Commission on Government Forecasting and Accountability

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MONTHLY BRIEFING FOR THE MONTH ENDED: JANUARY 2018

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INSIDE THIS ISSUE

ECONOMY: A Big Piece of the Economy – Consumer Spending

Julie Bae & Benjamin L. Varner, Economic Specialists

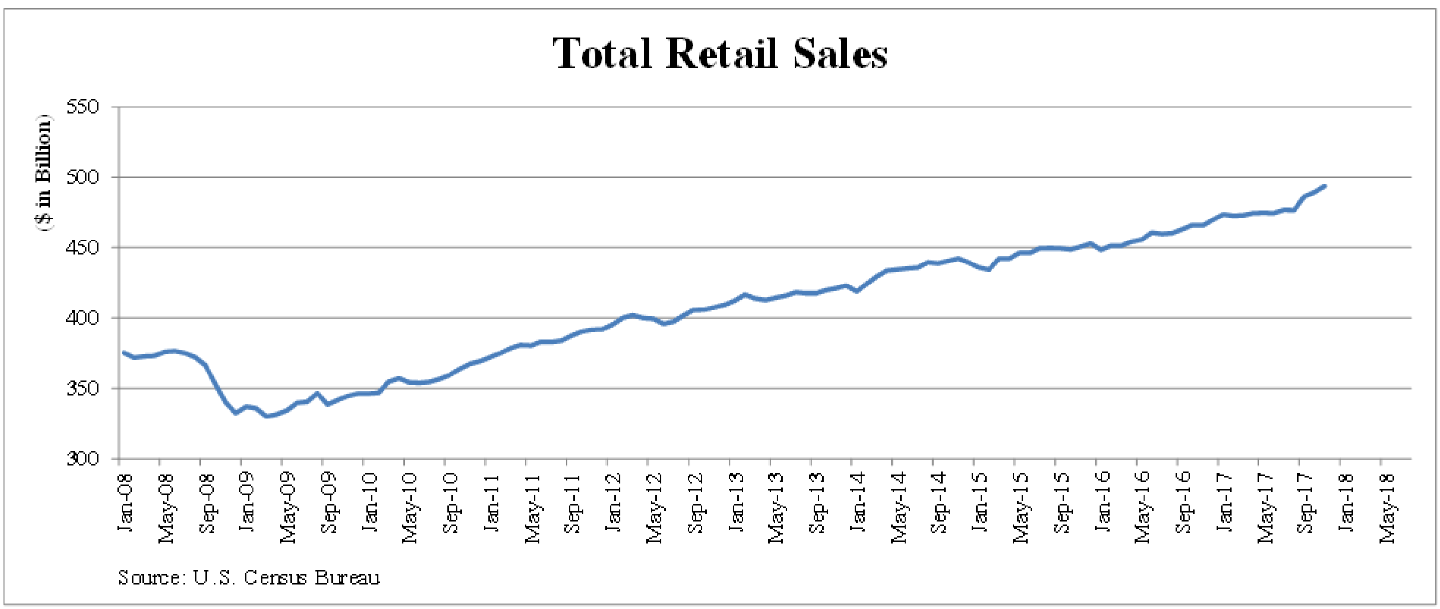
The U.S. economy ended 2017 on an upbeat and 2018 appears to be off to a good start. The Dow Jones Industrial Average, one of the most popular stock market indexes, set an all-time high reaching above 26,000 for the first time in January 2018 after hitting 25,000 in the same month. The new tax cuts are expected to stimulate the economy at least in the short-term. The jobless rate during the last quarter of 2017 stabilized at 4.1%, a 17-year low. The Federal Reserve is currently planning to raise the federal funds target rate three times this year reflecting the steadily growing economy and inflation which remains under control.

Retail sales are an important economic indicator as consumer spending plays a significant role, contributing about 70% of total spending in the economy. At the retail level, U.S. retail and food services amounted to \$495.4 billion in December 2017, an increase of 0.4% from the previous month or 5.4% greater than a year earlier according to the U.S. Census Bureau. During the 4th quarter of 2017, these sales rose 2.7% from the 3rd quarter, or 5.5% from the same period a year earlier. Total retail sales in November were revised up to show a 0.9% increase instead of the previously reported 0.8% increase. The 12-month total retail sales were up 4.2% in 2017 from 2016. Excluding auto and gasoline sales, the so-called core retail sales increased 0.3% from the upwardly revised November reading. These improved figures and upward revisions to the sales figures mirror the sharp growth in consumer confidence in 2017.

The holiday retail sales during November and December also observed some pleasant surprises. According to the National Retail Federation (NRF), the largest retail trade association in the world, the winter holiday retail sales were \$691.9 billion, an increase of 5.5% from the same period in 2016, which exceeded NRF's expectation of between $678.75 billion and $682 billion. NRF Chief Economist, Jack Kleinhenz said, "*Strong employment and more money in consumers' pockets along with the news of tax cuts clearly helped with the pace of shopping. The market conditions were right … and it all worked. We think the willingness to spend and growing purchasing power seen during the holidays will be key drivers of the 2018 economy.*"

Even with all these positive results, it is interesting to note that the University of Michigan Consumer Sentiment Index, showing the consumers' expectation on the overall U.S. economy, declined to 94.4 in their preliminary January report, following two previous declines in November and December. Even so, the indicator can be volatile and there was doubt at the time that the tax package would be passed. Thirty-four percent of all respondents mentioned the new tax laws, of whom 70% expected a positive impact on their financial health, although few at the time forecast the immediate and large response from businesses to employees. Experts had expected a rise in the index in January, given the sign of a strong economy provided by other measures. Indeed it will be interesting to follow these sales in the months ahead to see if there might be a delayed impact on this measure.

As shown in the chart, retail sales have been on a gradual upward trend since 2009. According to the Commission's forecasting service, IHS Market, "*Consumer fundamentals were already on solid footing entering 2018 - thanks to rising incomes and a solid job market - and lower tax rates enacted by the Tax Cuts and Jobs Act (TCJA) will modestly boost spending further over the next couple years.*"

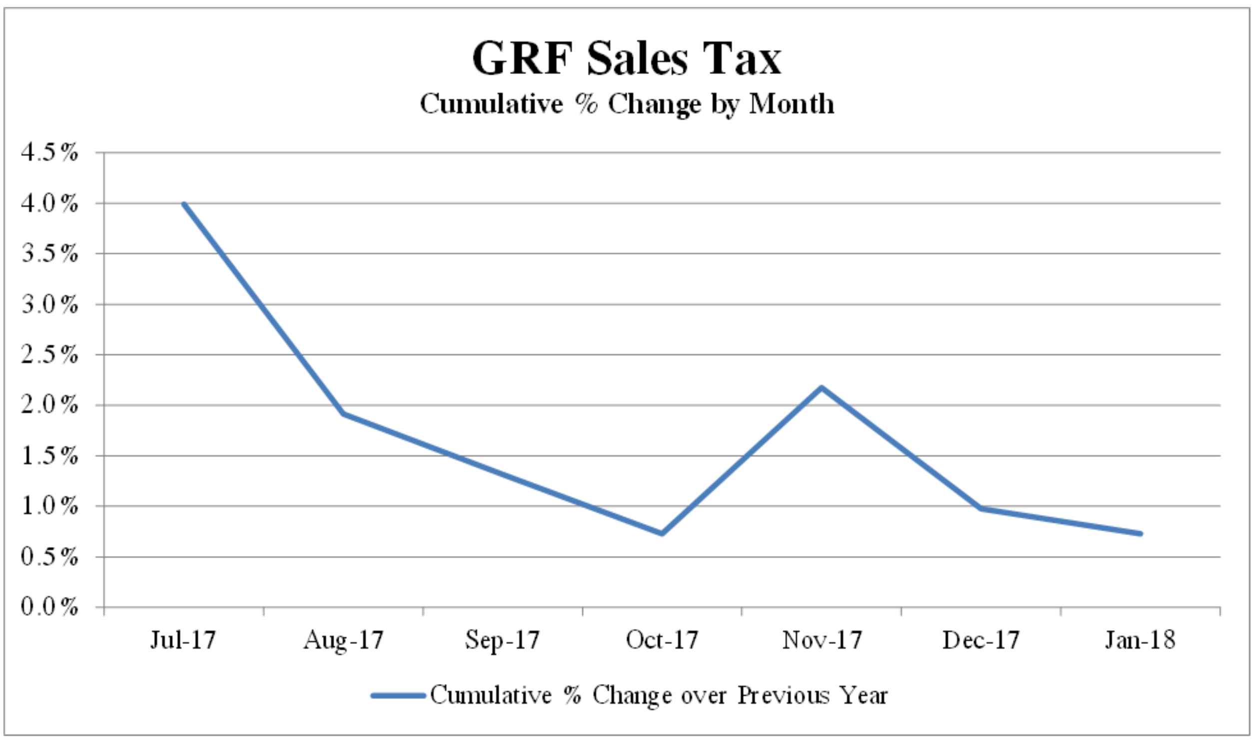


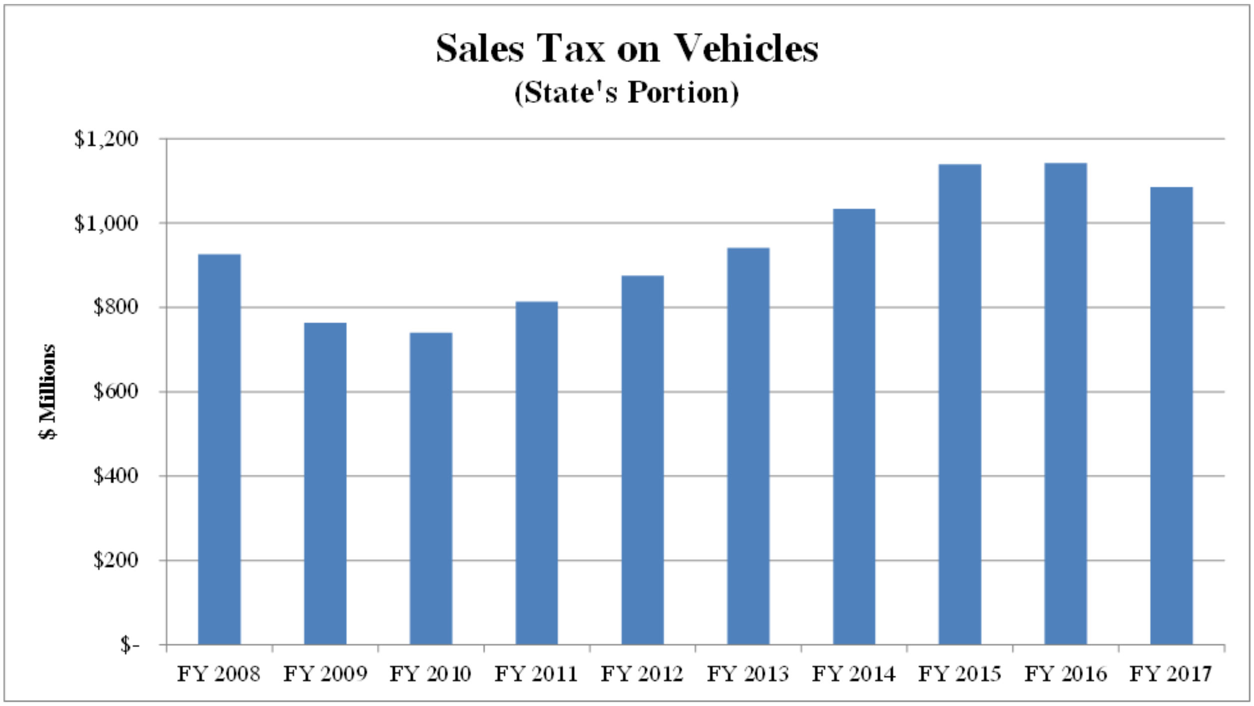
Unfortunately, while national sales measures are for the most part positive, in Illinois, based on actual sale tax receipts, performance is not near as rosy. Through January, general revenue sales tax collections are only up approximately 0.7% in FY 2018 [not including recent changes to direct transit funds distributions]. In fact, Illinois sales tax has been relatively weak since FY 2015. In FY 2015, sales tax receipts were up only 0.4%. Sales taxes were down -2.8% in FY 2017, but this was mostly due to a one-time distribution adjustment of approximately $140 million to other local government sales tax related funds by the Department of Revenue.

When this amount, which would normally be included in general funds sales tax receipts, is added back in, FY 2017's results would have improved to a still disappointing growth rate of 1.5%. That would remain below the long-term trend of sales tax growth, which is closer to 2.0% to 2.5% per year.

As shown in the below table, FY 2018 began with growth of almost 4% in July but has been flat or negative since then except for an increase in sales tax receipts in November. The Commission is expecting better performance during March and April as that is when the one-time distribution changes were made in FY 2017. Absent the expected growth from the timing of the one-time distribution change, the outlook for sales tax growth remains tepid. Lack of inflationary pressure over the last several years has likely contributed to this period of disappointing growth.

Another reason that sales tax receipts are not performing as well as hoped for is the decline in auto sales. Auto sales account for approximately 13-15% of general revenue sales tax collections. After the Great Recession, auto sales were a primary contributor to the growth in sales taxes. However, sales taxes from auto sales fell 5% in FY 2017 and are down approximately 2.4% through December of this fiscal year. [See table page 4]





INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS*	Dec. 2017	Nov. 2017	Dec. 2016
Unemployment Rate (Average)	4.8%	4.9%	5.7%
Inflation in Chicago (12-month percent change)	1.7%	1.8%	1.9%

	LATEST MONTH	CHANGE OVER PRIOR MONTH	CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (Dec.)	6,464.4	0.3%	-0.6%
Employment (thousands) (Dec.)	6,155.3	0.4%	0.4%
Nonfarm Payroll Employment (Dec.)	6,050,900	1,500	29,600
Single Family Housing Permits (Dec.)	579	-30.5%	3.6%
Total Exports ($ mil) (Nov.)	5,637.1	3.1%	12.0%
Chicago Purchasing Managers Index (Jan.)	65.7	-14.3%	20.3%

* Due to monthly fluctuations, trend best shown by % change from a year ago

State Employees Group Insurance Program Status Update

Anthony Bolton, Revenue/Pension Analyst

While historical underfunding has been a concern, the lack of an enacted budget the past two fiscal years has resulted in the State Employee Group Insurance Program (SEGIP) building up a large backlog of unpaid claims. With the passage of a state budget, money has been made available to pay bills in a timelier manner. However, there has not been sufficient funding provided to fully pay down the backlog of invoices accumulated over the course of the budget stalemate. Accordingly, the total of claims held by the State has risen from month to month. However, the State recently raised approximately $6.48 billion in bond revenues that is intended to partially pay down the backlog of bills owed by the State to various vendors, including those who are a part of the State Employees Group Insurance Program. According to statements by the Comptroller's Office, approximately $3.9 billion of the total raised is expected to be used to pay down unpaid state health insurance claims owed to medical providers. Additionally, $2.5 billion is expected to be spent towards Medicaid and other Federal reimbursements. The Comptroller has stated that this money is expected to be used towards paying down the longest-held bills and highest-interest-accruing vouchers in particular.

At the end of December 2017, approximately $1.4 billion in SEGIP claims were being held by the state from assorted insurers, organizations, and companies, an increase of $160 million from the previous month, but a decrease of approximately $3.7 billion from October 2017. Of this much lower (though still quite large) total, the largest portion was approximately $689 million in HMO/Medicare Advantage claims. The second largest portion, Open Access Plans, totaled $274 million. The third largest portion of the overall claims hold came from CIGNA and Aetna (PPO plans), which had $158 million in claims currently held by the state. Concurrently, the estimated time for claims to be held was 97-309 days for Managed Care/Medicare Advantage, 175-182 days for Open Access Plans, and 140-193 days for CIGNA/Aetna. These are all sharp declines from the previous few years, though they are slowly increasing as the current income for the SEGIP is insufficient to cover existing expenses (including interest). This information (and other pertinent data) is displayed in the chart on the next page.

It is necessary to note that without additional funding, the ability of the State to pay down the smaller (though still significant) backlog is extremely limited. In recent years, appropriations and revenues have been insufficient to cover expenses, leading to steadily increasing interest payments and held claim times. Increased revenues and/or appropriations over existing levels will be necessary to pay down the remaining held claims and avoid significant interest penalties. As of December 31, 2017, according to CMS, approximately $429 million is still owed by the State of Illinois in interest on claims. In regards to specific classifications of claims (not including interest), $738 million in Prompt Payment claims and $677 million in

Timely Payment claims are being held by the state.

As a result of the State Employees Group Insurance Program (SEGIP) building up a large backlog of unpaid claims from health care vendors, alternative options for payment have been explored. One option that has been utilized is a program called the Vendor Payment Program (VPP), which is organized through the Department of Central Management Services (CMS). Under the VPP, vendors for the state of Illinois who would otherwise receive prompt payment interest would instead partner with a "qualified purchaser" who would purchase the voucher from them. The vendor would receive approximately 90% of the total invoice owed to them with the other 10% paid to them once the qualified purchaser is paid by the state. The qualified purchaser would keep any interest paid out by the state on the voucher. However, the State has not been able to pay out vouchers without appropriation, so CMS has switched to the Vendor Support Initiative program (VSI), which is procedurally similar to the Vendor Payment Program, but does not require a voucher to receive payment.

The inclusion of the PPO vendor Aetna into the listing of held claims by the State of Illinois is a new addition for this month's update. Additionally, the current group insurance rates, premiums, co-payments, and other financing are expected to be maintained through the 2018 Fiscal Year.

Claims Hold Data for SEGIP
(as of December 31, 2017)

Vendor	Claims Hold	Length of Claims Hold (in days)	Interest Owed (Including Past Due Interest)
CIGNA - PPO (and Member)	$53,148,224	193	$2,563,804
CIGNA - Non-PPO	$2,807,795	193	$135,476
Aetna - PPO	$102,010,982	140	$956,513
Dental Claims Hold – PPO	$38,190,047	137	$1,012,036
Dental - Non-PPO	$17,986,908	256	$1,011,764
Magellan (Mental Health) Claims	$3,412,530	189	$57,525
Coventry HMO	$29,723,028	97	$10,383,823
Health Alliance HMO	$331,984,866	309	$168,783,568
HMO Illinois	$181,954,815	250	$89,172,746
Blue Advantage	$34,000,163	250	$13,975,954
HealthLink OAP	$222,958,670	175	$0
Coventry OAP	$50,909,986	182	$747,788
Medco	$0	844	$18,854,569
CVS/Caremark	$185,820,877	244	$50,761,642
Coventry Medicare Advantage (MA)	$5,164,754	250	$2,174,215
Health Alliance MA	$1,280,061	250	$425,151
Humana Benefit Plan MA	$149,229	250	$83,081
Humana Health Plan MA	$3,069,551	250	$1,666,935
United Healthcare MA	$101,531,916	250	$54,202,539
Fidelity (Vision)	$4,753,462	250	$1,700,769
Minnesota Life	$22,160,439	128	$175,511
Other Fees (ASC/etc.)	$22,223,400	159-250	$10,638,361
Total	**$1,415,241,703**	**97-309**	**$429,483,770**

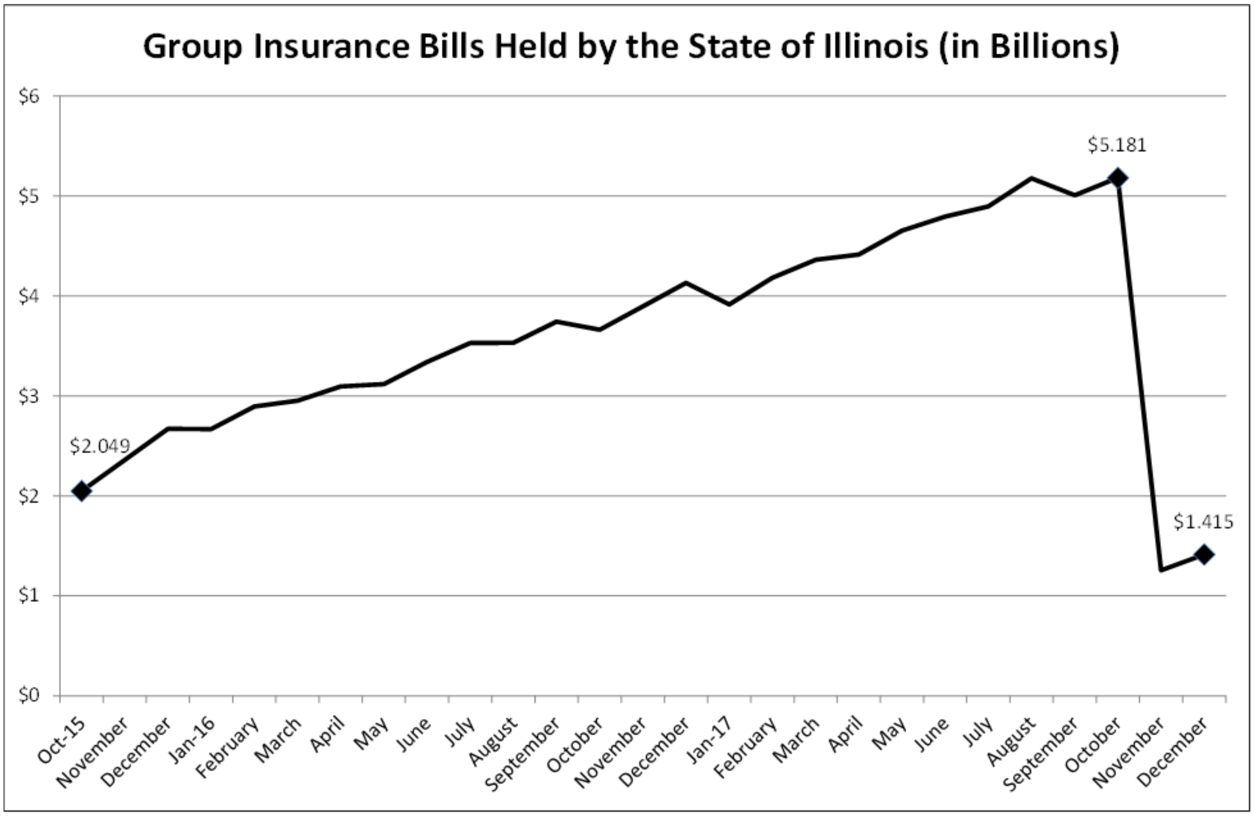
Source: CMS

The current interest owed on these claims is also noted in the previous chart. The interest on held claims is reflective of the 9 to 12 percent interest rates mentioned in previous monthly reports and is not included in the total claims hold figure of $1.4 billion.

State Employees' Group Insurance Program (SEGIP) Claims Hold Historical Analysis

The State of Illinois has had a chronic problem with properly funding its group insurance programs. Not only state employees, but retired teachers (TRIP), community college employees (CIP), and local government officials (LGHP) and the companies and individuals that serve their health needs have suffered from slow payments from the state. These slow payments and underfunding of the group insurance program are caused by various factors: medical cost inflation, insufficient appropriations, rising interest payments, etc. There are two main avenues for solutions to this problem: reducing expenses and/or increasing revenues. However, reducing expenses to the state is difficult to accomplish without substantially changing the insurance program itself or shifting costs away from the state towards individual members. Furthermore, increasing revenues typically relies on the difficult options of increasing contributions from members and/or finding extra money for appropriations in the state budget. Therefore, the SEGIP has very few easy or painless options to secure financial stability in the long-term. Accordingly, the issue of held bills has plagued the state for some time before dramatically rising over the last two years.

This problem is compounded by interest payments required under state law from the group insurance program that have risen from $50 million/year in FY 2012 to over $1 billion projected across the 2017-2018 fiscal years as of the last COGFA group insurance report. The $3.9 billion in bond financing to pay down the claims hold has helped with this problem in the near-term, but the subject of interest rates remains one of the greatest drivers of increasing liabilities in the SEGIP in fiscal years to come. For the purposes of understanding the claims hold issue, the following graph has been prepared to show the monthly amount of bills on hold from January of 2014 through the end of December 2017.



As shown in the graph, the bills held by the state totaled approximately $2 billion in October of 2015, up $500 million from a total of $1.5 billion in January 2014. From October 2015 onward, as the funding for group insurance was held up by the budget stalemate, the total bills on hold increased prodigiously over the next two years, to a maximum of $5.2 billion in October 2017 before the proceeds from the bond sale were applied. This had a result of lowering the total held bills to $1.3 billion at the end of November 2017. One item of interest in this period is the dip in total held bills in January of 2017 and again in September of that year along with a few other months throughout the approximately two-year period shown in the chart on the previous page. Though General Revenue appropriations were not made towards the group insurance program, funding from employee contributions was ruled applicable by the courts and was paid by the state towards the held bills, providing a small amount of relief during the budget impasse. In the event of a future stalemate, this is an avenue of limited relief for participants and vendors to the program. In the near-term, the passage of a state budget and a bonding program for (in part) paying down state group insurance bills has provided substantially greater relief than has been seen in years and a lower total held bills number than has been seen since at least 2015.

However, this total held bills number has already increased over $150 million as of the end of December 2017. Along with existing unpaid bills held by the state (and the interest accruing from them), the aforementioned burgeoning imbalance between SEGIP liabilities and revenues will continue to cause overall bills held by the state to increase absent significantly increased funding or decreased liabilities. Without changes to the funding/liabilities of this program, insufficient revenues combined with increased liabilities will result in increased imbalances (and increasing interest of 9 to 12% on these balances) that will continue to constrict the fiscal stability of this program and the options of policymakers and budgeteers to address this program in future years.

REVENUE
JANUARY RECIEPTS GROW ON STRONG INCOME TAX RECEIPTS—BUT PERFORMANCE LIKELY TIMING RELATED

Jim Muschinske, Revenue Manager

January receipts grew $886 million with the gain being almost entirely due to a strong month for both personal and corporate income taxes. While the component breakdown is not yet available, it is assumed that a large part of the increase, aside from this year's higher tax rates, was taxpayer behavior related to the recent federal tax reform package. Taxpayers would have been incentivized to pay their state tax liabilities within tax year 2017, so as to take advantage of the SALT deductions—prior to the limitations imposed under the federal reform. As a result, it's presumed a large amount of January's impressive income tax performance reflects strong estimated payments. As a consequence, those positive aspects may be short lived when future final payments are made, making it more of a timing issue than reflective of true underlying receipt performance. More time to analyze this issue will be necessary before a definitive explanation can be confirmed. In addition, January had one more receipting day when compared to last year.

Gross personal income tax receipts grew $980 million, or $851 million net of refunds and other changes enacted under P.A. 100-23. [See July briefing for further discussion of these changes]. Gross corporate income taxes not only reflected higher tax rates but also benefited from last year's volatility related to the IDoR ledger accounting conversion. For the month, corporate income taxes were up $97 million, or $74 million net of refunds and other changes. While other sources grew $27 million for the month, public utility taxes also fared well, rising $18 million. Cigarette taxes rose $6 million due to timing that impacted last year's receipts. Interest income continues to reflect higher rates of return, growing $4 million for the month.

A few revenue sources suffered declines in January, although most of the falloff simply reflects the exceptionally good performance a year earlier. For example, those fluctuations are the likely reason for a $24 million drop in corporate franchise taxes and a $19 million reduction in insurance taxes. While inheritance tax fell $13 million, it has proven to be very volatile on a monthly basis [but has fared very well year to date]. Unfortunately, as discussed in an earlier section of this briefing, sales tax receipts continue to disappoint, with January receipts dipping $5 million.

Overall transfers managed to post a modest $3 million for the month. While Lottery transfers dropped $9 million, that decline was offset by an increase of $12 million from other miscellaneous transfers. After dramatic fluctuations in federal sources over the last couple of months, January reimbursements were close to last year's receipts, growing a modest $10 million.

Year To Date

Excluding November's $2.5 billion bond sale transfer proceeds, as well as $354 million from interfund borrowing, base general funds grew $5.701 billion during the first seven months of the fiscal year. Increased income tax receipts [stemming from the recently enacted higher tax rates and timing elements presumably related to the aforementioned estimated payment abnormalities], as well as fund sweeps, and an increase in federal sources resulted in the significant gain.

Through January, gross personal income taxes are up $2.752 billion, or $2.536 billion net of refunds and other changes. Gross corporate income taxes are ahead of last year by $569 million, or $408 million net. Overall sales taxes are up only $36 million, although once direct sales tax receipts diverted to the transportation funds are included, net receipts are actually down $184 million. Smaller revenue sources posted a combined gain of $85 million.

Overall transfers, boosted by $207 million in fund sweeps, are up by $332 million. Federal sources, reflecting significantly higher reimbursable spending made possible by the November bond sale, generated $2.524 billion in growth.

JANUARY

FY 2018 vs. FY 2017

($ million)

Revenue Sources	Jan. FY 2018	Jan. FY 2017	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$2,755	$1,775	$980	55.2%
Corporate Income Tax (regular)	117	20	$97	485.0%
Sales Taxes	715	720	($5)	-0.7%
Public Utility Taxes (regular)	90	72	$18	25.0%
Cigarette Tax	32	26	$6	23.1%
Liquor Gallonage Taxes	20	20	$0	0.0%
Vehicle Use Tax	2	2	$0	0.0%
Inheritance Tax	14	27	($13)	-48.1%
Insurance Taxes and Fees	13	32	($19)	-59.4%
Corporate Franchise Tax & Fees	19	43	($24)	-55.8%
Interest on State Funds & Investments	6	2	$4	200.0%
Cook County IGT	0	0	$0	N/A
Other Sources	57	30	$27	90.0%
Subtotal	$3,840	$2,769	$1,071	38.7%
Transfers				
Lottery	42	51	($9)	-17.6%
Riverboat transfers & receipts	34	34	$0	0.0%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	0	0	$0	N/A
Fund sweeps	0	0	$0	N/A
Other	45	33	$12	36.4%
Total State Sources	$3,961	$2,887	$1,074	37.2%
Federal Sources	$326	$316	$10	3.2%
Total Federal & State Sources	$4,287	$3,203	$1,084	33.8%
Nongeneral Funds Distributions/Direct Receipts:				
Refund Fund				
Personal Income Tax	($270)	($198)	($72)	36.4%
Corporate Income Tax	($21)	(4)	($17)	425.0%
Fund for Advancement of Education	$0	(39)	$39	-100.0%
Commitment to Human Services Fund	$0	(39)	$39	-100.0%
LGDF--Direct from PIT	($135)	0	($135)	N/A
LGDF--Direct from CIT	($6)	0	($6)	N/A
Downstate Pub/Trans--Direct from Sales	($46)	0	($46)	N/A
Subtotal General Funds	$3,809	$2,923	$886	30.3%
Short-Term Borrowing	$0	$0	$0	N/A
Interfund Borrowing	$0	$0	$0	N/A
Income Tax Bond Fund Transfer	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$0	$0	$0	N/A
Total General Funds	$3,809	$2,923	$886	30.3%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 2-Feb-18

GENERAL FUNDS RECEIPTS: YEAR TO DATE

FY 2018 vs. FY 2017

($ million)

Revenue Sources	FY 2018	FY 2017	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$11,107	$8,355	$2,752	32.9%
Corporate Income Tax (regular)	1,180	611	$569	93.1%
Sales Taxes	4,944	4,908	$36	0.7%
Public Utility Taxes (regular)	505	485	$20	4.1%
Cigarette Tax	205	198	$7	3.5%
Liquor Gallonage Taxes	108	109	($1)	-0.9%
Vehicle Use Tax	16	17	($1)	-5.9%
Inheritance Tax	195	165	$30	18.2%
Insurance Taxes and Fees	206	199	$7	3.5%
Corporate Franchise Tax & Fees	128	151	($23)	-15.2%
Interest on State Funds & Investments	37	16	$21	131.3%
Cook County IGT	56	56	$0	0.0%
Other Sources	353	328	$25	7.6%
Subtotal	$19,040	$15,598	$3,442	22.1%
Transfers				
Lottery	380	398	($18)	-4.5%
Riverboat transfers & receipts	201	199	$2	1.0%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	0	0	$0	N/A
Fund sweeps	207	0	$207	N/A
Other	474	333	$141	42.3%
Total State Sources	$20,302	$16,528	$3,774	22.8%
Federal Sources	$3,846	$1,322	$2,524	190.9%
Total Federal & State Sources	$24,148	$17,850	$6,298	35.3%
Nongeneral Funds Distributions/Direct Receipts:				
Refund Fund				
Personal Income Tax	($1,089)	($937)	($152)	16.2%
Corporate Income Tax	($207)	(106)	($101)	95.3%
Fund for Advancement of Education	$0	(241)	$241	-100.0%
Commitment to Human Services Fund	$0	(241)	$241	-100.0%
LGDF--Direct from PIT	($546)	0	($546)	N/A
LGDF--Direct from CIT	($60)	0	($60)	N/A
Downstate Pub/Trans--Direct from Sales	($220)	0	($220)	N/A
Subtotal General Funds	$22,026	$16,325	$5,701	34.9%
Short-Term Borrowing	$0	$0	$0	N/A
Interfund Borrowing	$354	$0	$354	N/A
Income Tax Bond Fund Transfer	$2,500	$0	$2,500	N/A
Budget Stabilization Fund Transfer	$0	$0	$0	N/A
Total General Funds	$24,880	$16,325	$8,555	52.4%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 2-Feb-18