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AN ESSENTIAL STEP TOWARD RESOLVING THE STATE FISCAL CRISIS

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The recently enacted income tax increase is an essential step toward resolving the prolonged fiscal crisis in Illinois. Prior to this legislation, the projected General Funds budget deficit for FY 2012 was estimated at $15 billion, which represents about 60% of FY 2011 appropriations for all state agencies. The new revenue package is expected to generate about $7 billion over a full year. The temporary tax increase will enable the state to improve its credit rating, reduce the massive backlog of unpaid bills, and avert a full-scale fiscal meltdown. But it is not a panacea.

The state fiscal crisis is a product of both short-term and long-term factors: a *cyclical deficit* resulting from the Great Recession and a *structural deficit* resulting from an inadequate state revenue system that does not keep pace with long-term economic growth. The recession has severely battered state budgets across the nation. In Illinois, General Funds revenue from state sources plummeted by nearly $2 billion in FY 2009 and dropped another $1.7 billion during FY 2010.

The clearest manifestation of the structural deficit involves chronic underfunding of state pension obligations. Under a 50-year funding plan adopted in 1995, the state's annual contributions have been increasing substantially over the past several years. In FY 2008, GF pension costs, including both mandated contributions and pension-related debt service, totaled about $2 billion. In FY 2012, those costs will exceed $5 billion, even though mandated state contributions will be 20% lower than originally anticipated as a result of legislation enacted last spring.

Over the past several years, federal recovery funds have protected some important areas of the state budget — most notably, General State Aid to local school districts and Medicaid. But these funds will no longer be available after FY 2011. Many other programs and services have already been hit hard by the fiscal crisis. In the State Board of Education budget, for example, areas hurt by funding cuts since FY 2009 have included preschool programs, bilingual education, social-emotional learning, and student transportation. More than a dozen other programs have been eliminated entirely. Among all state agencies, the Department of Human Services has been most severely impacted by budget cuts. Funding for community-based service providers has been slashed by nearly 20% since FY 2009. The results include significant service reductions in mental health, developmental disabilities, and other programs for vulnerable populations.

A balanced and responsible solution to the state budget crisis requires a significant amount of new revenue, strategic restraints on spending, and meaningful fiscal reforms. The recently adopted revenue package is a big step forward, but it does not solve the entire problem. The legislation included no provisions to mitigate the effects of higher taxes on low-income families. Without debt restructuring bonds, the backlog of unpaid bills, which totaled $6.4 billion at the end of December, will be reduced by only about $2 billion by the end of FY 2011. Additional spending cuts remain inevitable, and state policymakers will face difficult choices in setting budget priorities. Since the tax increase is temporary, it will improve the short-term fiscal outlook, but it cannot address the long-term structural deficit. Finally, we need policy decisions that reflect both fiscal and social responsibility, which will require greater budget transparency from both the executive and legislative branches.

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