

Fiscal Year 2008 Budget



Investing in Illinois' Families

HEALTH CARE | EDUCATION | PENSIONS | TAX FAIRNESS



ROD R. BLAGOJEVICH
GOVERNOR, STATE OF ILLINOIS



Long Standing Issues

Structural Budget

- Not including the service economy
- Ineffective outdated corporate income tax
- Size and growth of state government

Pension

- Insufficient funding for more than 30 years
- Unfunded liability of \$40.7 billion
- An unpaid debt with interest of 8.5%



Long Standing Obligations

Structural Budget

- Reduce the size of government
- Change the direction of government spending
- Revenues that grow with the economy

Pensions:

- Initiated benefit reforms
- Increased funded ratio to 60%
- Reduce the future deferment of payments and reduce the pension debt to affordable level

Health Care:

- All Kids
- Family Care
- Managed care
- 1.4 million uninsured

Education:

- Invested \$3.8 billion in 4 years
- Opened access to universal preschool
- Raised performance standards for high schools
- Growing inequity in school funding



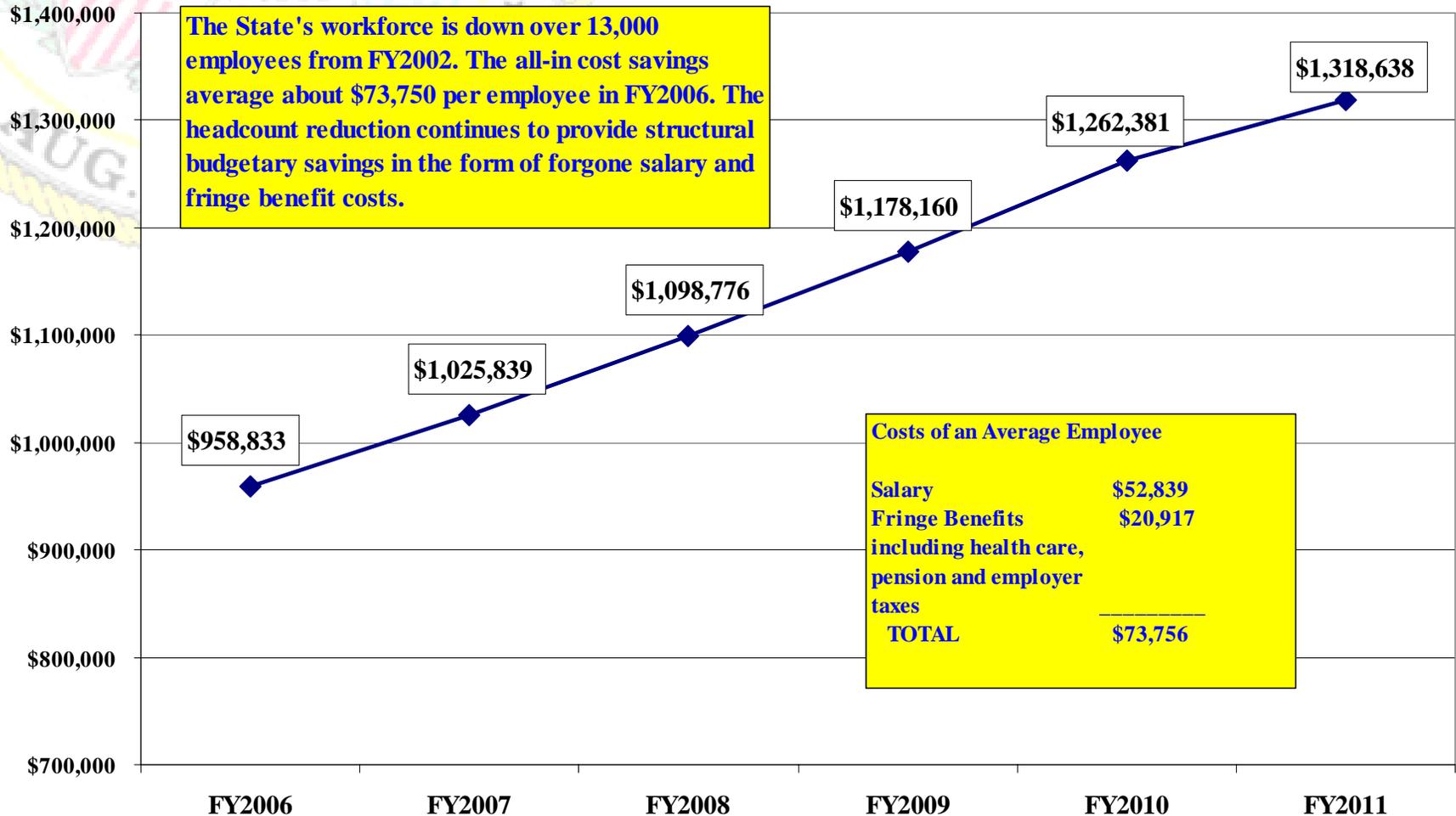
- Expected \$5 billion operating deficit
- \$43 billion pension debt—48% funded level
- \$4.1 billion existing GAAP deficit
- Inflated state payroll
- 250,000 jobs already lost during economic recession



- Eliminated expected operating deficit
- Reduced long-term pension debt, invested \$13 billion and increased funded level to 60.5%
- Reduced historical GAAP deficit by 44% - (to \$2.3 billion)
- Cut 13,000 state payroll positions, saving \$900 million annually
- Jobs:
 - Illinois leads Midwest in job growth for 3 years
 - In January, Illinois ranked #1 in the country with a gain of 19,900 new jobs
 - Three-month moving average unemployment rate was 4.3% in January, 3rd lowest average rate since May 1999



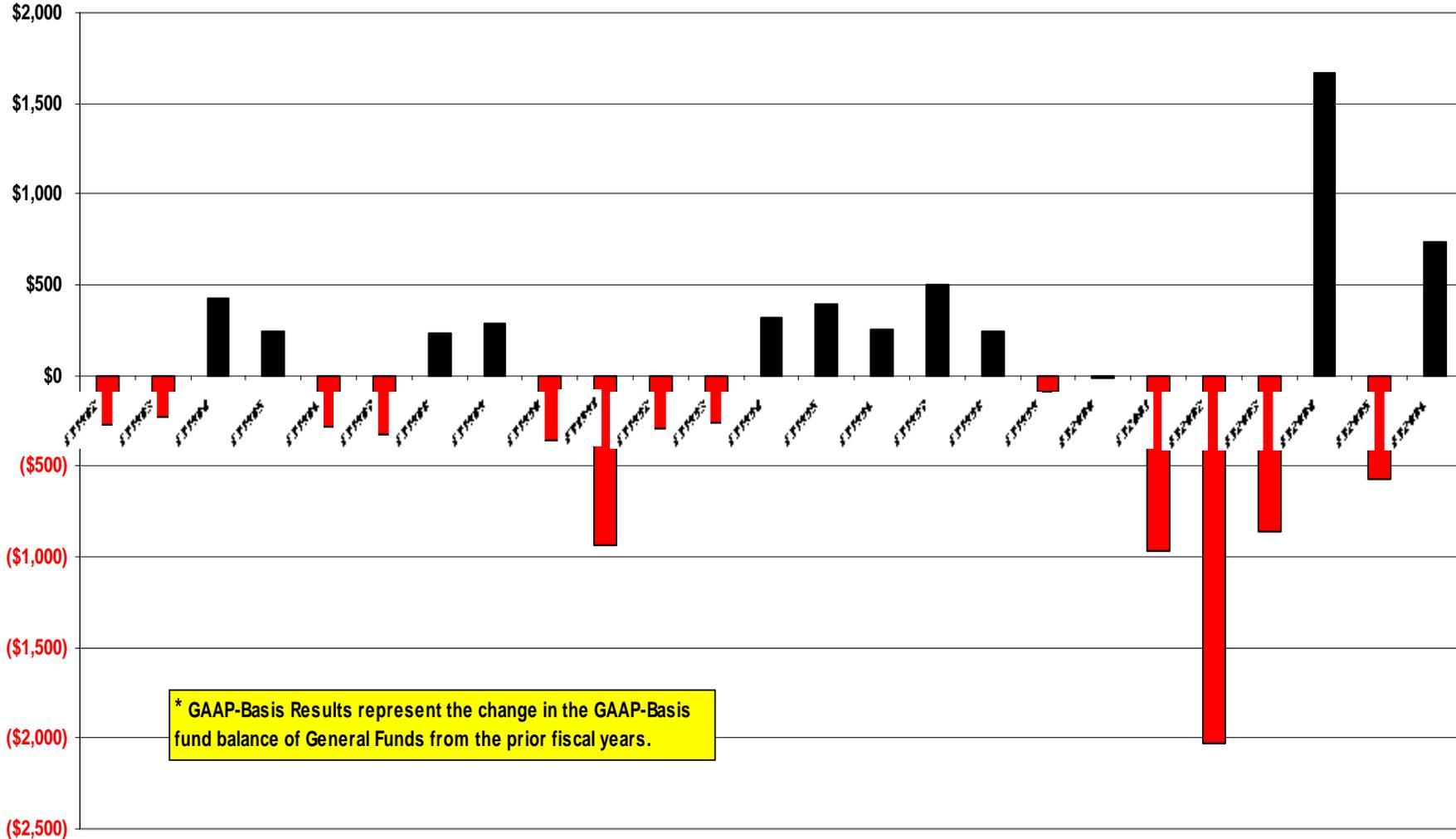
Savings From Headcount Reductions Increase Each Year





GAAP-BASIS ANNUAL RESULTS *

(in \$millions)

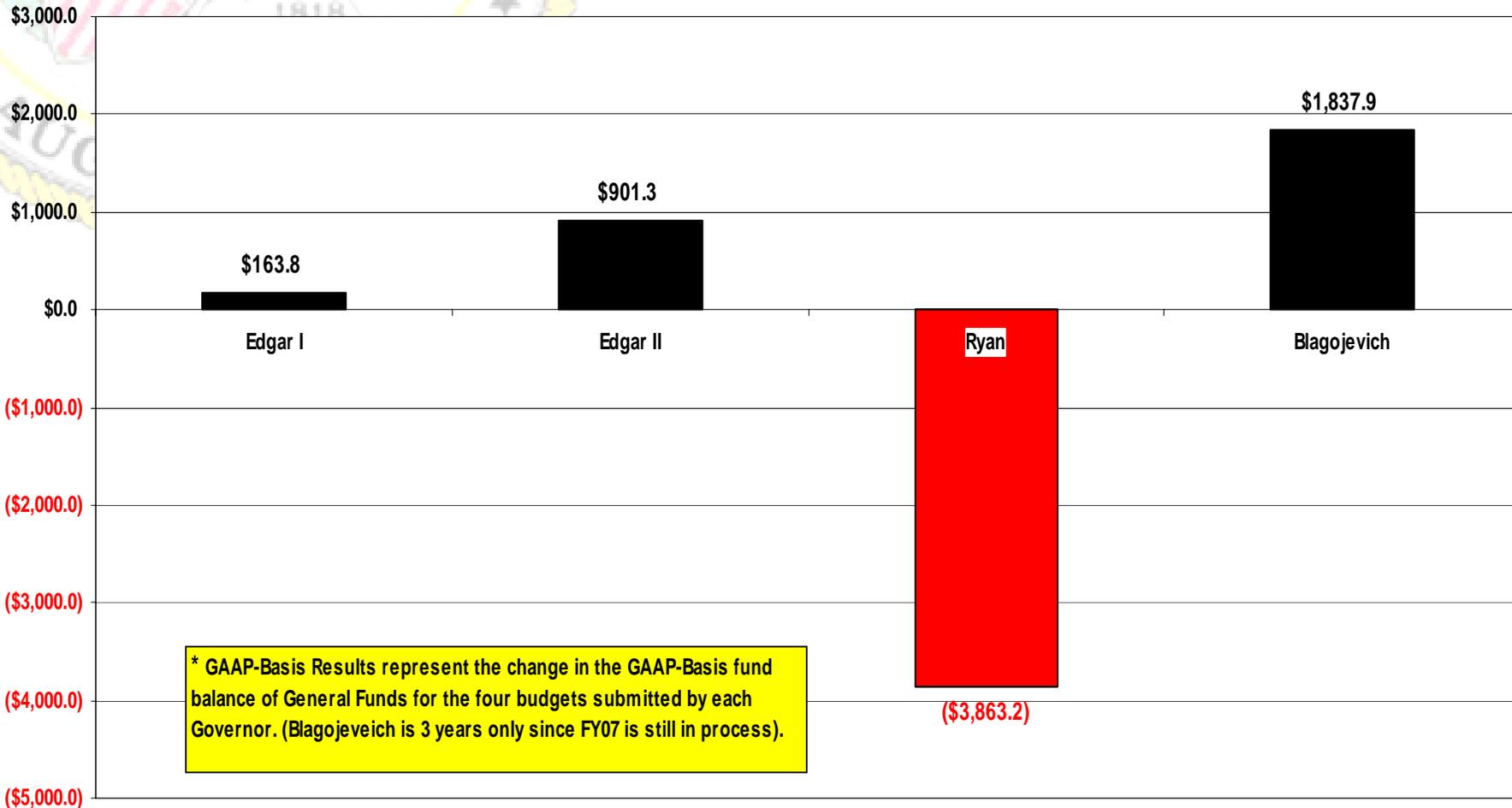


* GAAP-Basis Results represent the change in the GAAP-Basis fund balance of General Funds from the prior fiscal years.



GAAP-BASIS RESULTS BY GOVERNOR *

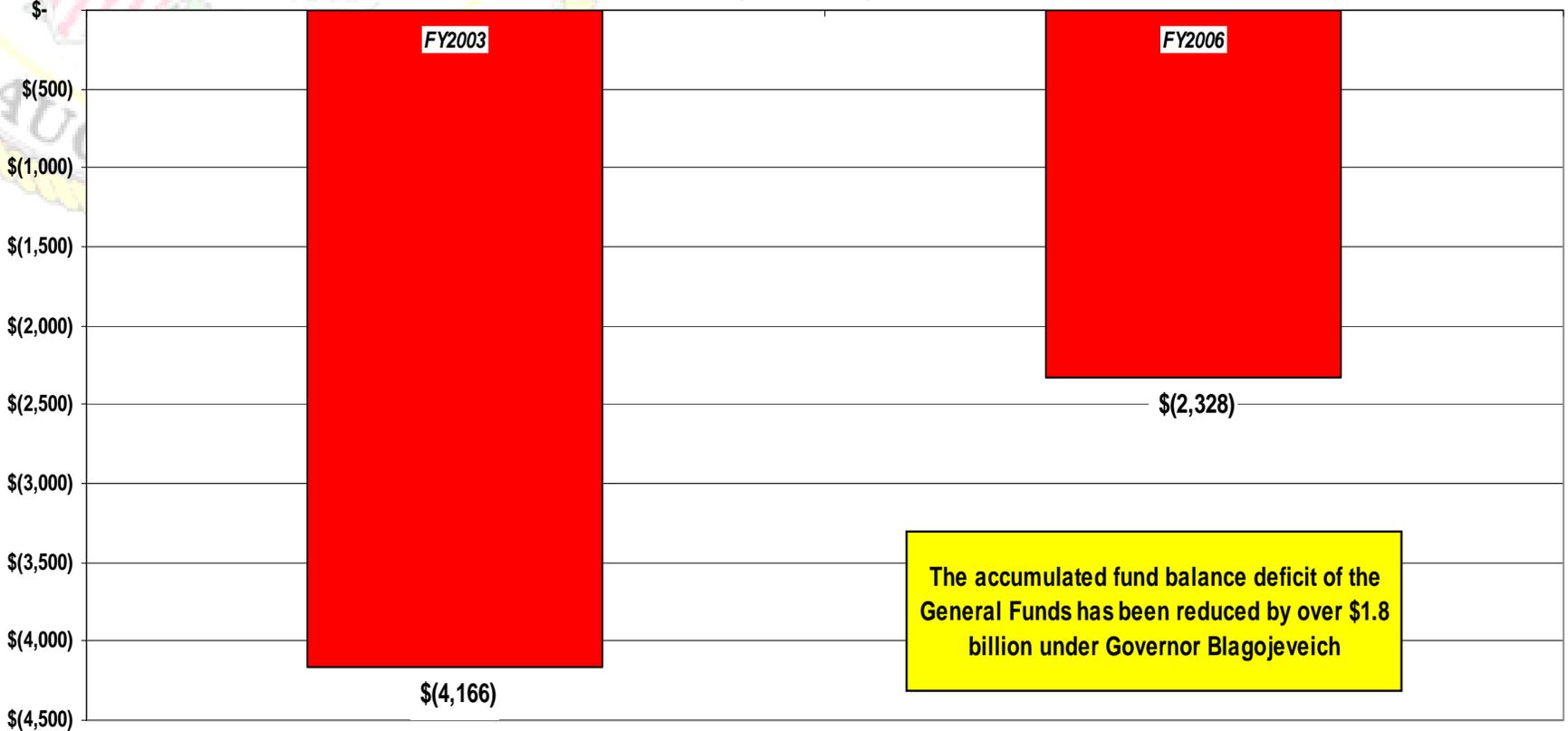
(in \$millions)





GENERAL FUNDS: GAAP-BASIS FUND BALANCE DEFICIT

(in \$ millions)



SOURCE: Illinois - Comprehensive Annual Financial Reports

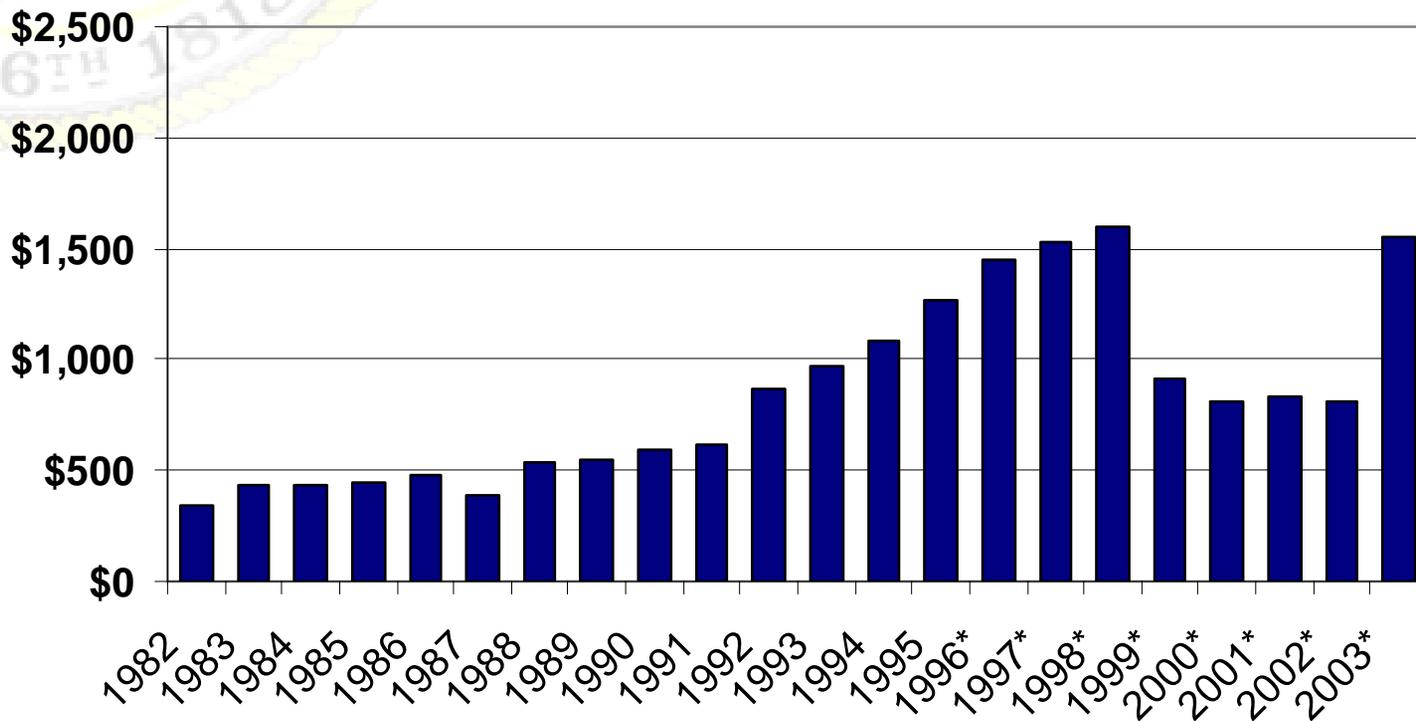


Where We Started—Escalating Pension Debt

From FY93 to FY03, pension payments were underfunded by at least \$870 million annually.

Pensions were underfunded every year for more than 30 years.

Annual Amount of Underfunding
Each Year (millions)

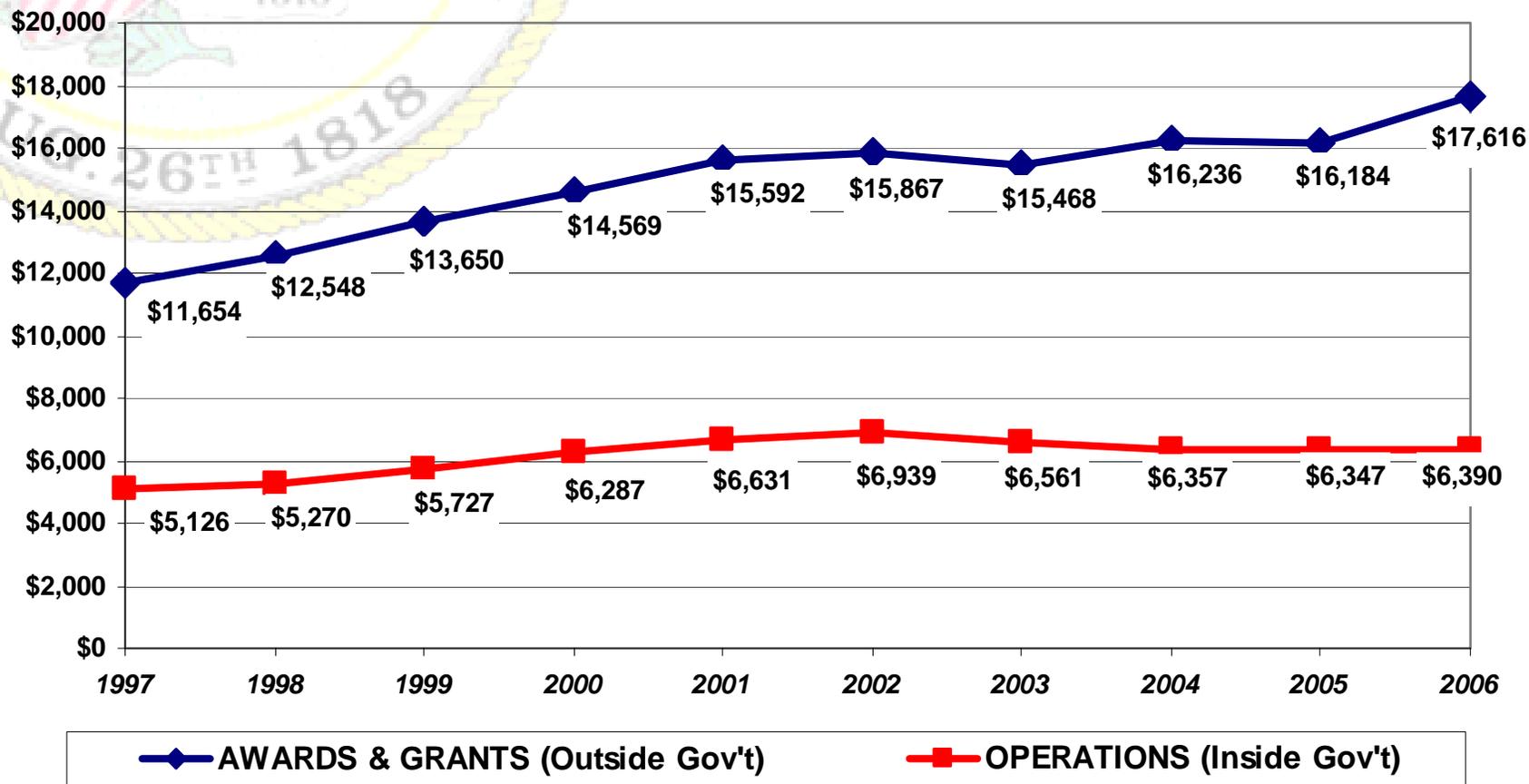


The Total **UNDERFUNDING** increased from 1982 – 2003 by \$18.5 Billion.



Reducing the Cost of Running Government

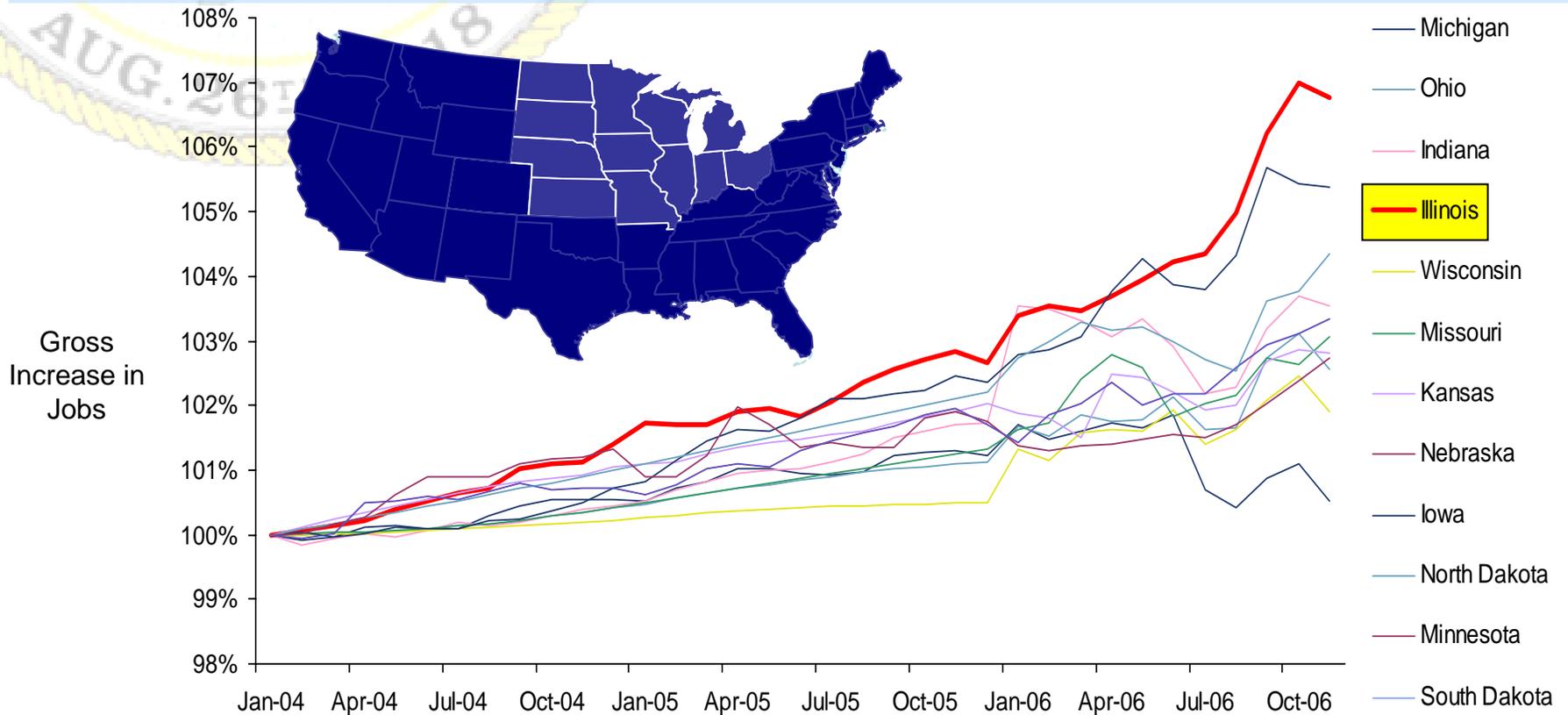
General Funds Spending 1997-2006





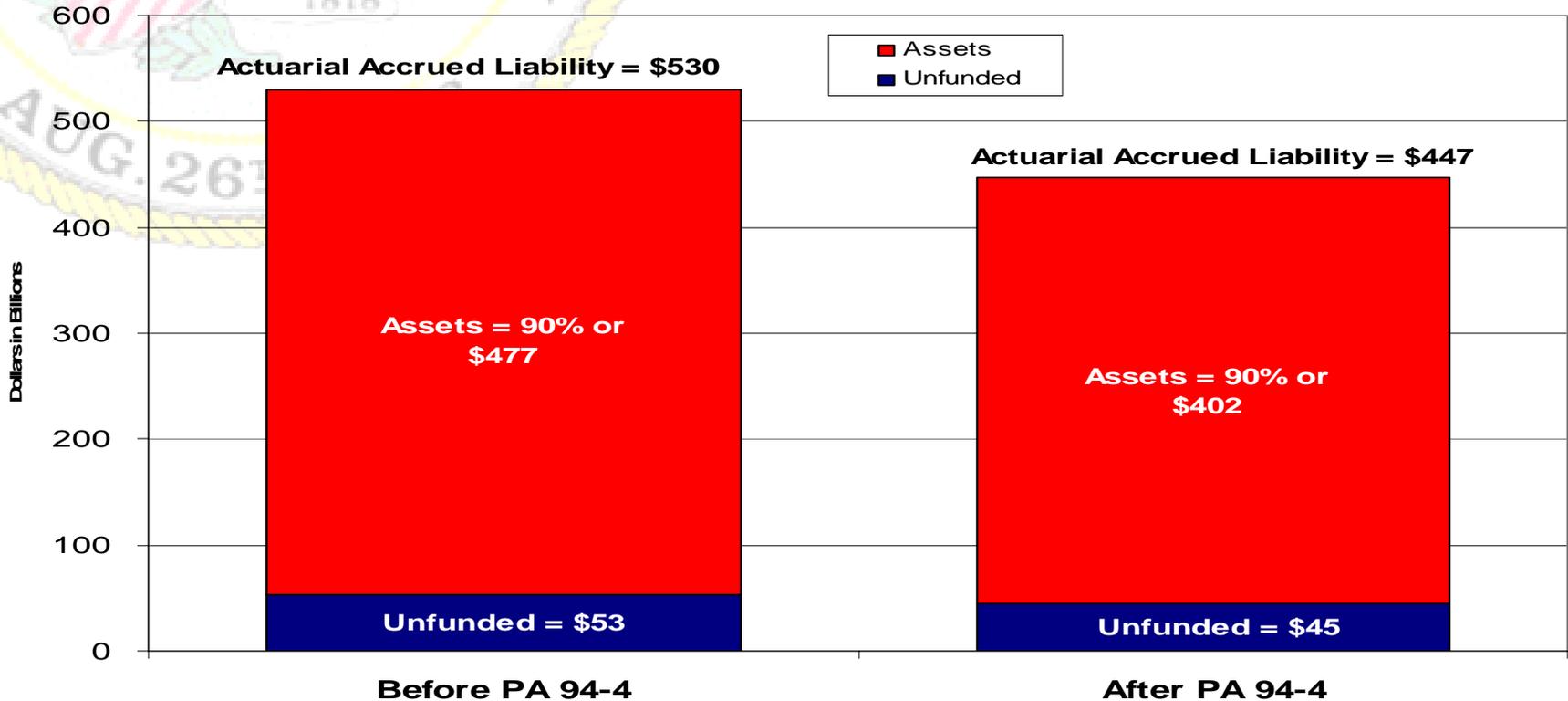
Illinois has had the highest job growth in the Midwest since 2004.

- Created 160,000 new jobs to bring unemployment levels down to near record lows
- Raised the minimum wage for 450,000 workers and guaranteed equal pay for women
- Unemployment of 4.6% is near all-time lows





Pension Systems Accrued Liability in 2045
PA 94-4 has already reduced pension liability by \$83 Billion (16%)

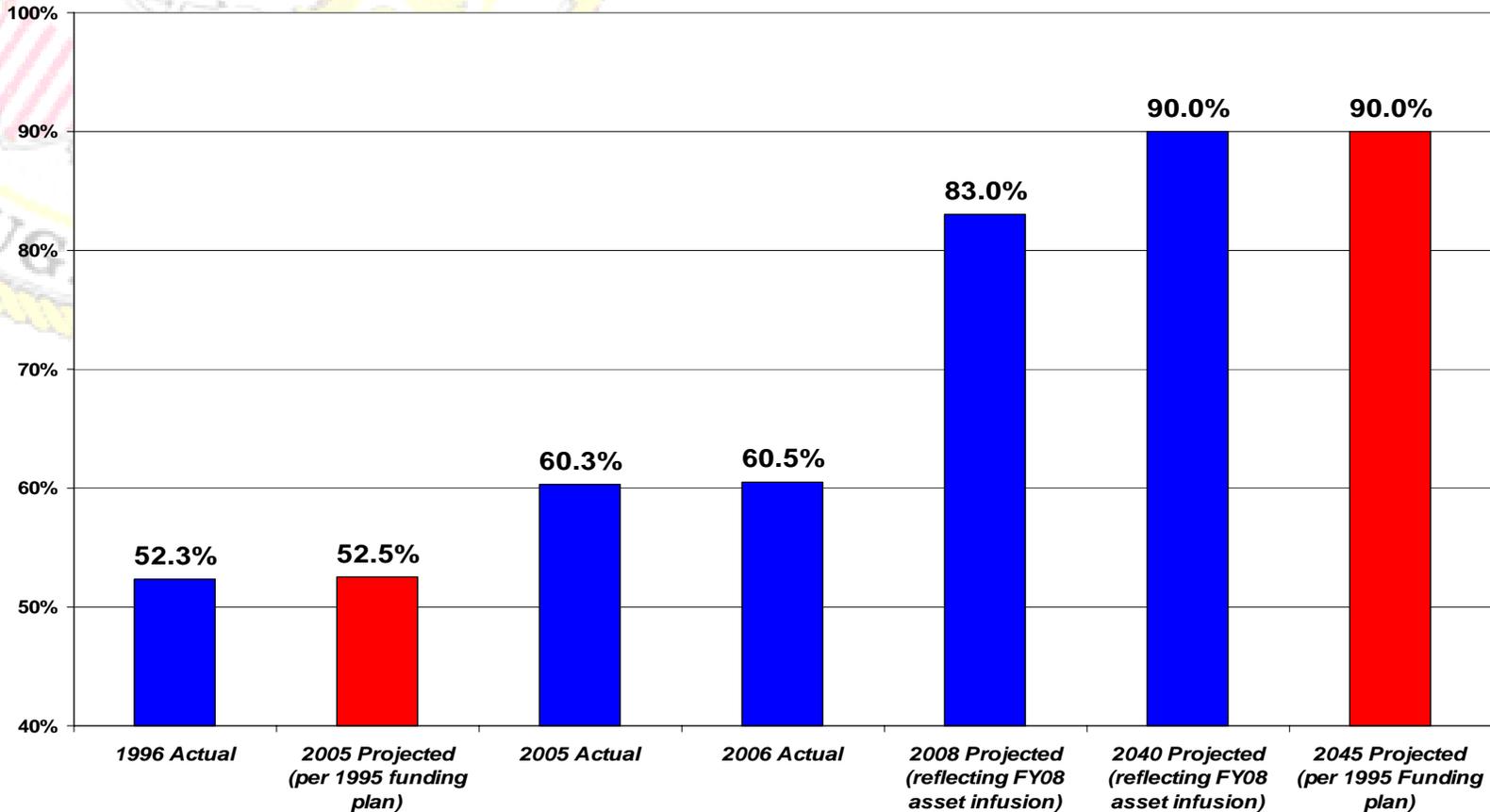


Pension reform also contains a long-term viewpoint – according to the system actuary reports, the liability of future generations of taxpayers has been reduced by \$83 billion as a result of pension reform passed and signed by Governor Blagojevich.



Funded Ratios

1995 Plan. Actual & Proposed Asset Infusion



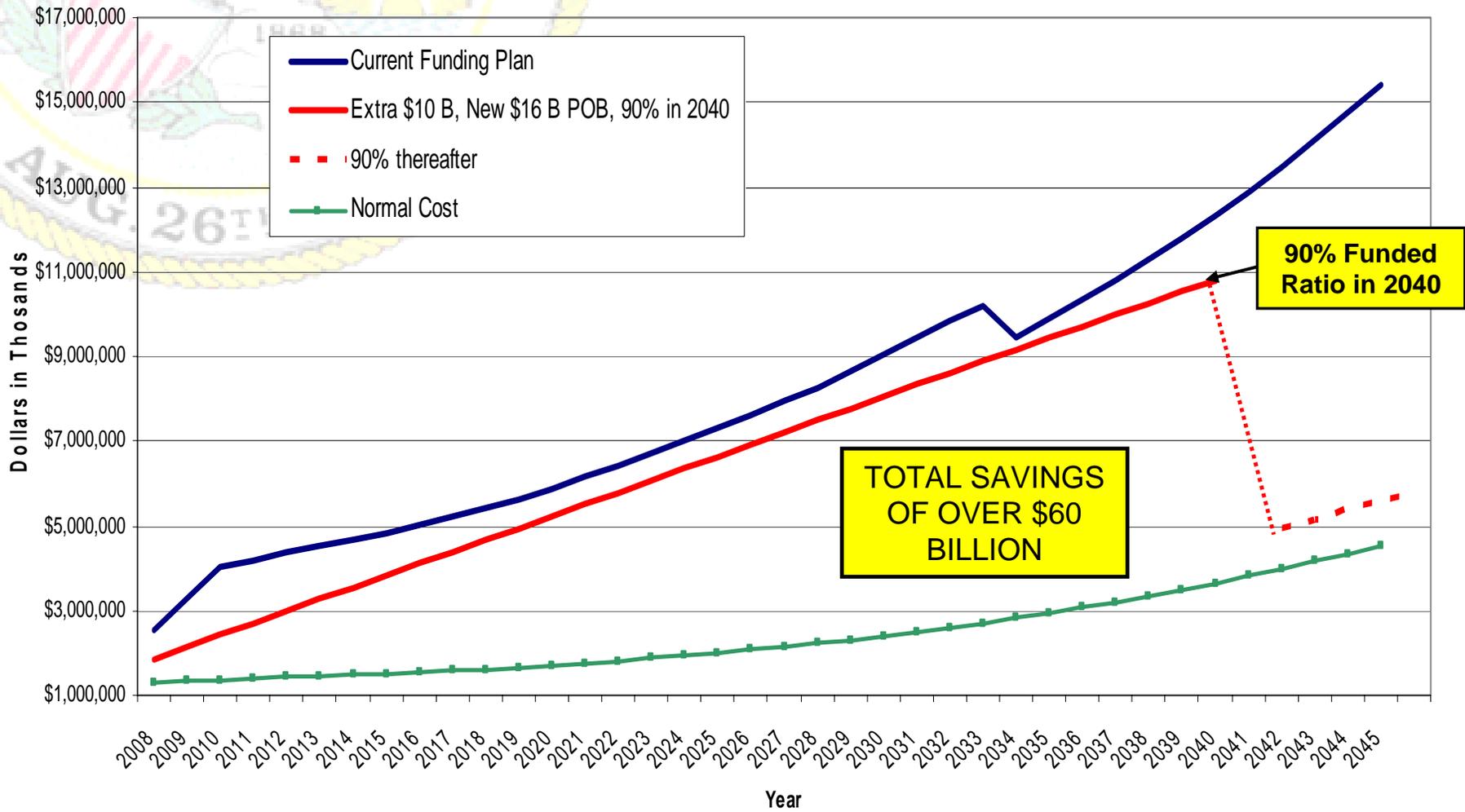
Source - System Actuarial Reports

Under the terms of the 1995 Funding Plan, a 60.5% funded ratio (Actual 2006) was not planned for until 2016



THE FY2008 PROPOSAL: \$26 BILLION ASSET INFUSION

State Contribution Including Debt Service





Immediate cash infusions allow the state to fund the annual pension contribution affordably

\$26 billion will:

- Immediately increase the pension system's funded ratio to over 83%, 34 years ahead of the current 50-year funding plan schedule.
- Make annual payment schedule more predictable and affordable and reach 90% funded ratio in 2040, five years early.
- Replace interest rate on \$16 billion in pension debt (at 8.5%) with a lower rate.
- Over the next 10 years, save over \$1 billion per year that the state can use to fund core priorities, like education and healthcare.
- Bottom Line: Saves over \$60 billion!



Pension Reforms Cure Structural Budget Deficits

(\$ in millions)	First Year	No Cash	Proposed Cash
	Costs	Infusion	Infusion
	<u>FY2008</u>	<u>FY2011</u>	<u>FY2011</u>
Revenues*			
Base Revenues	\$ 29,392	\$ 32,955	\$ 32,955
New Revenues (Less GRT)	\$ 147	\$ -	\$ -
Total Revenues	\$ 29,539	\$ 32,955	\$ 32,955
Spending**			
Base Agency Spending	\$ 27,488	\$ 30,544	\$ 30,544
Pension Funding (Includes Debt Service)	\$ 1,628	\$ 3,732	\$ 2,387
Total Spending	\$ 29,586	\$ 34,533	\$ 32,931
Base Surplus (Deficit)	\$ (47)	\$ (1,578)	\$ 24
New Revenue Surplus (Deficit)	\$ 65	\$ -	\$ -
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* Discounts Gross Receipts, Lottery Lease and Illinois Assessment Revenues

** Discounts Covered Illinois, Education Funding Increases, Property Tax Relief and Capital Program



Rising Uninsured, Rising Costs & Thoughtful Solutions

- **Rising uninsured:** Over 1.4 million adults in Illinois are uninsured.
 - **320,000 are below the Federal Poverty Level.**
($\$10,210$ for an individual, or $\$20,650$ /year for a Family of 4)
 - **Almost 800,000 are middle class.**
(Earn between 100% - 400% of the Federal Poverty Level)
- **Rising Costs:**
 - **Nationally, the cost of premiums for family coverage ($\$11,480$) exceeds the earnings of a full-time, minimum wage worker ($\$10,712$).**
 - **Health insurance premiums for employers increased nearly 87% between 2000 and 2006.**
- **Thoughtful Solutions:**
 - **Based upon the *Health Care Task Force's* deliberations including both mandated and non-mandated models**
 - **Navigant and Mathematica developed assumptions then analyzed and estimated costs**
 - **Mercer conducted independent audit of all estimates and assumptions**
 - **Budget reflects conservative forecasts**



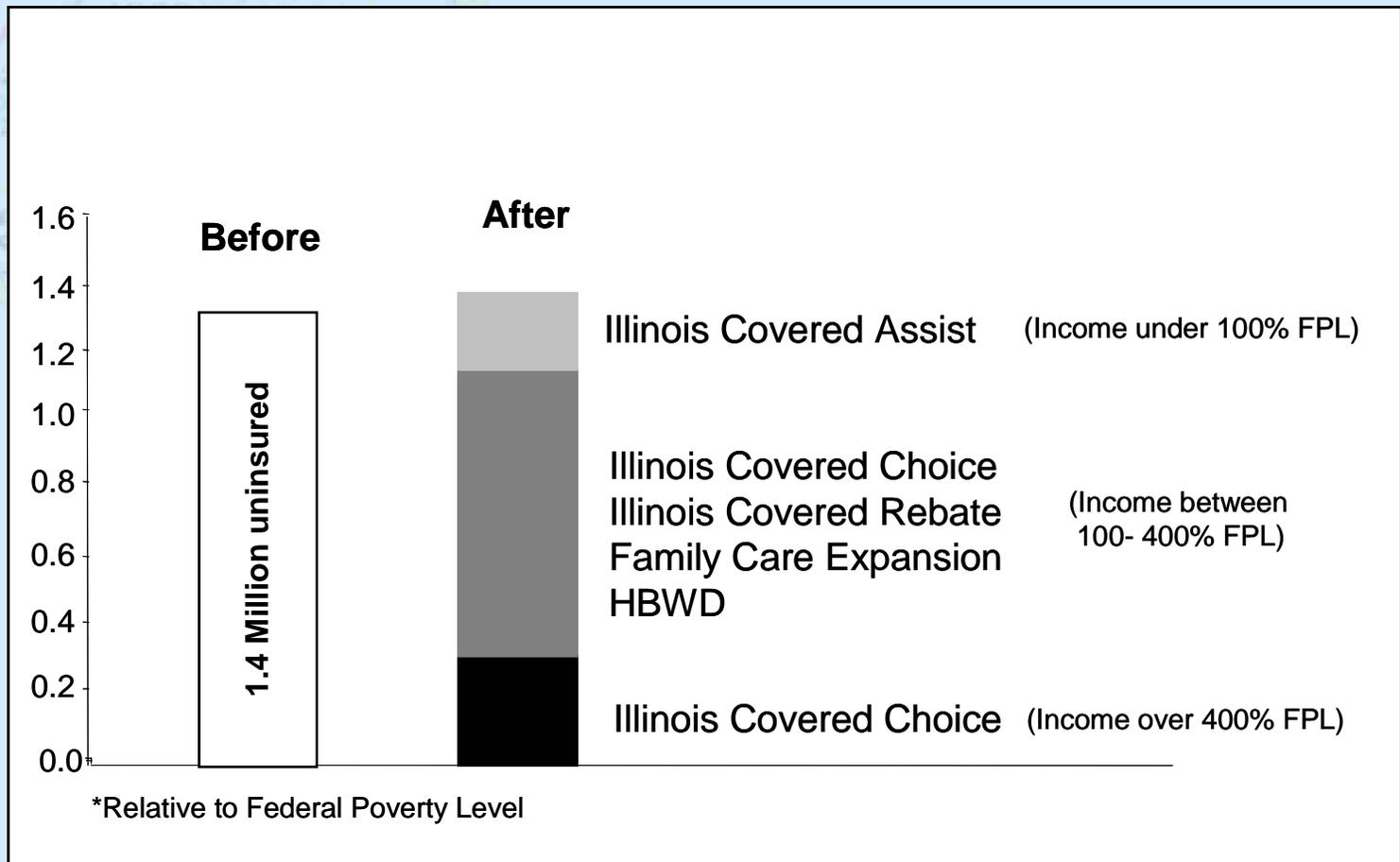
Affordable Healthcare for All



- 1. Illinois Covered Choice** – Small businesses and individuals will be able to buy into guaranteed, affordable private plans.
- 2. Illinois Covered Rebate** – Middle class families will be able to get help paying their premiums.
- 3. Illinois Covered Assist Expanding Existing Programs** – Low-income adults and middle class families will be able to get coverage through healthcare program expansions and a new program to cover adults under poverty without children.
- 4. Reform the Health System** – Strengthen family coverage, better manage chronic diseases, and make the system transparent.
- 5. Strengthen Family Coverage** – Allow parents to keep their young adult dependents on their insurance policy until they are age 29.



Who Does *Illinois Covered Cover*?





Illinois Covered – Everyone Will Benefit

- **Everyone in the state will benefit** from reforming the healthcare system through stronger family coverage, new consumer protections, system improvements and a roadmap to health for wellness and managing chronic disease. (Estimated Cost: \$16 million)
- **Over 1 million people and small businesses** will be able to purchase Illinois Covered *Choice*, a new guaranteed, affordable insurance product offered by the state. (Estimated Cost: \$225 million)
- **Millions of people** will be eligible for help paying their health insurance premiums through Illinois Covered *Rebate*. (Estimated Cost: \$850 million)
- **500,000 middle class and low-income families** will be eligible for coverage from Illinois Covered *Assist* or the *FamilyCare* expansion. (Estimated Cost: \$950 million)
- **Illinois Covered Assessment**- A payroll tax on businesses of 10 or more employees that choose not to pay or pay very little health care costs for their employees.



Helping Kids Learn

\$10 billion will be invested in schools over the next 4 years.

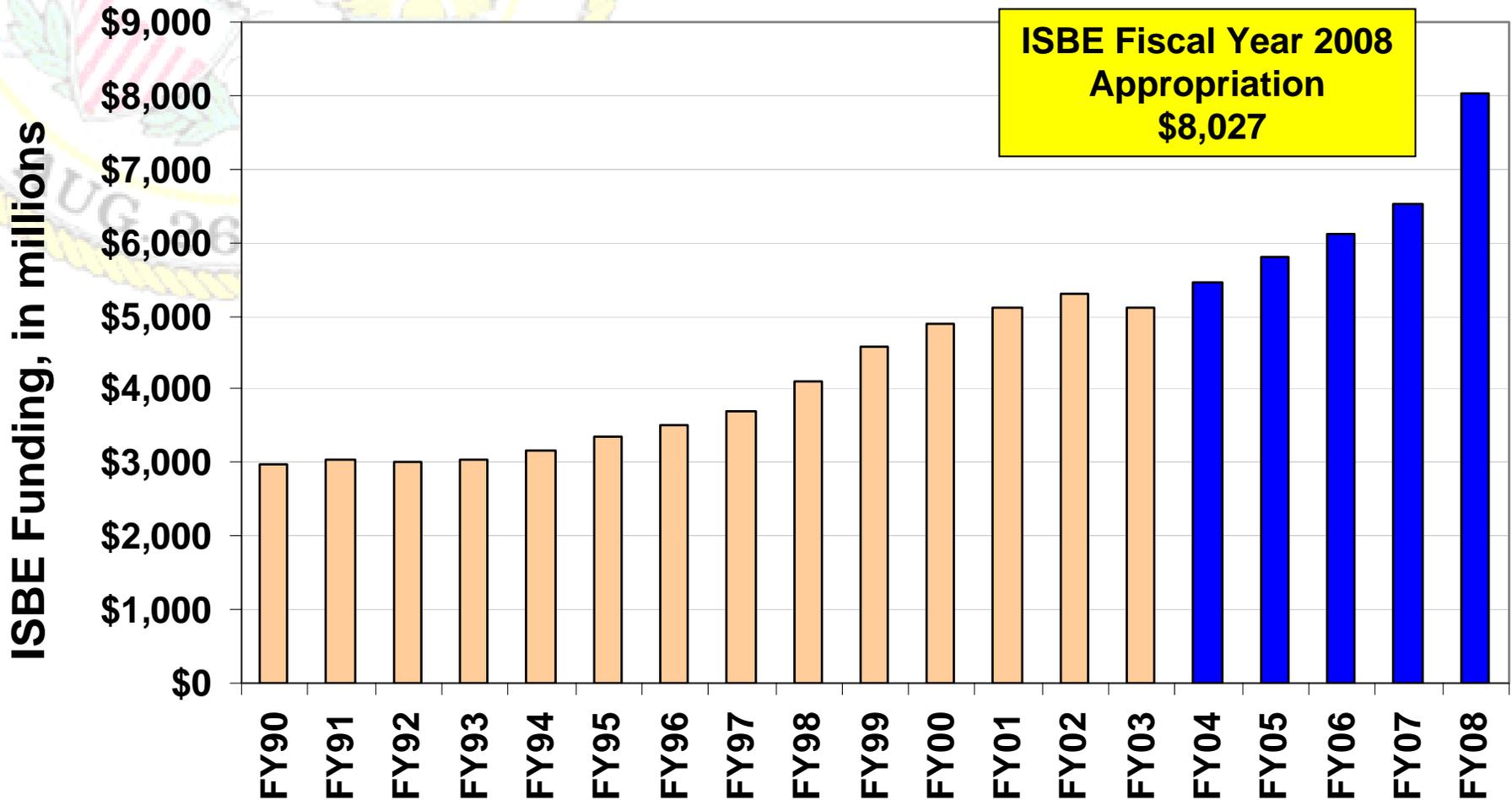
- **In Fiscal Year 2008 the state will invest \$1.5 billion.**
- **This is the largest one-year increase ever.**
- **Much of the increased funding is tied to performance & accountability measures.**

This continues Governor Blagojevich's record of providing more education funding than any administration in history.



Invest in Education

\$1.5 billion increase in education funding in FY 08





Illinois' Unfair Tax System

Tax burden on individuals is growing

- The tax burden on individuals has been steadily rising since the 1970s. Then, individuals paid \$4.00 in income taxes for every dollar paid by corporations. By 2004, the ratio jumped to \$7.12 – an increase of 75%.

Many large businesses avoid taxes because of loopholes and apportionment

- On average from 1997 - 2004, nearly half of all corporations with at least \$50 million in annual Illinois sales did not pay any state income taxes.
- 37 Fortune 100 companies paid NO Illinois state income taxes in 2004. These companies averaged \$1.2 billion in sales in Illinois during that year.

Illinois' tax system is out of date, and relies too heavily on "old economy" biz

- The Corporate Income Tax (CIT) is designed for taxing "old economy" businesses that produce goods and, therefore, doesn't adequately capture tax revenue from services businesses that make up the majority of today's economy:
 - Goods-based businesses make up only 35% of Illinois' economy, but pay 53% of CIT
 - Services-based businesses make up 65% of Illinois' economy, but pay only 47% of CIT

This flawed and unfair system must be reformed



Illinois' Unfair Tax System

What are some of the options for tax system reform?

- Corporate income tax increase: Regardless of how much the CIT rate is increased, it won't make those who already avoid paying taxes pay a penny more – only those who already pay taxes will. Not a fair alternative.
- Individual income tax increase: Individuals are already unfairly burdened with paying the far majority of income taxes, and it is a regressive tax. Not a fair alternative.
- Expanding sales tax on services: Already assessed at a high (5% to state) rate. Regressive tax on consumers. Not a fair alternative.

These alternative revenue options only reinforce existing tax inequities



Over \$7 billion per year in new revenue

- **Gross receipts tax will be applied beginning January 1, 2008.**
- **All taxes are imperfect and disruptive – broad base allows low rates to minimize both.**
- **Companies over \$2 million will pay**
 - 0.85% rate for sales, manufacturing, construction and related activities
 - 1.95% rate for services provided
- **Companies with more than \$2 million in Illinois sales will pay the GRT; companies with Illinois sales under \$2 million will pay CIT.**
- **Net of CIT credits, IDOR estimates over \$7 billion in new revenue generated per year when fully implemented.**
- **Provides \$1 billion in property tax relief to homeowners across Illinois.**
- **Provides a stable and growing revenue source to reduce structural pressures on the state budget.**



Governor Proposal	Other Proposals	Do Nothing
<ul style="list-style-type: none"> • Broad base (reaching all sectors of economy) • A low rate <ul style="list-style-type: none"> - .85% (goods) - 1.95% (services) 	<ul style="list-style-type: none"> • 5% individual income tax (on <u>all</u> personal income) • 8% corporate income tax • 5 - 9.25% sales tax • Some property tax reduction 	
<ul style="list-style-type: none"> • Funds education • Access to health care • Manages pensions • Structural budget reform 	<ul style="list-style-type: none"> • Funds education • No access to health care • Extends pension liability 50 additional years • Continues structural challenges 	<ul style="list-style-type: none"> • No funding for education • No access to health care • Ignores pension liability • No structural reform



Who will not be impacted?

- **Small Business.** Businesses that have total revenues of under \$2 million per year will not be subject to the Gross Receipts Tax. This represents more than **85%** of all businesses in Illinois.
- **Exporters.** All goods and services exported from Illinois to other states and globally are exempt. Imports will be taxed.
- **Essential Products.** Retail sales of foods and drugs will not be subject to the Gross Receipts Tax, and payments that hospitals, doctors, and dentists receive from the state for service Medicaid patients will also be exempt.
- **Industries with Alternative Taxation.** Gaming and Insurance products, which pay alternative taxes, will not be subject to GRT tax for those products.
- **Corporate Income Taxpayers.** All businesses who pay corporate income taxes will receive a 100% tax credit, and the corporate income tax will be ultimately eliminated.

**These are some of the steps in this plan that will help mitigate
“pyramiding” opportunities**



Does the GRT tax the following sales* ?

ISSUE: Does this GRT apply to specific sales* ?	Washington	Ohio	Illinois	Tribune Estimate
Sales between Company Divisions (Vertically integrated manufacturer like GM)	No	No	No	No
Sales to Unaffiliated Company (Wholesaler sells goods to retailer who sells to consumer)	Yes	Yes	Most <i>Small business/ policy exemptions</i>	Yes
Sales to Affiliated Companies (Combined reporting)	Yes	No ("Combination" rule)	No ("Combination" rule)	Yes
Exports to Out-of-State Destinations	Yes	No	No	Yes
Not-For-Profits	Some	No	No	Yes
Small Businesses	Yes	Exemption for Companies less than \$100k, fee for less than \$1m	Exemption for Companies with less than \$2 million	Yes
Capital assets and securities trading	Some	No	Differential Treatment	Yes

***NOTE:** Above responses reflect general rules; limited exceptions exist.



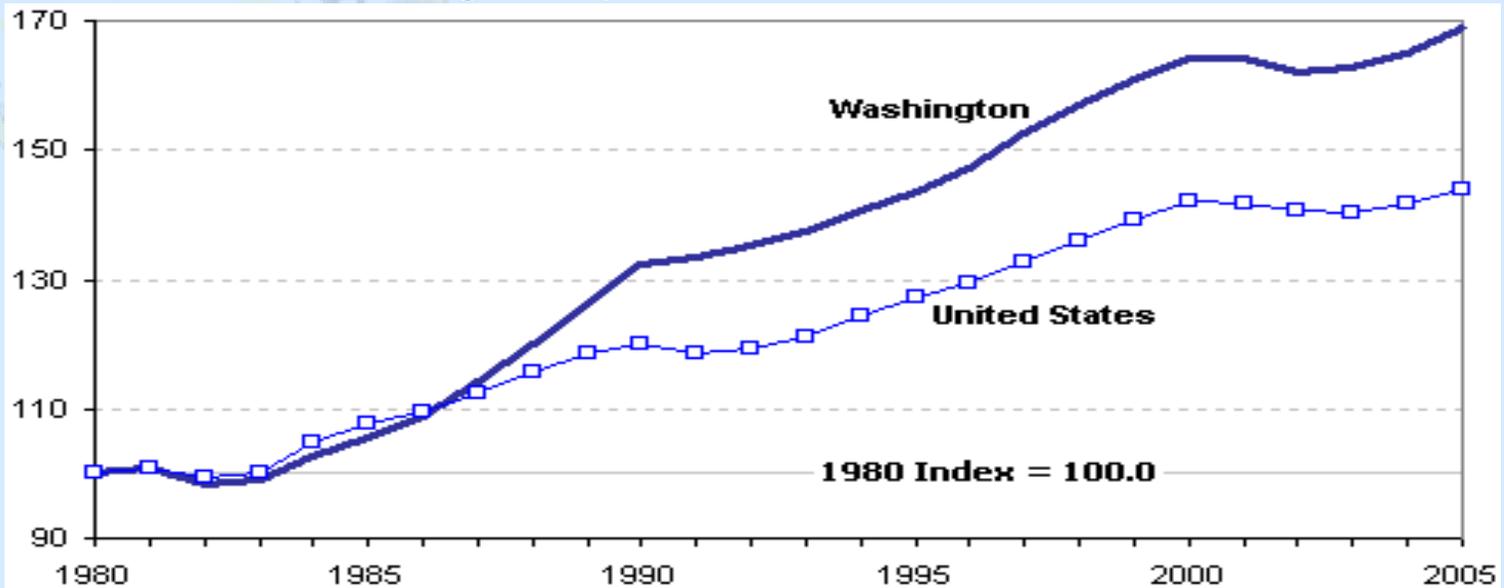
Difference between Estimates of GRT Base

Approach	Description	Base
Cook County Assessor Study	GRT estimate (\$1,300B) is based upon an expansive view of the tax base with no adjustments or exemptions. (NOTE: This is base used in Tribune editorial)	\$1,300B
<i>Less:</i> Adjustments	<p style="color: red;">Intermediate Sales (small businesses and combination rule),</p> <p style="color: red;">Policy Exemptions,</p> <p style="color: red;">Not-For Profits/Tax-Exempt Entities,</p> <p style="color: red;">Exports,</p> <p style="color: red;">Compliance (Collection) adjustment</p>	(\$525B)
<i>Equals:</i> State Estimate for FY2008	State's GRT estimate (\$775B) is based upon a narrower view of the tax base by reducing "pyramiding" effect, not taxing exports, and accounting for the actual compliance experience of Ohio. (Differs from GSP).	\$775B



Washington State Experiences Solid Economic Performance with Long-standing GRT

Washington State outperformed the US economy from 1980-2005 and is a larger exporter than Illinois at half its size



Washington State vs. United States Wage and Salary Employment 1980-2005

*Source: Washington State Office of Financial Management

Per U.S. Bureau of Economic Analysis, growth in Personal Income and Gross State Product for both Washington and Delaware exceeded U.S. averages over past 10



Pension Reforms Cure Structural Budget Deficits

(\$ in millions)	First Year Costs	No Cash Infusion	Proposed Cash Infusion
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New State Revenues Support Bold Initiatives

Senate Bill 1

	First Year Costs	Fully Implemented
(\$ in millions)	<u>FY2008</u>	<u>FY2011</u>
Revenues		
Illinois Gross Receipts Tax (rates .85%/1.95%-2 million floor)	\$ 3,246	\$ 8,426
Illinois Covered Assessment	\$ -	\$ 1,160
Federal Revenue from Illinois Covered	\$ 63	\$ 236
Total Revenues	\$ 3,309	\$ 9,821
Spending		
Increased Education Funding	\$ 1,500	\$ 3,000
Illinois Covered- Health Insurance	\$ 374	\$ 3200-4000
Increased Medical Provider Rates	\$ 90	\$ 478
Offset Road SOS and ISP to GRF	\$ 226	\$ 226
Property Tax Relief	\$ 500	\$ 1,000
Pension Reform (Lottery Revenues)	\$ 542	\$ 650
Capital Program Debt Service	\$ 12	\$ 140
Total Spending	\$ 3,244	\$ 8,694-9,494
Total Surplus (Deficit)	\$ 65	\$ 327-1,127

* Cost estimate depending on implementation of Individual Mandate

New revenues invested outside of State government



An Investment in Illinois' Future

\$14 billion capital program for projects including:

- \$4.8 billion for road construction projects
- \$650 million for construction at public colleges and universities
- \$200 million for public transit projects
- \$100 million for Illinois Community Assets Fund
- \$123 million for Governor's Energy Plan

\$7.5 billion in new bond authorization requested including:

- \$1.7 billion for K-12 school construction projects
- \$3 billion for road construction projects
 - Eliminates road fund transfers that began during Edgar administration
- \$750 million for Energy Plan
- \$600 million for Higher Education
- \$450 million for capital asset maintenance and improvements
- \$425 million for public transit projects
- \$200 million for environmental projects



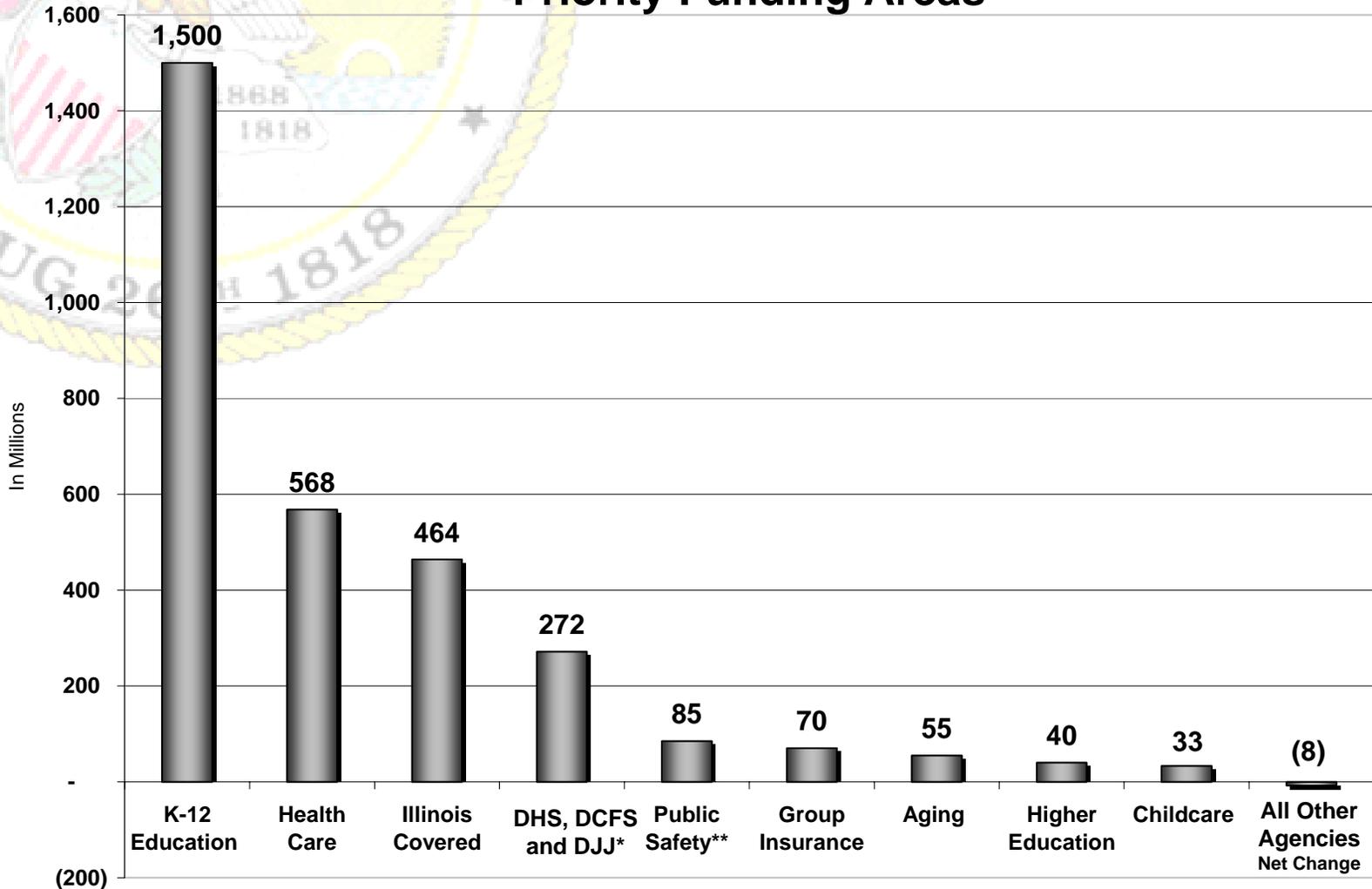
Fiscal Year 2008 Budget is Balanced and Funds Core Priorities

Fiscal Year 2008 Operating Budget					
	<u>FY07</u>	<u>FY08</u>	<u>Growth</u>	<u>Growth Rate</u>	
<u>Base Revenues</u>					
Total Revenue	\$ 28,493	\$ 28,742	\$ 249		0.9%
Economically Sensitive	\$ 18,174	\$ 18,828	\$ 654		3.6%
<i>Individual IT</i>	\$ 9,130	\$ 9,519	\$ 389		4.3%
<i>Corporate IT</i>	\$ 1,688	\$ 1,733	\$ 45		2.7%
<i>Sales Tax</i>	\$ 7,356	\$ 7,577	\$ 221		3.0%
<u>New Revenues</u>					
Gross Receipts Tax	\$ -	\$ 3,309			
Other New Revenues	\$ -	\$ 147	\$ 147		
Loss of Lottery	\$ 650	\$ 108	\$ (542)		
Total Revenues	\$ 28,493	\$ 32,306	\$ 3,813		
<u>Spending</u>					
Agency Appropriations*	\$ 18,346	\$ 19,713	\$ 1,367		7.5%
Statutory Transfers Out	\$ 3,091	\$ 3,101	\$ 10		0.3%
<i>Less Unspent Approp's</i>	\$ (510)	\$ (398)			
<u>New Spending</u>					
P-12 Education	\$ 7,420	\$ 8,909	\$ 1,489		20.1%
Property Tax Relief	-	\$ 500			
Illinois Covered/Healthcare	\$ -	\$ 464	\$ 464		
Total Spending	\$ 28,325	\$ 32,289	\$ 3,964		
Total Surplus	\$ 168	\$ 17			

* Excludes ISBE



General Funds Increases \$3 Billion from FY 2007 in Priority Funding Areas



*Department of Human Services, Department of Children and Family Services and Department of Juvenile Justice



The Fiscal Year 2008 budget:

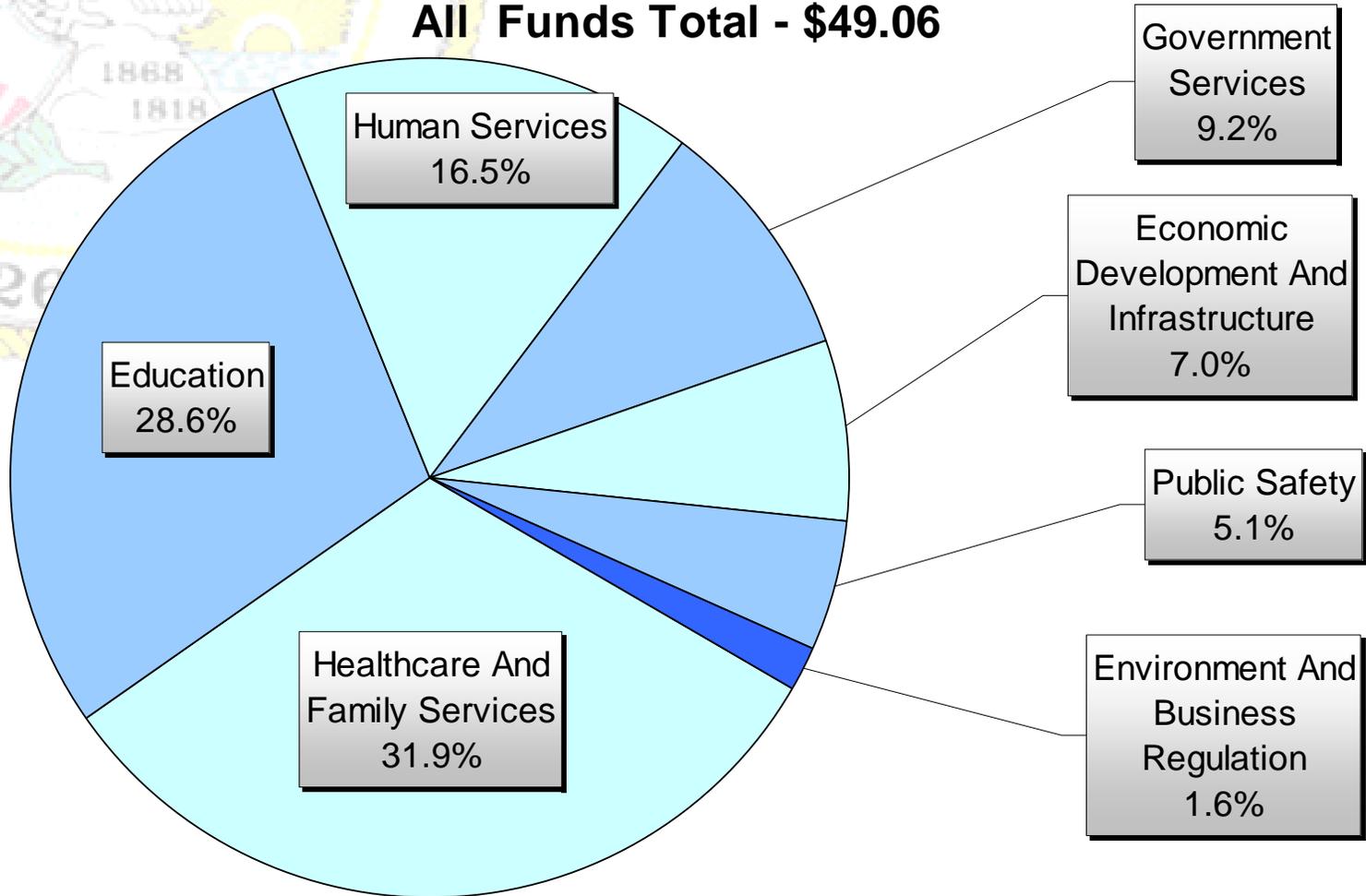
- Proposes a long-term revenue source to meet the on-going costs of providing state services such as education and health care.
- Proposes to reform the state's existing tax system and include all sectors of the economy.
- Provides every adult in the state with access to affordable health care, as already provided to our state's children.
- Provides our schools with the single largest one-year funding increase and an historic \$10 billion investment over the next four years.
- Improves Pension funding significantly: 83% funded, 90% attained 5 years earlier, and saves over \$60 billion.



Selected Financial Information



FY 2008 Operating Appropriations by Major Purpose All Funds Total - \$49.06





Fiscal Year 2008 Operating Appropriations by Major Purpose General Funds Total - \$28.86 Billion

