefit, compounded or 2) 3% of $1,000 multiplied by the number of years of service. Under this limit, a retiree not covered by Social Security with 30 years of service would receive a maximum annual increase of $900 a year. Current retirees receive unlimited compounded increases of 3%.
- Delay annual benefit increases until age 67 or until the fifth year after retirement, whichever comes first.
- Phase in higher retirement ages for those under 45.
- Cap the maximum salary on which a pension is based at the same level as Tier 2 employees. That level was $106,800 in 2011 and increases by 3% or one-half the increase in the Consumer Price Index, whichever is less.
- Increase employee contributions by 2 percentage points, phased in over two years.
- Guarantee that the State make its required contributions by specifying that pension funding has contractual status under the Illinois Constitution.
- Require that the systems be 100% funded by FY2045, rather than 90% funded as required by the State's existing funding plan.
- Use an actuarial method supported by the Governmental Accounting Standards Board to allocate annual benefit costs. This method, known as entry age normal, smoothes pension costs over time compared with the projected unit credit method used by the State, which increases costs over time.
- Require the State to make $1 billion a year in supplemental contributions from FY2020 through FY2045 to reduce the unfunded liability. These additional contributions begin as State debt service payments on outstanding pension bonds decline in FY2019.

[254] 98th Illinois General Assembly, Senate Bill 1, as amended by House Amendments 1 and 3.

Senate Bill 2404[255]

Senate President Cullerton's plan also includes a funding guarantee by the State. Unlike the Speaker's proposal, it would keep the funding schedule unchanged from existing law, with a requirement of 90% funding by FY2045.

Retirees and employees hired before January 1, 2011 would be offered the following choices, centered on keeping or reducing the existing 3% compounded automatic annual benefit increase:

- **Retirees**
  Choice A: Keep existing 3% compounded automatic annual benefit increase with staggered two-year freeze. Receive access to retiree health insurance.
  Choice B: No change to existing 3% compounded automatic annual benefit increase. No access to retiree health insurance.
- **Employees**
  Choice A: Annual automatic increase is reduced to 3% simple with a two-year delay. Receive access to retiree health insurance. All future salary increases are credited toward pensions.
  Choice B:
  Option 1: No change to existing 3% compounded automatic annual benefit increase. No access to retiree health insurance and no pension credit for future salary increases.
  Option 2: No change to existing 3% compounded automatic annual benefit increase, receive access to retiree health insurance and pension credit for future salary increases. Three-year delay in automatic annual adjustment and two percentage point increase in employee contributions phased in over two years.

[255] 98th Illinois General Assembly, Senate Bill 2404, Senate Amendments 2, 4 and 5.

APPENDIX D: TOTAL DEBT SERVICE

The following chart shows all outstanding General Obligation and Build Illinois Bond debt service owed by the State of Illinois as of July 1, 2013.

State of Illinois Total Debt Service: GO Bonds and Build Illinois Bonds Bonds Principal and Interest (in $ millions)

Fiscal Year	Capital GO	Pension GO	Build Illinois	Total Debt Service
2014	$ 1,490.4	$ 1,634.1	$ 348.4	**$ 3,472.9**
2015	$ 1,542.5	$ 1,797.9	$ 338.5	**$ 3,678.9**
2016	$ 1,494.8	$ 1,356.5	$ 322.3	**$ 3,173.5**
2017	$ 1,422.4	$ 1,647.3	$ 298.4	**$ 3,368.1**
2018	$ 1,349.9	$ 1,618.6	$ 274.8	**$ 3,243.4**
2019	$ 1,275.8	$ 1,586.1	$ 253.5	**$ 3,115.4**
2020	$ 1,216.5	$ 674.6	$ 229.5	**$ 2,120.5**
2021	$ 1,156.9	$ 713.4	$ 191.6	**$ 2,061.9**
2022	$ 1,085.6	$ 749.8	$ 196.5	**$ 2,031.9**
2023	$ 1,045.4	$ 783.7	$ 179.0	**$ 2,008.2**
2024	$ 961.8	$ 840.2	$ 166.2	**$ 1,968.1**
2025	$ 862.7	$ 892.2	$ 159.6	**$ 1,914.5**
2026	$ 839.9	$ 915.4	$ 152.4	**$ 1,907.7**
2027	$ 719.3	$ 936.1	$ 125.5	**$ 1,780.9**
2028	$ 669.4	$ 979.2	$ 99.6	**$ 1,748.2**
2029	$ 671.3	$ 1,018.5	$ 96.4	**$ 1,786.3**
2030	$ 589.2	$ 1,079.0	$ 84.8	**$ 1,753.0**
2031	$ 520.8	$ 1,134.4	$ 86.6	**$ 1,741.7**
2032	$ 440.0	$ 1,159.7	$ 77.6	**$ 1,677.3**
2033	$ 419.5	$ 1,156.1	$ 74.7	**$ 1,650.3**
2034	$ 431.0	$ -	$ 71.7	**$ 502.7**
2035	$ 324.0	$ -	$ 46.7	**$ 370.8**
2036	$ 209.2	$ -	$ 45.0	**$ 254.1**
2037	$ 152.2	$ -	$ 13.0	**$ 165.2**
2038	$ 90.0	$ -		**$ 90.0**
2039	$ 53.4	$ -		**$ 53.4**
Total	**$ 21,034.0**	**$ 22,672.7**	**$ 3,932.4**	**$ 47,639.1**

State of Illinois, General Obligation Bonds, Series of June 2013, *Official Statement* , July 2, 2013, p. 50; State of Illinois, Build Illinois Bonds, Series of May 2012, *Official Statement* , May, 21, 2012, p. 16; State of Illinois, Build Illinois Bonds, Junior Obligation Series of June 2013, *Official Statement* , June 15, 2013, p. 18.