Titanic and Sinking: The Illinois Budget Disaster

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By Richard F. Dye, Nancy W. Hudspeth and David Merriman

Recently, the state comptroller stated that Illinois is facing "the most dangerous fiscal conditions in modern history."

An Enormous Problem, Rapidly Getting Worse

Can states go bankrupt? Although technically the answer is no, *Crain's Chicago Business* reported in January 2010 that "Illinois appears to meet classic definitions of insolvency: its liabilities far exceed its assets, and the state is not generating enough cash to pay its bills."[1] The problem has only gotten worse in the time since that report appeared. A national survey of state budget gaps released in December 2010 reported that Illinois' $13 billion deficit accounted for about half the total of state deficits nationally and was nearly twice as large the deficit in California, the second largest.[2] By the end of FY2010, the shortage of ready cash was so severe that the state was 153 working days (more than seven months) behind in paying its bills.[3] Local school districts, state universities and other public institutions are owed billions of dollars and have been forced to lay off employees, impose furloughs or borrow money. Delays in the state's employee health insurance reimbursements have forced some state workers to pay medical providers up front. The severity of the payment delays to vendors who contract with the state—including pharmacies, funeral homes, and social service providers —has been ruinous for many of these businesses, their clients, and employees.[4] In an effort to minimize the short-term damage from its increasingly desperate predicament, Illinois officials have asked Wall Street investors to front cash so that the state can pay vendors more quickly. In return, Illinois would pay a generous annualized return of 12 percent.[5] Recently, the state comptroller stated that Illinois is facing "the most dangerous fiscal conditions in modern history."[6]

Although Illinois' increasingly dire fiscal situation is not exactly news—the last two issues of *The Illinois Report* have analyzed these problems—another year has passed and things are much, much worse.[7] There are several reasons for the continued deterioration in the state's fiscal condition. The state's own-source revenue has not yet rebounded from the effects of the 2007 to 2009 recession. The cuts in spending that have been implemented are nowhere near the magnitude needed to address the short- or long-term budget gap. Unfortunately, some recent budgetary actions have used short-term fixes to shift the problem ahead one or more years, making future problems even more difficult.

1 Merrion, Paul and Greg Hinz. 2010. "Illinois Enters a State of Insolvency," *Crain's Chicago Business*, January 18 edition.

2 Murray, Sara. 2010. "States face budget shortfalls of $26.7 billion," New York Times December 8 edition.

3 Illinois Office of the Comptroller, *Comptroller's Quarterly*, July 2010 edition.

4 Michael Powell, "Illinois Stops Paying Its Bills, But Can't Stop Digging Hole." *New York Times*. July 3, 2010 edition.

5 Spector, Mike and Michael Corkery. "Illinois Seeks Wall Street Cash," *Wall Street Journal*, December 11, 2010 edition.

6 Illinois Office of the Comptroller, *Comptroller's Quarterly,* October 2010 edition. http://www.ioc.state.il.us/common/getLocalFile.cfm?fileName=CQ_October_2010.pdf.

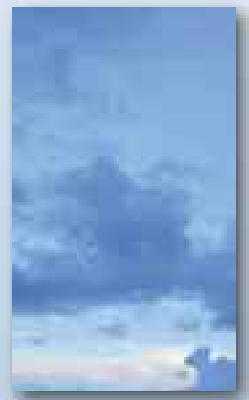
7 Richard F. Dye and Daniel P. McMillen, "Illinois' Fiscal Future and the State's Economy," *The Illinois Report 2009*; and Richard F. Dye, Nancy Hudspeth and Daniel P. McMillen, "Fiscal Condition Critical: The Budget Crisis in Illinois," *The Illinois Report 2010*.

Official estimates of the General Funds budget gap for fiscal year 2011—which include unfunded obligation from prior years' deficits—are more than $12 billion.[8] According to an October 2010 report issued by the comptroller's office, there is a very real possibility that the deficit will be $15 billion by spring 2011, when the budget for fiscal 2012 will be drafted.[9] (For comparison, the state's General Funds' operating budget is around $33 billion, annually.) If the Illinois state constitution requires a balanced budget, how can there be such an enormous deficit? The short answer is that the constitution does not limit unpaid bills or other unfunded liabilities and requires only that the budget be balanced prospectively, at the beginning of the budget year, not retrospectively, when the year-end results are tallied.

It is hard to overstate the depth of the fiscal hole the state is in. The enormous carry-over deficit and operating deficit are not the only problems.

- **There is reason to believe that the official FY2011 operating deficit is understated.** IGPA's Fiscal Future model uses a "Consolidated Funds" budget concept that is broader and more meaningful than the more commonly reported General Funds budget and finds a FY2011 deficit of $10.9 billion in addition to the more than $6 billion carried over from prior years.[10]

- **Borrowing to cover the operating deficit has burdened future budgets**. For example:
  - State bonds to cover its 2010 pension payment of $3.5 billion, must be paid back with interest over five fiscal years (2011-2015).
  - There are insufficient funds to cover the scheduled $4.1 billion FY2011 pension payment.[11] Skipping the scheduled contribution—as some have proposed—would increase unfunded liabilities directly and, by causing the state's pension funds to sell income-earning assets, indirectly.
  - Past choices to implicitly borrow by not putting aside sufficient funds to cover future pension liabilities have made Illinois pension underfunding the worst in the nation. In April, Governor Pat Quinn signed legislation that raises the retirement age and limits pension benefits of *future* employees, and also allows lower state contributions based on these reduced benefits.[12] In May, due in part to "new pension math," the funded ratio for



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[8] Commission on Governmental Forecasting and Accountability (COGFA), State of Illinois *Budget Summary Fiscal Year 2011*, Illinois General Assembly, 2011.

[9] Illinois Office of the Comptroller, *Comptroller's Quarterly* October 2010 edition: http://www.ioc.state.il.us/common/getLocalFile.cfm?fileName=CQ_October_2010.pdf.

[10] See our chapter in IGPA's *The Illinois Report 2010* for more on the consolidated funds budget.

[11] Dan Hankiewicz, "Pensions: Fiscal Impact of a FY2011 Pension Holiday," Commission on Government Forecasting and Accountability. *Monthly Briefing*. May 2010: 7-10.

[12] Mary Williams Walsh, "The Illusion of Pension Savings: A Risky Pension Accounting Tactic is Spreading." *New York Times*, September 17, 2010 edition. Also see Matt Hopf, "Gov. Quinn to Sign Pension Reform Bill Today," *The State Journal-Register*, April 13, 2010 edition. http://www.sj-r.com/carousel/x1173974205/Quinn-wont-commit-on-approving-pension-bill (accessed Oct. 12, 2010).

Neither of the two basic options—cutting expenditures and increasing taxes—is going to be easy. But it is even worse to do nothing, because while the state is doing nothing, liabilities continue to grow and borrowing becomes more costly and difficult.

2010 had increased to 46.9 percent. But if there is no pension payment made in 2011, the funded ratio would drop to only 37 percent by 2014.[13]

- The FY2011 budget is funded in part by $1.2 billion in proceeds from the sale of rights to 15 years of future income from the tobacco settlement.[14]

- **Borrowing has become more costly, because Illinois' bond rating has been downgraded several times in the past year.** Only California has a lower bond rating than Illinois. In September 2010, after lowering Illinois' general obligation debt rating three times in a little more than a year, Moody's Investors Service revised Illinois' rating ``outlook'' to negative and stated that "We view the failure to enact significant new recurring fiscal measures as a troublesome indicator with respect to Illinois' governance and management profile."[15] Also in September 2010, Eaton Vance, a major municipal bond fund manager, announced that it would not hold Illinois bonds, at least partly because of the risk posed by the under-funded pension system.[16] A recent Civic Federation report asserts that if Illinois had been able to maintain its AA bond rating, it would have saved up to $3.2 billion in interest on the bonds sold in 2010.[17] Illinois' bond rating downgrades have also hurt state agencies. In June, the Regional Transportation Authority's bond rating was lowered because of its reliance on state funding.[18]

No Easy Solutions

How does Illinois get out from under its enormous deficit and pay off the mountain of unpaid bills left over from FY2009-2011? Neither of the two basic options—cutting expenditures and increasing taxes—is going to be easy. But it is even worse to do nothing, because while the state is doing nothing, liabilities continue to grow and borrowing becomes more costly and difficult. Also, uncertainty about the state's fiscal and economic future has a negative effect on individuals' decisions to live and work in Illinois, and on business' decisions to locate in, or invest in, Illinois. Declines in jobs, workers, and investment lead to diminished economic growth, and the vicious cycle continues.

What Are the Possible Solutions and Why Are They Not Easy?

We have used the IGPA Fiscal Futures Model to analyze the impact of various economic and policy changes on Illinois'

[13] Dan Hankiewicz, "Pensions: Fiscal Impact of a FY2011 Pension Holiday," Commission on Government Forecasting and Accountability. *Monthly Briefing*. May 2010: 7-10. Skipping the 2011 pension payment would cost the state $58 billion through 2045.

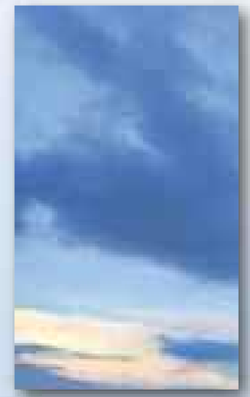
[14] Craig L. Johnson, "The State of the Tobacco Settlement: Are Settlement Funds Being Used to Finance State Government Budget Deficits? A Research Note." *Public Budgeting and Finance* 2004 24(1): 113-125.

[15] Moody's Investors Service quoted in: Edward McClelland, "Why Illinois' Bond Rating is Worse Than It Seems." NBC Chicago Ward Room, June 23 2010 edition. http://www.nbcchicago.com/blogs/ward-room/Springfield-is-in-denial-about-the-budget-crisis-96811129.html#ixzz12Fz4eCPe (accessed Oct. 12, 2010).

[16] Michael Quint and William Glasgall, "Eaton Vance Shuns Illinois Bonds on Unfunded Pension," Bloomberg, Sept. 15, 2020. http://www.bloomberg.com/news/2010-09-15/eaton-vance-shuns-illinois-bonds-on-unfunded-pension-update1-.html (accessed Nov. 19, 2010).

[17] Civic Federation, "Cost of the Crisis: An Analysis of the Additional Bond Costs Paid by the State of Illinois Due to the State's Ongoing Fiscal Crisis," 2010. http://www.civicfed.org/iifs/blog/state-paid-additional-551-million-last-year%E2%80%99s-bonds (accessed Aug. 19, 2010).

[18] Lorene Yue, "Moody's Goes Negative on $25B in Illinois Bonds." *Crain's Chicago Business*, Sept. 23, 2010 edition. http://www.chicagobusiness.com/article/20100923/NEWS02/100929929/moodys-goes-negative-on-25b-in-illinois-bonds (accessed Oct. 12, 2010).



fiscal condition. The Fiscal Futures Project and its model that projects the state budget into the future were introduced in the last two issues of *The Illinois Report*.[19] We have made a number of refinements to the model, incorporating the most currently-available data and estimates for FY2010 and 2011 and creating links between revenue sources and expenditure categories.[20] The revised model with these improved data and assumptions generates a baseline FY2012 consolidated funds deficit of $11.9 billion. In addition, the state could face approximately $13-15 billion in unpaid bills at the start of FY2012. The model also projects that, if past trends hold, total spending will grow by an average of 4.7 percent per year while total receipts will grow an average of only 3.4 percent per year, creating a growing, unsustainable gap between revenue and expenditures.

The Fiscal Futures model is also able to generate estimates of possible short-term reactions to the immediate budget crisis, including: doing nothing (waiting for the economy to improve, continuing to accumulate obligations, and borrowing); possible revenue-increasing scenarios (increasing the income tax rate or base, increasing the sales tax rate or base); freezing spending; or balancing the budget with expenditure cuts. As will be shown in the following analysis, there is no single solution or course of action that will balance the budget.

Wait For the Economy to Improve?

Economic recovery in Illinois is at least several years away and, unless there are dramatic changes, in several years the fiscal problems we have identified will be much, much worse. It has been three years since the beginning of the most recent recession (December 2007) and a year and a half since the bottom point (June 2009) yet Illinois' unemployment rate is still very high: 9.6 percent in November 2010, with only seven states higher. If the economy somehow reached full employment, there would, of course, be a surge in income, consumption, and thus tax collections. But even the revenue generated under this optimistic scenario would fall short. If personal income, corporate income, and general sales taxes returned to their 2008 peak levels in inflation-adjusted dollars, state revenue would increase by about $2.8 billion (net of revenue transfers to local government), far short of the amount needed to close the budget gap, much less the carry-over from prior years.

Continue to Accumulate Obligations?

As long as the state continues to spend more than it receives while doing nothing but postponing its obligations, the backlog of unpaid bills will grow at a frightening rate. Figure 1 illustrates the consequences of following this path. Beginning with the existing carry-over, we add the projected deficit for each year from the Fiscal Futures Model assuming no changes in spending or revenue policy. The left-hand scale of Figure 1 (on page 32) shows the cumulative dollar amount of unpaid obligations under these assumptions. The

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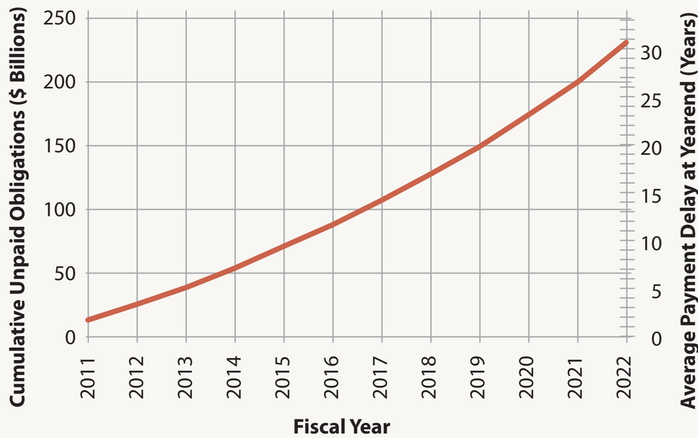
[19] Richard F. Dye and Daniel P. McMillen, "Illinois' Fiscal Future and the State's Economy," *The Illinois Report 2009*; and Richard F. Dye, Nancy Hudspeth and Daniel P. McMillen, "Fiscal Condition Critical: The Budget Crisis in Illinois," *The Illinois Report 2010*. See our website (http://igpa.uillinois.edu/content/fiscal-futures-project) for more on data sources, assumptions, and the model.

[20] For example, we developed a new way of measuring Medicaid expenditures and included a link from Medicaid spending to federal matching funds in the same year. We have also added data for FY2010 (with some assumptions because the lapse period for carry-over payments has been extended to the end of calendar year 2010 and final figures are not yet available). In order to develop a more current baseline for projections, we estimated FY2011 amounts from official revenue projections, beginning of year appropriations, and assumptions about how some items changed from FY2010. Then we estimated FY2012 amounts based on FY2011 figures.

Figure 1
Do Nothing but Accumulate Obligations Scenario



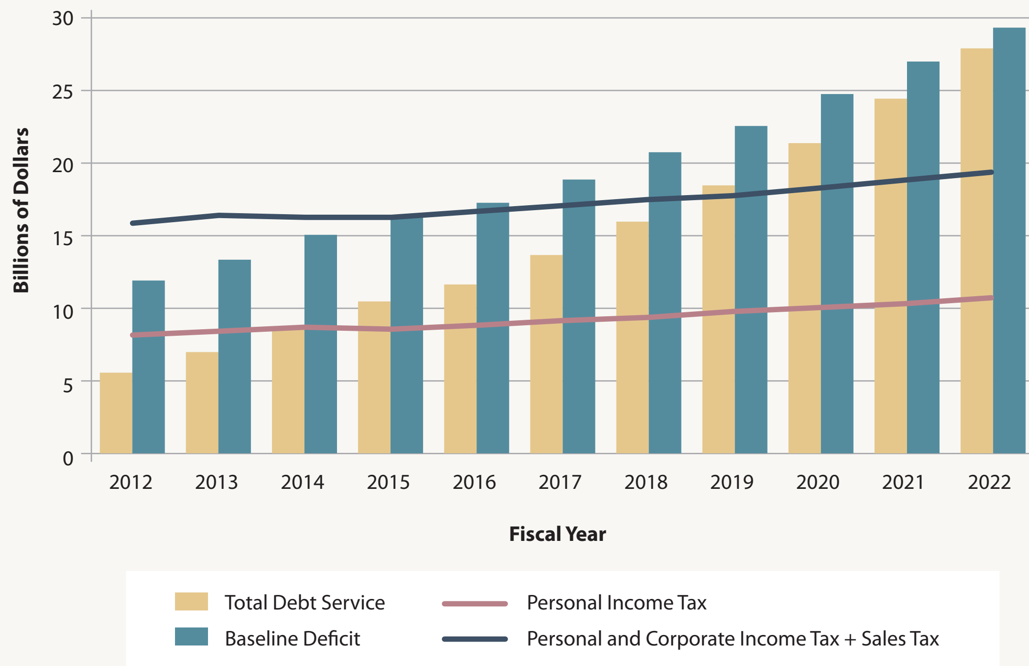
Source: IGPA Fiscal Futures Model, December 2010

right-hand scale estimates the corresponding time lag to pay those bills. Under this scenario, the payments backlog could be close to $40 billion by the end of FY2013, with an associated payment delay of more than five years. In 2022, the backlog would be on the order of $230 billion and the payment delay would exceed 30 years.

Borrow Our Way Out?

Borrowing is not a real solution either because, even though borrowing increases current cash receipts, it will have an even larger adverse effect on budget gaps in the future. Moreover, if the state does not adopt a credible and comprehensive plan to solve its fiscal problems it is unlikely to find willing lenders for even one more year. To simulate this scenario, we use the Fiscal Future Model and assume that, at the beginning of each new fiscal year, new debt can be sold in an amount equal to the current deficit.[21] Figure 2 shows the debt-service costs that result from this borrow-only scenario. For reference, the baseline deficit is shown in the same graph and the diagram also shows the projection of

Figure 2
Do Nothing and Finance Deficits with New Debt Scenario



Source: IGPA Fiscal Futures Model, December 2010

[21] Specifically, we assume that each year's borrowing is for a 10-year term, with equal payments, a 0.5 percent issuance cost, and a 4.50 percent interest rate.

several major revenue sources. On this path, by 2014 the debt service costs would consume all of the receipts from the personal income tax, and by 2019 the debt service costs would obligate every dollar received from personal income, corporate income, and sales taxes combined. Doing nothing but borrow is an impossible path.

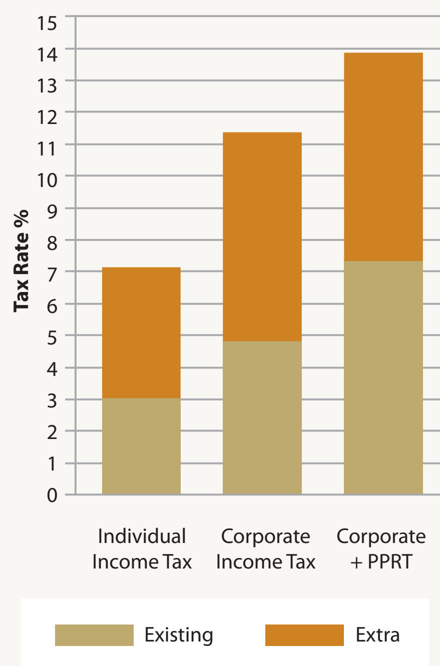
So, assuming that doing nothing except issuing bonds or delaying payment is not an option, the state will have to find some way to increase its revenue, cut its expenditures, or probably some combination of both. To answer basic questions about what the state can do to balance the budget, we used the Fiscal Futures Model to quantify the impact of a variety of hypothetical scenarios. We use FY2012 as the baseline year for the simulations. To be conservative, we assume that most spending categories are required to "hold the line" at FY2011 levels but that revenue grows from FY2011 to FY2012 as projected by the model. The benchmark FY2012 consolidated budget deficit projection that flows from these assumptions is $11.9 billion. (We measure the deficit before any new borrowing or decreases in pre-existing fund balances).

Increase the Income Tax Rate?

A number of proposals have been put forth to increase Illinois' personal income tax rate from its current flat rate of 3 percent. Governor Quinn has proposed an increase to 4 percent. Others have proposed going as high as 5 percent.[22] Usually these proposals are packaged with changes in the corporate rate and in personal exemptions or credits. Putting aside the political difficulties of raising the rate at all, each percentage point increase in the income tax would raise about $2.5-$3 billion (net of the local share).

So the recent proposals to increase the income tax rates by one or two percentage points would fall far short of closing the existing budget gap. We used the Fiscal Futures Model to determine what kind of tax rate increase would be needed to eliminate the deficit. We assumed a proportional increase in the corporate income tax rate so that it continued to be 8/5ths of the personal income tax rate.[23] As Figure 3 shows, to achieve a balanced budget in 2012 the individual income tax and corporate income tax rates would have to go up to 7.1 percent and 11.3 percent, respectively. In reality, it is likely that the revenue realized would be lower than needed, because if such high taxes were actually going to be implemented, political pressure would compel more generous personal exemptions and credits to soften the burden on lower- and middle-income families. Also, tax increases of this magnitude probably would have a significant negative effect on

Figure 3
Personal Income and Corporate Income Tax Rates that Would be Needed to Close the Entire FY 2012 Budget Gap



Note: An additional 2.5 percent Personal Property Replacement Tax (PPRT) rate is paid by all corporations.
Source: IGPA Fiscal Futures Model, December 2010

[22] Voices for Illinois Children, "The Time Is Now: Illinois Needs to Raise the Income Tax," (May 2009) http://www.voices4kids.org/getinvolved/files/TimelsNow.pdf (accessed Nov. 17, 2010); Center for Tax and Budget Accountability, "Funding Our Future," Oct. 29, 2010. http://www.ctbaonline.org/New_Folder/Budget,%20Tax%20and%20Revenue/FINAL%20Funding%20Our%20Future-CTBA%20Report%2010.29.2010.pdf (accessed Nov. 17, 2010). The Civic Federation. 2010. "A Fiscal Rehabilitation Plan for the State of Illinois" http://civicfed.org/sites/default/files/IllinoisFiscalRehabilitationPlan.pdf (accessed Nov. 18, 2010).

[23] The Illinois Constitution requires that the corporate income tax rate is no more than 8/5ths of the personal income tax rate.

business activity. The model does not account for this decrease in the tax base.

Increase the Income Tax Base?

For a number of years, the Illinois comptroller has provided annual estimates of the revenue that would be generated if Illinois taxed retirement and Social Security benefits as many other states do.[24] Starting with official estimates of foregone revenue from exempting retirement income in past years, we projected the share of revenue from retirement income in FY2012 to FY2022. The Fiscal Futures Model suggests that taxing retirement income would reduce the deficit by $1.1 billion in FY2012 and $1.8 billion in FY2022.

Increase the Sales Tax Rate?

The other major source of tax revenue in Illinois is the general sales tax. The current statewide sales tax rate is 6.25 percent, with 5 percent going to the state and 1.25 percent passed back to municipalities and transit authorities. In addition, home-rule units of government can levy their own sales taxes. As Figure 4 shows, it would take a state sales tax rate of 13.5 percent to balance Illinois' budget in FY2012. That is, of course, impossibly high, especially when the home-rule rates of Cook County and Chicago or other units of local government are added on.[25]

Increase the Sales Tax Base?

Illinois' general sales tax is mostly a tax on consumer goods and includes very few services in the tax base. Most states—including neighbors Indiana, Iowa, Michigan, and Wisconsin—tax many more consumer services than Illinois.[26] Because consumption of services has been growing faster than consumption of goods, a tax on services would increase the growth rate of what has been a fairly stagnant revenue source. However, simply expanding sales taxes to consumer services would not be sufficient to balance the budget. A thorough 2009 study found that a very ambitious expansion of the sales tax base to include every service taxed by any other

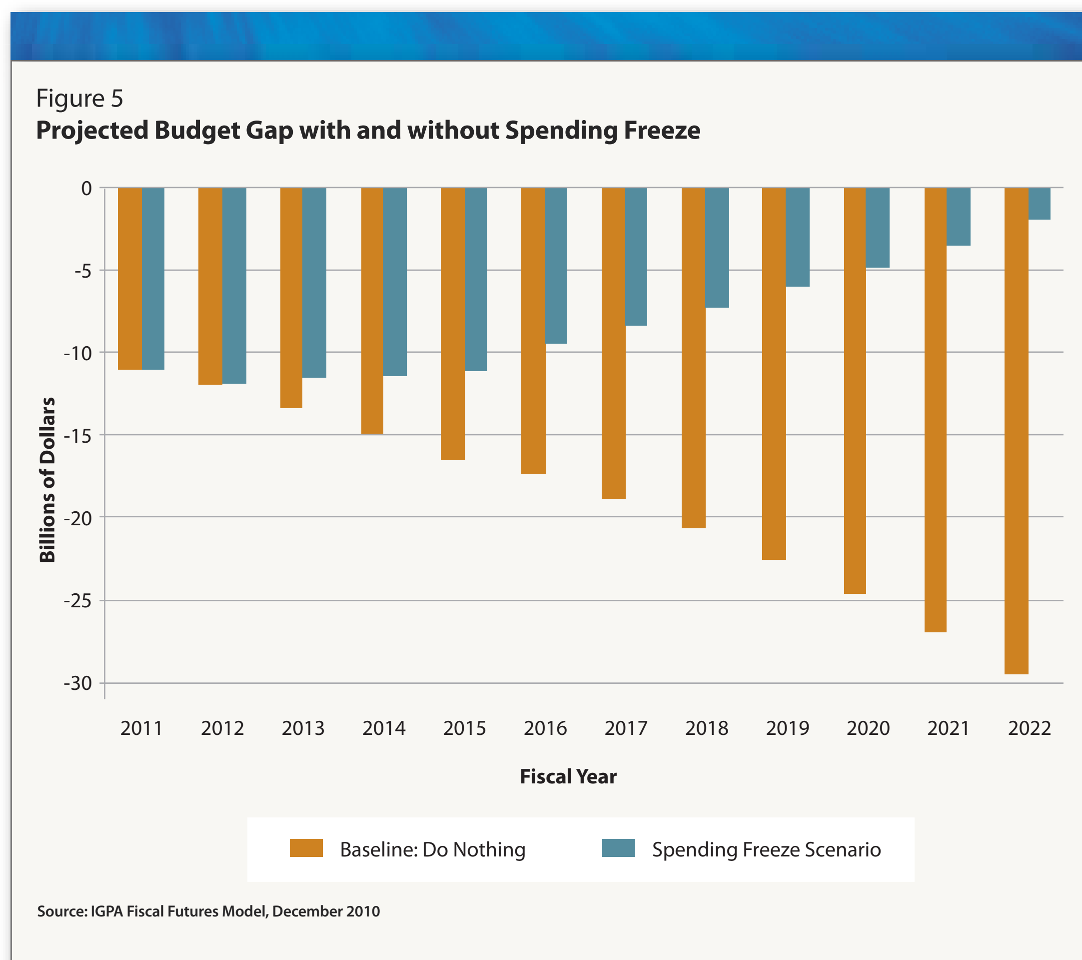
Figure 4
General Sales Tax Rate that Would be Needed to Close the Entire FY 2012 Budget Gap

Note: Residents of Chicago pay an additional 1.25 percent to the city, 1.25 percent to Cook County, and 1.0 percent to the Regional Transit Authority (RTA). Many other home-rule jurisdictions also have additional sales tax rates.
Source: IGPA Fiscal Futures Model, December 2010

[24] Illinois Office of the Comptroller, *Tax Expenditure Report FY2008*. http://www.apps.ioc.state.il.us/ioc-pdf/2008_Tax_Expenditure_Report.pdf (accessed Nov. 22, 2010). See also AARP Public Policy Institute, "State Taxation of Social Security and Pensions in 2006," Issue Brief No. 84 http://assets.aarp.org/rgcenter/econ/ib84_taxation.pdf (accessed Nov. 19, 2010).

[25] While these local-option taxes are not included in the Fiscal Futures Model calculations (the state is merely the collection agent), the local add on rates are relevant for additional burden they put on certain taxpayers.

[26] Federation of Tax Administrators, Sales Taxation of Services, 2007 Update, Oct. 2008, http://www.taxadmin.org/fta/ftapub.html.



state would raise at most $4.5 billion ($3.6 billion state share plus $0.9 billion local share), assuming that business-to-business service transactions would not be taxed.[27]

Spending Freeze?

Total spending on a consolidated funds basis has grown an average 5.7 percent per year since 1997 and, assuming past relationships continue to hold, the Fiscal Futures Model projects it to grow at an average of 4.7 percent per year over the next 10 years. Because the model projects that revenue will only grow at 3.4 percent per year, a growing budget gap is projected. Suppose that, somehow, total nominal state spending was frozen at FY2011 levels.[28] Note that this does not necessarily mean a freeze in spending for every program—some spending categories could increase as long as there were equivalent reductions elsewhere. Figure 5 illustrates that even this dramatic austerity would fall short of eliminating the budget gap in the next decade.

Spending Cuts?

The total of General Fund appropriations and statutory transfers in the FY2011 budget is $33.5 billion; total consolidated budget spending (i.e., including non-General funds) will be more than $65 billion. In the spring of 2009, the Taxpayer Action Board (an expert committee empanelled by Governor Quinn) released a detailed report of budget cuts and cost savings totaling at most about $2.2 billion for FY2011, not including pension reform and reduced benefits for future employees.[29] In February 2010, the Civic

[27] Commission on Government Forecasting and Accountability. "Service Taxes, 2009 Update." http://www.ilga.gov/commission/cgfa2006/Upload/2009-JULY%20SERVICE%20TAXES%20Update%20REPORT.pdf (accessed Oct. 12, 2010). For a list of the services that would be taxed and the estimated revenues for the state (5 percent share, refined base), see Appendix A, pages 19-23.

[28] Our spending-only simulations assume that debt service, pension payments and transportation spending are off limits and are not cut. Debt service for already existing bonds is contractual. Pension payments are scheduled by law and do not even cover the full amount of increased pension liability accrued in each year. Transportation spending relies mainly on dedicated revenue sources from federal aid, motor fuel taxes, and tolls.

[29] Report of the Taxpayer Action Board (June, 2009) http://www2.illinois.gov/budget/Documents/TAB report.pdf accessed Nov. 18, 2010).

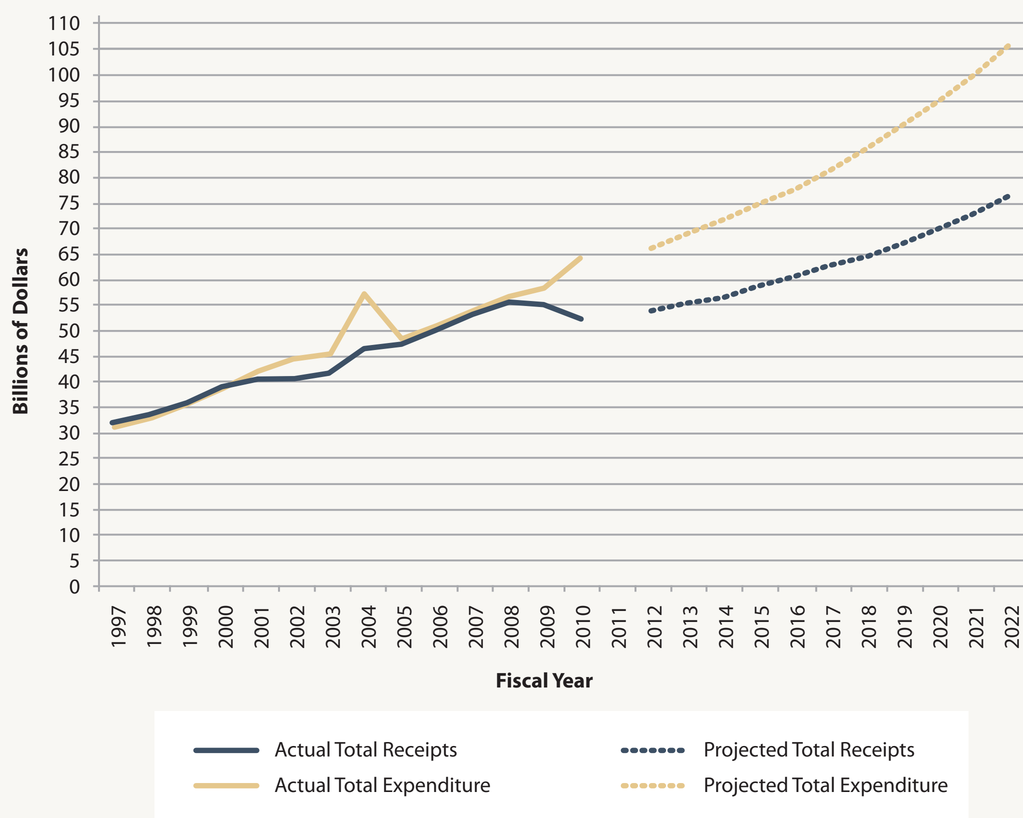


Figure 6
Actual (FY 1997-2010) and Projected (FY 2012-2022) Illinois Consolidated Total Receipts and Expenditures with No New Borrowing in Receipts.

Source: IGPA Fiscal Futures Model, December 2010

[30] The Civic Federation. "A Fiscal Rehabilitation Plan for the State of Illinois" (Feb. 2010). http://civic fed.org/sites/default/files/IllinoisFiscalRehabilitationPlan.pdf (accessed Nov. 18, 2010).

Federation's *Fiscal Rehabilitation Plan for Illinois* recommended reducing General Funds expenditures to FY2007 levels, for everything except Medicaid and general state aid to elementary and secondary education, for a savings of about $2.1 billion.[30] During the 2010 gubernatorial campaign, one of the candidates proposed cutting the General Funds budget by 10 percent, or about $3.4 billion.

So recent proposals to cut spending are not large enough to close the entire budget gap. To determine the amount of cuts that would be necessary to balance the budget in FY2012, we did a simulation of expenditures and revenue using the Fiscal Futures Model, which takes into account that some spending (such as Medicaid) is explicitly linked to federal transfers so cutting spending would also reduce revenue. The model suggests that if the budget is to be balanced only with budgetary cuts, total spending (other than debt service, pensions, and transportation) would have to be cut by 26 percent. That's equivalent to cutting more than the entire budget for education, or more than the entire budget for human services and related agencies, or more than the state spends on government operations, economic development, corrections, public safety, and natural resources combined. It is completely implausible that cutting only non-essential programs, political "pork," or

Richard F. Dye has been on the IGPA faculty since 1990. His research and public service activities have focused on state and local government finance as it relates to economic development. Professor Dye initiated IGPA's study of the impact of property tax caps on the Illinois collar counties since 1991 and a study of the impact of tax increment financing on local economic development in Illinois. He has written on the impact of property tax classification on business activity, voter preferences for the equalization of school property taxes, earmarking revenues for specific public expenditures, the growth and stability of different state revenue sources, and the impact of stadiums and professional sports on local development.

"waste, fraud and abuse" can even begin to balance the budget.

Another point to consider is that even if such cuts in spending were put in place, it would still be necessary to slow the growth rate of spending to no more than the growth rate projected for receipts (3.4 percent per year) to maintain a balanced budget over time. That means there would have to be additional policy actions taken to slow the growth of spending and maintain budget balance over time.

It Gets Even Worse: Illinois' Fiscal Future

So far, we have focused on Illinois' budget crisis in the near term, but our long-term projections for Illinois are equally daunting. We use the Fiscal Futures Model to generate growth projections for each spending and income category. We assume that FY2012 spending for most categories is held to FY2011 levels but that the growth projected by the model resumes after that.

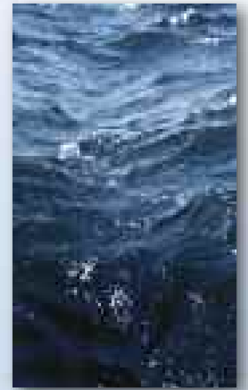
Budget Projections

The most recent projections of the model are summarized in Figure 6. For comparison, the figure also shows the historical levels of total spending and total receipts in the Illinois consolidated budget. So that past and future values are comparable, new borrowing is not counted as a receipt. The past or projected deficit is the gap between projected total spending and projected total receipts. The consolidated funds deficit shown in Figure 1 was $11.7 billion in FY2010 (an estimate because even though the fiscal year ended on June 30, 2010, the books did not close on outstanding bills until December 31, after this chapter went to press) and is projected to rise to $29.4 billion in FY2022 (in current dollars, which is $23.9 billion in real 2010 dollars).

Because expenditures are projected to grow much faster than revenue, our model suggests that even if the state adopts the drastic spending cuts and revenue increases necessary to balance the current budget, deficits will re-emerge unless additional measures are adopted.

Conclusion

Illinois' fiscal problems are so enormous that no single option is going to balance the budget. Economic recovery will be slow, and even a dramatic decline in the unemployment rate would not come close to eliminating the deficit. Taking on even more debt is not a solution, because it just makes the fiscal situation worse in the future. No single revenue increase—at least not any of plausible magnitude—will be sufficient to eliminate the $11.9 billion deficit projected for FY2012, much less the extra $13-15 billion deficit that includes the



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Bringing Illinois to fiscal solvency will require state government to implement multiple and massive policy changes. If nothing is done soon, the state of Illinois faces a very bleak future.

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carry-over from imbalance in FY2009-2011. We start so out of balance that even an absolute freeze on all spending will not achieve balance in a 10-year time horizon. Spending cuts would have to be of a magnitude that would shut down entire core functions of state government. Bringing Illinois to fiscal solvency will require state government to implement multiple and massive policy changes. If nothing is done soon, the state of Illinois faces a very bleak future.

First and foremost, the state needs a plan that recognizes the near-insolvent situation it is in and lays out the actions that will be taken to get out of that situation. Taxpayers and recipients of state services need to see that they are not the only ones forced to sacrifice. Those supporting a tax increase need a plan that acknowledges the cuts and other actions that will also be taken. Those supporting spending cuts need to concede that patience and additional revenue will be required. In the near term, there will need to be a transitional period of reckoning for the state to get its fiscal affairs in order and to generate a plan to resolve its immediate deficit and gain long-term fiscal sustainability. Without such a plan, lenders will almost certainly be unwilling to help the state resolve its immediate cash-flow crisis.

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