Fiscal Focus

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DANIEL W. HYNES

STATE OF ILLINOIS COMPTROLLER

Comptroller Hynes' office strives to assist taxpayers and the people of Illinois. This report is designed to provide fiscal information of general interest.

Illinois State Pension Needs Put Pressure on the State Budget

State pension funding is again at the center of the discussion of Illinois state government's financial difficulties. An investment portfolio negatively impacted by the overall economic downturn since fiscal year 2000 has exacerbated years of inadequate pension funding and left Illinois supported retirement systems with large unfunded pension liabilities. A 1995 plan to amortize much of this debt combined with double digit returns on investments significantly improved the financial picture of the pension systems by the end of fiscal year 2000. Unfortunately, the poor performance of investments during the following three fiscal years and initiatives such as the 2002 Early Retirement Incentive (ERI) have again left the state facing a large unfunded pension debt. The retirement systems share of the proceeds from the $10 billion pension funding bond issue at the beginning of fiscal year 2004 helped improve their financial picture by shifting some of the pension systems' liabilities to general obligation debt. The continuing financial struggle faced by Illinois' General Funds has led to a search for additional means of reducing pension contributions to free funds to meet other pressing needs.

There are five retirement systems that the State of Illinois is responsible for employer contributions (listed by size of membership) – Downstate Teachers' Retirement System (TRS), State Employees' Retirement System (SERS), State Universities Retirement System (SURS),

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FROM THE COMPTROLLER

Dear Readers:

This issue of *Fiscal Focus* reviews the status of the state's five retirement systems that support the pensions for retired teachers, university employees and state employees (including judges and legislators). With several recent years of poor investment performance following years of inadequate pension funding, the growth in required contributions to meet the promises of the 1995 funding plan has contributed to the challenge of balancing Illinois' General Funds budget.

As discussed in the Cover Story, the five pension systems ended fiscal year 2004 with a 60.9% funded ratio, with $35.1 billion in unfunded liabilities. Under Illinois law, the state is expected to contribute approximately $500 million in additional monies from the General Funds in fiscal year 2006 as a step towards reducing this liability.

The continuing financial struggle facing the General Funds has led to a search for ways to minimize the budgetary impact of the state's pension contributions. As various proposals for change surface in the next few months, these issues are expected to be thoroughly debated. It is my hope that this issue of *Fiscal Focus* will help provide relevant information for those observing and participating in these discussions.

As always, your comments about this and our other publications are welcome. Your input can be sent directly, or via the web site at www.ioc.state.il.us.

Sincerely,

Daniel W. Hynes
Comptroller

Fiscal Focus Features

Fiscal Focus

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Editorial Staff: David Griffith and Alexis Sturm. Writers & Analysts: Bill Dracos, Kevin Fitzpatrick, Loren Iglarsh, David Griffith, and Alexis Sturm. Production: Rhonda Rathbone, Susan Hansen, Brenda Mansholt, Frank Weitzel, Larry Hopkins and Mike Petropoulos.

Fiscal Focus is published by Comptroller Daniel W. Hynes, 201 State House, Springfield, Illinois 62706. Questions or comments may be directed to (217)782-6000.

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Fiscal $marts

Pension Bonds: A Closer Look

On June 12, 2003, Illinois issued $10 billion of pension funding general obligation (GO) bonds under the authority provided by Public Act 93-2. The bonds, which will be repaid by the general revenues of the state, were issued in order to improve the funded ratio of the state's five retirement systems and to provide budget relief to the state in fiscal year 2003 and fiscal year 2004.

Issuance of the Bonds

The bonds are scheduled to be repaid over 30 years with an interest rate of 5.05%. The proceeds from the sale of the bonds were allocated as listed in the accompanying table. Using some of the proceeds for capitalized interest delayed the impact of the bond sale on the state's budget until fiscal year 2005.

The budget relief was split as follows: $300 million was moved into the General Revenue Fund (GRF) in the 4th quarter of fiscal year 2003, while the remaining $1.86 billion was scheduled to be moved to GRF in pieces over the course of fiscal year 2004 (essentially whenever the state made a payment to one of the five retirement systems, there would be a deposit into GRF from the proceeds). This schedule was altered later by P.A. 93-665 changing the cash flow, but the end result was the same - $1.86 billion in budget relief for GRF.

The investment by the five retirement systems took place in early July 2003. The proceeds were allocated among the systems based on their unfunded liability at the end of fiscal year 2002. The amount of pro-

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HOW Illinois Stacks Up

Illinois Public Retirement Systems' Funding Lags Other States

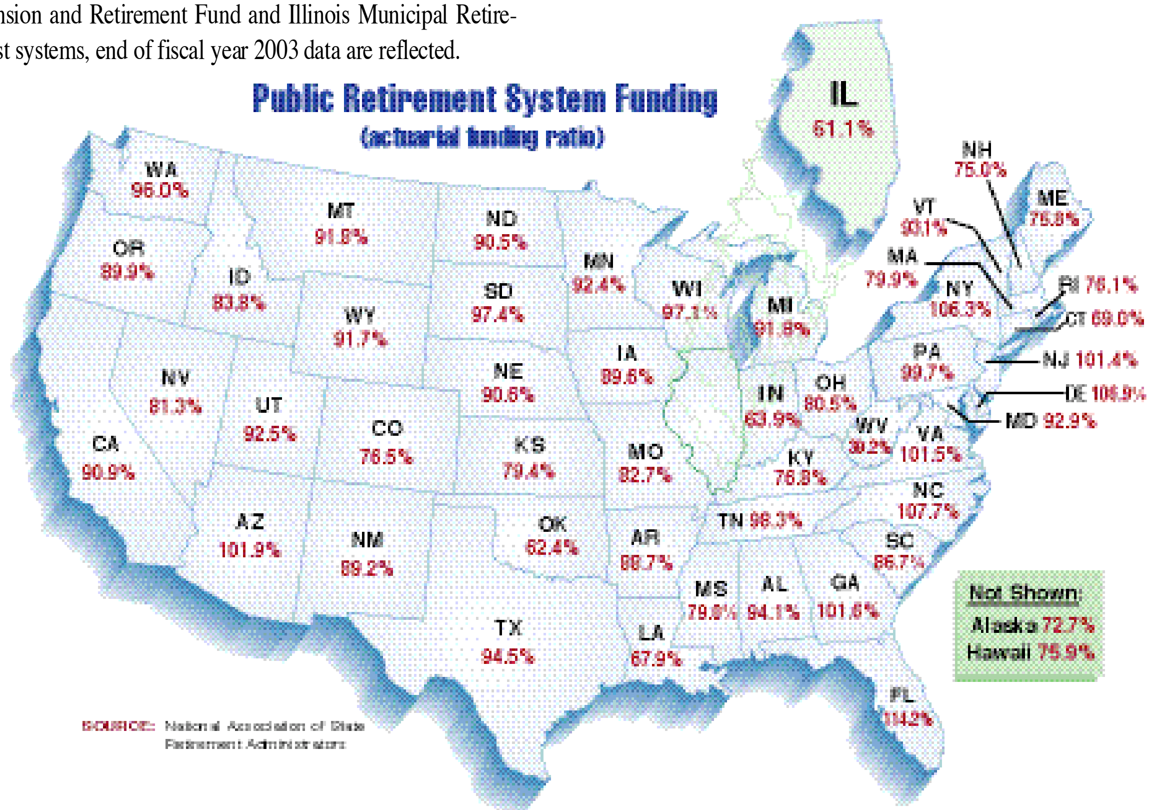
One measure used to indicate the health of a pension system is the funded ratio. This is calculated by dividing the actuarial value of a system's assets by the actuarial value of the system's liabilities at a given point in time. The Governmental Accounting Standards Board (GASB) statement #25, issued in November 1994, stipulated that this ratio be reported for state and local government defined benefit plans.

A survey released in September 2004 by the National Association of State Retirement Administrators includes the most recent actuarial statistics for 101 public retirement systems, estimated to represent more than 85% of the public retirement systems community. It includes data on teachers and local government employee retirement systems in addition to state employee systems. For example, the Illinois retirement systems included are the ones discussed elsewhere in this report – SERS, SURS, and TRS – but also the Chicago Public School Teachers Pension and Retirement Fund and Illinois Municipal Retirement Fund. For most systems, end of fiscal year 2003 data are reflected.

Although not all local systems are included in this survey, summing the reported data by state provides an overall perspective of the health of the retirement systems in a state at multiple levels of government. Eight states had an average ratio greater than 100%. Florida's systems had the highest ratio (114.2%) followed by North Carolina (107.7%), Delaware (106.9%), New York (106.3%), and Arizona (101.9%). (It should be noted that New York's system for state and local employees uses an aggregate cost actuarial valuation method which does not identify an unfunded liability thereby increasing the funded ratio for the system to 100%).

Seventeen states had an overall ratio between 90% and 100% funded, while nine states fell between 80% and 90%. Sixteen states, including Illinois, had an overall ratio under 80%. The reported Illinois retirement systems had a funded ratio of 61.1% that ranked Illinois 49th out of the 50 states. West Virginia, with an average ratio of 39.2% due to a severely under funded teachers retirement system, was the only state that ranked lower.

Another measure of comparison is the value of the unfunded liabilities of the retirement systems. This amount is the amount of additional assets that a retirement system would need to have invested in order for assets to equal the system's liabilities. Here, too, Illinois fares poorly and was ranked last of the 50 states. As of the end of fiscal year 2003, the Illinois systems included in this survey had unfunded liabilities totaling \$43.5 billion. California's set of systems has the next largest unfunded liability, with approximately \$32.4 billion needed for its systems. However, California's larger systems cover approximately 2.1 million active employees and annuitants, while the Illinois systems only cover approximately 758 thousand active employees and annuitants. Illinois' reported unfunded liabilities of \$43.5 billion were approximately 17.8% of the nationwide total of unfunded liabilities included in this report. ■



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ceeds received by each of the systems is listed in the accompanying table.

How are the Pension Bonds Supposed to Save the State Money?

The fundamental idea behind the pension bonds is that the state can borrow at a lower rate than the state can earn in investing the funds. In this case, the estimated rate of investment return for the bond proceeds is around 8.5%. The state borrowed (and is repaying bondholders) at an average rate of around 5.05%. The difference between these amounts is the projected "savings."

Total Allocation of Pension Funding Bond Proceeds

Deposit into the five retirement systems	$7,317,292,916
Budget Relief	$2,160,000,000
Capitalized Interest (to cover 1st year's debt service)	$481,038,333
Discount/Cost of Issuance	$41,668,750

For this bond issue, the amount of "savings" was estimated before the bond proceeds were invested and used for fiscal year 2003 and fiscal year 2004 budget relief. This left only $7.3 billion available for investment to offset the $10 billion debt. Not all of the "savings" were used for budget relief, so the investments by the retirement systems can earn around 7.0% a year over the 30 years for the state to break even. The success of the gamble hinges on the rate of return earned on the pension proceeds.

Impact on Payments to the Retirement Systems

There will not be a direct payment by the retirement systems to the bond holders. The bonds are general obligation bonds and will be paid out of the General Revenue Fund like most of the other state GO bonds.

To offset this increased debt service payment out of GRF (approximately $490 million a year in the earliest years increasing to over $1 billion by the end of the 30 years), the legislation reduced the funding formula for the annual payments to retirement systems from the prior formula. The appropriations to the systems are (and will be) reduced so that the pension payments plus debt service on the bonds do not exceed what would have been paid to the systems if the bonds had not been issued. This adjustment was included to protect the overall state budget.

The new retirement payment calculation negates the General Funds' budget impact of the pension bonds for the four retirement systems (TRS, SURS, JRS, GARS) that receive most of their state payments from the General Funds. However, SERS does receive payments from other state funds since their payments are a percentage of the payroll costs of an agency. Approximately 35% of total state payroll is paid from other funds. Fiscal year 2005 budget implementation bills established a mechanism for SERS to collect a portion of the pension funding bonds debt service from these other funds to hold the General Funds harmless.

First Year Experience

The bond proceeds were deposited in July 2003. The state hit a turning point in the market right before an upswing.

Bond Proceeds by Retirement System

Retirement System	$ in billions	% of total
Teachers' Retirement System	$4.330	59.2%
State Universities Retirement System	$1.432	19.6%
State Employees' Retirement System	$1.386	18.9%
Judges' Retirement System	$0.142	1.9%
General Assembly Retirement System	$0.027	0.4%
Total	$7.317	100.0%

SERS earned approximately 16.4%, SURS 16.9% (preliminary), GARS approximately 16%, JRS approximately 15.9%, and TRS earned approximately 15.4%. These rates of return exceeded the systems' actuarial assumptions and the rate needed to break even on the pension funding bonds' repayment. However, this is just one year's return among the 30 years the bonds will be outstanding. ■

New Payment Calculation

Each year, the five state retirement systems follow a three-step process:

1. Calculate what the payment to the system would have been if the bonds had not been issued, then subtract the system's prorated share of the debt service on the pension funding bonds. This is the maximum state payment.
2. Calculate what the statutory payment to the system will be given the pension funding bonds were issued. This is the formula state payment.
3. Compare the maximum payment to the formula payment and whichever is less will be the state's payment.

By defining the maximum payment as above, the state's overall budget is held harmless if the bond proceeds underperform the rate of return for a few years. The "maximum state payment" was deemed to be the lower one for fiscal year 2005 and future fiscal year 2006 payment. Generally, the formula state payment will not be the lower one until there are several years of investment overperformance. This process will still enable the state to reach the 90% funded ratio by 2045, the goal established in 1995. ■

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Judges' Retirement System (JRS), and General Assembly Retirement System (GARS). The state also provides a portion of the employer contribution to the Chicago Teachers' Retirement System (CTRS), but Chicago is responsible for the employer liability and contribution through a locally imposed property tax.

Each of the five systems offers a defined benefit pension plan with a guaranteed lifetime benefit calculated upon retirement. The calculation formula takes into account compensation level, years of service, whether the employee has a survivor who may also receive benefits, and whether the employee is covered by Social Security. After retirement, there is an automatic annual cost of living increase applied to the pension benefit in accordance with state law. Per the Illinois Constitution, public pension benefits are a contractual right that cannot be diminished.

SURS also offers a defined contribution plan where the employer is only liable for its contribution. Upon retirement, the member receives an annuity based on the accumulated value of employee and employer contributions and investment income earned on those contributions. The defined contribution plan may be desirable for employees who do not expect to spend their career under SURS because it increases the pension contributions that are transferable or allows investment in a plan that may also be available from future employers.

Pension benefits are a significant component of the compensation package for public school teachers, public college and university faculty, and state government employees. Long-term government employees often can qualify for a pension in their 50's. For example, a state government worker who joins government at the age of 25, can retire with a pension equal to 50% of their base salary (computed as their highest four year average among their final ten years of service) at age 55. (Credit is earned as 1.67% of salary for each year's service and this employee would qualify for retirement under the rule of 85 with 30 years service at age 55). Higher benefit formulas are available for employees in high risk occupations such as state police and corrections officers.

A large portion of the Illinois population contributes to, or receives benefits from, state pension systems. At the conclusion of fiscal year 2004, the five state pension systems reported 310,735 active members and 171,220 recipients of retirement, survivors, and disability benefits. These 481,955 active members and beneficiaries (including beneficiaries residing outside Illinois) equal 3.8% of Illinois' 12.7 million population. Active membership included 157,785 active full, part time, substitute, and hourly teachers belonging to TRS, 81,242 full time and part time members of SURS, and 70,621 members of SERS. Similarly, the largest number of beneficiaries receives benefits from TRS (77,165) with 38,487 receiving benefits from SURS, and 54,298 receiving SERS benefits.

Profile of Illinois' Pension Systems

	TRS	SURS	SERS	JRS	GARS	Total
Active Members	157,785	81,242	70,621	906	181	310,735
Beneficiaries	77,165	38,487	54,298	873	397	171,220

TRS - Teachers' Retirement System
SURS - State Universities Retirement System
SERS - State Employees' Retirement System
JRS - Judges Retirement System
GARS - General Assembly Retirement System

Funded Ratios

The financial health of retirement systems can be measured in several ways. One of the simplest is the funded ratio which is calculated by dividing net assets by net accrued liabilities. If net assets equal the accrued liability, the funded ratio is 100% and the system has sufficient assets to cover the amount of pension benefits that have been earned by current beneficiaries and employees at the time the calculation was performed.

If assets are less than the accrued liability (i.e., a funded ratio less than 100%), the difference is called an unfunded liability. While unfunded liabilities are often less of a concern for public pension plans than private plans (which may be terminated when the private sponsor goes out of business or is acquired by another firm), significant unfunded liabilities indicate that future taxpayers will likely have to pay for liabilities incurred in past years.

Once a major pension system becomes significantly under funded, eliminating the shortfall can prove to be very burdensome. With a fully funded system, the employer normally only needs to contribute its share of the "cost" of benefits earned during the year to remain fully funded. With a significantly under funded system, the employer needs to contribute the cost of benefits earned during the year, plus the additional investment income that would have been earned if the system were fully funded, plus a payment toward reducing the unfunded liability.

Funding Policy for Illinois Pension Systems

Public Act 88-593, effective July 1, 1995, created a fifty-year funding plan with an ultimate goal of achieving 90% funding of system liabilities. The funding plan provides for a 15-year phase-in period to allow the state to adapt to the increased financial commitment. Once the phase-in period is complete, the state's contribution is to

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FOCUS On Spending

Operating Costs of State Government

For fiscal year 2004, operations spending from appropriated funds to conduct state government business totaled $11.100 billion, $214 million or 1.9% less than fiscal year 2003. The decrease in operations spending in fiscal year 2004 was the second consecutive annual decrease in operations costs and fiscal year 2003 and fiscal year 2004 represented the only two such decreases over the last decade. Many people believe that the predominate cost of state government operations is payroll, however, direct salary expenses accounted for only 33.0% or $3.661 billion of the total operational costs in 2004.

Operations Spending Breakdown
All Appropriated Funds
Dollars in Millions

	Fiscal Year									
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Personal Services:										
Regular Positions	3,737.2	3,879.8	3,745.9	3,866.0	4,071.7	3,117.4	3,281.4	3,426.8	3,329.1	3,169.8
Other Personal Services	249.5	266.3	277.5	283.8	297.2	305.4	321.6	333.5	324.4	305.5
Total, Personal Services	3,986.7	4,146.1	4,023.4	4,149.8	4,368.9	3,422.8	3,603.0	3,760.3	3,653.5	3,475.3
Retirement	187.7	251.9	300.6	380.4	509.8	541.2	575.4	605.7	630.7	580.1
Social Security	184.2	192.6	197.9	204.8	215.5	217.4	230.4	241.5	235.0	223.4
Group Insurance	497.6	450.9	548.7	581.9	632.1	724.8	806.1	876.6	965.7	1,157.0
Contractual	788.9	916.0	873.5	935.2	868.2	976.3	1,032.2	1,070.8	1,072.6	878.3
Travel	44.5	46.8	41.9	43.1	43.8	42.8	43.1	39.0	32.9	31.9
Commodities	182.7	185.5	185.2	191.7	197.7	192.1	198.5	189.5	165.0	181.4
Printing	20.8	22.7	20.4	19.1	19.0	19.4	21.6	20.1	18.3	16.1
Equipment	122.8	124.3	104.3	105.9	94.2	89.8	92.4	67.3	38.9	44.4
Electronic Data Processing	87.1	93.7	102.8	106.6	122.1	117.4	117.0	133.3	119.9	105.9
Telecommunications	171.7	168.2	166.1	178.0	203.7	212.7	221.6	204.6	193.9	192.5
Automotive Equipment	53.5	53.5	54.7	55.1	56.3	60.9	70.8	63.2	64.0	68.2
Lump Sums	1,585.4	1,354.2	1,687.6	1,638.5	1,978.1	3,518.6	3,770.8	4,214.3	4,123.3	4,145.3
Total	7,913.6	8,006.4	8,307.1	8,590.1	9,309.4	10,136.2	10,782.9	11,486.2	11,313.7	11,099.8

State Payroll

Expenditures for state payroll declined by $127 million or 3.4% from the $3.788 billion expended in fiscal year 2001 to $3.661 billion in fiscal year 2004. Monthly payroll spending reached a peak of nearly $345 million in July of 2002 (just prior to the early retirement incentives) and had a low of $293 million in April of 2003. The accompanying chart shows a surge in the month of January of 2003 reaching $381 million; however, this spike includes roughly $80 million in lump sum payouts for unused sick and vacation time cashed in by retirees.

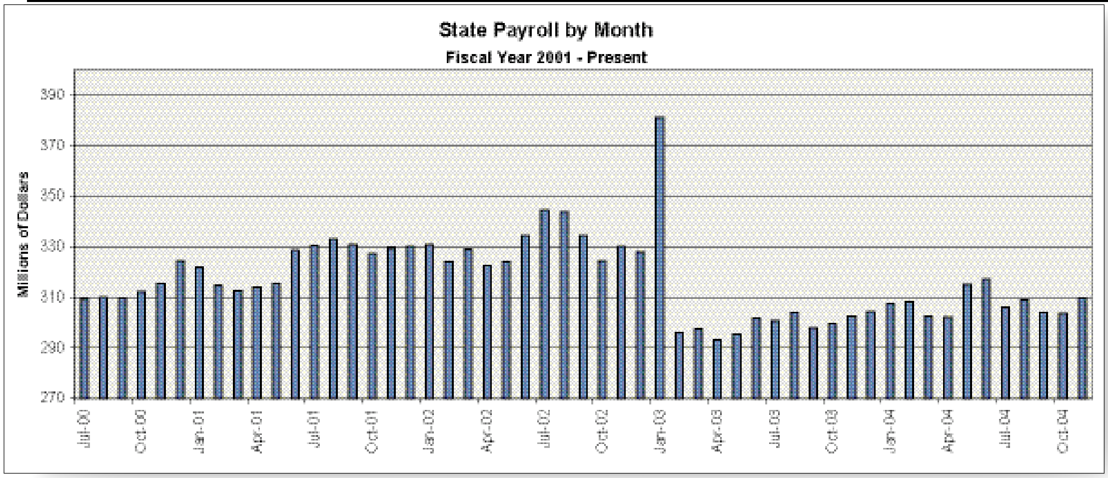
The chart also reveals an up tick in state payroll spending by month over the last seven or eight months of fiscal year 2004 even though headcount levels have remained fairly level. Despite the recent increase, payroll spending levels still remain below those of fiscal year 2001. For the first five months of fiscal year 2005 the average monthly payroll was $307 million, $6 million or 2.0% higher than the first five months of fiscal year 2004.

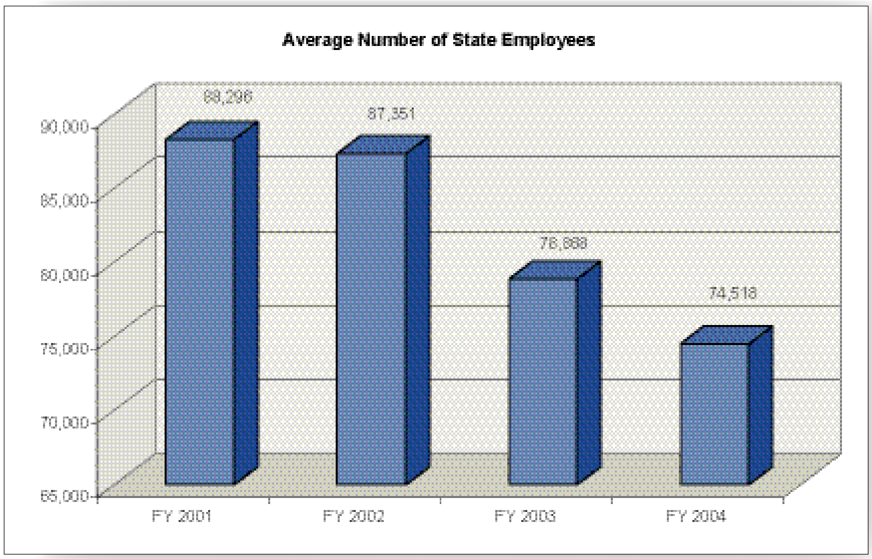
At the end of fiscal year 2004 the number of state employees totaled 75,412, 166 more than at the end of fiscal year 2003 but 14,270 less than at the end of fiscal year 2001. This large decrease is due primarily to the early retirement incentives which took effect at the beginning of fiscal year 2003 and to a smaller extent, layoffs and attrition.

Operations by Object

The largest areas of operations spending are lump sum payments and personal services expenditures which accounted for 68.7% of operations spending in fiscal year 2004. The $4.1 billion spent on lump sums in fiscal year 2004 was up only $22 million or 0.2% from 2003 but up 161.5% from fiscal year 1995. The accompanying table shows a significant increase in lump sum spending from fiscal year 1999 to fiscal year 2000. This was due primarily to the decision to appropriate higher education allocations as lump sums rather than personal services or other specific categories of spending in order to give higher education institutions more latitude in their spending decisions. A corresponding decrease can be seen between 1999 and 2000 in personal services and other categories of operations spending. For fiscal year 2004, nearly $1.3 billion in lump sums was expended by state universities.

Personal services spending, which includes salaries for regular state employees, judges, elected officials and employee retirement paid by the state totaled nearly $3.475 billion in fiscal year 2004, a decrease of $178 million or 4.9% from fiscal year 2003. Just as total operations and lump sums have decreased over both of the last two fiscal years, so has personal services. Personal services expenditures do not include all of state payroll costs as some employees are paid out of lump sums. Total state payroll in fiscal year 2004 was $3.661 billion.





Payroll related expenditures include retirement, social security and group insurance payments. Due to the significant increases in medical costs, group insurance spending is the fastest growing segment of operations spending, up 19.8% or $191 million over fiscal year 2003. Retirement costs have increased significantly over the past ten years due to legislation which created a fifty-year funding plan aimed at restoring the financial health of the state retirement systems and achieving a 90% level of funding of system liabilities. Retirement spending for regular state employees increased from $187.8 million in fiscal year 1995 (2.4% of operational spending) to $631 million in 2003 (5.6% of operational spending) and $580 million in 2004. The decrease from 2003 to 2004 is due to the sale of the state's pension funding bonds.

Contractual services also represent a sizable amount of operational expenditures. In fiscal year 2004 contractual spending totaled $878 million, $194 million or 18.1% less than the $1.073 billion spent in fiscal year 2003. Professional and artistic contracts for specialized services account for a large portion of contractual services spending.

Other objects of operational spending, which are relatively small when compared to payroll, include travel, commodities, printing, equipment, electronic data processing, telecommunications and automotive equipment. Collectively, these sectors of operations spending declined by $8 million or 1.3% from fiscal year 2003.

Restraint appears to be the word that best describes the use of operational dollars for state government in recent years. Necessitated by a downturn in the economy and the ensuing fiscal crisis for state government, operational spending in fiscal year 2004 is below the level in fiscal year 2002. ■

Fiscal Year 2004 Fee Imposition Report Issued

In fiscal year 2004, the State of Illinois collected $5.1 billion from 1,463 fees administered by 80 state agencies. Fee revenues were up $543 million or 12.0% from their prior year level. As a source of revenue, fees collected represent 8.1% of revenues into Illinois' main operating fund groups. Among revenue sources, fees are surpassed only by federal aid ($12.9 billion), income taxes ($9.7 billion), and sales taxes ($7.4 billion). Most of what is collected is deposited into restricted funds. Only $410 million in fee revenue was deposited into the General Funds. In contrast, 32% of fee revenue was deposited into Special State Funds and 25% was deposited into Highway Funds.

The fiscal year 2004 edition of the Fee Imposition Report is now available from the Comptroller's Office, and it can be accessed from the Comptroller's website at http://www.ioc.state.il.us/.

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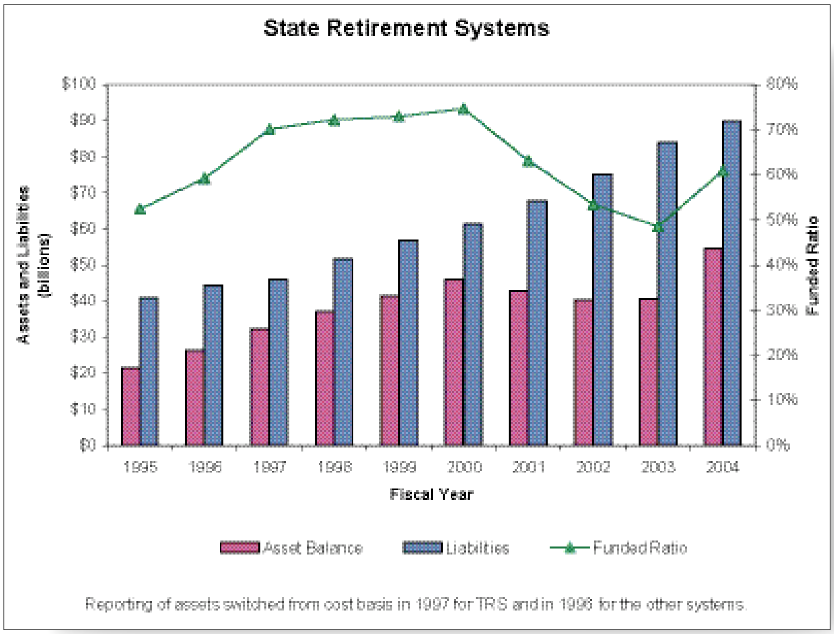
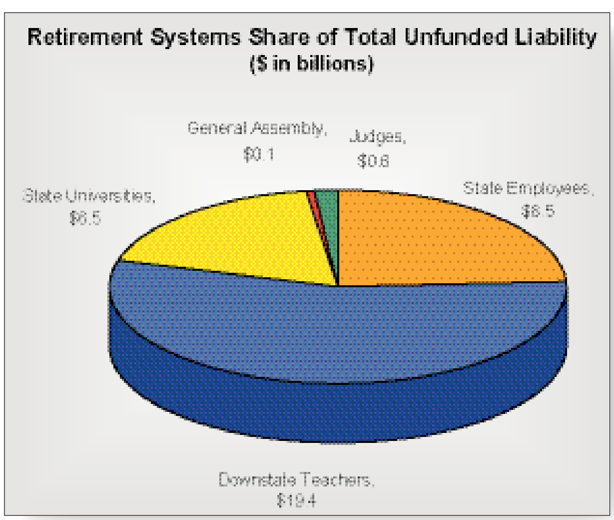
remain a level percentage of payrolls for 35 years until the 90% funded level is achieved. An additional funding computation is made for the SERS' 2002 ERI. In its current form the additional liability from this initiative is to be paid over the twelve fiscal years following its effective date with two $70 million payments followed by 10 years of level amortization of the remaining liability. SERS actuaries compute a $280.5 million annual cost over these ten years beginning in fiscal year 2006.



The 1995 funding plan was strengthened by creating continuing appropriations for the required state contributions. The state is to provide funding to the pension systems based on actuarial cost requirements and amortization of the unfunded liability with continuing appropriations created if the legislated appropriations prove to be insufficient.

Current Financial Status of Illinois Pension Systems

The five Illinois pension systems concluded fiscal year 2004 with a 60.9% funded ratio. The systems had combined assets of $54.7 billion versus liabilities of $89.8 billion leaving $35.1 billion in unfunded liabilities. TRS holds over half of the assets and is responsible for over half of the liabilities. At the end of fiscal year 2004, TRS had a 61.9% funded ratio with $50.9 billion in liabilities, $31.5 billion in assets, and $19.4 billion in unfunded liabilities. SURS had a 66.0% funded ratio with $12.6 billion in assets versus $19.1 billion in liabilities and SERS had a 54.2% funded ratio with $10.0 billion in assets and $18.4 billion in liabilities. Each retirement system's share of total unfunded liability is illustrated in the accompanying graph.



The most seriously under funded systems were the systems that serve judges and members of the General Assembly. GARS had a 40.1% funded ratio with $83 million in assets and $208 million in liabilities, while JRS had a 46.2% ratio with $535 million in assets and $1.156 billion in liabilities.

During fiscal year 2004, retirement system income was $18.4 billion including $7.8 billion in investment income and $7.3 billion from the distribution of the proceeds of the pension funding bonds. Revenues were $14.0 billion in excess of expenditures of $4.4 billion and $12.4 billion greater than the $6.0 billion increase in pension liabilities.

Funding Trends

The combined funded ratio for the five retirement systems has been on a roller coaster over the past ten years. It peaked at almost three-quarters (74.7%) funded at the end of fiscal year 2000, increasing from a 52.4% low point in fiscal year 1995. The improvement was due to above average returns on investments as well as a change in the method of valuing assets from cost to fair market value. The retirement systems reported combined investment income of over $4.0 billion for each of the four years between fiscal year 1997 and fiscal year 2000.

At the end of fiscal year 2000, the systems held almost $46 billion in assets. Investment losses caused a drop in asset values of almost $5.2 billion during the next three years which combined with a $22.3 billion increase in liabilities led to the decline in the funded ratio to 48.6% at the conclusion of fiscal year 2003. The infusion of monies from the pension funding bond issue plus the renewal of robust investment returns restored the funded ratio to 60.9% at the conclusion of fiscal year 2004.

Fiscal year 2004 pension system liabilities were almost 2.2 times their fiscal year 1995 level. Growing liabilities reflect the impact of higher

State Retirement Systems Fiscal Year 2004 ($ in thousands)	State Employees	Downstate Teachers	State Universities	General Assembly	Judges	Total
Beginning Net Asset Balance	$7,502,111	$23,124,823	$9,714,547	$49,676	$330,054	$40,721,212
Income	3,486,413	10,743,816	3,833,771	46,400	266,327	18,376,727
Member contributions	199,826	768,661	243,824	1,596	13,721	1,227,628
State contributions	1,864,674	1,103,337	1,757,547	32,952	178,593	4,937,103
Investment income	1,421,913	4,485,729	1,832,400	11,852	74,013	7,825,907
Other	0	4,386,089	0	0	0	4,386,089
Expenditures	998,337	2,323,910	962,012	12,868	61,801	4,358,928
Benefits and Refunds	990,644	2,310,349	950,496	12,564	61,353	4,325,406
Administration	7,693	13,561	11,516	304	448	33,522
Other	0	0	0	0	0	0
Ending Net Asset Balance	9,990,187	31,544,729	12,586,306	83,208	534,580	54,739,011
Actuarial Liability	18,442,665	50,947,451	19,078,583	207,593	1,156,093	89,832,385
Unfunded Accrued Liability	8,452,478	19,402,722	6,492,277	124,385	621,513	35,093,375
Net Asset/Actuarial Liabilities Ratio	54.2%	61.9%	66.0%	40.1%	46.2%	60.9%

salaries and an aging workforce as well as additional liabilities that have been incurred from upgrading benefit levels for pension system members. For example, during this period, TRS and SERS benefit levels were raised, the number of high risk job titles covered by the SERS alternative formula was expanded, and a significant early retirement initiative was implemented.

Pension Funding Bonds

In June 2003, Illinois sold $10 billion in general obligation bonds for pension funding purposes. The bonds were sold at a favorable interest rate of just over 5%. Of the proceeds, $7.3 billion were distributed to the systems for immediate investment. The remaining $2.7 billion was reserved for state pension contributions for the final quarter of fiscal year 2003 and for fiscal year 2004 as well as for capitalized interest and offering expenses for the bonds. The objective is that a higher return on the investments (estimated at 8.5% by retirement system actuaries) will yield savings to the state as the reduction in pension contributions is in excess of the required debt service amount. (See “Pension Bonds: A Closer Look” on page 2 for additional details.)

The swap of unfunded pension liability for general obligation debt is a gamble that the investment markets will perform well during the life of the bonds. If the investments do perform well (as occurred during the 1990’s), the reduced contribution requirements from the higher level of reserves will more than offset the debt service payments. However, if the investments perform poorly (as during the early 2000’s), the savings from reduced pension contributions will not offset the new debt service requirements. Both New Jersey and Pittsburgh issued pension funding bonds in the late 1990’s that, due to unfortunate market timing, fell far short of achieving expected fiscal benefits. Fortunately for Illinois, the timing of the Illinois pension bond issuance to date appears for the moment to be favorable, catching the stock market on an upswing.

Debt service for the pension funding bonds starts at $481 million in fiscal year 2004 and increases to $1.156 billion when the bonds mature in fiscal year 2033. Principal repayments begin in fiscal year 2008 with almost half of the principal scheduled for repayment between fiscal years 2029 and 2033.

Future Funding Requirements

The logic behind the fifteen-year acceleration in the fifty-year funding formula is to moderate the impact of raising state contributions to a level that will meet current obligations and begin eliminating the substantial unfunded liability. Even if investments and other actuarial factors were at their actuarially forecast values, contributions would experience above average growth during the ramp up period. Deviations in investment performance and retirement or salary trends from actuarial assumptions as well as improvements in the retirement package cause actual contributions to vary from the actuarial estimates.

Each year’s actuarial valuation of the retirement systems includes projections of the required employer contributions assuming actuarial assumptions hold in future years. Employer contributions are largely from the General Funds, but also include contributions from other state funds that support payrolls, some educational institutions, and the State Pensions Fund (the fund receives the proceeds from the sale of unclaimed property which are dedicated for contributions to the state pension systems).

The law authorizing pension bonds sets an additional limit on state pension contributions. Throughout the life of these bonds, the state contribution to each system cannot exceed the amount that would have been appropriated had the bonds not been sold reduced by the total debt service for each system’s portion of the proceeds.

In examining trends in required employer contributions, pension funding bond debt service is combined with required contri-

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butions to the systems since the debt service is indirectly a payment to reduce the pension liability. The combined payments increased 43.8% from $1.7 billion in fiscal year 2003 to almost $2.5 billion in fiscal year 2004 as the first year of bond debt service added almost $500 million to payments. Since fiscal year 2004 was the year the employers' share was largely paid from a reserved portion of the bond proceeds, these payments had no impact on the General Funds. With the hold harmless provision limiting contributions plus debt service payments, required payments should decline 8.3% to $2.249 billion in fiscal year 2005. Starting in fiscal year 2006, however, combined employer contributions and debt service for pensions are forecast to resume double digit growth rates.

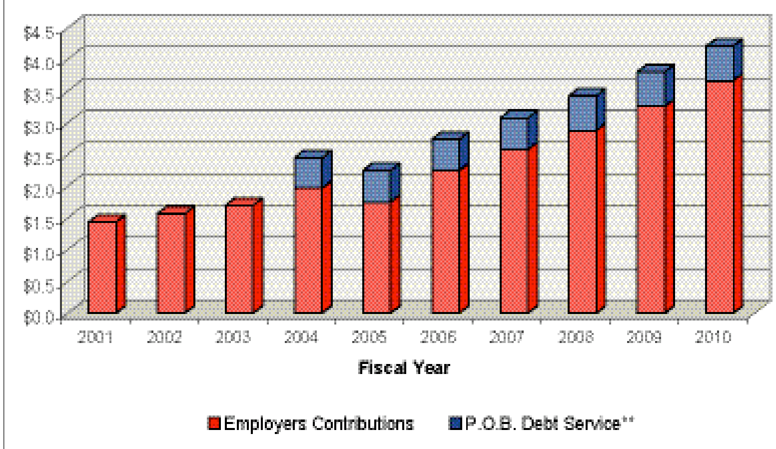
The Fiscal Year 2006 Pension Issues

The General Funds payments to the retirement systems are computed as the total required certified contributions minus payments from school districts and for federally funded programs to TRS and SURS, payments for employees on non-General Funds payrolls to SERS, and pension contributions from surplus unclaimed property deposited into the State Pensions Fund.

Estimated General Funds retirement and debt service contributions are $1.8 billion in fiscal year 2005. Based on retirement system certifications and debt service requirements, General Funds contributions are scheduled to increase approximately $500 million to $2.3 billion in fiscal year 2006.

In part, the significant growth in potential contributions reflects two factors that reduce General Funds contributions in fiscal year 2005. Accumulated unclaimed property monies plus an $80 million General Revenue Fund transfer will be used to obtain an estimated $242 million in pension contributions from the State Pensions Fund in fiscal year 2005. For fiscal year 2006, the contributions from the State Pensions Fund are expected to return to a more normal $80 million. The required ERI payment to SERS is estimated at $68.1 million in fiscal year 2005, but is expected to increase to $280.5 million in fiscal year 2006 as the ten-year amortization process under current law begins.

Employers Contributions and POB Debt Service*
($ in billions)



*Actual contributions for fiscal year 2001 to 2004. Fiscal year 2005 to fiscal year 2010 amounts are estimated and projected contributions contained in actuarial valuations as of June 30, 2004. TRS excludes Guaranteed Minimum Annuity Reserve.

**Fiscal Year 2004 debt service was collected in fiscal year 2005.

None of the options to relieve the 2006 fiscal pressure of pension obligations on the General Funds is attractive. For example, the ERI funding formula could be adjusted legislatively to shift payments to the future such as by blending the ERI liability into the fifty-year funding plan. Any delay in pension funding just shifts the funding issue to future years. It also puts pressure on the systems investment portfolios since employee and employer contributions currently do not match benefit payments requiring annual cash withdrawals from retirement investment pools.

With continued low interest rates, the option of another bond issue has been discussed. As pointed out previously, this strategy relies upon long-term returns on pension investments exceeding interest obligations and would increase the State's pension and debt service obligations if investments perform significantly worse than projected. The Economic and Fiscal Commission has recently examined the ERI funding issue and has endorsed the issuance of pension funding bonds for the approximately $1.9 billion liability.

The Governor's Commission on State Pensions has been considering possible means of reducing the long-term pension burden and the fiscal year 2006 budget impact. Since the Illinois Constitution prevents any reduction in pension benefits that have been earned, options are limited to reducing benefit levels for new employees or increasing contributions by members of the pension systems. Among the benefit reductions for new hires that were offered to the Governor and General Assembly for examination and consideration were 1) reducing guaranteed cost of living increases, 2) raising the full benefit retirement age, 3) restricting enrollment in the alternative formula for high risk occupations, 4) limiting state liability for benefits from end-of-career salary boosts, and 5) eliminating the money purchase option that can raise pension benefits above the level determined by the normal formula. Members' contributions were indirectly increased in the past when the service necessary to fully vest health care benefits for SERS members was increased from 8 years to 20 years.

The state's retirement systems will continue to be financially challenging to the state's General Funds. A long history of underpayments to the systems and pension 'holidays' helped to create the current situation. Attempts to limit funding for the systems will likely only exacerbate cash flow problems and increase the burden on future budgets. ■

A Monthly Look At State Finance

Vital Statistics

The Heartbeat of Illinois' Finance

Fiscal Position Deteriorates Despite Improving Economic Revenues

Through the halfway point of fiscal year 2005, the state's backlog of unpaid bills continues to mount. The dollar amount held (over $1.5 billion) and the number of days payments are delayed (30 days) have increased significantly since the first quarter, even while the economy and the revenues of related sources increased as expected in the first half of the fiscal year. This growth, however, was unable to offset the decline from one-time revenues collected last fiscal year. Fiscal year-to-date, both General Funds revenues and expenditures have been greatly impacted by the loss of federal funds and the short-term borrowing for Medicaid in June of 2004.

Last fiscal year, the federal Jobs and Growth Tax Relief Reconciliation Act temporarily increased the Medicaid reimbursement rate and granted the state $422 million in additional aid. As a result, federal sources through six months of fiscal year 2005 now are down $763 million compared to last year. Another fiscal year 2004 source of one-time revenues were the transfers from the Pension Contribution Fund that totaled $965 million in the first six months. The decline in General Funds transfers in was partially offset by a $433 million transfer from the Medicaid Provider Relief Fund to pay the first installment of the June 2004 short-term borrowing debt. Therefore, even with the economic driven and other state sources of revenue increasing by $474 million, total General Funds base revenues through the first half of fiscal year 2005 are down $705 million in comparison with fiscal year 2004.

On the expenditure side, Department of Public Aid grants have decreased by $677 million from last year at this time. Medicaid expenditures have grown in the second quarter but not enough to offset the reduced spending in the first quarter. Teachers retirement grants, higher education and operations spending all posted declines through the first half of fiscal year 2005. The decreases in spending were partially offset by the increase in transfers out of the General Funds including the repayment of short-term borrowing.

At the end of the second quarter of fiscal year 2005, the backlog of unpaid bills exceeded the end of December backlog for the past four years. As seen in the chart, the adjusted General Revenue Fund balance was a negative $1.564 billion with a balance of $25 million and a backlog totaling $1.589 billion. Payables have increased by $1.053 billion since the end of the first quarter. Payment delays have grown from 11 to 30 working days in the past three months.

Base Revenues Decrease 5.4%

Total base revenues into the General Funds were $12.391 billion, a decrease of $705 million or 5.4% below six months revenues last year. Federal sources declined $763 million or 26.6% while state sources increased $58 million or 0.6%.

The decrease in federal revenues is due largely to factors associated with the federal bailout of last year. Under a federal initiative, the state received a $422 million relief grant and Medicaid reimbursement rates were increased from 50% to 53%. Compared to the first half of last year, Department of Public Aid Medicaid expenditures were down by $677 million, resulting in less federal reimbursement opportunity.

State sources increased as cash receipts were up $474 million or 5.7% and transfers in decreased $416 million or 22.2%. Transfers are down due to the Pension Contribution Fund, a one-time source last year that provided $965 million. This decline was partially offset by a $433 million transfer from the Medicaid Provider Relief Fund to help pay for the June 2004 short-term borrowing. Other increases include the Lottery Fund, chargeback transfers and legislated (fund sweep) transfers.

Cash receipt growth was led by improvement in economic driven sources. Individual income taxes were up $150 million or 4.7% and corporate income taxes increased $7 million. Sales taxes grew 3.1% or $100 million. While these increases are not by themselves significant, last year's figures included an additional $287 million from the tax amnesty program. Excluding the tax amnesty factor, the growth would have been: individual income taxes up $184 million, corporate income taxes up $156 million, and sales taxes up $195 million. Income tax growth was also impacted by a reduction in the amount allocated to the Refund

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Fund. Adjusting for the amnesty payments in fiscal year 2004 and changes to the Refund Fund contribution rate, individual income taxes were up 4.0%, sales taxes up 6.2%, and corporate income taxes were up 44.0%. Although these are the best growth rates seen since fiscal year 2000, they are more akin to the growth rates seen in the mid-1990s than in the late 1990s. Some of the growth is also attributable to “loophole closures” provided for in the budget.

Other sources of revenue to the General Funds in six months of fiscal year 2005 increased $217 million or 14.2%. Cigarette taxes went up due to the one-time reallocation of $50 million to the General Funds. Commercial distribution fees are up $34 million. This and other fees did not generate receipts early in the fiscal year last year. Inheritance taxes increased due to the settlement of some large estates and decoupling from the federal tax last year.

Base Expenditures Down 3.6%

Through December, base General Funds spending (which excludes transfers to repay short-term borrowing) totaled $12.598 billion, $465 million or 3.6% below the previous year. When repayment for short-term borrowing in fiscal year 2004 is factored in, fiscal year 2005 expenditures in the first six months were actually $695 million or 5.2% below last year. General Funds appropriations are up $202 million or 0.9% over last year. Through the first half of fiscal year 2005, 47.6% of General Funds appropriations have been expended compared to 57.1% last year.

The decline in both the amount and pace of spending is primarily attributable to the decrease in Medicaid grant spending by the Department of Public Aid. Medicaid grant spending of $2.898 billion is down $677 million or 18.9% from last year. The decline in Medicaid spending is in part due to higher spending in the first quarter of last fiscal year done in order to take advantage of the aforementioned higher federal Medicaid reimbursement rates. In addition, the short-term borrowing directed to Medicaid spending in June 2004 accelerated medical assistance spending from the beginning of fiscal year 2005 to the end of fiscal year 2004. These two factors contributed to a $505 million decrease in Medicaid appropriations for the Department of Public Aid.

Other areas of spending which decreased from last year include higher education operations (down $135 million or 14.3%), regular state agency operations (down $48 million or 1.9%), teachers retirement grants (down $51 million or 10.2%), and higher education grants (down $15 million or 4.0%).

Areas of spending which increased include Human Services grants (up $154 million or 11.1%), State Board of Education grants (up $146 million or 5.8%), and transfers out (up $1.302 billion or 148.8%). The large increase in transfers out is due primarily to debt service transfers which have increased by $907 million from last year. Debt service transfers are utilized to pay both general obligation bond and short-term borrowing repayments.

What Lies Ahead?

The economically driven state revenues continue to perform reasonably well with some year- over-year improvement in income and sales taxes. Although these improvements can be partially explained by tax law changes for the fiscal year 2005 budget, there is hope that Illinois will not see its economic revenues stagnate as in some recent years. Expenditures are likely to slow as one of the largest components of spending (Medicaid) exhausts its appropriation in the late spring. In addition, this year there will not be a repayment of short-term borrowing as in the latter parts of fiscal years 2003 and 2004.

The backlog of bills is expected to continue to increase over the next few months but will be reduced when large income tax payments arrive in the spring and spending slows. However, without a dramatic improvement in revenues, the state is likely to continue to hold a significant amount of General Funds bills at the end of this fiscal year.

This worsening of the state’s fiscal position during the course of fiscal year 2005 will have a negative impact on the development of the fiscal year 2006 budget. Unpaid bills carried over to the next fiscal year will have first claim on next year’s revenues and must be accommodated within the budget plan. Without a fiscal year 2005 supplemental appropriation (which in itself would create current fiscal year spending pressures), any Medicaid backlog will have to be paid for out of fiscal year 2006 appropriations. Economic forecasts call for continued albeit moderate growth. This limited revenue growth will occur in tandem with increasing and long building pressure to adequately address the state’s pension obligations and rapid growth in Medicaid and health care costs among other factors. Even with one-time revenue measures and redirection of non-GRF funds into the General Funds (practices that have yet to clear all judicial tests) and stable revenue growth, the state’s cash position has not improved. It seems apparent that even substantial growth in economy driven sources will not in and of itself allow policy makers to address continuing budgetary pressures. ■

GENERAL FUNDS REVENUES, EXPENDITURES AND BALANCES
(Dollars in Millions)

	Oct. 2004	Four Months FY 2005	Change From Prior Year $	Change From Prior Year %
Total General Funds				
Available Balance	$ 292	$ 182	$ (135)	(42.6) %
Revenues	2,017	8,576	(501)	(5.5)
Expenditures	1,969	8,418	(718)	(7.9)
Ending Balance	$ 340	$ 340	$ 82	31.8 %
General Revenue Fund				
Available Balance	$ 22	$ 24	$ 23	N/A %
Revenues	1,665	7,253	(637)	(8.1)
Expenditures	1,603	7,193	(675)	(8.6)
Ending Balance	$ 84	$ 84	$ 61	265.2 %
Common School Special Account Fund				
Available Balance	$ 110	$ 12	$ (50)	(80.6) %
Revenues	136	553	30	5.7
Expenditures	169	488	(24)	(4.7)
Ending Balance	$ 77	$ 77	$ 4	5.5 %
Education Assistance Fund				
Available Balance	$ 121	$ 124	$ (85)	(40.7) %
Revenues	91	382	4	1.1
Expenditures	100	394	(59)	(13.0)
Ending Balance	$ 112	$ 112	$ (22)	(16.4) %
Common School Fund				
Available Balance	$ 38	$ 22	$ (22)	(50.0) %
Revenues	295	877	53	6.4
Expenditures	265	831	(9)	(1.1)
Ending Balance	$ 68	$ 68	$ 40	142.9 %

Note: Total General Funds excludes interfund transfers while the individual funds include such transfers. Numbers may not add due to rounding.

GENERAL FUNDS REVENUES
(Dollars in Millions)

	Oct. 2004	Four Months FY 2005	Change From Prior Year $	Change From Prior Year %
Revenues:				
State Sources:				
Cash Receipts:				
Income Taxes:				
Individual	$ 531	$ 2,207	$ 129	6.2 %
Corporate	32	240	89	58.9
Total, Income Taxes	$ 563	$ 2,447	$ 218	9.8 %
Sales Taxes	541	2,214	112	5.3
Other Sources:				
Public Utility Taxes	68	318	(9)	(2.8)
Cigarette Taxes	42	183	50	37.6
Inheritance Tax (gross)	19	88	25	39.7
Liquor Gallonage Taxes	12	50	7	16.3
Insurance Taxes and Fees	0	94	14	17.5
Corporation Franchise Tax and Fees	18	60	11	22.4
Investment Income	5	13	(9)	(40.9)
Cook County IGT	54	130	0	0.0
Riverboat Gambling Taxes	13	55	11	25.0
Other	28	154	77	100.0
Total, Other Sources	$ 259	$ 1,145	$ 177	18.3 %
Total, Cash Receipts	$ 1,363	$ 5,806	$ 507	9.6 %
Transfers In:				
Lottery Fund	$ 41	$ 184	$ 23	14.3 %
State Gaming Fund	55	208	(7)	(3.3)
Pension Contribution Fund	0	0	(669)	(100.0)
Other Funds	89	789	505	177.8
Total, Transfers In	$ 185	$ 1,181	$ (148)	(11.1) %
Total, State Sources	$ 1,548	$ 6,987	$ 359	5.4 %
Federal Sources:				
Cash Receipts	$ 193	$ 1,268	$ (943)	(42.7) %
Transfers In	0	45	33	275.0
Total, Federal Sources	$ 193	$ 1,313	$ (910)	(40.9) %
Total, Base Revenues	**$ 1,741**	**$ 8,300**	**$ (551)**	**(6.2) %**
Short-Term Borrowing	0	0	0	0.0
Transfer from Budget Stabilization Fund	276	276	50	22.1
Total, Revenues	$ 2,017	$ 8,576	$ (501)	(5.5) %

GENERAL FUNDS ANALYSIS OF EXPENDITURES
(Dollars in Millions)

	Oct. 2004	Four Months FY 2005	Change From Prior Year $	Change From Prior Year %
Expenditures:				
Awards and Grants:				
Public Aid	$ 562	$ 1,844	$ (840)	(31.3) %
Elem. & Sec. Education:				
State Board of Education	429	1,562	17	1.1
Teachers Retirement	81	285	(49)	(14.7)
Total, Elem. & Sec. Education	$ 510	$ 1,847	$ (32)	(1.7) %
Human Services	238	1,043	93	9.8
Higher Education	78	219	0	0.0
All Other Grants	161	468	34	7.8
Total, Awards and Grants	$ 1,549	$ 5,421	$ (745)	(12.1) %
Operations:				
Other Agencies	$ 398	$ 1,663	$ 34	2.1 %
Higher Education	127	491	(113)	(18.7)
Total, Operations	$ 525	$ 2,154	$ (79)	(3.5) %
Regular Transfers Out	$ 344	$ 1,759	$ 1,143	185.6 %
All Other	$ 1	$ 50	$ 37	284.6 %
Vouchers Payable Adjustment	$ (450)	$ (966)	$ (1,024)	N/A
Total, Base Expenditures	**$ 1,969**	**$ 8,418**	**$ (668)**	**(7.4) %**
Transfers to Repay GRF Short-Term Borrowing*	0	0	(50)	(100.0)
Total, Expenditures	$ 1,969	$ 8,418	$ (718)	(7.9) %

COMPARISON OF SPENDING FOR OPERATIONS BY OBJECT
(Dollars in Millions)

	Oct. 2004	Four Months FY 2005	Change From Prior Year $	Change From Prior Year %
Personal Services:				
Regular Positions	$ 297	$ 1,120	$ 417	59.3 %
Other Personal Services	14	63	(15)	(19.2)
Total, Personal Services	$ 311	$ 1,183	$ 402	51.5 %
Contribution Retirement	29	173	(30)	(14.8)
Contribution Social Security	14	57	6	11.8
Contribution Group Insurance	85	314	56	21.7
Contractual Services	40	179	(16)	(8.2)
Travel	2	7	1	16.7
Commodities	9	39	(2)	(4.9)
Printing	0	2	0	0.0
Equipment	1	14	3	27.3
Electronic Data Processing	3	16	(6)	(27.3)
Telecommunications	5	20	0	0.0
Automotive Equipment	1	6	(1)	(14.3)
Other Operations	25	144	(492)	(77.4)
Total, Operations	$ 525	$ 2,154	$ (79)	(3.5) %

COMPARISON OF SPENDING FOR AWARDS AND GRANTS
(Dollars in Millions)

	Oct. 2004	Four Months FY 2005	Change From Prior Year $	Change From Prior Year %
State Board of Education:				
General State Aid	$ 305	$ 940	$ 54	6.1 %
All Other	124	622	(37)	(5.6)
Public Aid	562	1,844	(840)	(31.3)
Human Services	238	1,043	93	9.8
Higher Education:				
Student Assistance Commission	56	114	(1)	(0.9)
Community College Board	11	93	(1)	(1.1)
Other	11	12	2	20.0
Teacher's Retirement	81	285	(49)	(14.7)
Children and Family Services	44	217	2	0.9
Aging	18	81	1	1.3
Revenue	2	3	2	200.0
All Other	97	167	29	21.0
Total, Awards and Grants	$ 1,549	$ 5,421	$ (745)	(12.1) %

GENERAL FUNDS REVENUES, EXPENDITURES AND BALANCES
(Dollars in Millions)

	Nov. 2004	Five Months: FY 2005	Change From Prior Year: $	Change From Prior Year: %
Total General Funds				
Available Balance	$ 340	$ 182	$ (135)	(42.6) %
Revenues	1,745	10,320	(745)	(6.7)
Expenditures	1,894	10,311	(815)	(7.3)
Ending Balance	$ 191	$ 191	$ (65)	(25.4) %
General Revenue Fund				
Available Balance	$ 84	$ 24	$ 23	N/A %
Revenues	1,457	8,709	(835)	(8.7)
Expenditures	1,528	8,720	(810)	(8.5)
Ending Balance	$ 13	$ 13	$ (2)	(13.3) %
Common School Special Account Fund				
Available Balance	$ 77	$ 12	$ (50)	(80.6) %
Revenues	133	686	29	4.4
Expenditures	137	625	(32)	(4.9)
Ending Balance	$ 73	$ 73	$ 11	17.7 %
Education Assistance Fund				
Available Balance	$ 112	$ 124	$ (85)	(40.7) %
Revenues	90	472	0	0.0
Expenditures	101	495	(56)	(10.2)
Ending Balance	$ 101	$ 101	$ (29)	(22.3) %
Common School Fund				
Available Balance	$ 68	$ 22	$ (22)	(50.0) %
Revenues	202	1,079	(31)	(2.8)
Expenditures	266	1,097	(8)	(0.7)
Ending Balance	$ 4	$ 4	$ (45)	(91.8) %

Note: Total General Funds excludes interfund transfers while the individual funds include such transfers. Numbers may not add due to rounding.

GENERAL FUNDS REVENUES
(Dollars in Millions)

	Nov. 2004	Five Months: FY 2005	Change From Prior Year: $	Change From Prior Year: %
Revenues:				
State Sources:				
Cash Receipts:				
Income Taxes:				
Individual	$ 529	$ 2,735	$ 161	6.3 %
Corporate	17	257	(8)	(3.0)
Total, Income Taxes	$ 546	$ 2,992	$ 153	5.4 %
Sales Taxes	530	2,745	109	4.1
Other Sources:				
Public Utility Taxes	77	395	(7)	(1.7)
Cigarette Taxes	33	216	50	30.1
Inheritance Tax (gross)	25	113	25	28.4
Liquor Gallonage Taxes	13	63	9	16.7
Insurance Taxes and Fees	1	95	14	17.3
Corporation Franchise Tax and Fees	16	76	18	31.0
Investment Income	8	21	(4)	(16.0)
Cook County IGT	40	170	17	11.1
Riverboat Gambling Taxes	13	69	14	25.5
Other	26	179	85	90.4
Total, Other Sources	$ 252	$ 1,397	$ 221	18.8 %
Total, Cash Receipts	$ 1,328	$ 7,134	$ 483	7.3 %
Transfers In:				
Lottery Fund	$ 31	$ 215	$ 14	7.0 %
State Gaming Fund	50	258	(7)	(2.6)
Pension Contribution Fund	0	0	(817)	(100.0)
Other Funds	4	792	484	157.1
Total, Transfers In	$ 85	$ 1,265	$ (326)	(20.5) %
Total, State Sources	$ 1,413	$ 8,399	$ 157	1.9 %
Federal Sources:				
Cash Receipts	$ 322	$ 1,589	$ (987)	(38.3) %
Transfers In	10	56	35	166.7
Total, Federal Sources	$ 332	$ 1,645	$ (952)	(36.7) %
Total, Base Revenues	**$ 1,745**	**$ 10,044**	**$ (795)**	**(7.3) %**
Short-Term Borrowing	0	0	0	0.0
Transfer from Budget Stabilization Fund	0	276	50	22.1
Total, Revenues	$ 1,745	$ 10,320	$ (745)	(6.7) %

GENERAL FUNDS ANALYSIS OF EXPENDITURES
(Dollars in Millions)

	Nov. 2004	Five Months: FY 2005	Change From Prior Year: $	Change From Prior Year: %
Expenditures:				
Awards and Grants:				
Public Aid	$ 540	$ 2,383	$ (710)	(23.0) %
Elem. & Sec. Education:				
State Board of Education	417	1,979	77	4.0
Teachers Retirement	81	366	(50)	(12.0)
Total, Elem. & Sec. Education	$ 498	$ 2,345	$ 27	1.2 %
Human Services	263	1,306	163	14.3
Higher Education	118	338	(19)	(5.3)
All Other Grants	92	560	40	7.7
Total, Awards and Grants	$ 1,511	$ 6,932	$ (499)	(6.7) %
Operations:				
Other Agencies	$ 403	$ 2,067	$ 21	1.0 %
Higher Education	150	640	(162)	(20.2)
Total, Operations	$ 553	$ 2,707	$ (141)	(5.0) %
Regular Transfers Out	$ 236	$ 1,995	$ 1,256	170.0 %
All Other	$ 0	$ 50	$ 37	284.6 %
Vouchers Payable Adjustment	$ (406)	$ (1,373)	$ (1,383)	N/A
Total, Base Expenditures	**$ 1,894**	**$ 10,311**	**$ (730)**	**(6.6) %**
Transfers to Repay GRF Short-Term Borrowing*	0	0	(85)	(100.0)
Total, Expenditures	$ 1,894	$ 10,311	$ (815)	(7.3) %

COMPARISON OF SPENDING FOR OPERATIONS BY OBJECT
(Dollars in Millions)

	Nov. 2004	Five Months: FY 2005	Change From Prior Year: $	Change From Prior Year: %
Personal Services:				
Regular Positions	$ 323	$ 1,443	$ 563	64.0 %
Other Personal Services	14	77	(20)	(20.6)
Total, Personal Services	$ 337	$ 1,520	$ 543	55.6 %
Contribution Retirement	29	203	(77)	(27.5)
Contribution Social Security	14	71	8	12.7
Contribution Group Insurance	86	400	58	17.0
Contractual Services	33	212	(23)	(9.8)
Travel	1	8	0	0.0
Commodities	8	47	(2)	(4.1)
Printing	1	3	0	0.0
Equipment	1	15	3	25.0
Electronic Data Processing	3	19	(6)	(24.0)
Telecommunications	4	23	(4)	(14.8)
Automotive Equipment	2	8	0	0.0
Other Operations	34	178	(641)	(78.3)
Total, Operations	$ 553	$ 2,707	$ (141)	(5.0) %

COMPARISON OF SPENDING FOR AWARDS AND GRANTS
(Dollars in Millions)

	Nov. 2004	Five Months: FY 2005	Change From Prior Year: $	Change From Prior Year: %
State Board of Education:				
General State Aid	$ 305	$ 1,245	$ 72	6.1 %
All Other	112	734	5	0.7
Public Aid	540	2,383	(710)	(23.0)
Human Services	263	1,306	163	14.3
Higher Education:				
Student Assistance Commission	40	154	(16)	(9.4)
Community College Board	76	169	2	1.2
Other	2	15	(5)	(25.0)
Teacher's Retirement	81	366	(50)	(12.0)
Children and Family Services	46	263	11	4.4
Aging	26	107	9	9.2
Revenue	2	5	(2)	(28.6)
All Other	18	185	22	13.5
Total, Awards and Grants	$ 1,511	$ 6,932	$ (499)	(6.7) %

GENERAL FUNDS REVENUES, EXPENDITURES AND BALANCES
(Dollars in Millions)

	Dec. 2004	Six Months FY 2005	Change From Prior Year $	Change From Prior Year %
<u>Total General Funds</u>				
Available Balance	191	182	(135)	(42.6)
Revenues	2,347	12,667	(655)	(4.9)
Expenditures	2,287	12,598	(695)	(5.2)
Ending Balance	251	251	(95)	(27.5)
<u>General Revenue Fund</u>				
Available Balance	13	24	23	N/A
Revenues	1,979	10,688	(668)	(5.9)
Expenditures	1,967	10,687	(648)	(5.7)
Ending Balance	25	25	3	13.6
<u>Common School Special Account Fund</u>				
Available Balance	73	12	(50)	(80.6)
Revenues	147	834	27	3.3
Expenditures	144	770	51	7.1
Ending Balance	76	76	(74)	(49.3)
<u>Education Assistance Fund</u>				
Available Balance	101	124	(85)	(40.7)
Revenues	115	587	(1)	(0.2)
Expenditures	101	596	(54)	(8.3)
Ending Balance	115	115	(32)	(21.8)
<u>Common School Fund</u>				
Available Balance	4	22	(22)	(50.0)
Revenues	296	1,374	22	1.6
Expenditures	265	1,361	(8)	(0.6)
Ending Balance	35	35	8	29.6

Note: Total General Funds excludes interfund transfers while the individual funds include such transfers. Numbers may not add due to rounding.

GENERAL FUNDS REVENUES
(Dollars in Millions)

	Dec. 2004	Six Months FY 2005	Change From Prior Year $	Change From Prior Year %
Revenues:				
State Sources:				
Cash Receipts:				
Income Taxes:				
Individual	602	3,337	150	4.7
Corporate	161	419	7	1.7
Total, Income Taxes	763	3,756	157	4.4
Sales Taxes	589	3,333	100	3.1
Other Sources:				
Public Utility Taxes	117	511	(10)	(1.9)
Cigarette Taxes	33	250	50	25.0
Inheritance Tax (gross)	25	138	38	38.0
Liquor Gallonage Taxes	13	76	12	18.8
Insurance Taxes and Fees	74	168	15	9.8
Corporation Franchise Tax and Fees	11	87	12	16.0
Investment Income	6	28	(2)	(6.7)
Cook County IGT	23	193	17	9.7
Riverboat Gambling Taxes	15	84	14	20.0
Other	26	205	71	53.0
Total, Other Sources	343	1,740	217	14.2
Total, Cash Receipts	1,695	8,829	474	5.7
Transfers In:				
Lottery Fund	65	280	30	12.0
State Gaming Fund	60	318	(7)	(2.2)
Pension Contribution Fund	0	0	(965)	(100.0)
Other Funds	64	856	526	159.4
Total, Transfers In	189	1,454	(416)	(22.2)
Total, State Sources	1,884	10,283	58	0.6
Federal Sources:				
Cash Receipts	463	2,053	(797)	(28.0)
Transfers In	0	55	34	161.9
Total, Federal Sources	463	2,108	(763)	(26.6)
Total, Base Revenues	**2,347**	**12,391**	**(705)**	**(5.4)**
Short-Term Borrowing	0	0	0	0.0
Transfer from Budget Stabilization Fund	0	276	50	22.1
Total, Revenues	2,347	12,667	(655)	(4.9)

GENERAL FUNDS ANALYSIS OF EXPENDITURES
(Dollars in Millions)

	Dec. 2004	Six Months FY 2005	Change From Prior Year $	Change From Prior Year %
Expenditures:				
Awards and Grants:				
Public Aid	515	2,898	(677)	(18.9)
Elem. & Sec. Education:				
State Board of Education	668	2,647	146	5.8
Teachers Retirement	81	447	(51)	(10.2)
Total, Elem. & Sec. Education	749	3,094	95	3.2
Human Services	235	1,542	154	11.1
Higher Education	25	362	(15)	(4.0)
All Other Grants	110	670	23	3.6
Total, Awards and Grants	1,634	8,566	(420)	(4.7)
Operations:				
Other Agencies	406	2,473	(48)	(1.9)
Higher Education	167	806	(135)	(14.3)
Total, Operations	573	3,279	(183)	(5.3)
Regular Transfers Out	182	2,177	1,302	148.8
All Other	1	51	37	264.3
Vouchers Payable Adjustment	(103)	(1,475)	(1,201)	N/A
Total, Base Expenditures	**2,287**	**12,598**	**(465)**	**(3.6)**
Transfers to Repay GRF Short-Term Borrowing*	0	0	(230)	(100.0)
Total, Expenditures	2,287	12,598	(695)	(5.2)

COMPARISON OF SPENDING FOR OPERATIONS BY OBJECT
(Dollars in Millions)

	Dec. 2004	Six Months FY 2005	Change From Prior Year $	Change From Prior Year %
Personal Services:				
Regular Positions	329	1,772	717	68.0
Other Personal Services	14	91	(25)	(21.6)
Total, Personal Services	343	1,863	692	59.1
Contribution Retirement	30	232	(74)	(24.2)
Contribution Social Security	14	85	9	11.8
Contribution Group Insurance	94	493	(3)	(0.6)
Contractual Services	41	254	(23)	(8.3)
Travel	2	10	1	11.1
Commodities	9	56	(4)	(6.7)
Printing	0	3	0	0.0
Equipment	4	19	7	58.3
Electronic Data Processing	2	21	(7)	(25.0)
Telecommunications	5	28	(4)	(12.5)
Automotive Equipment	2	10	0	0.0
Other Operations	27	205	(777)	(79.1)
Total, Operations	573	3,279	(183)	(5.3)

COMPARISON OF SPENDING FOR AWARDS AND GRANTS
(Dollars in Millions)

	Dec. 2004	Six Months FY 2005	Change From Prior Year $	Change From Prior Year %
State Board of Education:				
General State Aid	305	1,550	92	6.3
All Other	363	1,097	54	5.2
Public Aid	515	2,898	(677)	(18.9)
Human Services	235	1,542	154	11.1
Higher Education:				
Student Assistance Commission	23	176	(11)	(5.9)
Community College Board	0	170	3	1.8
Other	2	16	(7)	(30.4)
Teacher's Retirement	81	447	(51)	(10.2)
Children and Family Services	64	326	14	4.5
Aging	21	128	9	7.6
Revenue	4	9	(5)	(35.7)
All Other	21	207	5	2.5
Total, Awards and Grants	1,634	8,566	(420)	(4.7)

Cost of Living Adjustment vs. Inflation

The five state retirement systems provide a cost of living adjustment to retirees to partially enable the value of the benefit to keep up with inflationary pressures. Currently, the increase is set at 3.0% per year. How does this rate keep up with the rate of inflation?

Recent times have had relatively low inflation rates. Looking at the Consumer Price Index for Urban Consumers, the nationwide inflation rate has been below 3.0% every year except for one (2000) since 1993. During this 12-year span, the average rate of inflation was just over 2.5%. However, the rate of inflation has exceeded 3% during 18 of the last 30 years, averaging 4.62%.

According to the Teachers' Retirement System's Fiscal Year 2004 Comprehensive Annual Financial Report, the average original benefit payment to TRS retirees with 26-30 years of service who retired in the years 1974-1978 was $7,080 per year. The 2004 benefit payment to these retirees was approximately $16,500 per year - based on a 3% adjustment from the original benefit per year up until 1990, 2 statutory increases in the 1980's, and a compounded 3% increase since 1990. (If the increase had been a 3% compounded COLA as per current law, the 2004 payment would have been $16,680.) The inflation adjusted value of the original payment from 1975 would be approximately $24,800 today, representing $8,300 in lost buying power. ■

Comptroller Daniel W. Hynes is the chief fiscal officer for the state, managing its financial accounts, processing more than 18 million transactions a year, and performing a watchdog role to assure that all payments meet the requirements of the law. The Comptroller's Office also provides timely and accurate fiscal information and analysis to the Governor, the Illinois General Assembly, and local government officials so they can make informed budget decisions. In addition, the Office oversees the state's private cemetery and funeral home industry.

COMPTROLLER DANIEL W. HYNES

Contact us at our web address: http://www.ioc.state.il.us

Fiscal Focus
QUARTERLY

COMPTROLLER DANIEL W. HYNES
Capitol Building
Springfield, Illinois 62706