



DANIEL W. HYNES  
COMPTROLLER

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# **EXECUTIVE SUMMARY**

— Fiscal Year 2003 —

FINANCIAL  
REPORT

Comptroller Daniel W. Hynes is the Chief Fiscal Officer for the State of Illinois, 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.





May, 2004

DANIEL W. HYNES

## *A Message to Illinois Taxpayers*

The mission and priorities of my administration include providing taxpayers with useful and understandable information about the fiscal operations of the State of Illinois. This presentation of the *Executive Summary*, also known by the financial community as Illinois' popular annual financial report, is written to enhance public understanding of the state's financial statements.

The report combines information based on the state's *Comprehensive Annual Financial Report* prepared in accordance with Generally Accepted Accounting Principles (GAAP) for government and cash basis budgetary information contained in the *Traditional Budgetary Financial Report*. Both of these other reports can be accessed at our Web site, [www.ioc.state.il.us](http://www.ioc.state.il.us), or by calling at (217)782-6000 or (312) 814-2451.

Under the GAAP reporting system, revenues accrue to the period in which they are earned and expenditures are counted against the period in which the liability was obligated. Under the cash basis reporting system, revenues and expenditures are compared for the budgetary period regardless of when they were incurred. The State of Illinois budgets on a cash basis.

In this *Executive Summary*, as in past reports, we examine the economic and fiscal climate in which future budgets will be considered. It is valuable for policy-makers to understand these issues in order to make informed decisions. It is also a useful resource for taxpayers to measure the effectiveness of governmental programs.

This year's report highlights that for the fifth consecutive year, the General Funds GAAP balance has deteriorated after five years of deficit reduction. The state ended fiscal year 2003 with a negative General Funds balance of \$4.166 billion indicating that the state's GAAP deficit had worsened by \$1.218 billion compared to the prior year. The cash position appeared to improve as the available balance increased from \$256 million at the end of fiscal year 2002 to \$317 million at the end of fiscal year 2003 and the budgetary balance increased by \$126 million, from a deficit of \$1.220 billion to a deficit of \$1.094 billion. However, neither of these figures takes into account the \$1.5 billion in short-term borrowing in fiscal year 2003 that must be repaid in fiscal year 2004. When the borrowing is taken into account, the effective cash position declined by over \$1.3 billion from fiscal year 2002 to 2003.

In addition to the degeneration of both the GAAP balance and the effective cash position of the General Funds, for the sixth year in a row Section 25 liabilities experienced growth, standing at \$1.849 billion as of June 30, 2003. The continuing economic recession coupled with these negative fiscal balances pose serious challenges for the future. Policy makers may be well-served to consider these issues carefully in crafting future budgets and continue to develop budgetary methods and practices that minimize the impact on state programs due to these phenomena. The Rainy Day Fund established in fiscal year 2000, long a policy objective of this office, is an example of a budget innovation that once properly funded, will permit the state to address these issues.

We hope you find this report to be both informative and useful. Please share with us any suggestions or comments you may have about this report and its contents.

Sincerely,

Daniel W. Hynes  
Comptroller



# Award for Outstanding Achievement in Popular Annual Financial Reporting

PRESENTED TO

**STATE OF ILLINOIS**

For the fiscal year ending  
June 30, 2002



*William Patrick Pate*  
President

*Jeffrey L. Essler*  
Executive Director



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# INTRODUCTION

## State Government Background

Geographically located in the central portion of the United States, Illinois is a diverse state that covers almost 56,000 square miles of land. Many of Illinois' approximately 12.4 million inhabitants live in urban areas, although there is a strong rural presence in the state as well. Nearly one-fourth or approximately 2.9 million of the state's residents live in Chicago, the third largest city in the country. Six other municipalities including Rockford, Aurora, Naperville, Peoria, Joliet and the state's capitol of Springfield have populations in excess of 100,000 with another 19 municipalities' populations estimated to be in excess of 50,000.

The framework of government for Illinois and its 12.4 million residents is set forth by the Constitution. Since joining the Union in 1818, Illinois government has evolved through four Constitutions. The current Constitution, adopted and ratified in 1970, recognized three main branches of state government. The Executive Branch has six elected officers: a Governor, Lieutenant Governor, Attorney General, Secretary of State, Comptroller, and Treasurer. The Legislative Branch includes two chambers, a Senate with one senator from each of the 59 Senate districts, and a House of Representatives with one representative from each of the 118 House districts. The Judicial Branch consists of a seven-member Supreme Court, Appellate Courts in five judicial districts and Circuit Courts in twenty-two judicial circuits.

Responsibility for most of the day-to-day operations of state government and its programs resides in the executive branch, with the Governor overseeing the largest portion. Under the purview of the Governor there were twenty-three major departments in fiscal year 2003 including Human Services, Transportation, Public Aid, and Revenue. There are also approximately forty-five other agencies, and over one hundred miscellaneous boards and commissions under the jurisdiction of the Governor. In addition, the other five elected officers under the executive branch oversee their respective agencies. State government agencies combined directly employed approximately 76,200 persons at the end of fiscal year 2003, 12,300 less than one year earlier due to early retirement incentives implemented to help combat the fiscal crisis. The Departments of Human Services (15,515), Corrections (13,920) and Transportation (7,423) account for nearly half of all direct government employees.

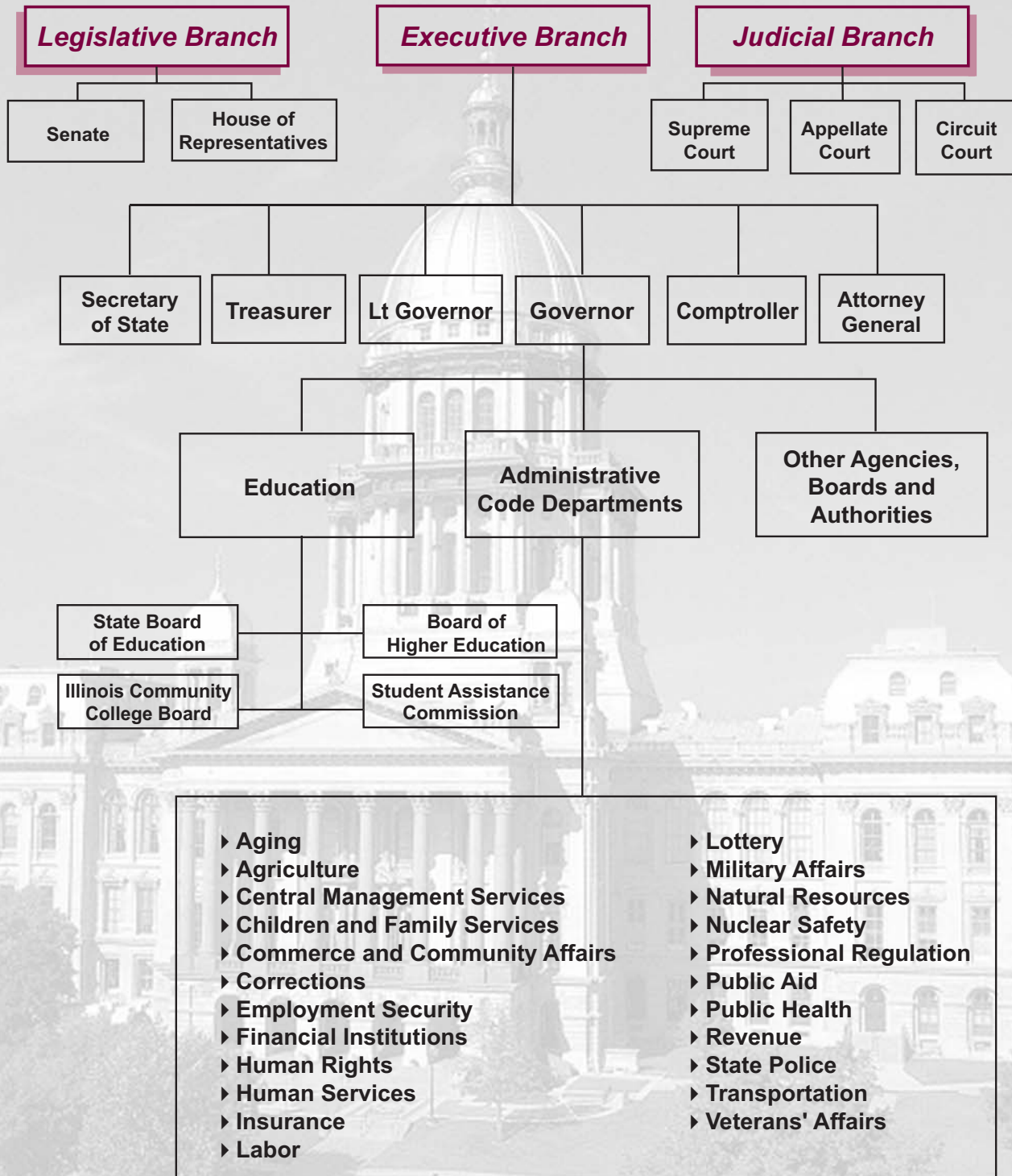
Oversight of the elementary and secondary education system in Illinois is the responsibility of the State Board of Education whose nine members are appointed by the Governor, with the consent of the Senate. The Board sets state educational policies and guidelines for schools, with local school boards administering educational services throughout 891 school districts and 3,915 schools. In fiscal year 2003, more than two million public school children were instructed by nearly 127,400 full-time, certified teachers throughout Illinois.

The 15-member Board of Higher Education plans and coordinates higher education policy for all sectors of Illinois Higher Education. Administration of Illinois' public universities and community colleges is conducted by ten boards including: the Boards of Trustees of the University of Illinois, Southern Illinois University, Chicago State University, Eastern Illinois University, Governors State University, Illinois State University, Northeastern Illinois University, Northern Illinois University, Western Illinois University, and the Community College Board. Approximately 781,000 students were enrolled in Illinois colleges and universities during the 2003 fiscal year.

In addition to education, medical assistance and highway maintenance and construction are the largest state programs. The Department of Public Aid's Division of Medical Programs administers the state's Medicaid and KidCare programs with more than 1.8 million people in Illinois covered by Medicaid health services. The Department of Transportation administers the state's highway program through nine district offices with responsibility for the state's 17,000-mile state highway system.

Total state spending for these major programs and all other operations of state government in fiscal year 2003 was \$75.4 billion or approximately \$6,081 for every person in Illinois. Total state revenues for the year were \$84.5 billion with sales taxes (\$9.6 billion), income taxes (\$9.8 billion), federal revenues (\$10.6 billion) and bond issue proceeds (\$15.2 billion) as the largest sources. The largest functions of spending included General Government (\$32.6 billion), Health and Social Services (\$15.5 billion) and Education (\$13.2 billion).

# ELECTORATE



# Economic Outlook

## Fiscal Year 2003

Fiscal year 2003 was a year of decline for the Illinois economy with lower employment and a higher unemployment rate. The Illinois unemployment rate increased from 6.0% in fiscal year 2002 to 6.5% for 2003, its highest level since 6.6% in fiscal year 1994. Illinois' non-agricultural employment (derived from survey data from Illinois companies) averaged 5.881 million workers in fiscal year 2003, a decrease of 43,000 jobs or 0.7% below 2002 employment and 164,000 jobs or 2.7% below peak employment of 6.045 million jobs in fiscal 2001. During the nine consecutive years of employment growth culminating in fiscal year 2001, Illinois added 830,000 non-agricultural jobs (a 15.9% increase).

Manufacturing continues to be the hardest hit sector of the Illinois economy. Average fiscal year 2003 employment of 744,000 jobs was down 35,000 jobs or 4.5% from fiscal year 2002 and down 163,000 jobs or 18.0% from the cyclical peak manufacturing employment of 907,000 jobs during fiscal year 1998. Foreign competition has squeezed the profits of Illinois manufacturers. Increased reliance on automation has cut costs in many cases to match the competition, but has also resulted in layoffs and plant closings that have reduced employment.

A more comprehensive measure of Illinois' economic performance is the change in state personal income adjusted for inflation which declined 0.4% for the second consecutive year in fiscal year 2003. A 1.8% increase in nominal personal income was more than offset by a 2.2% increase in the consumer price index. This was the first two-year decrease in real Illinois personal income since fiscal years 1982 and 1983. This recession followed a ten-year period where annual growth was at least 1.2%.

The Illinois labor market did show signs of improvement during the fiscal year as the average Illinois unemployment rate declined from 6.7% to 6.4% between its first and second halves. Average employment (from the household survey used to estimate the unemployment rate) increased from 5.941 million to 5.982 million, while the average number of unemployed decreased from 424,000 to 408,000.

### Fiscal Year 2004 and Beyond

With the economic recovery beginning in fiscal year 2004, an improved Illinois economy is expected with an upturn in the demand for business equipment as higher profits encourage companies to expand their investment budgets and the reduced value of the dollar eases pressure from foreign competitors. Illinois is a major participant in the international economy with exports valued at \$25.7 billion in calendar 2002 ranking 7th highest among the states. The Illinois economy's close interconnection with the World economy offers both great risks and great opportunities. Having to compete with regions with significantly lower input costs, particularly for labor, puts Illinois at a distinct competitive disadvantage. This can be offset by maintaining superior transportation and communication infrastructures, providing educational and training opportunities to support a skilled and adaptable labor force, and fostering businesses that create and transfer new technologies into the workplace.

The Illinois economy contains strengths in each of these areas. Chicago is the transportation hub of the United States and is home to O'Hare Airport which was again ranked as the "World's Busiest Airport" in 2002. Efforts to improve the infrastructure include plans for airport expansion and alleviating the congestion affecting rail traffic flows through Chicago. Through expanding private networks and the state initiatives such as the Illinois Century Network which links educational institutions throughout the state, Illinois is creating an environment where high quality information links are universally available for educational, job training, commercial, and industrial purposes.

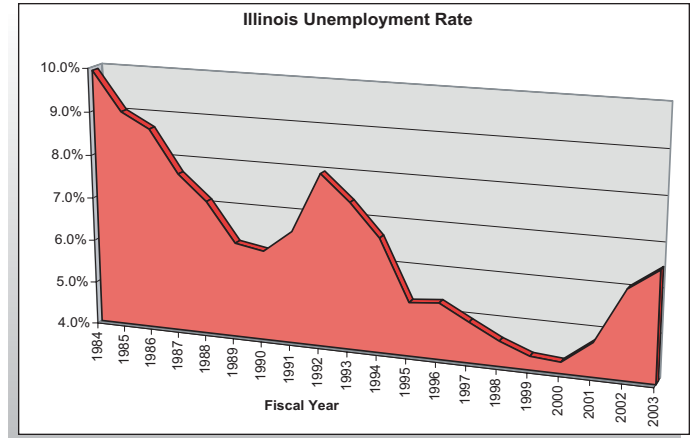
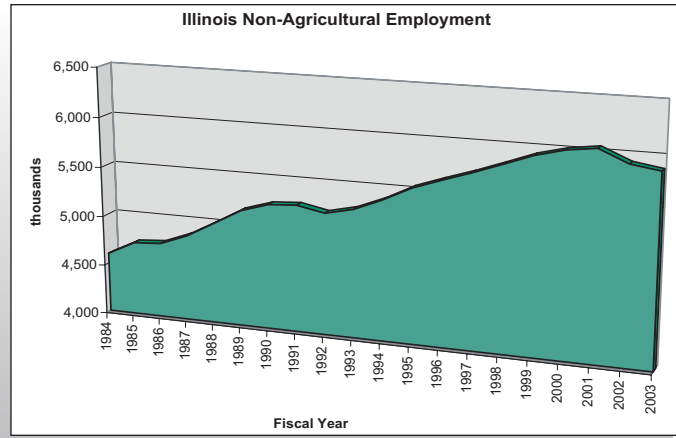
Illinois' educational resources include private universities such as the University of Chicago and Northwestern University as well as the twelve campus public system. In fiscal year 2003, Illinois private institutions served 227,000 students with another 200,000 served by the public universities. A statewide system of community colleges (354,000 students) and other training resources provide many additional educational opportunities.

Illinois can take advantage of its role as an important scientific research center. The state is a leader in the production of farm and construction machinery and health care products. Illinois is home to major government research laboratories, such as the Argonne National Laboratory and the Fermi National Accelerator Lab, major corporate labs in electronics, mechanical engineering and the biosciences, major academic research centers such as the National Center for Supercomputing Applications at the University of Illinois, and venture capital firms specializing in identifying and financing promising innovations from these labs.

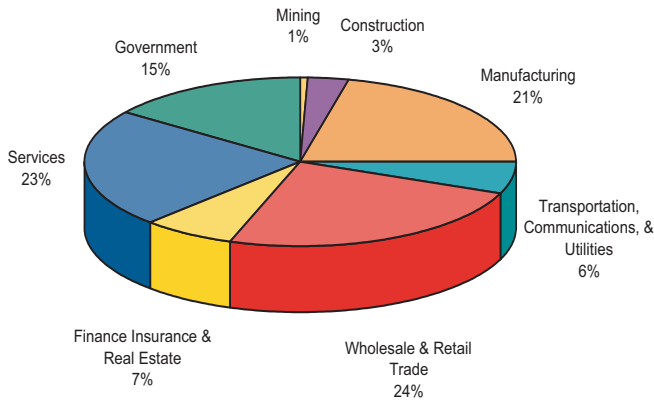
Illinois is the logical regional headquarters for companies doing business in the Midwest. Illinois is a premier center for meetings and conventions and has an extensive network of financial institutions with an emphasis on futures and derivatives reflecting Illinois' agricultural background, law and advertising resources. Illinois is home to 35 of the Fortune 500 companies, ranking 4th among the states.

The key Illinois farm sector (Illinois farmers had cash receipts from farm marketings of \$7.5 billion in 2002 with exports, largely corn and soybeans, of \$3.3 billion) enters 2004 with soybeans and corn following divergent trends over the past year. The record U.S. corn crop has served to limit price increases. In contrast, lower soybean production has boosted bean prices. For each crop, an improved exchange rate and an international economic recovery, particularly in Asia, is likely to lead to an increase in the value of farm exports. The growing Illinois ethanol industry promises to expand the market for Illinois corn, while reducing the need for imported oil. Illinois' immense coal reserves provide another potential energy source with almost 33 million tons mined accounting for almost \$1 billion in revenues in 2002 largely to serve electric generating plants. Illinois sponsors the largest coal research and development program in the U.S. with a goal of developing clean and efficient technologies than allow an expanded use of Illinois coal.

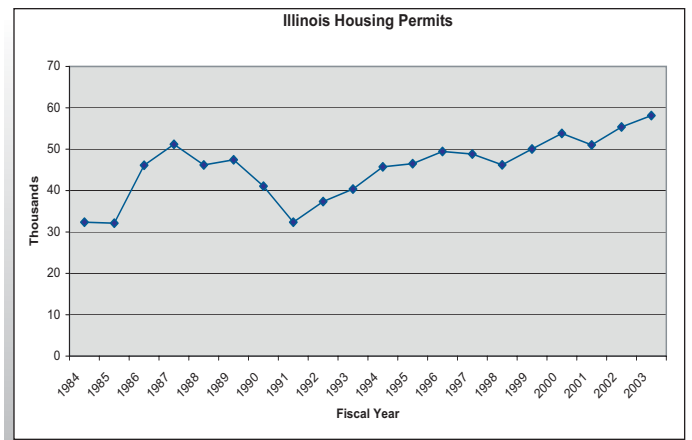
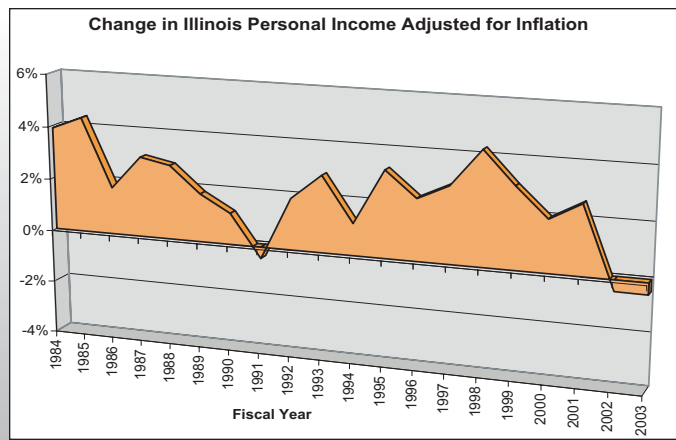
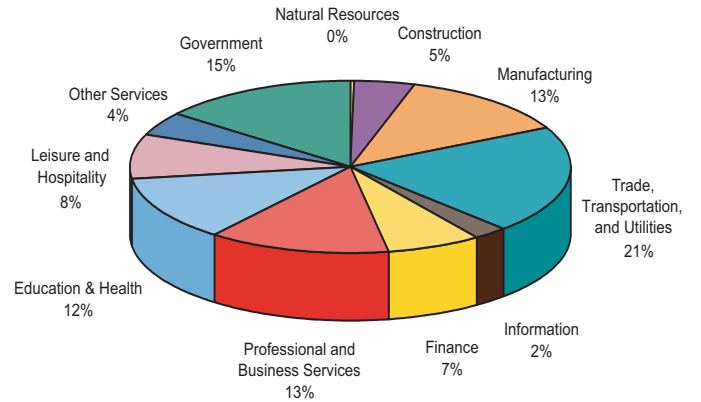
# Year-End Economic Summary



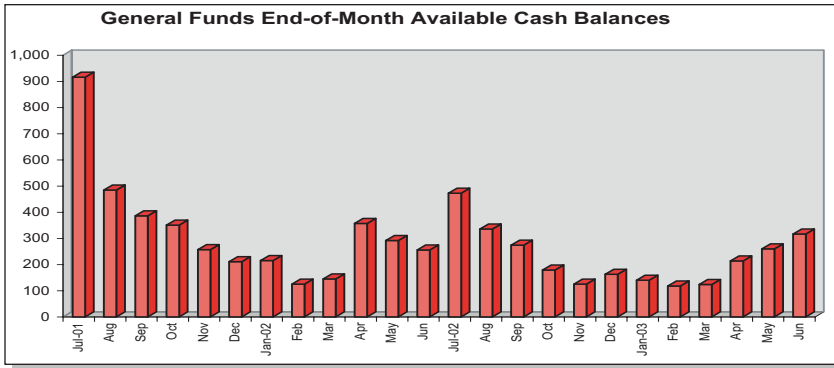
Illinois Employment by Industry  
Fiscal Year 1984



Illinois Employment by Industry  
Fiscal Year 2003



# Year-End Fiscal Summary



**Taxes Receivable**

(in millions)	6/30/02	6/30/03	Change
Gross Balance	\$2,435	\$2,289	(\$146)
Uncollectibles	\$836	\$772	(\$64)

**Major Unfunded and Long Term Liabilities**

(in millions)	FY 2002	FY 2003
Net Pension Obligation	\$ 14,633	\$ 16,001
General Obligation Bonds	\$ 8,405	\$ 19,600
Build Illinois and Civic Center Bonds	\$ 2,003	\$ 2,091

**G.O. Bond Rating**

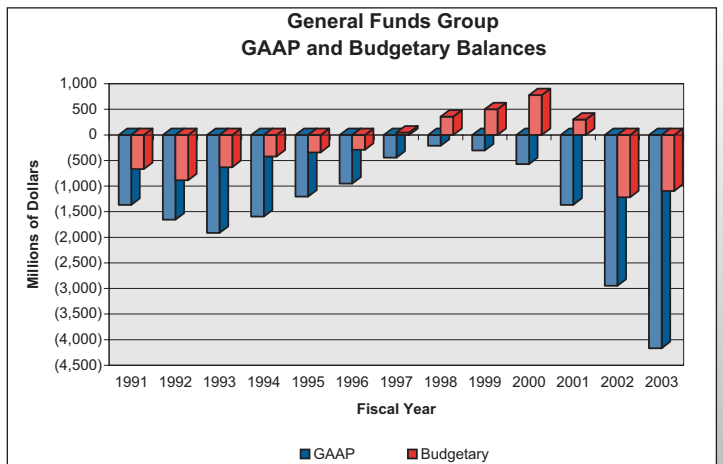
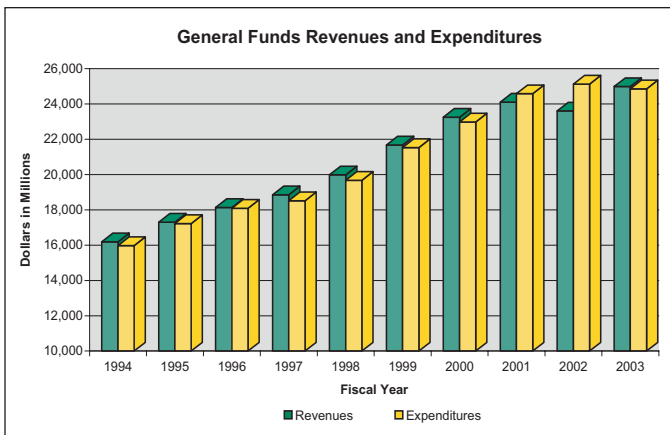
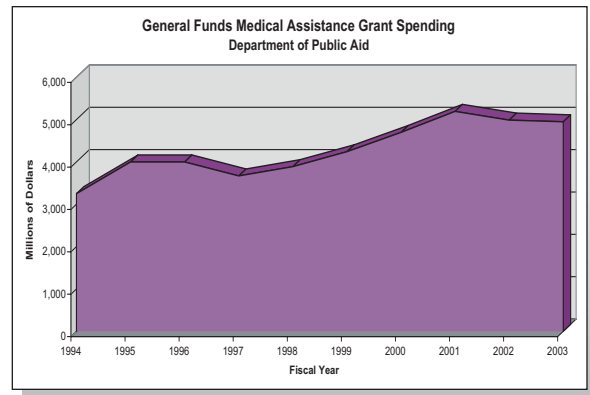
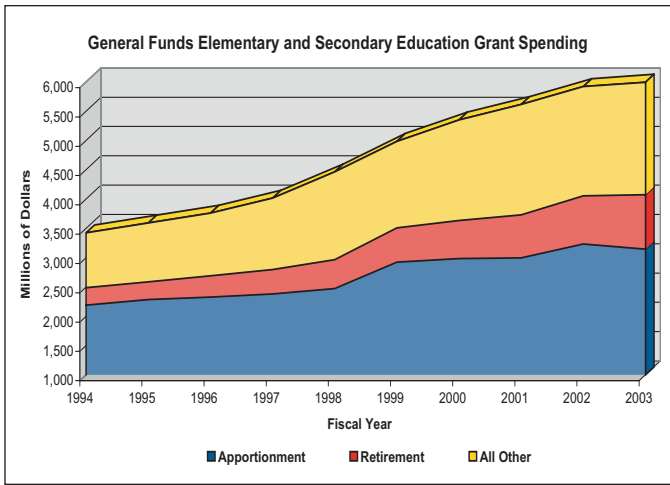
Moody's	Aa3
S&P	AA

**Section 25 Liabilities**

(in millions)	6/30/02	6/30/03	Change
Liabilities	\$1,436	\$1,849	\$413

**General Funds Fiscal Activity**

(in millions)	FY 2002	FY 2003	Change
Beginning Balance	\$ 1,126	\$ 256	(\$ 870)
Revenues	\$ 23,605	\$ 24,987	\$ 1,382
Expenditures	\$ 24,475	\$ 24,926	\$ 451
Ending Balance	\$ 256	\$ 317	\$ 61
Lapse Period Warrants	\$ 1,476	\$ 1,411	(\$ 65)
Budgetary Balance	\$ (1,220)	\$ (1,094)	\$ 126



# GAAP BASIS

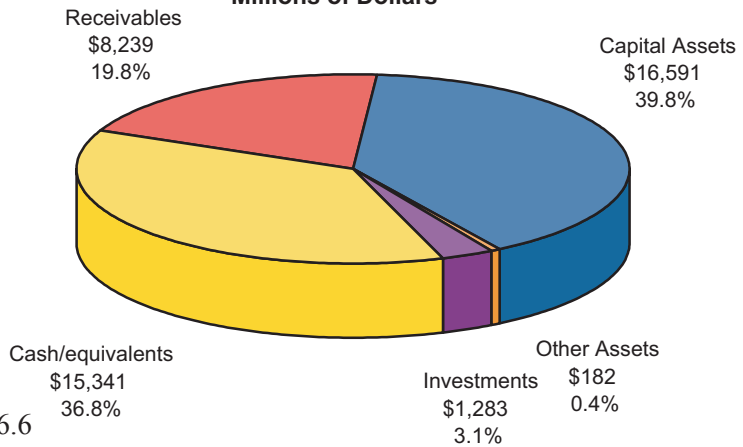
## GAAP Basis Financial Information Summary

The following information has been condensed from the statements included in the State of Illinois *Comprehensive Annual Financial Report* utilizing the total column of the primary government.

### ASSETS

Total assets of the State of Illinois at June 30, 2003, were approximately \$41.6 billion, an increase of \$10.5 billion from June 30, 2002. The main reason for the increase was \$10.0 billion in proceeds from pension obligation bonds issued in June 2003 which were yet to be disbursed at June 30, 2003. Capital assets of the state consist of \$16.6 billion (40%) of the state's assets.

**Total Assets (Primary Government)**  
June 30, 2003  
Millions of Dollars



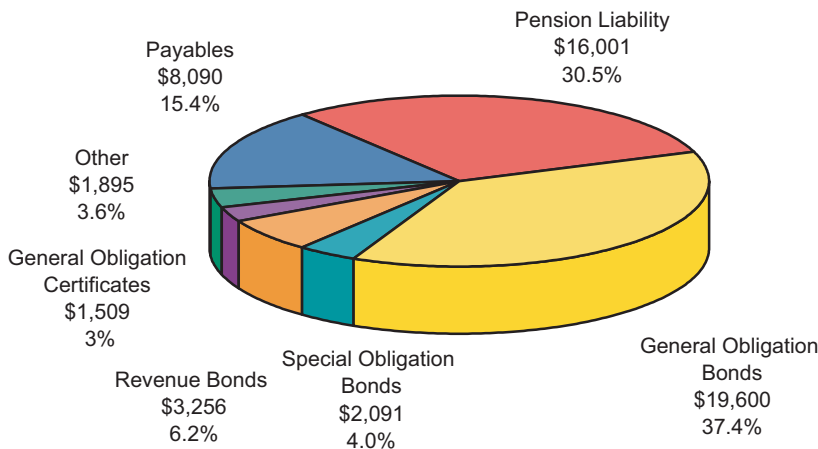
### LIABILITIES

Total liabilities of the state were approximately \$52.4 billion at June 30, 2003, an increase of \$15.4 billion

from June 30, 2002. The state's largest liability balances are the pension liability of \$16.0 billion and the general and special obligation debt liability of \$21.7 billion.

### Pension Liability (APC)

**Total Liabilities (Primary Government)**  
June 30, 2003  
Millions of Dollars

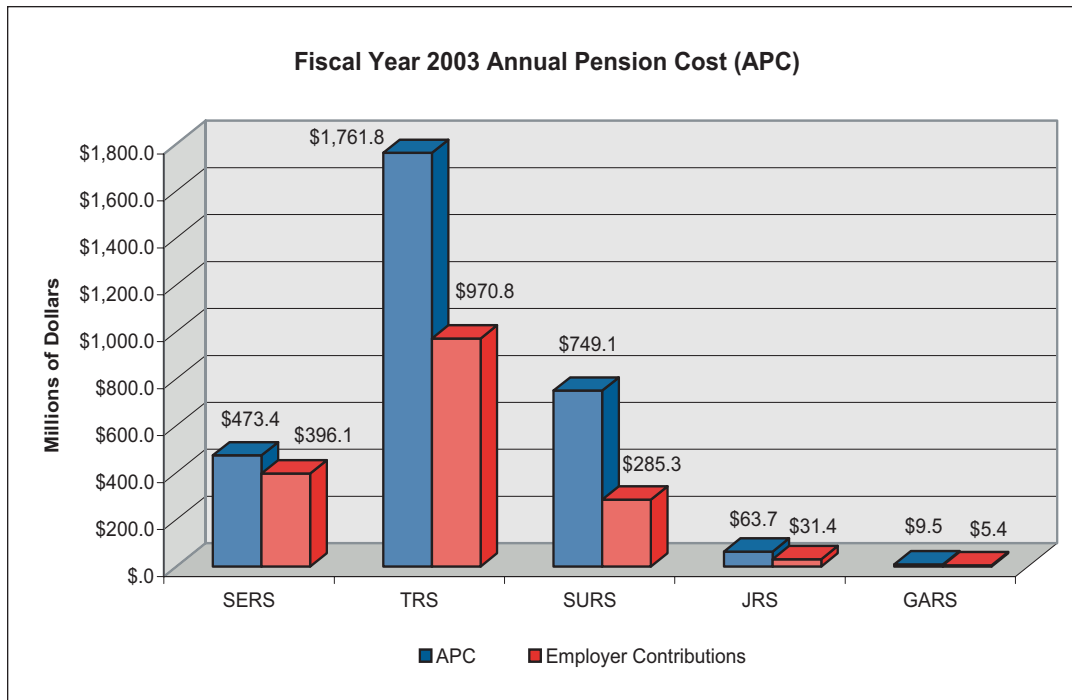


The liability at June 30, 2003, for the state's five pension trust funds was over \$16.0 billion, an increase of approximately \$1.4 billion from June 30, 2002. The pension liability compares the annual pension costs (APC) to the employer contributions received as can be seen in the bar chart on page 7.

### Funding Policy and Annual Pension Cost

Member contributions are based on fixed percentages set by statute ranging from 4.0% to 11.5%. The state's funding requirements have been established by statute (Public Act 88-593) effective July 1, 1995, and provide for a systematic 50-year funding plan

# Liabilities

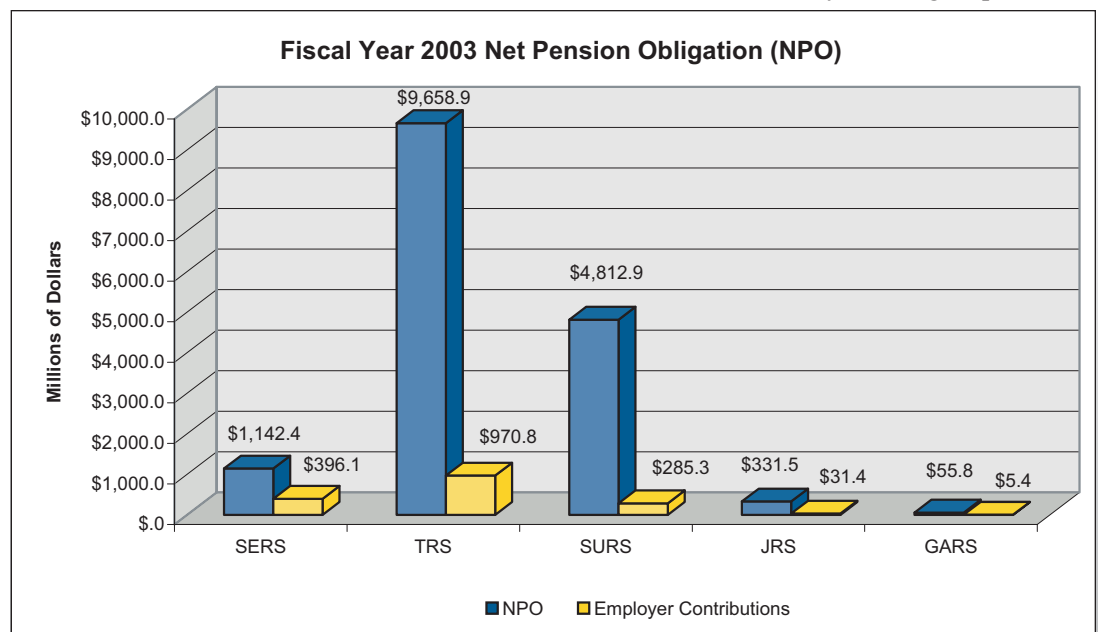


tions. The current statutory law includes a “continuing appropriation” which means that the state must automatically provide funding to the pension systems based on actuarial cost requirements and amortization of the unfunded liability without being subject to the General Assembly’s appropriation

with an ultimate goal to achieve “90% funding” of the systems’ liabilities. In addition, the funding plan provides for a 15-year phase-in period to allow the state to adapt to the increased financial commitment.

process. In addition, contributions to the Teachers’ Health Insurance Security Fund can reduce required contributions to the Teachers’ Retirement System for school districts. This statutory funding requirement

Once the 15-year phase-in period is complete, the state’s contribution will then remain at a level percentage of payroll for the next 35 years until the 90% funding level is achieved. As illustrated in the chart above, the state met its funding requirement established by statutory law for the fiscal year ended June 30, 2003.

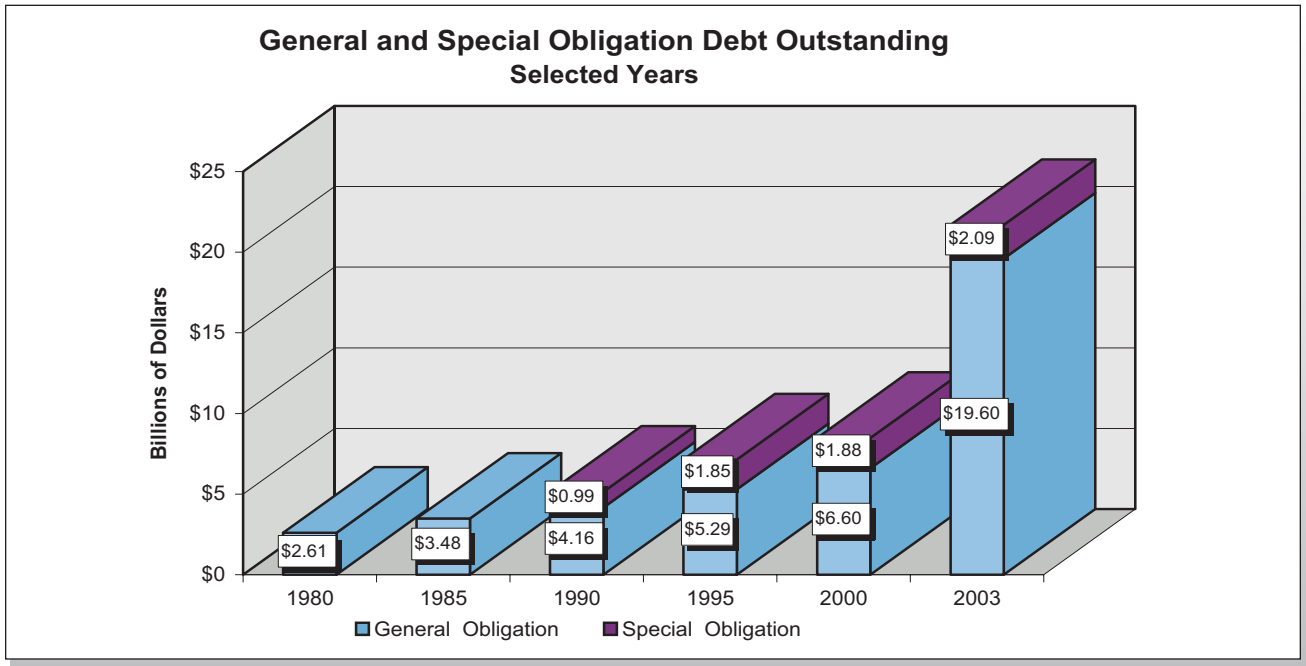


Actual contributions varied slightly from contributions required by statute mainly because of differences between estimated and actual federal contribu-

tions. The state’s APC for the current year and related information for each plan are included in the chart.

# Bonds/Debt

GAAP BASIS

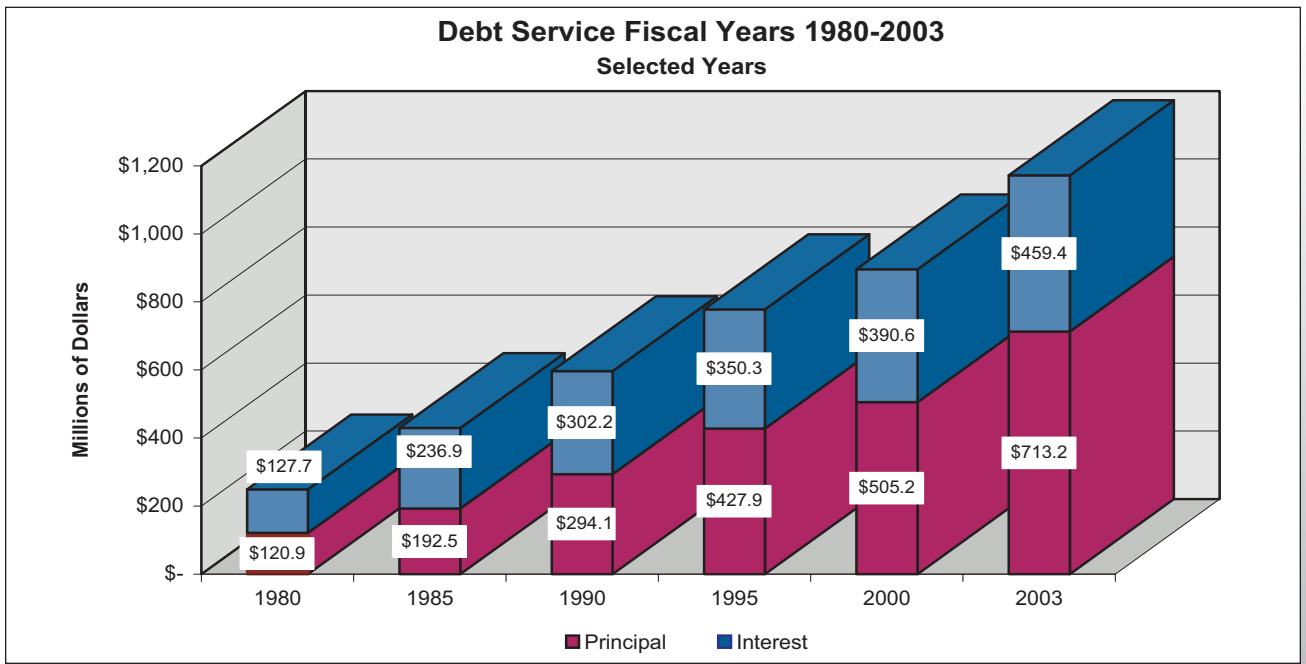


## General and Special Obligation Bonds

General and special obligation bonds, excluding refunding bonds, aggregating \$11.7 billion and \$182.2 million, respectively, were issued during fiscal year 2003 at average interest rates ranging from 2.5% to 5.375%.

## Debt Administration

The state's general obligation bond ratings are as follows: Moody's Investors Service-"Aa3", Standard & Poor's Corporation (S & P)-"AA", and Fitch Ratings-"AA". Special obligation bond ratings for Build Illinois Bonds were the same as general obliga-





# Governmental Activity Revenues

tion bond ratings for Moody’s Investors Service and Fitch Ratings while S & P rated special obligation Build Illinois bonds as “AAA” and Moody’s Investors Service rated special obligation Civic Center bonds as “A1”.

## Debt Service

Debt service principal and interest costs of \$713.2 million and \$459.4 million, respectively, were paid in fiscal year 2003 for general and special obligation bonds. The dramatic increase since fiscal year 1980 is displayed in the chart on page 8.

## NET ASSETS

Net assets for the state were (\$10.8) billion at June 30, 2003. The state has \$11.6 billion of net assets invested in capital assets (net of related debt), \$3.8 billion of restricted net assets, and (\$26.2) billion of unrestricted net assets.

## GOVERNMENTAL FUND REVENUES

The governmental activities of the state are presented in the governmental fund types (the general, special revenue, capital projects, debt service, and permanent funds) on the modified accrual basis of accounting.\*

Revenues on the modified accrual basis are recognized when they are both measurable and available to finance current operations. Revenues from various sources for fiscal year 2003 for governmental funds are as follows.

Fiscal year 2003 governmental funds revenues increased by \$1.3 billion (3%) over fiscal year 2002 revenues. State-imposed taxes including income, sales, motor fuel, public utility, and miscellaneous other taxes remained the largest overall revenue source for fiscal year 2003, increasing \$167 million (1%), and comprised nearly 59% of total state revenues.

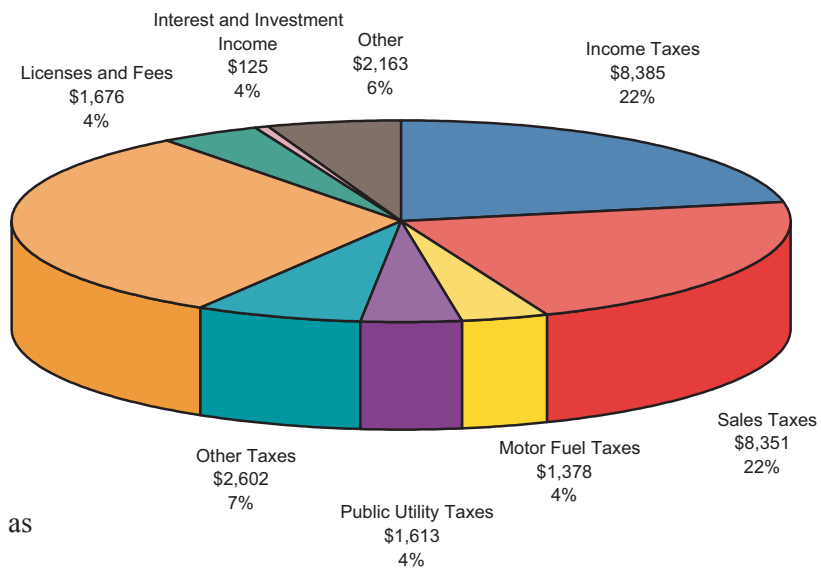
## Income Taxes

Income tax revenues for fiscal year 2003 were \$8.4 billion which is a \$259 million (3%) decrease from fiscal year 2002 income tax revenues of \$8.6 billion. The decrease is generally the result of a continuing sluggish economy.

## Sales Taxes

Sales taxes remained the second largest tax revenue source for fiscal year 2003 increasing \$44 million from fiscal year 2002.

**Fiscal Year 2003 Governmental Fund Revenues**  
Millions of Dollars



\* Note: The Comptroller’s Office publishes a number of reports, including sections of this *Executive Summary*, that summarize the status of General Fund revenues and expenditures on a cash basis. These reports are available on the web site at [www.ioc.state.il.us](http://www.ioc.state.il.us) or by request.

# Governmental Activity Expenditures

## Federal Government Revenues

Federal government revenues increased \$801 million from \$11.1 billion in fiscal year 2002 to \$11.9 billion, and continued as the second largest overall revenue source for the state's governmental funds. The majority of the increase resulted from an increase of \$310 million in Medicaid reimbursements received.

## GOVERNMENTAL ACTIVITY EXPENDITURES

Expenditures for governmental activities are presented on the modified accrual basis of accounting and are generally recognized when the fund liability is incurred regardless of when payment is made except for long-term liabilities. Expenditures for long-term liabilities are recognized in the period in which the liability has matured. Governmental fund expenditures of \$43.0 billion in fiscal year 2003 increased \$1.0 billion (2%) over 2002 and were \$4.8 billion more than revenues on a GAAP basis.

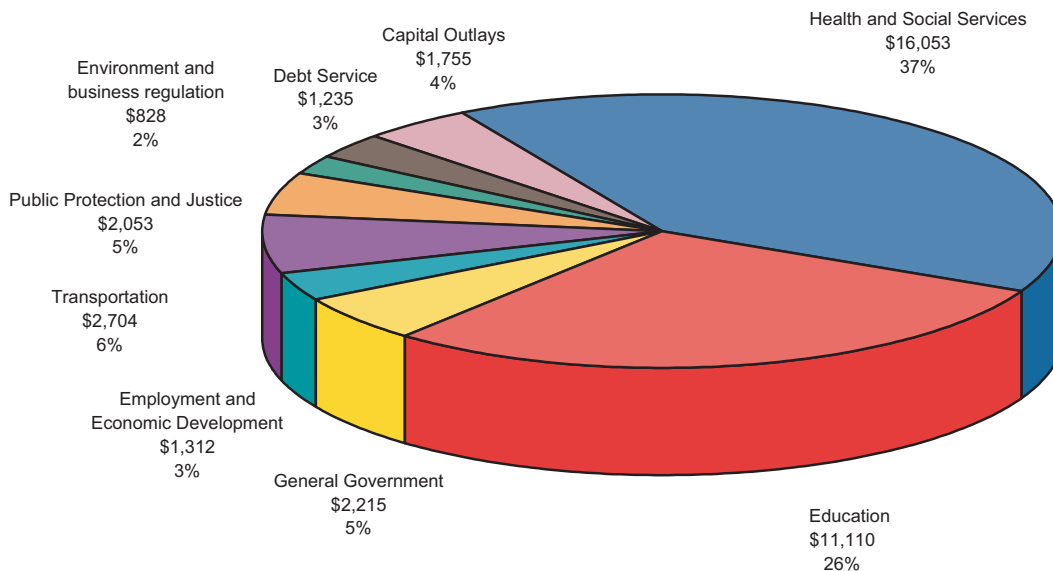
## Health and Social Services Expenditures

Health and social services expenditures of \$16.1 billion were the largest expenditure function for fiscal year 2003, increasing by \$579 million (4%) over fiscal year 2002. This expenditure function is 37% of total spending on a GAAP basis. The Department of Public Aid accounted for the majority of the increase in governmental fund spending for the state's Medicaid Program.

## Education Expenditures

Education expenditures were once again the second largest expenditure function in the governmental funds for fiscal year 2003. Education expenditures increased \$243 million (2%) from fiscal year 2002 on a GAAP basis. The majority of this increase is due to a continuing budgetary emphasis on education.

**Fiscal Year 2003 Governmental Fund Expenditures**  
Millions of Dollars



GAAP BASIS

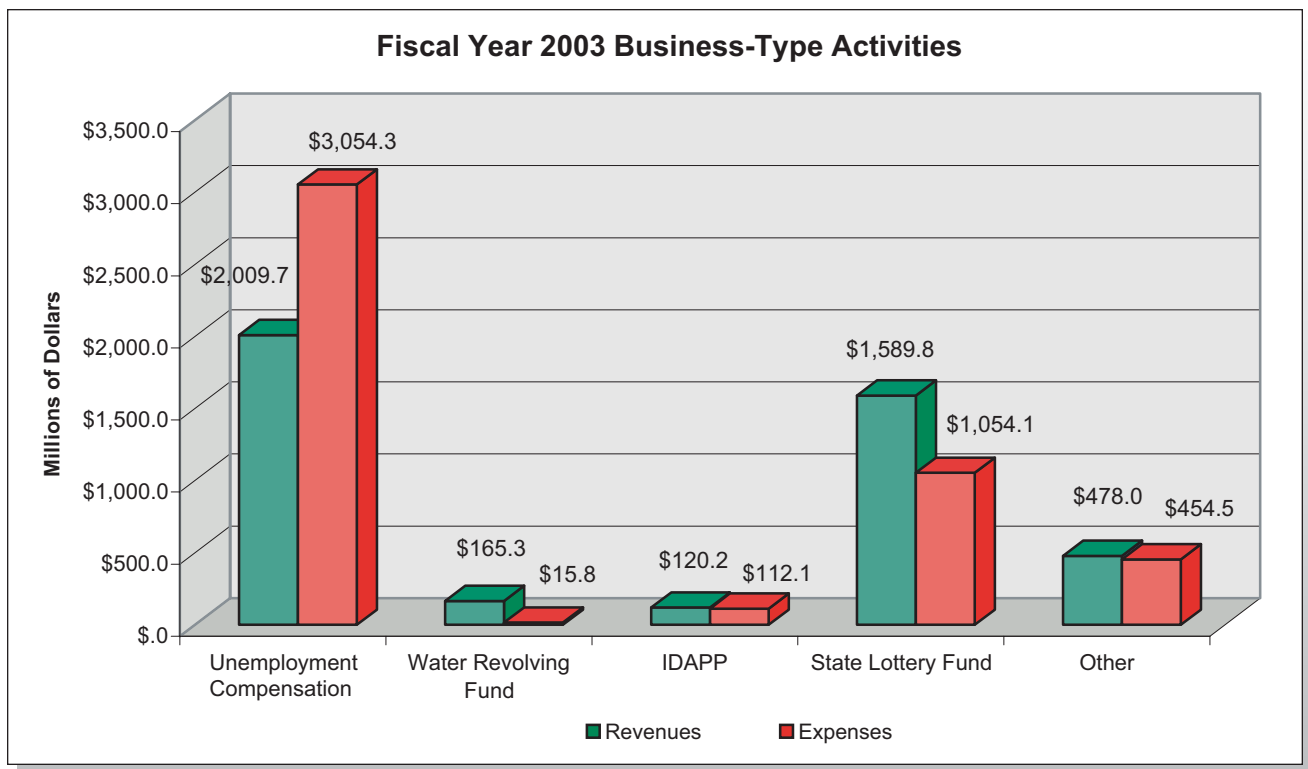
# Business-Type Activities

## BUSINESS-TYPE ACTIVITY REVENUES AND EXPENDITURES

Revenues and expenditures for the state's business-type activities are accounted for in proprietary fund types. Proprietary fund types (enterprise funds and internal service funds) are accounted for on the accrual basis. Enterprise funds are used to report activities for which a fee is charged to external users for goods or services. Internal Service funds are used to report activities that provide goods or services to other funds of the state on a cost-reimbursement basis. Revenues and expenses of internal service funds are eliminated in the Statement of Activities. The state's main business-type activities are providing unemployment insurance benefit claims, lending to local governments for drinking water and waste-

water infrastructure facilities (Water Revolving Fund), lending to full-time college students (Illinois Designated Account Purchase Program), operating the State Lottery, and administering insurance programs for other governments in the State. The revenues and expenses of each of these activities are presented in the chart below.

The large excess of expenses over revenues for unemployment business-type activities results from the increase in claims for unemployment for fiscal year 2003. Expenditures increased \$1.0 billion during fiscal year 2002. As a result, the state has received approval and is borrowing from the federal government in order to pay unemployment benefits to claimants.



# BUDGETARY BASIS

## Fiscal Summary

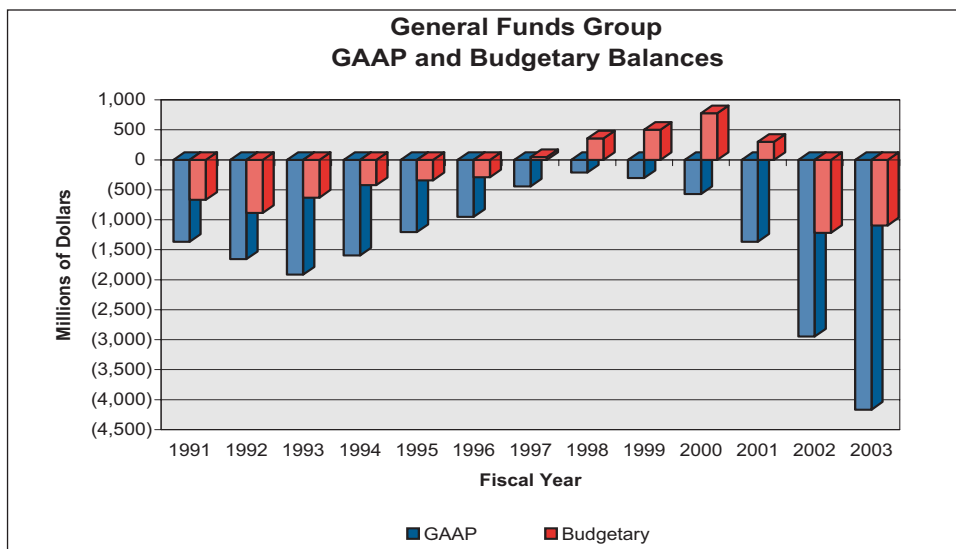
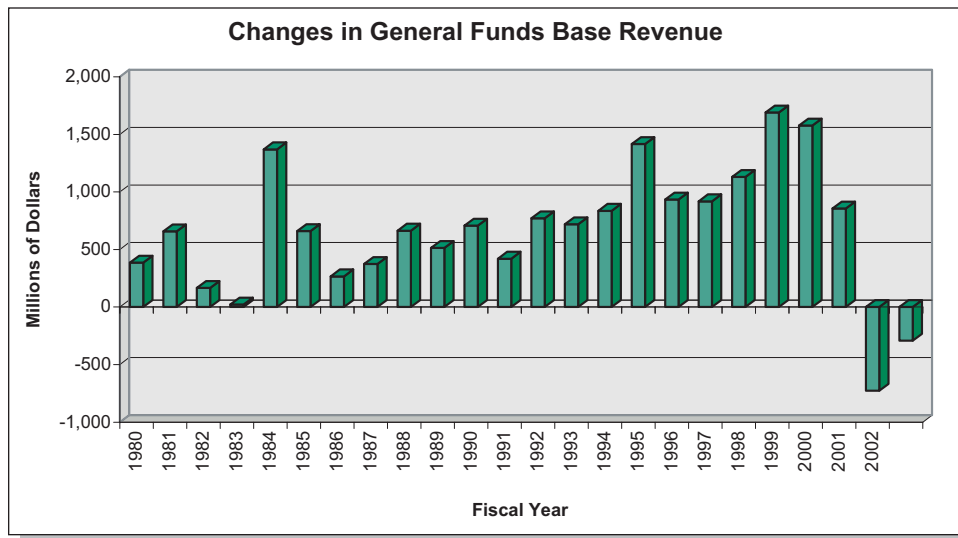
For fiscal year 2003, General Funds base revenues decreased \$293 million. This was the second consecutive year revenues decreased and the only two declines in revenue in modern history. Revenues were impacted by a sluggish economy as the state's largest sources of revenue, income and sales taxes, declined or showed minimal growth. Base expenditures declined \$974 million for the year in an effort to offset the decline in revenues.

Fiscal year 2003 resulted in a modest improvement in the General Funds budgetary balances (measured on a

cash basis). The balance increased from a \$1.220 billion *deficit* in fiscal year 2002, the largest deficit ever recorded, to a \$1.094 billion *deficit* this year.

However, the state's General Funds GAAP balance deteriorated from a \$2.948 billion deficit in fiscal year 2002, to a \$4.166 billion deficit in fiscal year 2003. The improvement in the budgetary balances is misleading and due to short-term borrowing that was not repaid at the end of the fiscal year. If the short-term debt is included, the budgetary balance would have experienced a decline comparable to the GAAP balance.

BUDGETARY BASIS



## General Funds “Base” Revenue- Down 3.0% in Fiscal Year 2003

General Funds revenue grew \$1.382 billion or 5.9% in fiscal year 2003, increasing to \$24.987 billion from \$23.605 billion in fiscal year 2002. Excluding the transfer of \$226 million from the Budget Stabilization Fund and short-term borrowing of \$1.675 billion, base revenues fell \$293 million or 1.3%. This is the second decline in revenues in modern history, following last year’s decrease of \$727 million. The sluggish economy was primarily responsible for the decline in revenues.

State sources increased \$25 million or 0.1% as cash receipts fell \$479 million and transfers in from other funds increased by \$504 million. Federal sources decreased \$318 million or 7.5%.

in the percentage allocated to the Income Tax Refund Fund.

The slowing of the economy is also reflected in retail sales for the year. Revenues from the state sales tax totaled \$6.059 billion in fiscal year 2003, an increase of \$8 million or 0.1%.

Gaming revenues grew \$64 million or 6.1% to \$1.105 billion for the year. Lottery transfers fell by \$15 million due to rollovers and a large jackpot last year. Riverboat receipts increased \$90 million in fiscal year 2003 due to a tax increase, with riverboat gambling transfers increasing \$84 million.

General Funds Revenue (Millions of Dollars)											Change From FY1994 to FY2003	
	Fiscal Year										Amount	Percent
	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003		
Personal Income Tax	\$ 4,947	\$ 5,333	\$ 5,669	\$ 6,139	\$ 6,847	\$ 7,226	\$ 7,686	\$ 7,996	\$ 7,471	\$ 7,341	\$ 2,394	48.4 %
Corporate Income Tax	755	898	978	1,085	1,136	1,121	1,237	1,036	803	738	(17)	(2.3)
Sales Taxes	4,371	4,651	4,798	4,992	5,274	5,609	6,027	5,958	6,051	6,059	1,688	38.6
Gaming Sources:												
Lottery Fund	552	588	594	590	560	540	515	501	555	540	(12)	(2.2)
Riverboat Gaming	118	171	205	185	170	240	330	460	470	554	436	369.5
Miscellaneous	12	12	12	12	11	11	9	7	16	11	(1)	(8.3)
Total, Gaming	682	771	811	787	741	791	854	968	1,041	1,105	423	62.0
Public Utility Taxes	784	743	833	873	912	1,019	1,116	1,146	1,104	1,006	222	28.3
Other Tax Sources	1,123	1,170	1,181	1,400	1,404	1,779	1,924	2,230	2,207	2,007	884	78.7
Other Transfers In	234	338	327	309	346	411	514	452	444	890	656	280.3
<b>Base State Sources</b>	<b>\$ 12,896</b>	<b>\$ 13,904</b>	<b>\$ 14,597</b>	<b>\$ 15,585</b>	<b>\$ 16,660</b>	<b>\$ 17,956</b>	<b>\$ 19,358</b>	<b>\$ 19,786</b>	<b>\$ 19,121</b>	<b>\$ 19,146</b>	<b>\$ 6,250</b>	<b>48.5 %</b>
Federal Sources	2,690	3,098	3,339	3,269	3,324	3,718	3,892	4,320	4,258	3,940	1,250	46.5
<b>Total Base Revenue</b>	<b>\$ 15,586</b>	<b>\$ 17,002</b>	<b>\$ 17,936</b>	<b>\$ 18,854</b>	<b>\$ 19,984</b>	<b>\$ 21,674</b>	<b>\$ 23,250</b>	<b>\$ 24,106</b>	<b>\$ 23,379</b>	<b>\$ 23,086</b>	<b>\$ 7,500</b>	<b>48.1 %</b>
Transfer from Budget												
Stabilization Fund	0	0	0	0	0	0	0	0	226	226	226	N/A
Short-Term Borrowing	600	300	200	0	0	0	0	0	0	1,675	1,075	179.2
<b>Total Revenue</b>	<b>\$ 16,186</b>	<b>\$ 17,302</b>	<b>\$ 18,136</b>	<b>\$ 18,854</b>	<b>\$ 19,984</b>	<b>\$ 21,674</b>	<b>\$ 23,250</b>	<b>\$ 24,106</b>	<b>\$ 23,605</b>	<b>\$ 24,987</b>	<b>\$ 8,801</b>	<b>54.4 %</b>

The decline in cash receipts was led by a \$130 million (1.7%) decrease in personal income taxes. Over the year, employment in Illinois fell by 42,900 jobs as wage and salary income declined 0.3%. In addition, the stock market experienced a decline and interest rates fell, which can result in decreased capital gains and dividend income. Obviously, these economic factors had a major impact on income and the decline in personal income tax receipts. Corporate income tax receipts decreased \$65 million or 8.1%. This occurred even though before tax corporate profits increased 9.4%. Income tax receipts were also impacted by an increase

For fiscal year 2003, public utility taxes declined 8.9% with telecommunications tax revenues \$122 million lower, revenues from the natural gas tax up \$24 million, while electric tax receipts increased less than \$1 million. Continued discounts in phone services and the use of phone cards spurred the decline in telecommunication receipts. Gas and electric are consumption-based taxes and grow only with increased usage.

Receipts from other tax sources were down \$200 million or 9.1% for the year. Investment income fell \$70 million or 51.6% because of lower investable balances

# General Funds Revenue *concluded*

and interest rates as the Federal Reserve kept interest rates low in an effort to stimulate the economy. Inheritance taxes decreased \$92 million (28.0%) as the federal estate tax is being phased out. The transfer from the Build Illinois escrow account fell \$265 million as expected. Some of the decline was offset by an increase of \$110 million from the new Cook County intergovernmental transfer agreement and insurance taxes and fees which increased (\$41 million) due to the decline in corporate profits which are allowed as a deduction. Also, per court order, \$88 million in tobacco settlement monies were deposited into the General Revenue Fund.

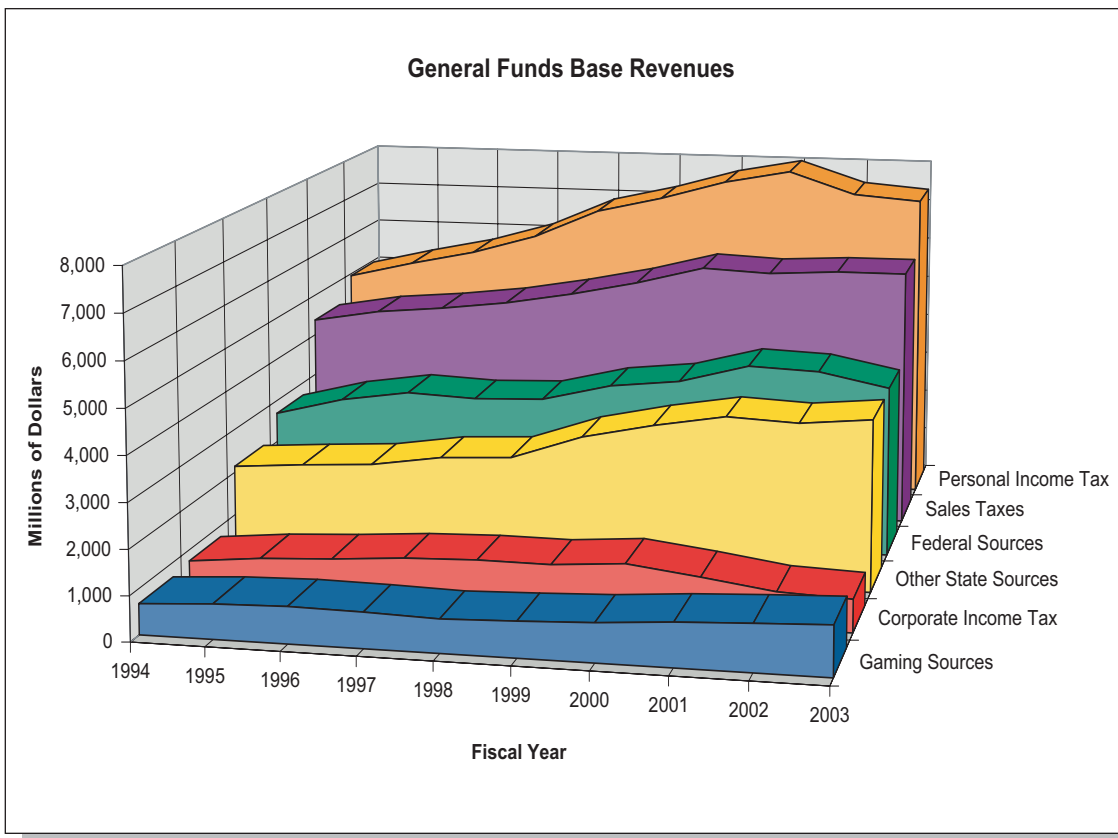
The \$446 million increase for other transfers in reflects a \$300 million transfer from the Pension Contribution Fund and \$165 million in surplus transfers from various funds. The Pension Contribution Fund received the pro-

ceeds from a \$10 billion bond issue with \$2.160 billion to be transferred to the General Revenue Fund to offset pension costs with \$300 million specified for fiscal year 2003.

Federal sources decreased \$318 million or 7.5% in fiscal year 2003. This drop was due primarily to the shifting of federally reimbursable spending from the General Funds to other funds.

For fiscal year 2003, income and sales taxes brought in 61.2% of total General Funds base revenues, while federal sources and other sources accounted for 17.1% and 21.7%, respectively. The reliance on sources driven by the economy makes the sluggish economy a major factor in determining General Funds revenue growth next year.

BUDGETARY BASIS



# General Funds “Base” Spending- Up 1.3% in Fiscal Year 2003

General Funds “base” expenditures for fiscal year 2003, excluding a \$936 million short-term borrowing repayment, totaled \$23.925 billion, a decrease of \$974 million or 3.9% from fiscal year 2002 spending. The \$974 million decrease in spending is the largest decrease ever and the first decrease since fiscal year 1983. General Funds spending had increased by an average of \$1.191 billion over the nine previous fiscal years. Among the various categories of spending, operations decreased by \$490 million, awards and grants decreased \$331 million, and regular transfers out declined \$128 million. All other spending declined \$25 million from the prior year.

For fiscal year 2003, General Funds awards and grants spending totaled \$15.400 billion, \$331 million or 2.1% below fiscal year 2002. Grants accounted for 64.4% of total base spending from the General Funds for the fiscal year, up from 63.2% in 2002.

Prior to fiscal year 1998, the largest grant spending agency had been the Department of Public Aid. However, due to reorganization in the delivery of social services, Public Aid became the second largest grant spending agency behind the State Board of Education. Due to rapidly increasing medical costs, Public Aid once again became the largest grant spending agency from the General Funds in fiscal year 2001. Public Aid’s distinction as the largest grant spending agency lasted only one year, however, as a continuing emphasis on elementary and secondary education, along with the transfer of some Medicaid programs to other funds, vaulted the State Board of Education back to the top in both fiscal years 2002 and 2003. State Board grant spending of \$5.061 billion in fiscal year 2003 is \$35 million or 0.7% lower than fiscal year 2002 and accounts for 32.9% of total General Funds grant spending. General state aid to school districts accounts for the largest portion (67.4%) of State Board grant spending with \$3.142 billion expended in 2003.

	Fiscal Year										Change from FY 1994 to FY 2003	
	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	Amount	Percent
<b>Operations:</b>												
Higher Education	\$ 1,091	\$ 1,139	\$ 1,232	\$ 1,308	\$ 1,392	\$ 1,478	\$ 1,574	\$ 1,662	\$ 1,765	\$ 1,660	\$ 569	52.2 %
Corrections	659	700	771	832	908	1,019	1,095	1,168	1,222	1,149	490	74.4
Human Services	0	0	0	0	958	1,008	1,015	1,067	1,101	998	1,015	N/A
Central Management Services	465	425	391	475	515	560	645	698	733	818	353	75.9
Children and Family Services	149	181	247	254	261	273	285	286	298	284	135	90.6
Public Aid	382	396	413	455	102	113	208	126	166	154	(228)	(59.7)
Mental Health	514	520	535	546	0	0	0	0	0	0	(514)	(100.0)
Other Operations	942	982	1,091	1,245	1,183	1,276	1,476	1,623	1,671	1,403	461	48.9
<b>Total, Operations</b>	<b>\$ 4,202</b>	<b>\$ 4,343</b>	<b>\$ 4,680</b>	<b>\$ 5,115</b>	<b>\$ 5,319</b>	<b>\$ 5,727</b>	<b>\$ 6,298</b>	<b>\$ 6,630</b>	<b>\$ 6,956</b>	<b>\$ 6,466</b>	<b>\$ 2,264</b>	<b>53.9 %</b>
<b>Awards and Grants:</b>												
State Board of Education:												
Apportionment	\$ 2,186	\$ 2,285	\$ 2,326	\$ 2,378	\$ 2,471	\$ 2,922	\$ 2,983	\$ 2,995	\$ 3,232	\$ 3,142	\$ 956	43.7 %
Other	1,230	1,302	1,133	1,283	1,562	1,477	1,716	1,885	1,864	1,919	689	56.0
<b>Total, State Board of Education</b>	<b>3,416</b>	<b>3,587</b>	<b>3,459</b>	<b>3,661</b>	<b>4,033</b>	<b>4,399</b>	<b>4,699</b>	<b>4,880</b>	<b>5,096</b>	<b>5,061</b>	<b>1,645</b>	<b>48.2</b>
Public Aid:												
Medical Assistance	3,249	3,997	3,997	3,668	3,887	4,239	4,695	5,192	4,986	4,945	1,696	52.2
Aid to Families with Dependent Children	938	963	956	878	0	0	0	0	0	0	(938)	(100.0)
Other	177	185	143	140	0	0	0	0	0	0	(177)	(100.0)
<b>Total, Public Aid</b>	<b>4,364</b>	<b>5,145</b>	<b>5,096</b>	<b>4,686</b>	<b>3,887</b>	<b>4,239</b>	<b>4,695</b>	<b>5,192</b>	<b>4,986</b>	<b>4,945</b>	<b>581</b>	<b>13.3</b>
Human Services	0	0	0	0	2,287	2,392	2,420	2,660	2,566	2,504	2,504	N/A
Higher Education	542	599	599	638	670	730	758	807	872	811	269	49.6
Teachers Retirement	5	4	299	354	429	584	649	732	821	931	926	N/A
Children and Family Services	521	598	657	689	660	616	635	634	607	540	19	3.6
Aging	109	118	123	142	159	182	202	220	227	230	121	111.0
Mental Health	418	470	791	893	0	0	0	0	0	0	(418)	(100.0)
Alcoholism and Substance Abuse	88	137	99	97	0	0	0	0	0	0	(88)	(100.0)
Other Awards and Grants	467	485	496	549	425	507	509	551	556	378	(89)	(19.1)
<b>Total, Awards and Grants</b>	<b>\$ 9,930</b>	<b>\$ 11,143</b>	<b>\$ 11,619</b>	<b>\$ 11,709</b>	<b>\$ 12,550</b>	<b>\$ 13,649</b>	<b>\$ 14,567</b>	<b>\$ 15,676</b>	<b>\$ 15,731</b>	<b>\$ 15,400</b>	<b>\$ 5,470</b>	<b>55.1 %</b>
Other General Funds Warrants Issued	12	13	11	27	35	45	82	60	53	28	16	133.3
<b>Total, General Funds Warrants Issued</b>	<b>\$ 14,144</b>	<b>\$ 15,499</b>	<b>\$ 16,310</b>	<b>\$ 16,851</b>	<b>\$ 17,904</b>	<b>\$ 19,421</b>	<b>\$ 20,947</b>	<b>\$ 22,366</b>	<b>\$ 22,740</b>	<b>\$ 21,894</b>	<b>\$ 7,750</b>	<b>54.8 %</b>
Regular Transfers Out	1,225	1,414	1,572	1,666	1,768	2,106	2,029	2,217	2,159	2,031	806	65.8
<b>Base General Funds Expenditures</b>	<b>\$ 15,369</b>	<b>\$ 16,913</b>	<b>\$ 17,882</b>	<b>\$ 18,517</b>	<b>\$ 19,672</b>	<b>\$ 21,527</b>	<b>\$ 22,976</b>	<b>\$ 24,583</b>	<b>\$ 24,899</b>	<b>\$ 23,925</b>	<b>\$ 8,556</b>	<b>55.7 %</b>
Short-Term Borrowing Repayment	609	308	205	0	0	0	0	0	226	936	327	53.7
<b>Total, General Funds Expenditures</b>	<b>\$ 15,978</b>	<b>\$ 17,221</b>	<b>\$ 18,087</b>	<b>\$ 18,517</b>	<b>\$ 19,672</b>	<b>\$ 21,527</b>	<b>\$ 22,976</b>	<b>\$ 24,583</b>	<b>\$ 25,125</b>	<b>\$ 24,861</b>	<b>\$ 8,883</b>	<b>55.6 %</b>

## General Funds “Base” Spending *concluded*

The second largest portion (32.1% in fiscal year 2003) of General Funds awards and grants expenditures were by the Department of Public Aid. Grant spending by Public Aid totaled \$4.945 billion in fiscal year 2003, \$41 million or 0.8% below 2002. All of the grant spending by the Department was for medical assistance payments as the Aid to Families with Dependent Children Program along with other grant award programs were transferred into the newly formed Department of Human Services at the beginning of fiscal year 1998.

The Department of Human Services consolidated all or parts of six state social service agencies with the goal of achieving a more efficient and effective delivery of social services in Illinois. Merged in whole into Human Services were the Departments of Mental Health, Alcoholism and Substance Abuse, and Rehabilitation Services while components of the Departments of Children and Family Services, Public Health, and Public Aid were also merged. In the sixth year of operation for the Department, grant spending totaled \$2.504 billion, \$62 million or 2.4% below 2002. Together, the State Board of Education and the Departments of Public Aid and Human Services accounted for 81.2% of all General Funds awards and grant expenditures in fiscal year 2003.

Two other sectors of government education spending garner a significant amount of General Funds grant dollars. Higher education had awards and grants spending of \$811 million in fiscal year 2003, \$61 million or 7.0% lower than fiscal year 2002. Grant spending for teachers' retirement of \$931 million in fiscal year 2003 represented an increase of \$110 million or 13.4% over the prior year. Since fiscal year 1996, when grant spending for teachers' retirement was shifted from the State Board of Education to the Teachers' Retirement systems, expenditures have increased by \$632 million or 211.4%. Altogether, education grant spending from the General Funds in fiscal year 2003 totaled \$6.803 billion and accounted for 44.2% of total General Funds grant spending.

Spending for operations from the General Funds in fiscal year 2003 totaled \$6.466 billion, \$490 million or 7.0% lower than fiscal year 2002. Operations accounted for 27.0% of total General Funds base expenditures in 2003.

Higher education institutions accounted for the largest amount of spending for operations. In fiscal year 2003, higher education operations expenditures of \$1.660 billion were \$105 million or 5.9% lower than fiscal year 2002 and accounted for 25.7% of total operations. Illinois' flagship university, the University of Illinois, accounted for \$726 million or 43.7% of higher education operations in fiscal year 2003.

The largest state agency in terms of operations expenditures from the General Funds and the second largest in terms of employee headcount is the Department of Corrections. Fiscal year 2003 expenditures by the Department for operations totaled \$1.149 billion, \$73 million or 6.0% below the previous year. The number of employees at Corrections totaled 13,920 at the end of fiscal year 2003, down 3,127 from 17,047 at the end of fiscal year 2002.

With the largest headcount of any single state agency, the Department of Human Services recorded operations expenditures of \$998 million in fiscal year 2003. At the end of the fiscal year the Department's employee headcount was 15,515, a decrease of 3,508 or 18.4% from the previous year.

Although employee salaries drive most state agency operational expenditures, this is not the case at the Department of Central Management Services (CMS). CMS is the third largest state agency in terms of operational expenditures; however, their employee headcount is not even among the top ten agencies. Fiscal year 2003 General Funds expenditures of \$818 million included \$769 million for group insurance contributions to pay for the health benefits of state employees. The \$818 million expended by CMS in fiscal year 2003 for operations was \$85 million or 11.6% higher than 2002. Group insurance contributions were up \$84 million or 12.3% while the remainder of CMS operations increased by \$1 million from 2002.

Over the last ten years, General Funds base expenditures grew \$8.556 billion or 55.7%. Of this growth, awards and grants represented 63.9% while operations accounted for 26.5% and transfers out accounted for 9.4%.



# Fiscal Climate Fiscal Year 2003

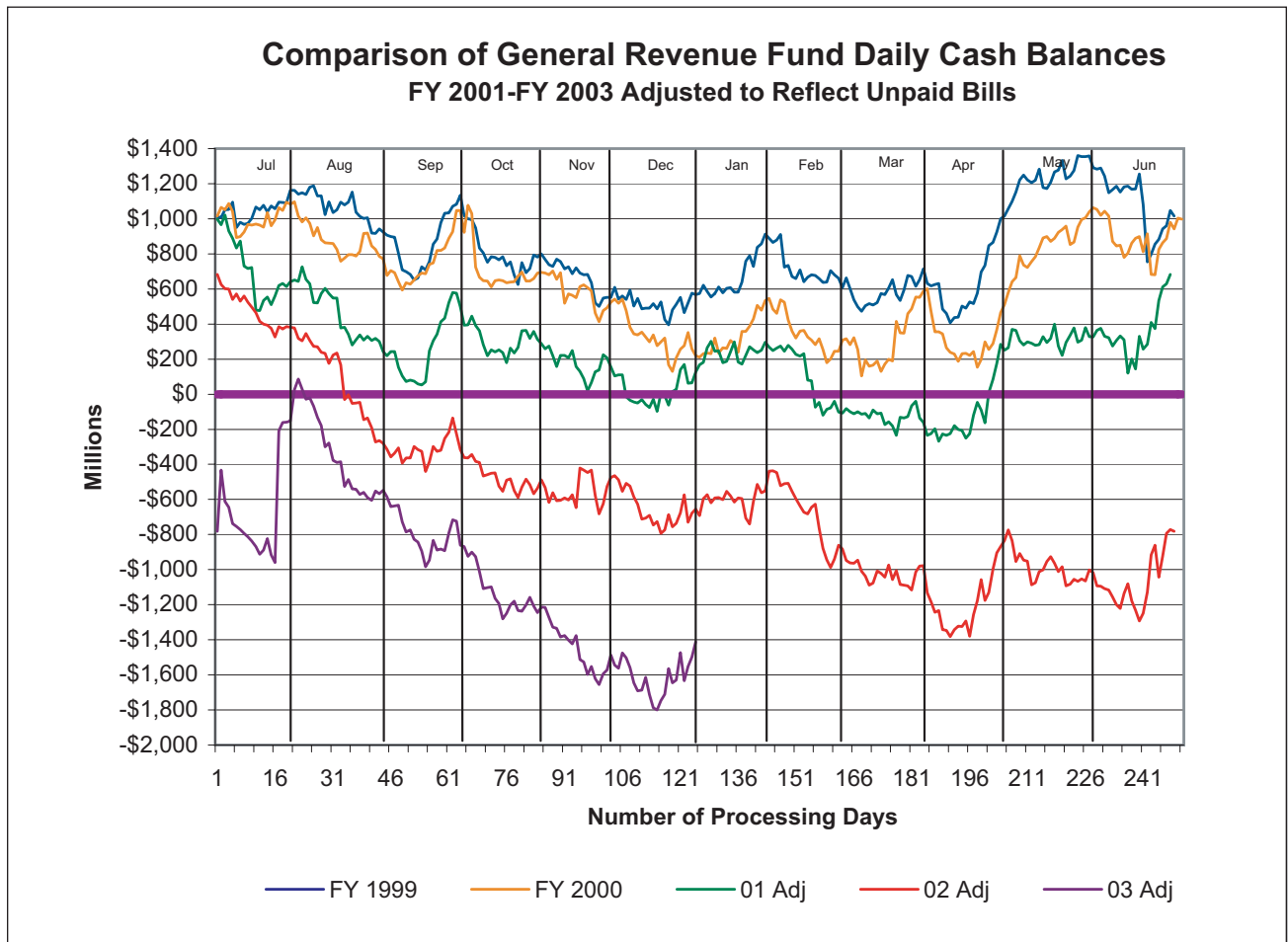
Fiscal year 2003 began on a terrible note, following what was the worst General Funds performance in history. Fiscal year 2002 set records for lowest balances, delayed payments, highest levels of unpaid bills and record deficits. As a result, a total of \$1.0 billion in short-term borrowing was entered into in July 2002. Of that amount \$700 million was dedicated to the General Revenue Fund, \$150 million to the Long-Term Care Provider Fund, and \$150 million to the Income Tax Refund Fund.

The General Revenue Fund (GRF), the state's main operating fund, began fiscal year 2003 with \$781 million in unpaid bills and payment delays of 29 business days. In July, the state used the \$700 million short-term loan and transfers of \$156 million in surplus money from other funds, as well as \$226 million from the Budget Stabilization Fund, to prop up the GRF. These revenues were used to pay the backlog of unpaid bills and by the end of July the backlog and payment delays were down to zero. By August 6<sup>th</sup>, payment delays and the backlog of unpaid bills resumed.

As the fiscal year progressed, revenues continued to be disappointing. Excluding the previously mentioned borrowing and transfers, revenues by March were below fiscal year 2002. A sluggish economy kept income and sales taxes depressed while other sources, including federal sources, declined. Efforts to reduce spending, including an early retirement program and appropriation reserves, helped to alleviate some of the pressure but it was not enough. The backlog of bills and payment delays continued to grow reaching highs of \$2.3 billion and 52 days on May 21.

The state utilized another short-term loan of \$1.5 billion in May 2003, with \$975 million deposited into the GRF, \$475 million into the Income Tax Refund Fund and \$50 million into the Long-Term Care Provider Fund. Backlogs and payment delays were greatly reduced with the infusion of borrowing.

In May the state issued \$10.0 billion in General Obligation Bonds to fund the pension systems. Of this



BUDGETARY BASIS

# Fiscal Climate *continued*

total, \$300 million was transferred to the GRF and \$1.860 billion was to be transferred as retirement payments were made in the following fiscal year.

By the end of the year, the General Funds had experienced another dismal performance in revenues. Base revenues were down for the second year in a row with a decrease of \$293 million or 1.3%. However, base spending declined for the first time since fiscal year 1983 decreasing \$974 million or 3.9%. On June 30<sup>th</sup> the backlog of unpaid bills was \$874 million. While this figure is higher than last year's, lapse period spending was reduced from \$1.476 billion to \$1.410 billion.

Therefore, the fiscal year 2003 General Funds ending budgetary balance, a negative \$1.094 billion, showed a modest but misleading improvement of \$126 million over fiscal year 2002. The short-term loan in May 2003 allowed for payment of current year obligations but

deferred re-payment of the loan to fiscal year 2004. Adjusting for the \$975 million in borrowing would result in a negative budgetary balance of \$2.069 billion. If the General Funds obligation of paying the Refund Fund borrowing portion is included, the state's budgetary balance would have deteriorated by \$1.324 billion.

## A Look at Fiscal Year 2004

The General Funds began fiscal year 2004 not only with a record backlog of unpaid bills and the second largest lapse period spending, but also \$1.45 billion in short-term debt. To fill this budget hole, deficit reduction initiatives totaling over \$3.5 billion were proposed including the previously mentioned pension bond transfers. However, most of the deficit reduction sources are one-time revenues or transfers. Estimated transfers include \$1.6 billion from pension bonds and \$144 million in surplus fund transfers. One-time revenue sources

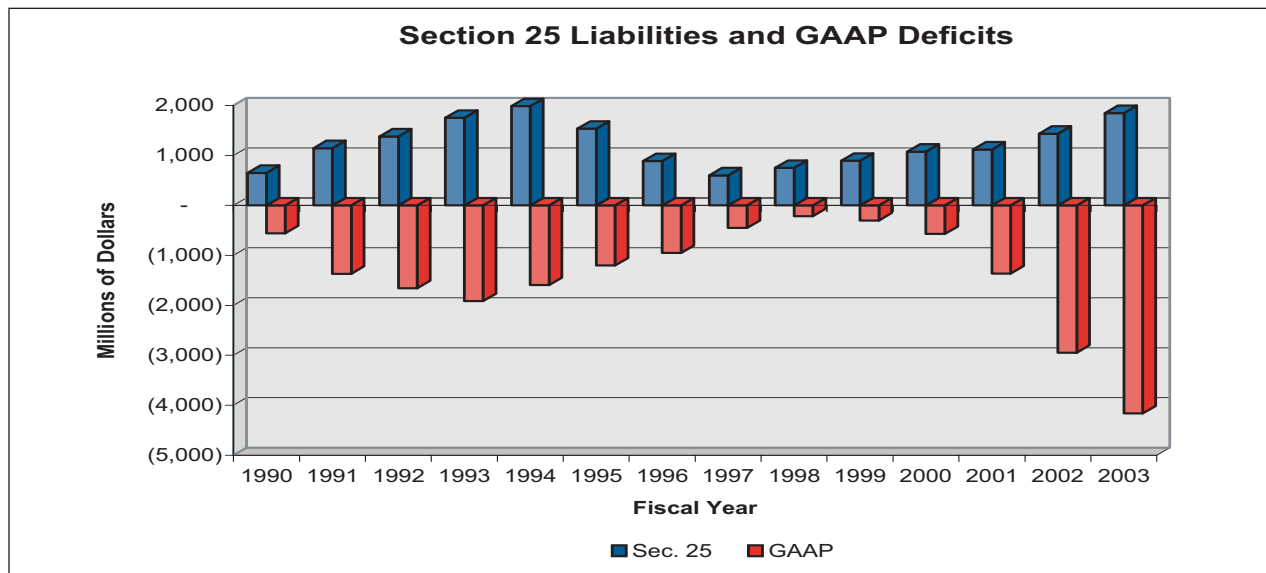
include approximately \$350 million from sale of a riverboat license, \$233 million from sale/leaseback of state assets, \$125 million from an environmental fund transfer, and monies from a tax amnesty program. Recurring revenue increases were from various license and fee increases (over \$400 million), closing tax loopholes (\$152 million), and administrative charges to other funds (\$422 million).

Early in the fiscal year, the state received \$422 million in grants and increased Medicaid reimbursements from the federal Jobs and Growth Tax Relief Reconciliation Act. Increased federal sources and pension

**General Funds GAAP Balance and  
Cash-Basis Budgetary Balance  
(Millions of Dollars)**

Fiscal Year	General Funds				General Revenue Fund	
	GAAP Balance	Change	Budgetary Balance	Change	Budgetary Balance	Change
1986	(261)		(153)		(185)	
1987	(587)	(326)	(319)	(166)	(360)	(175)
1988	(355)	232	(76)	243	(143)	217
1989	(74)	281	148	224	7	150
1990	(557)	(483)	(191)	(339)	(242)	(249)
1991	(1,368)	(811)	(666)	(475)	(702)	(460)
1992	(1,656)	(288)	(887)	(221)	(828)	(126)
1993	(1,916)	(260)	(630)	257	(607)	221
1994	(1,595)	321	(422)	208	(447)	160
1995	(1,204)	391	(341)	81	(354)	93
1996	(952)	252	(292)	49	(299)	55
1997	(443)	509	45	337	106	405
1998	(213)	230	356	311	281	175
1999	(303)	(90)	503	147	184	(97)
2000	(572)	(269)	777	274	278	94
2001	(1,365)	(793)	300	(477)	(124)	(402)
2002 *	(2,948)	(1,583)	(1,220)	(1,520)	(1,470)	(1,346)
2003	(4,166)	(1,218)	(1,094)	126	(1,409)	61

\* GAAP balance as restated.



bond transfers led to a dramatic growth in revenues. However, backlogs of unpaid bills have continued throughout the year. It is hoped that many of the deficit reduction sources will generate the necessary revenues to reduce the backlog later in the year.

Section 25 of the State Finance Act provides the timeline for paying the state's liabilities and for allowing the deferral of certain payments, primarily Medicaid, to the next fiscal year. While Section 25 liabilities increased in fiscal year 2003 by \$413 million and totaled \$1.849 billion, it is the current pace of Medicaid spending that will present a problem this year. By the end of November, the Department of Public Aid had spent \$3.078 billion on medical assistance or 56.8% of the year's total appropriation. If other funds do not pick up these expenditures, Section 25 liabilities could increase dramatically.

The growth of Section 25 liabilities is troublesome because of the relationship between changes in those deferrals and changes in the General Funds GAAP financial position. Through the 1990's, the increase in the GAAP deficit closely

matched the growth in Section 25 deferrals. Most of Section 25 liabilities are for Medicaid, so the current pace of spending is worrisome.

So far the economy remains sluggish and the revenue growth anticipated from income and sales taxes may not materialize. Also, some of the deficit reduction sources may not generate the revenues anticipated. However, it is the unexpected federal revenues and tax amnesty revenues that should help alleviate many of the problems this year. Nevertheless, it is these sources and the one-time nature of many of the other sources that could create problems next year.

