

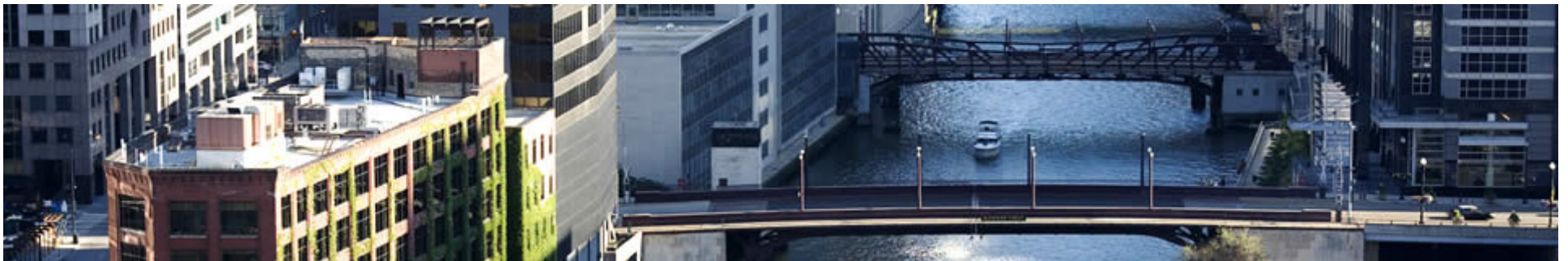


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Illinois' Fiscal Crisis

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President, the Civic Federation
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About the Civic Federation

- Non-profit, non-partisan government research organization founded in 1894.
- Funded by major corporate and professional service firms in the Chicagoland region.
- Purpose:
 - To serve as a technical resource, providing nonpartisan research and information.
 - To promote rational tax policies and efficient delivery of quality government services.
 - To offer solutions which guard against excessive taxation, enhance financial reporting and improve the quality of public expenditures.

www.civicfed.org for more information



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Illinois' Fiscal Crisis

- Many years in the making.
- Rooted in the underfunding of Illinois' public pension system and the state persistently spending more than it could reasonably expect in revenue.
- \$12.9 billion deficit going into FY2011.
- Moody's and Fitch downgraded the State's debt rating in reaction to the budget passed by the General Assembly and further ratings reductions are likely.
- Borrowing and ignoring bills has replaced the pressure to balance expenditures with reasonable revenue projections.



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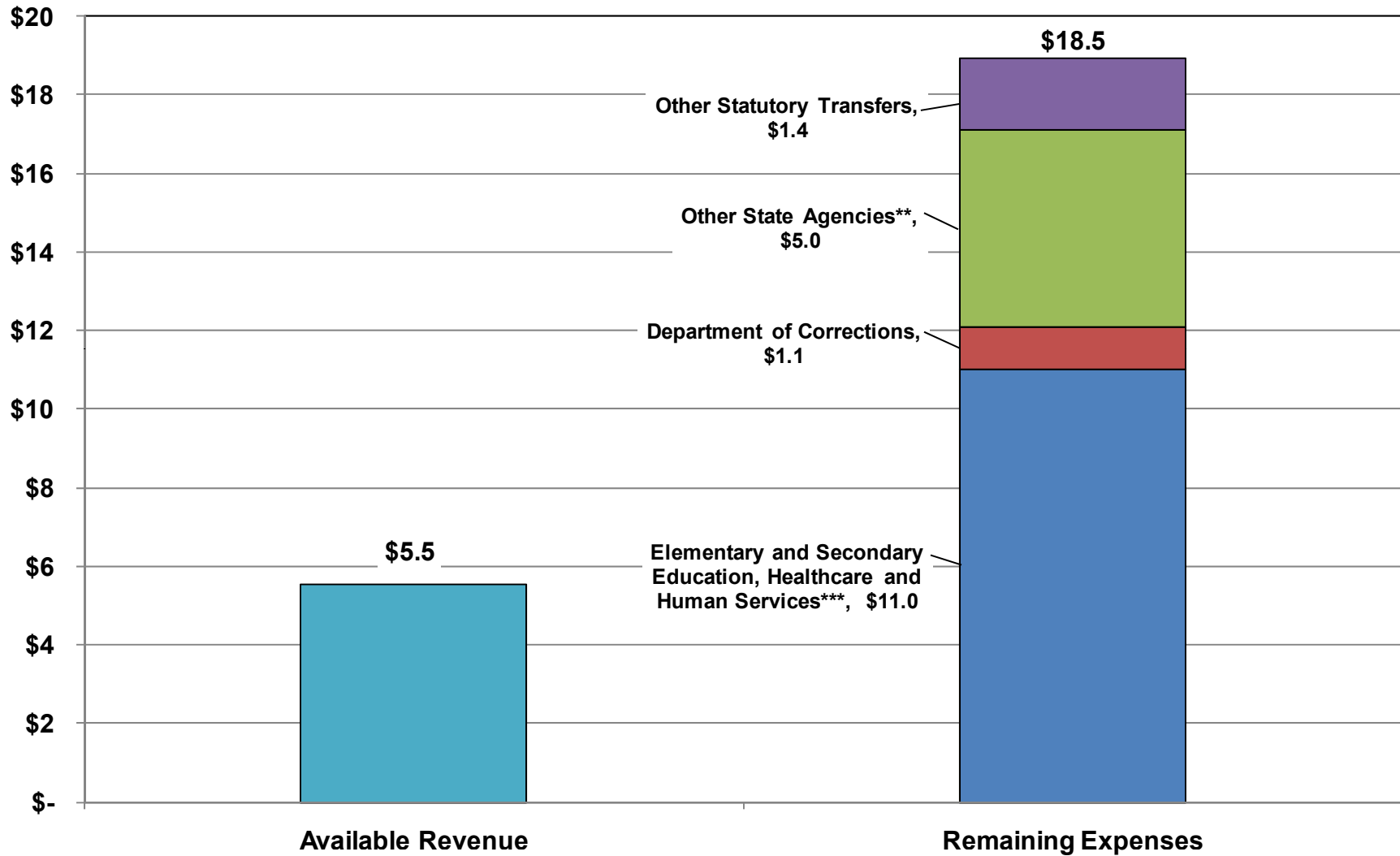
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What was the Deficit Entering FY2011?

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

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

**Illinois' FY2011 Budget Dilemma:
Available Revenue Compared to Remaining Expenses (in \$ billions)
(After Funding Deficit and Other Necessary Expenses*)**



*Includes Debt Service, state-source General Funds Medicaid spending and General State Aid.

**Other state agencies include the Judiciary, the State Police, the Secretary of State, elections, and other government operations.

***Excludes state-source General Funds Medicaid spending and General State Aid to elementary and secondary education.



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Revenue Solutions

- Even if the State raised personal and corporate tax rates to equal the highest currently levied in the country (6.0% flat personal income tax and 9.9% corporate income tax), it would still have a \$4.0 billion deficit.
- The State would need to raise the personal income tax rate to at least 7.6% to cover the total budget deficit through the income tax only.
- Illinois already charges the seventh highest sales tax rate of any state for general merchandise at 6.25% and Chicago has the highest composite sales tax rate of any major metropolitan area at 10.25%.
- The State sales tax rate and resulting local composite rates are too prohibitively high to allow further sales tax increases.



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Potential Asset Sales

- In 2006, the Illinois Tollway was valued between \$13 billion and \$15 billion for a long-term lease of 274 miles of toll roads in northern Illinois.
- Privatization of the Illinois Lottery had an estimated value of \$10 billion in 2008, but drew a negative opinion from the U.S. Department of Justice during legislative deliberation.
- Market conditions could be unfavorable to either transaction and likely would reduce the total valuation of these assets.
- Asset privatization revenue **should not** be used to solve current or near term budget shortfalls. Proceeds from asset sales should only be used to reduce debt or pay down pension liabilities.



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Recent Local Asset Sales

- The City of Chicago's \$2.5 billion Midway Airport privatization deal collapsed in 2009 due to poor market conditions.
- The majority of the proceeds from Chicago Skyway lease and parking meter lease were used for current operations.
- A rush to fill the City's operating budget deficit may have caused the Chicago parking meter lease to be undervalued by millions.
- Using revenues from asset sales to fill current or near term budget shortfalls creates future budget deficits.



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Civic Federation Rehab Plan for Illinois

- Illinois' crisis requires a comprehensive approach to stabilizing the State's finances.
- Illinois must implement comprehensive reform of its pension systems.
- Expenditures in FY2011 must be rolled back by \$2.5 billion with exceptions for Medicaid and some education spending.
- Only if pension reform and significant spending cuts are made should Illinois raise the income tax on individuals and corporations, end the exemption for retirement income, and raise the cigarette tax.



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Evaluating Budget Ideas

Deficit Reduction Plan Comparison				
Principle	Budget Cuts Only	Budget Cuts and Borrowing	Revenue Increases Only	Civic Federation Plan
Does not use borrowing to fund operating deficits	Yes	No	Yes	Yes
Provides funding for critical services	No	No	Yes	Yes
Creates incentives to find government efficiencies	Yes	Yes	No	Yes
Does not harm local governments	No	No	Yes	Yes
Does not reduce funding for programs eligible for federal recovery funds	No	No	Yes	Yes
Properly funds statutorily-required contributions to the pension systems	No	No	Yes	Yes
Does not create an economically prohibitive environment	No	No	No	Yes
Reduces the future structural deficit	Yes	Yes	Yes	Yes



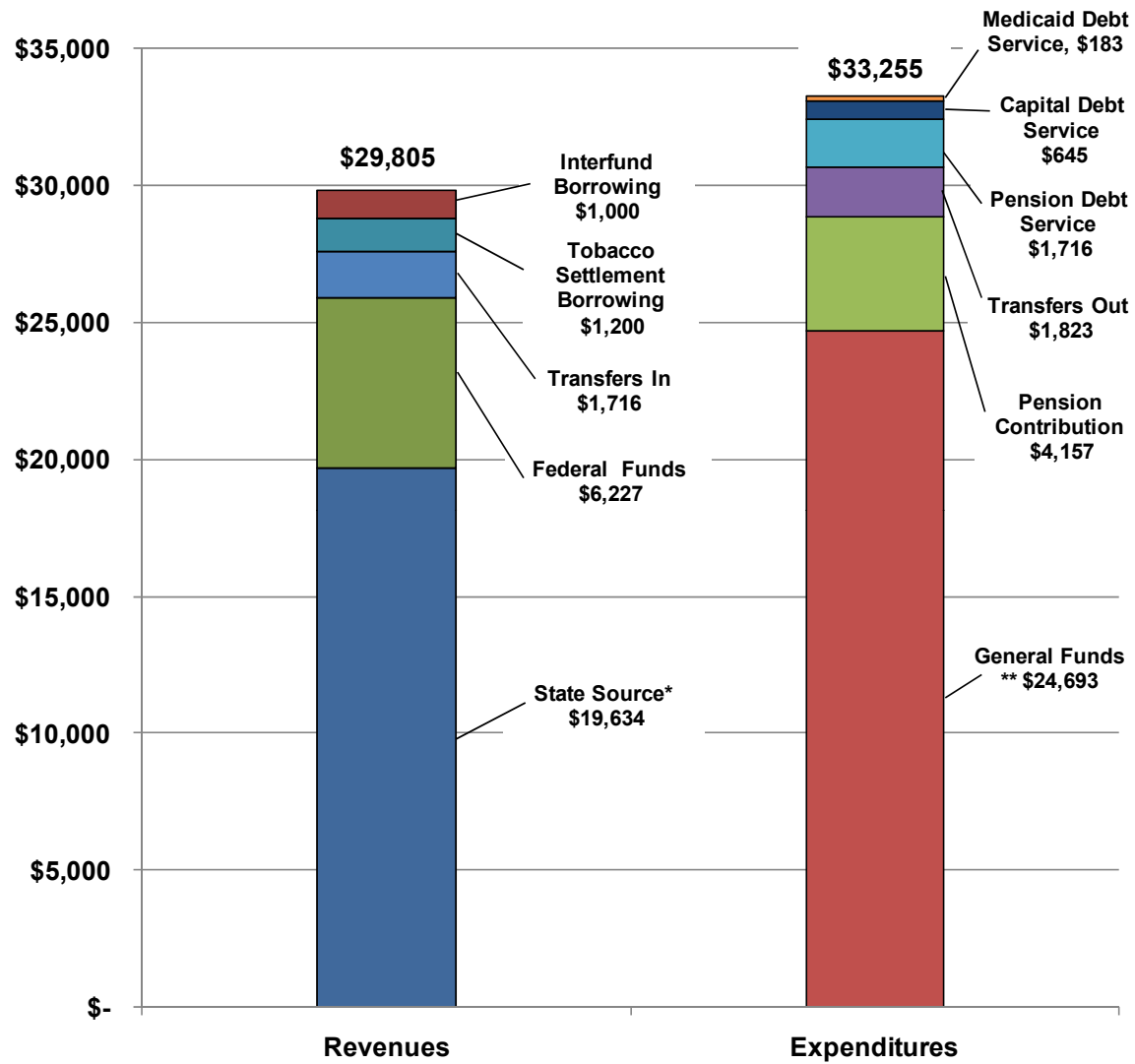
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An Important First Step Toward Pension Reform: SB1946

- Earlier this spring, the Illinois General Assembly passed and Governor Quinn signed into law pension reform legislation.
- Applies to all state pension plans and most local plans except police and firefighters.
- Benefit changes only apply to future, not current, employees.
- Raises retirement age to 67, early retirement to 62.
- Limits maximum pensionable salary to \$106,800.
- Eliminates double-dipping.
- Overhauls cost of living adjustments.
- Allows CPS to take a partial pension holiday for the next three budget years.
- No increases to employer/employee contributions.
- Civic Federation supports this bill and urges further reforms.

State of Illinois FY2011 Budget Remains Unbalanced



Sources: State of Illinois, Preliminary Official Statement, \$300 million, General Obligation Bonds, Taxable Build America Bonds, Series 2010-4, June 3, 2010, p. 30 and Civic Federation communication with Governor's Office of Management and Budget, June 3, 2010.

*State Source Revenues reduced by \$50 million for estimated cost of sales tax holiday.

** General Fund Appropriations of \$26.0 billion reduced for expenditures by procurement reform (\$300 million) and estimated FY2010 salvage (\$1,020 million).



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Consequences of the Current Budget Crisis

- The FY2011 budget does nothing to reduce the \$6 billion backlog of bills from FY2010 and increases the delay in payments.
- Fitch and Moody's have downgraded State of Illinois' debt rating, citing the General Assembly's failure to pass a balanced budget, growing debt burden and continued use of one-time revenues for operations.
- By enacting appropriations beyond expected revenues and continuing to delay paying bills, the State creates uncertainty and instability for vendors, service providers and agencies that depend on state funding or provide services for the State.
- The State deficit will most likely grow in FY2012 due to the cost of borrowing, the loss of one-time revenues and a possible increase in pension contributions.
- By not dealing with the crisis now, deeper cuts and larger revenue increases will be needed in the future to cope with growing deficit, debt and liabilities.