

# CENTER FOR TAX AND BUDGET ACCOUNTABILITY

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## *The Illinois Funding Crisis*

Prepared For:  
Wednesday, August 26, 2009; 1:00 pm  
Pension System Modernization Task Force

Presented by:  
**Ralph Martire**  
Executive Director

# ILLINOIS' ECONOMY IS LARGE

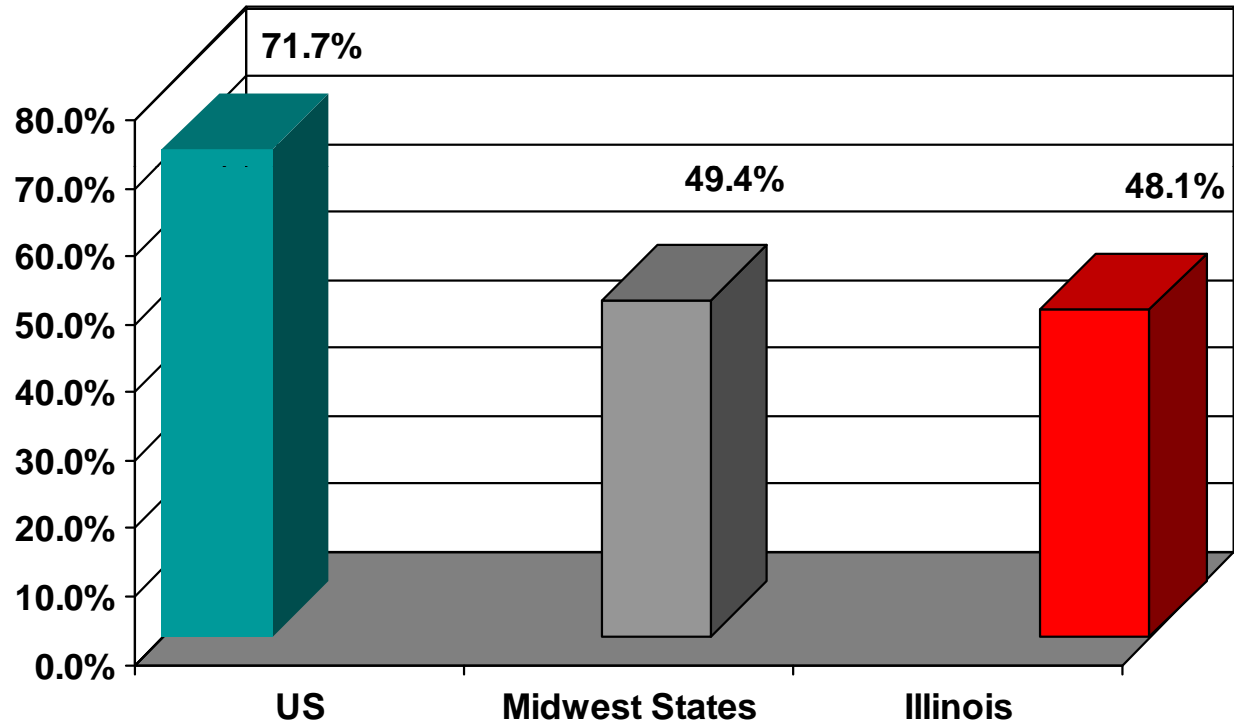


## The Context: **BIG 'N RICH**

- In 2008, Illinois ranked fifth nationally with a Gross State Product in excess of \$633 billion (BEA).
- That would be the 27<sup>th</sup> largest economy of any nation in the world-greater than Egypt, Saudi Arabia, Colombia, Belgium, Sweden, Greece, Ireland, Portugal, Norway and Nigeria, to name a few.<sup>2</sup>

# Illinois GDP Growth Lags

But, IL Gross State Product Grew Less than U.S. or Midwest States, 1990-2007



Source: Bureau of Economic Analysis, US Dept. of Commerce

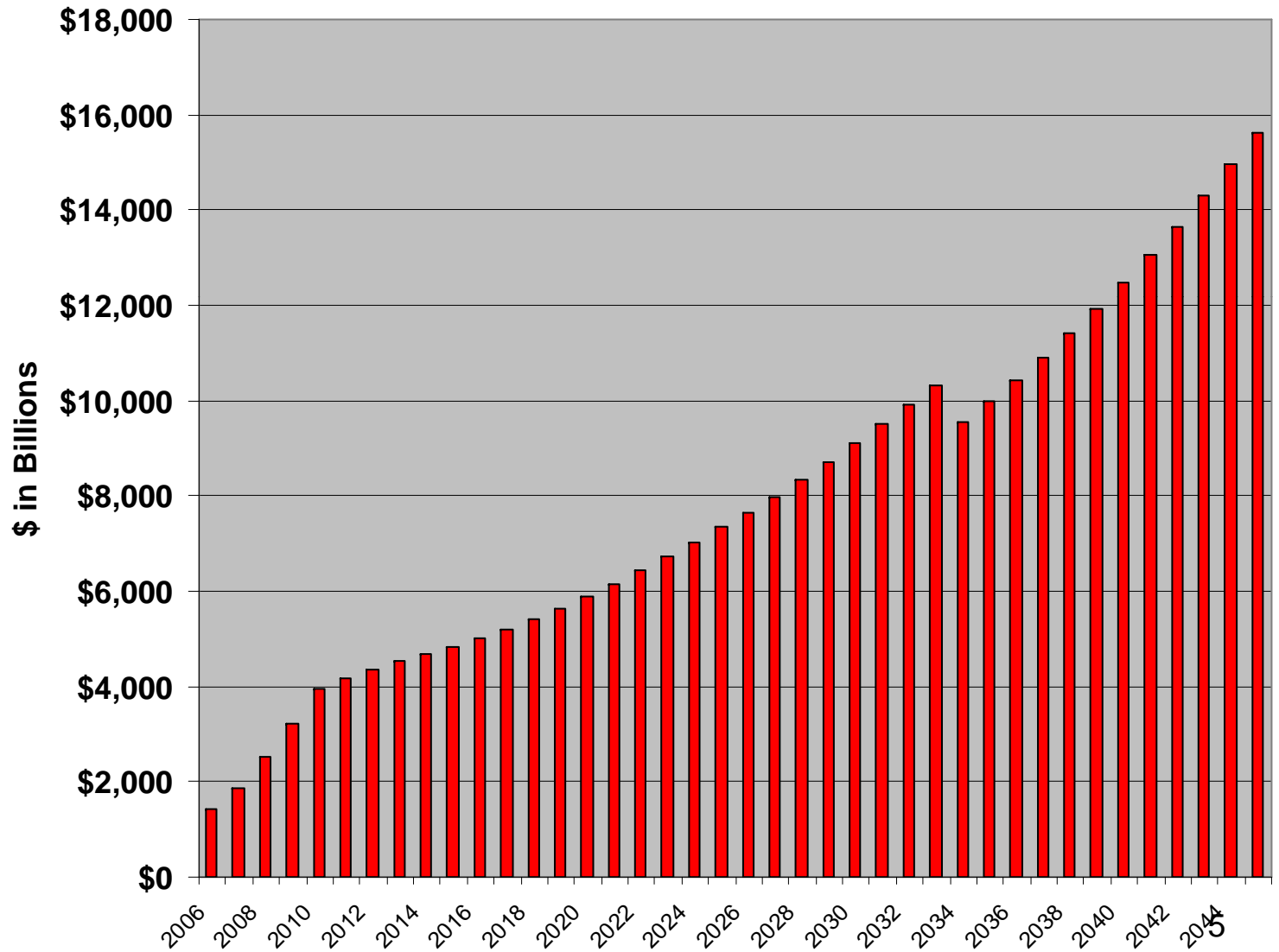
## Why the Economic Problems?

– NOT TAX BURDEN OR WASTEFUL SPENDING

- Illinois' total state *AND* local tax burden, as a percentage of personal income ranks only 41<sup>st</sup> in the nation.
- The second lowest tax burden in the Midwest to Missouri (Missouri is all of one-tenth of one percent lower).
- Illinois also ranks only 45<sup>th</sup> in spending among the states

**THE RAMP**

**The "Ramp" before the 2008 Economic meltdown!  
Required Yearly Pension Payments:  
FY 2006 - FY 2045**



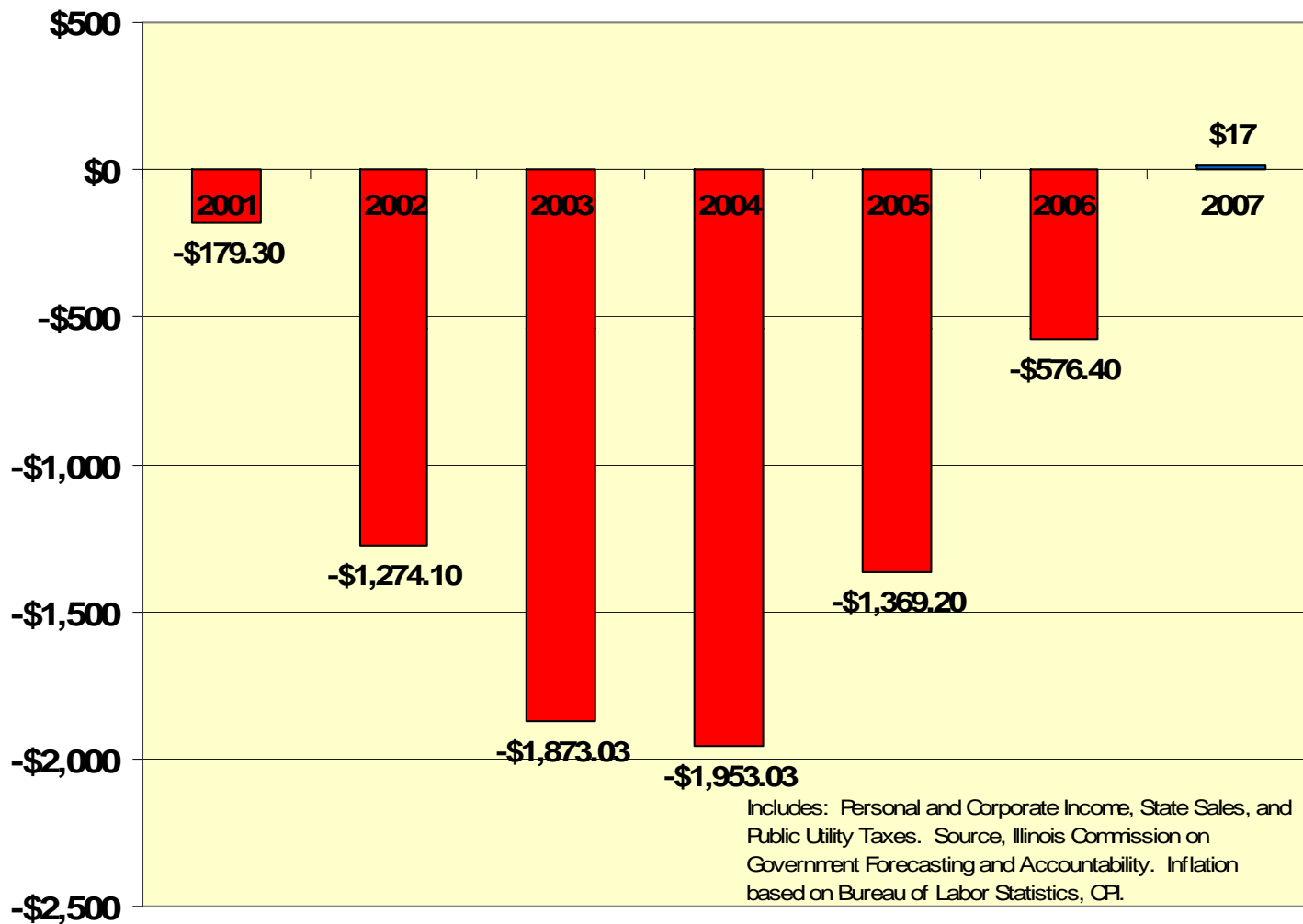
## ***WHAT SHOULD BE:***

FAIR	→	<b>PROGRESSIVE</b>
RESPONSIVE	→	<b>TO MODERN ECONOMY</b>
STABLE	→	<b>DURING POOR ECONOMIES</b>
EFFICIENT	→	<b>DOESN'T DISTORT PRIVATE MARKETS</b>

***BUT ISN'T***

**NOT SO MUCH**

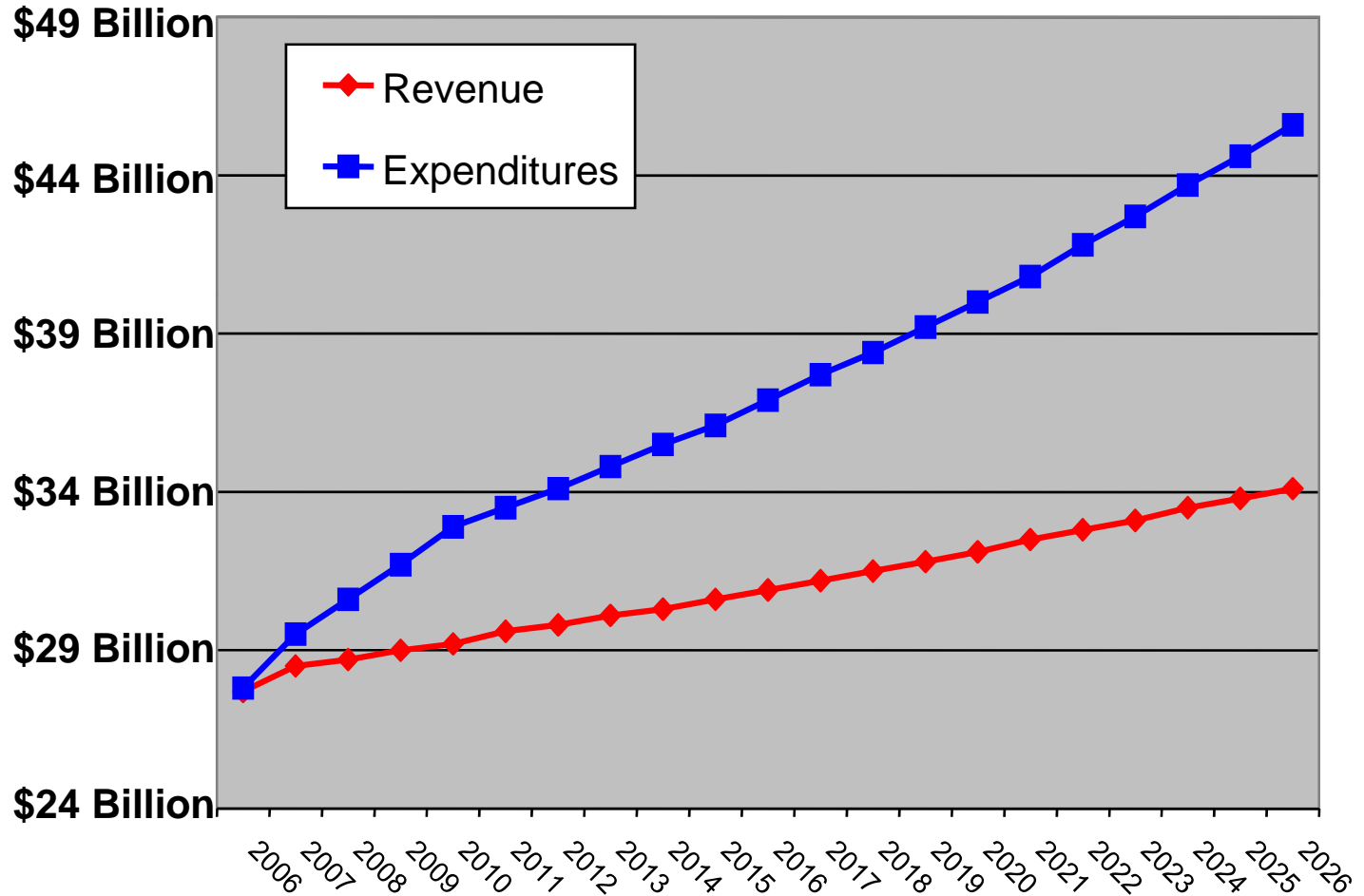
### Illinois State Major Tax Revenues Have Not Kept Up With Inflation by Over \$7 Billion Since 2000



# STRUCTURAL DEFICIT

## WHICH CREATES:

The Illinois Structural Deficit  
(How Revenue Growth Will Not Keep Pace With The Cost of Current Services)



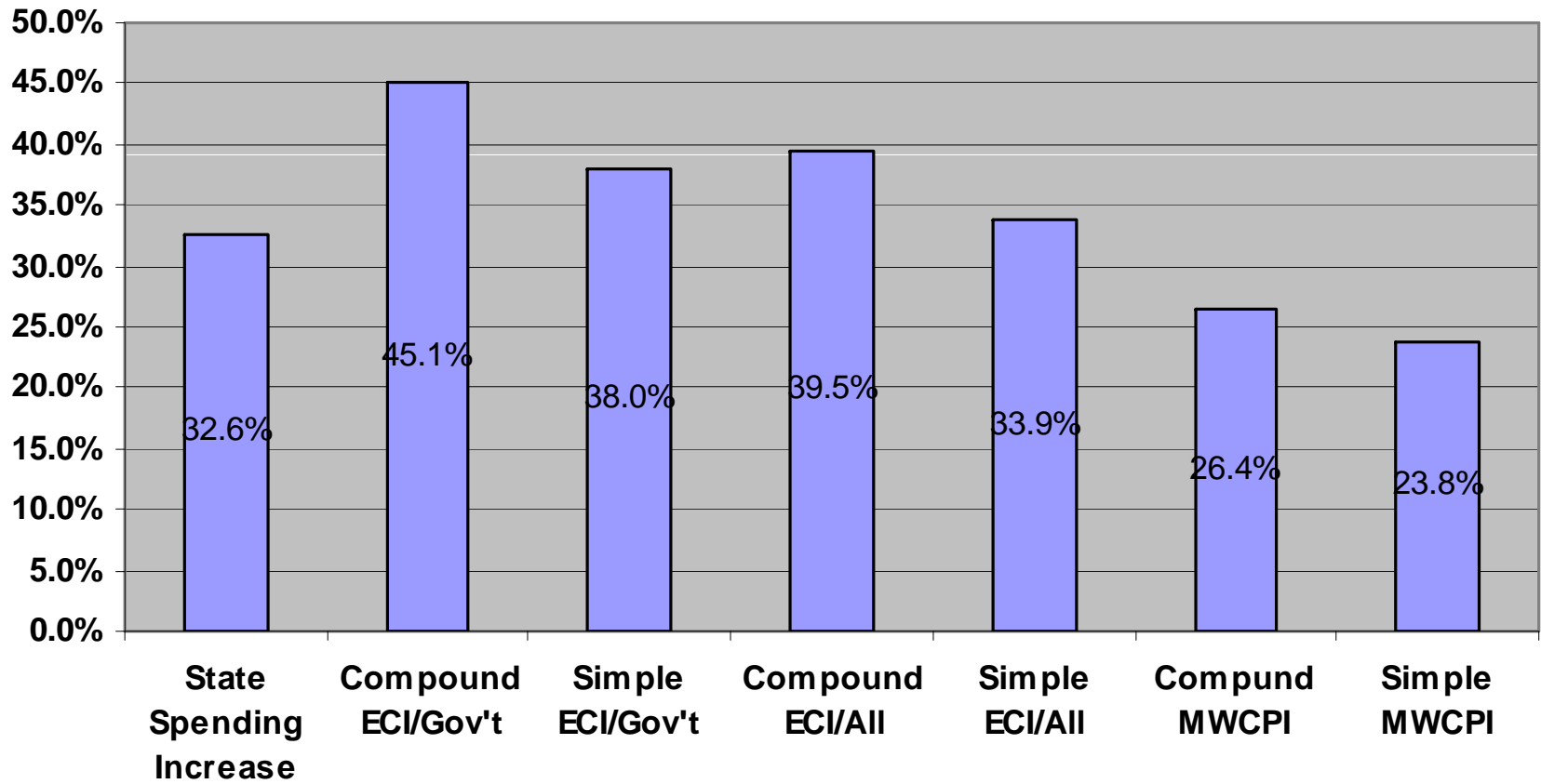
\*Adjusts solely for historic rates of inflation and population growth, and assumes normal economic growth.

# IS THE PROBLEM CONTRIBUTIONS OR BENEFITS?

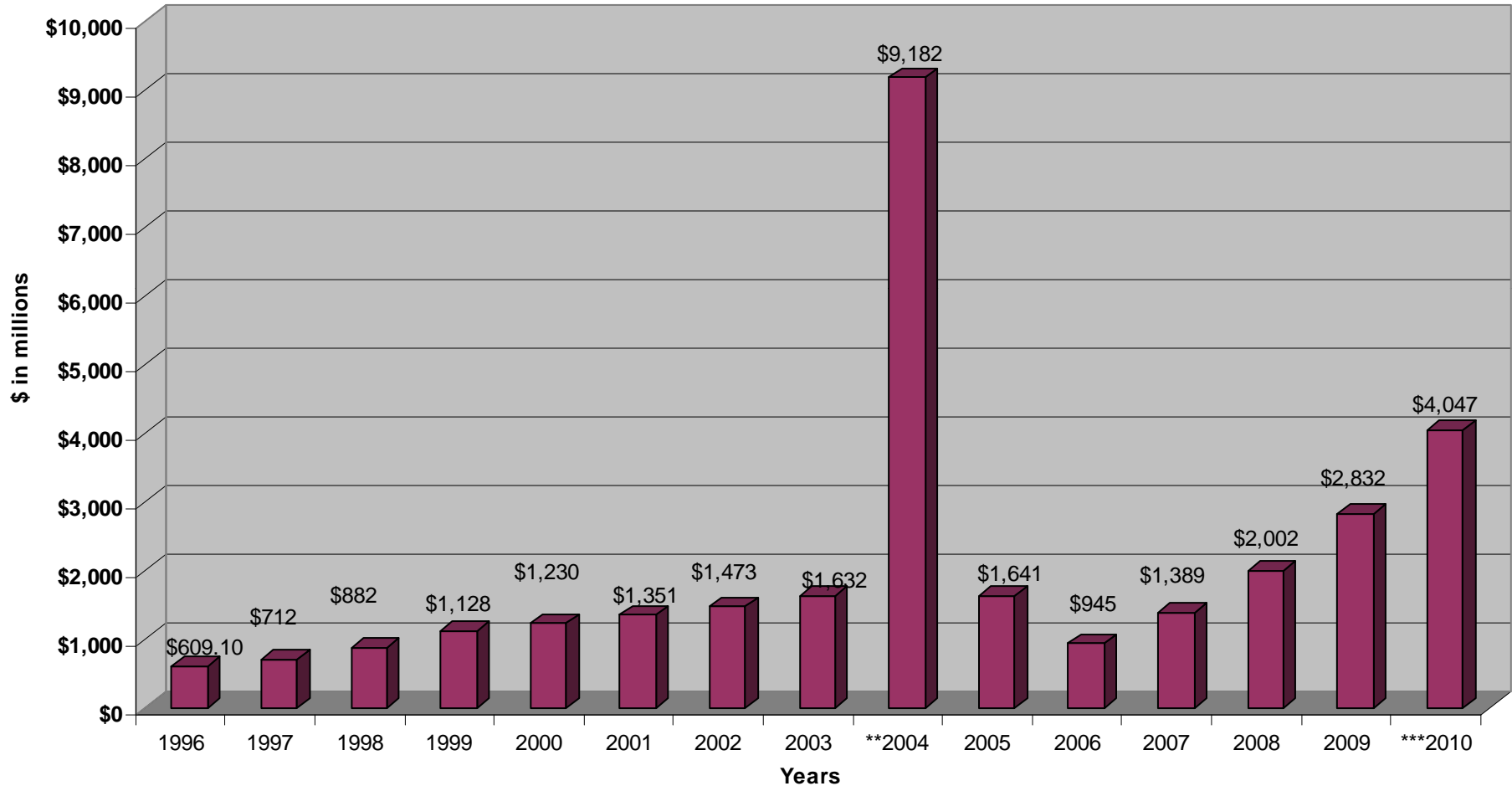
**NEITHER** – It is a Revenue not a Spending Problem.

Item	Amount
FY 2010 Appropriations	\$ 26.085 B
FY 2000 Appropriations	\$ 21.294 B
Nominal Dollar Increase	\$ 4.791 B
Scheduled FY 2010 Pension Ramp increase over 2000 levels	-( <b>\$ 3.422 B</b> )
Nominal difference in Appropriations for Services in FY 2010 over FY 2009, Net of Pension Increase	<b>\$ 1.369 B</b>

**Percentage Increases in Illinois General Fund Spending  
(Net of Pension Ramp) versus Inflation  
FY2000 - FY2009**



## State Contributions Annually since the 1995 Pension Ramp Passed



\*\*FY 2004 State appropriations authorized include \$7.3 billion in proceeds from the sale of the pension obligation bonds.

\*\*\*Scheduled future payment per P.A. 88-593

Source: Commission on Government Forecasting & Accountability

# **TWO PART SOLUTION: Revise Revenue the Right Way**



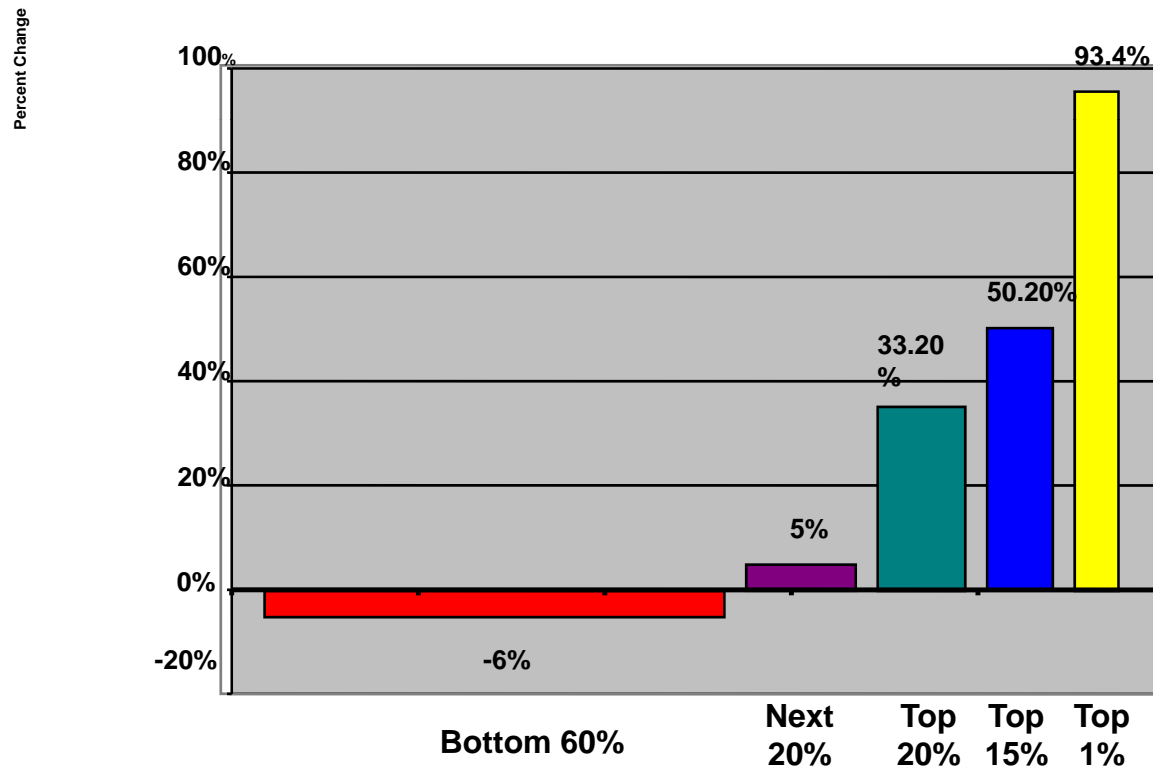
## **Re-think the Ramp**

# INCOME INEQUALITY

## Fair? Responsive?

Income Growth in the United States 1979-1999  
(Real 1999 Dollars)

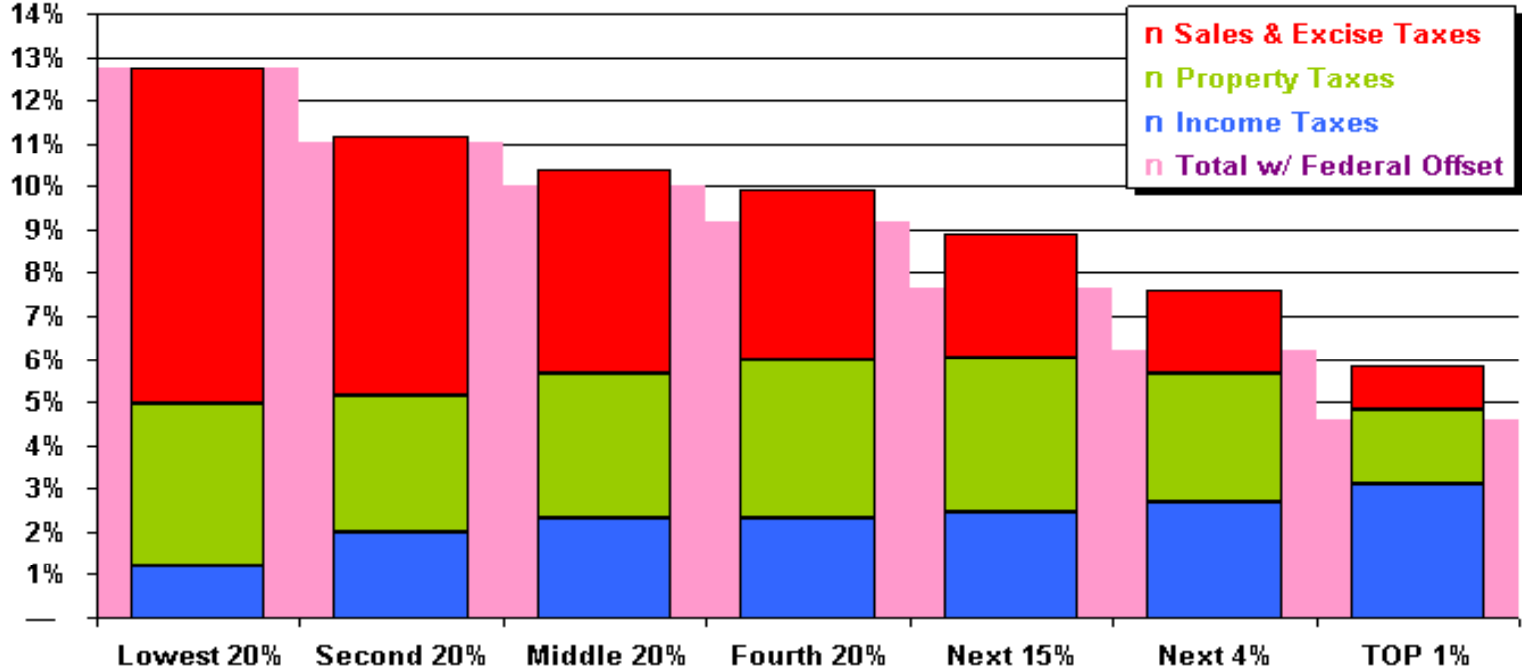
\*Source U.S. Census Data



REGRESSIVE

# Fair? Responsive?

## State & Local Tax Burden as a Percentage of Income



Income Range	Less than \$16,000	\$16,000 – \$30,000	\$30,000 – \$48,000	\$48,000 – \$77,000	\$77,000 – \$148,000	\$148,000 – \$295,000	\$295,000 or more
Average Income	\$8,900	\$22,600	\$38,500	\$61,100	\$101,400	\$203,600	\$1,322,100
<b>Tax Burden</b>	<b>12.7%</b>	<b>11%</b>	<b>10%</b>	<b>9.2%</b>	<b>7.7%</b>	<b>6.2%</b>	<b>4.6%</b>

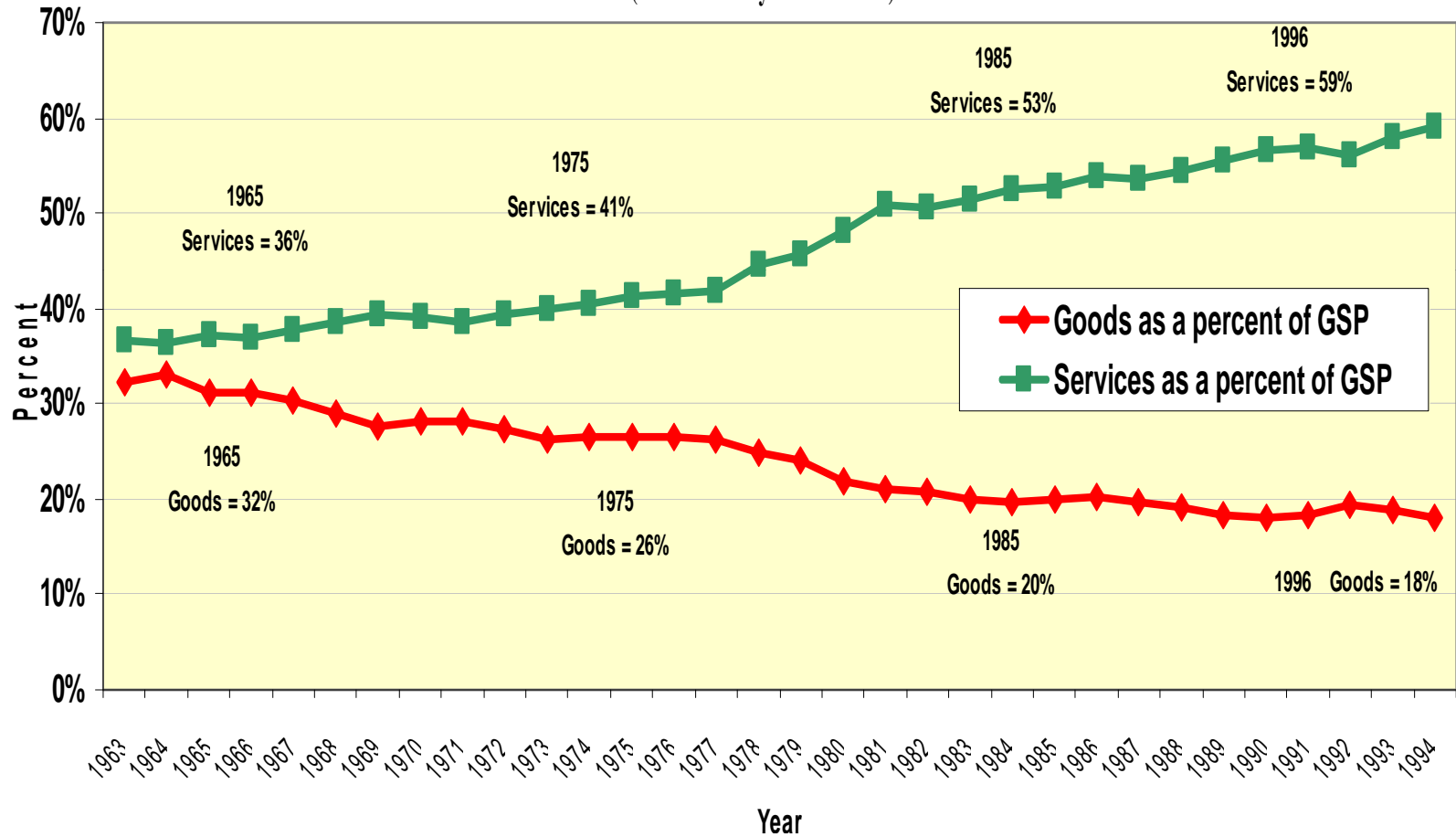
# INCOME TAX INCREASE

3% → 5%

3% + 2% = 5%

2/3 = 67%

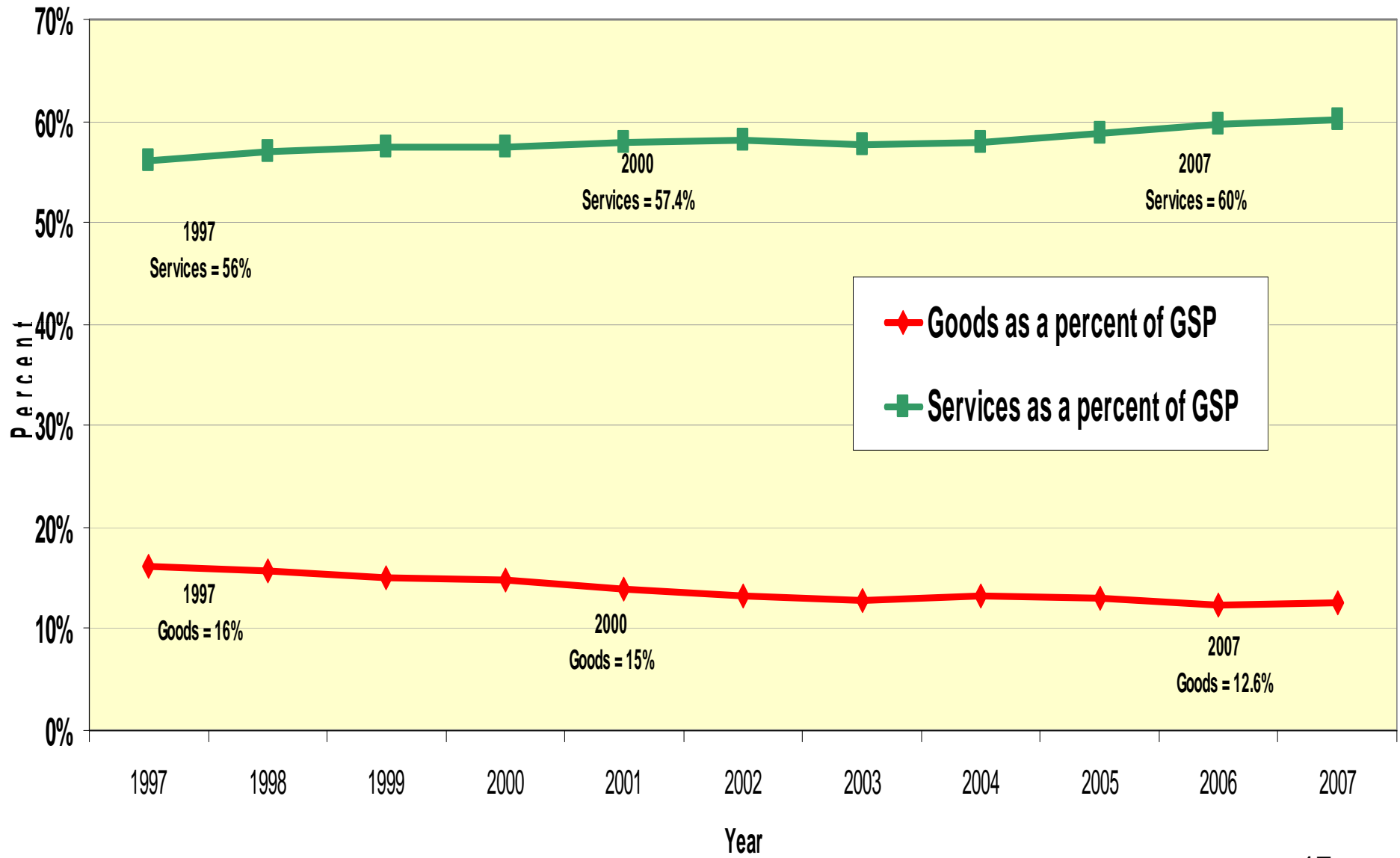
## Revenues of Goods and Services as a Percent of Gross State Product: Illinois 1965 - 1995 (SIC Industry Standards)



Center for Tax and Budget Accountability analysis of United States Bureau of Economic Analysis Data.

# Revenues of Goods and Services as a Percent of Gross State Product: Illinois 1997-2007

(NAICS Industry Standards)

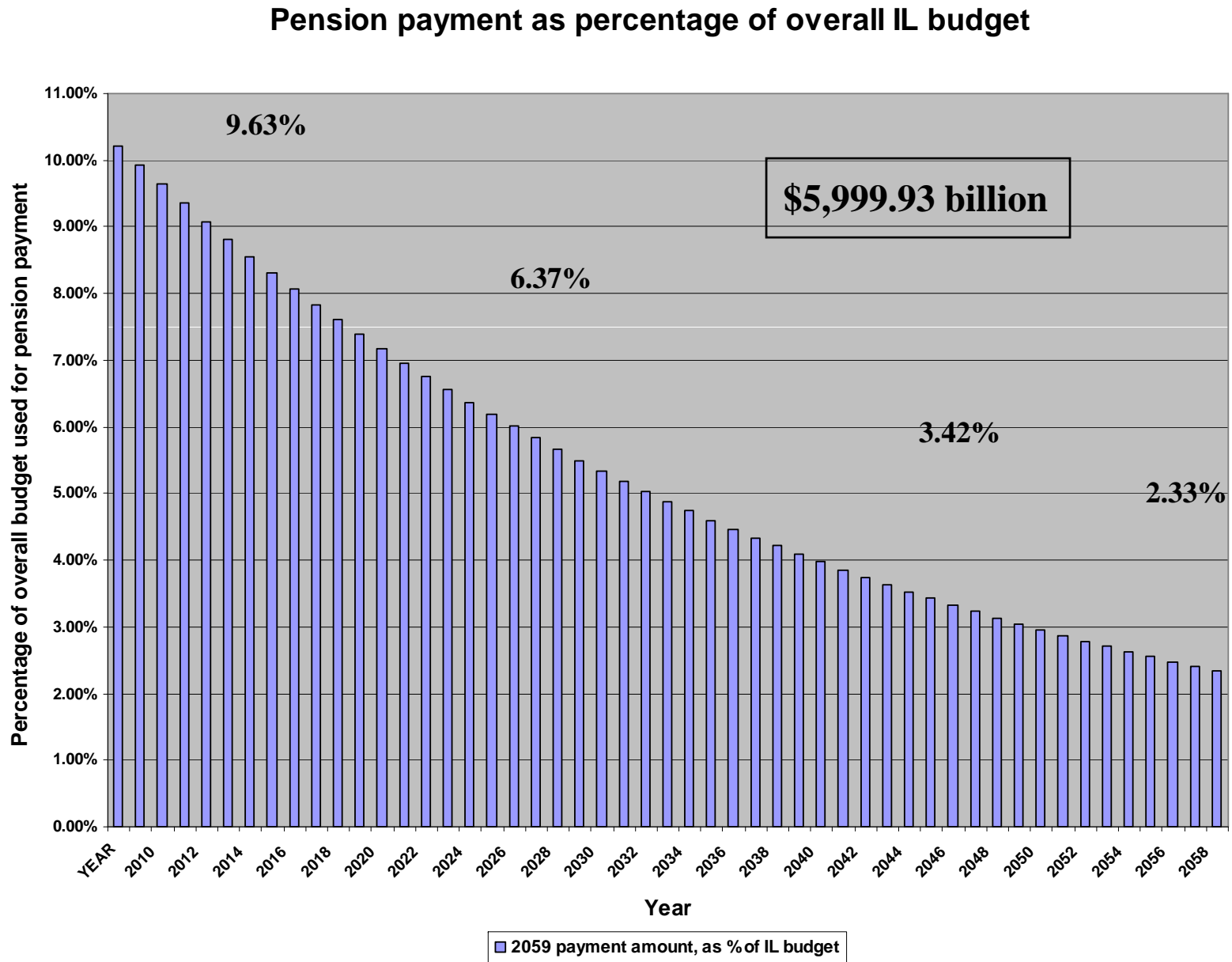


## “Amortization” the Responsible Funding Solution

- Payment amounts assume an unfunded liability of \$73.4 billion and an interest rate of 8.0% over a 36 and 50 year period, respectively.
- Illinois budget projections are based upon the average annual historic CPI (consumer price index) of 3.0% for a 15 year period of 1983-2008.
- For purposes of these projections we assume that the Illinois budget will keep pace with inflation, increasing at an average rate of 3% per year.

**SOLVING THE UNFUNDED PENSION  
LIABILITY**

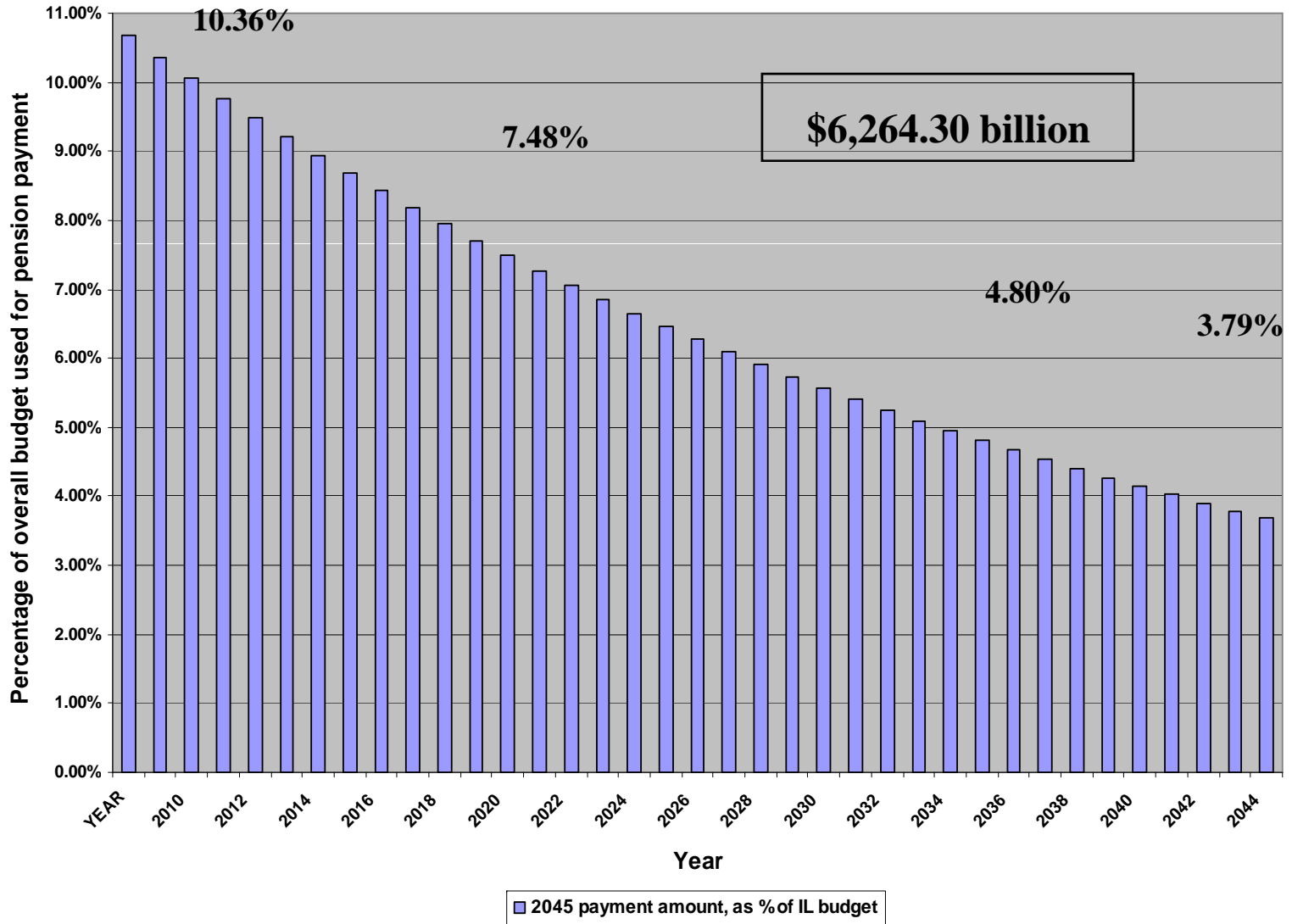
# 2059 Payment as Percentage of Illinois Budget



**SOLVING THE UNFUNDED PENSION  
LIABILITY**

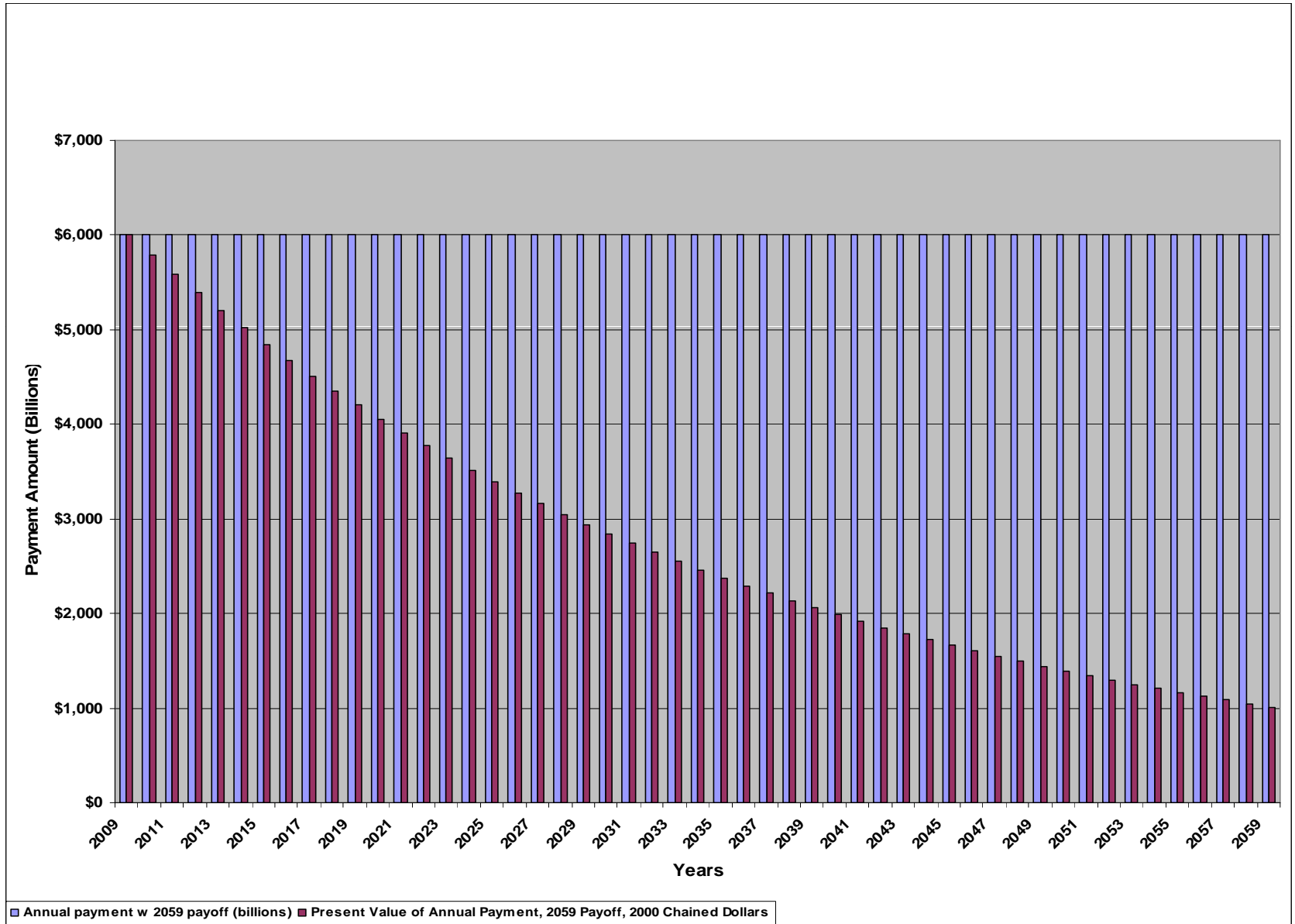
# 2045 Payment as Percentage of Illinois Budget

**Pension payment as percentage of overall IL budget**



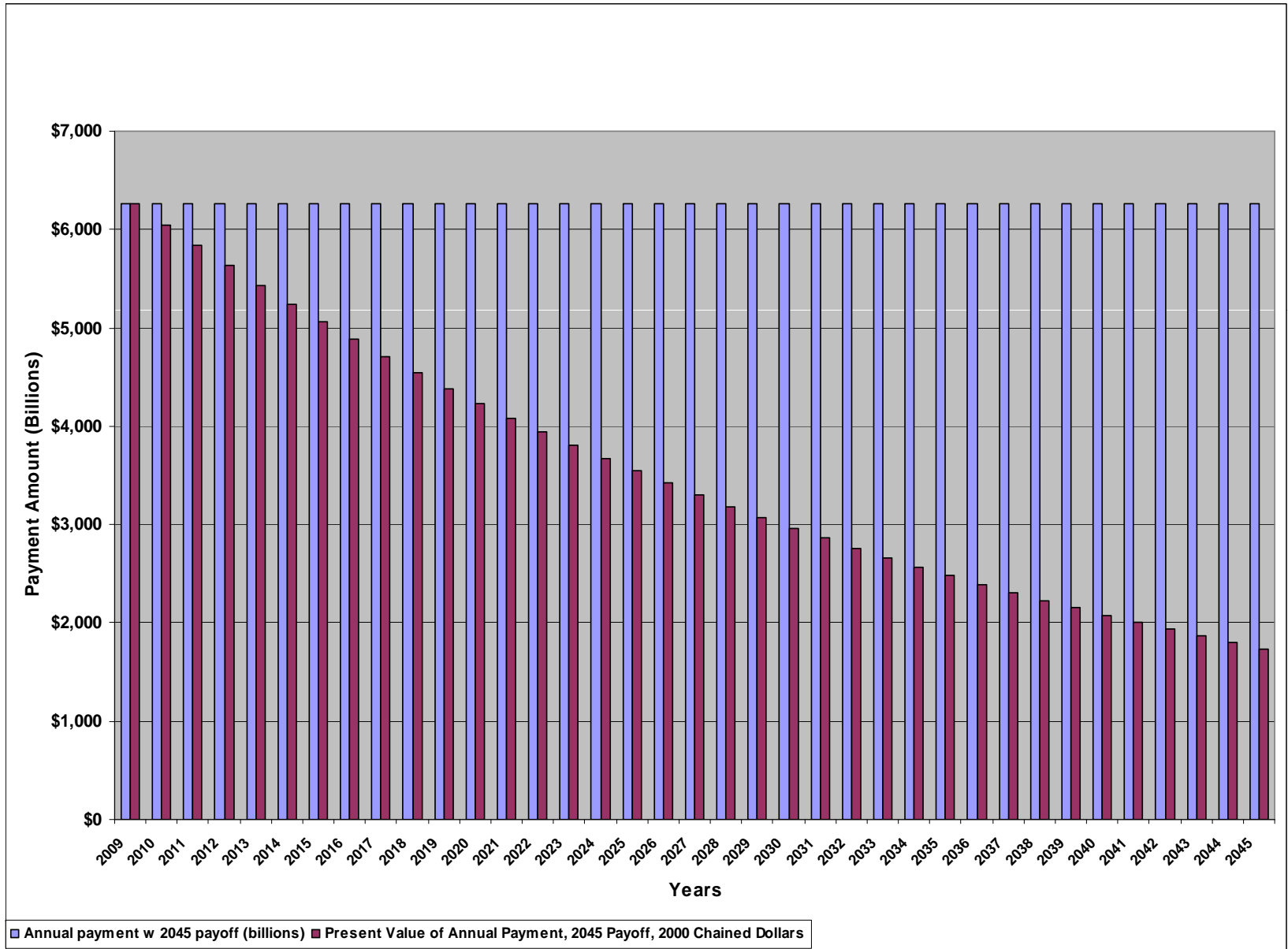
# SOLVING THE UNFUNDED PENSION LIABILITY

## Annual Payment Compared to Present Value of Annual Payment, 2059 Payoff



# SOLVING THE UNFUNDED PENSION LIABILITY

## Annual Payment Compared to Present Value of Annual Payment, 2045 Payoff



## WHERE **AON CONSULTING** GOT IT RIGHT...

*“If Plan Anticipated to be Insolvent in Short Time”:*

“Must Change Cash Flows in Short Time”

“New Tiers Won’t Help”

“Time is of the Essence”

“Cash infusion from other revenue sources”

\*\*Due to lack of revenue the 5-state funded retirement systems are in danger of becoming **insolvent**.\*\*

## WHERE **AON CONSULTING** GOT IT WRONG...

### Benefit Cuts:

- current workers
- current recipients

**Section 5 of Article XIII of the Illinois Constitution states that “membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall be diminished or impaired.” (This clause is commonly referred to as the “pension protection clause.”)**

### Cash Infusion through **Borrowing**

**Borrowing simply prolongs the inevitable tanking of the retirement systems and takes an already debilitating debt from bad to worse. Identifying a revenue source will permit the state to pay its pension obligations.**

**Under P.A. 88-0593 (Funding Plan for State-Funded Retirement Systems) , also known as the PENSION RAMP...**

**...Illinois would have to contribute \$437.6 billion through 2045.**

- Average of **\$12.2 billion a year** – an already unattainable amount proven by the growing unfunded liability.
- The “Pension Ramp” was supposed to address the state’s unfunded liability.
  - It **FAILED** due to the absence of a revenue stream to support the ramp.

## **Under the Governor's proposed Stair Step Funding Plan and Two-Tier proposal...**

**...Illinois would contribute substantially more, \$532.3 billion through 2045.**

**-Average of \$14.8 billion a year – which ironically costs more than existing law!**

**- The Governor's plan to underfund pensions will cost the state an additional \$94.7 billion between now and 2045.**

(Source; Stair Step Funding Proposal, Governor's Office, 5/8/2009)

The Commission on Government Forecasting and Accountability's actuary concluded that the Governor's proposal to reduce benefits for new employees is not appropriate for reducing costs.

(SOURCE: COGFA's Fiscal Analysis of the Governor's Pension Reform Proposal)

# FOR MORE INFORMATION:

**CENTER FOR TAX AND BUDGET ACCOUNTABILITY**

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