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March 15, 2011

MEMORANDUM

TO: The Honorable Pat Quinn, Governor, State of Illinois
The Honorable Michael Madigan, Speaker of the House of Representatives
The Honorable John Cullerton, President of the Senate
The Honorable Tom Cross, Minority Leader of the House of Representatives
The Honorable Christine Radogno, Minority Leader of the Senate

FROM: Dan R. Long, Executive Director 

RE: FY 2012 GAAP (Generally Accepted Accounting Principles) Report

Introduction

Included in this memorandum are the Commission on Government Forecasting and Accountability's revenue estimates formulated on a modified accrual basis in accordance with generally accepted accounting principles (GAAP). Public Act 90-0479, a synopsis of which is included in the Appendix, requires modified accrual basis estimates for the general funds, the Agricultural Premium Fund, the Road Fund, and the Motor Fuel Tax Fund.

Recognition of revenue and liability in the fiscal year of collection or payment has been the premise for formulating the Illinois budget and is known as cash basis budgeting. Estimates formulated on a modified accrual basis instead recognize revenue and liability in the fiscal year of accrual and provide an alternative perspective to the budget process.

Modified Accrual Basis Estimates

The Commission on Government Forecasting and Accountability estimates that fiscal year 2011 revenue to the general funds on a modified accrual basis will be \$37.9 million lower than the cash basis estimate. The differential between the two estimates is largely because lapse period collections in FY 2012 are expected to be slightly lower than FY 2011 lapse

period collections, particularly in the area of federal sources. Lapse period collections from the income taxes are expected to increase in FY 2012 due to the income tax increases that became effective January 1, 2011. However, this increase from income tax related lapse period spending is offset by the expected decrease in lapse period-related spending from federal sources.

The Commission estimates that there will be no difference between modified accrual basis revenue to the Agricultural Premium Fund, the Road Fund, and the Motor Fuel Tax Fund in fiscal year 2012.

The following table summarizes the Commission’s estimates, while tables at the back of this document provide more detail of the analysis.

FY 2012 REVENUE ESTIMATES			
Summary Table			
(\$ in Millions)			
Estimated Revenue by Fund	CGFA Cash Basis vs. Modified Accrual Basis		
	CGFA Base FY 2012 Cash Basis	CGFA Base FY 2012 Modified Accrual Basis	Difference
General Funds	\$34,882.0	\$34,844.1	-\$37.9
Agricultural Premium Fund	\$25.9	\$25.9	\$0.0
Road Fund	\$3,100.0	\$3,100.0	\$0.0
Motor Fuel Tax Fund	\$1,265.0	\$1,265.0	\$0.0

The Governor’s Office of Management and Budget included their modified accrual revenue estimates in the FY 2012 Budget Book. The GOMB’s FY 2012 cash basis revenue estimate is \$33,932 million. This estimate is \$950 million lower than the Commission’s comparable cash basis estimate of \$34,882 million.

Much of this difference is due to the Commission anticipating a significant lagged impact of the recently passed income tax increase on individual income tax receipts. Because of the January 13, 2011 enactment date of the tax increase and the fact that the tax increase was retroactive to January 1, 2011, businesses were not immediately able to adjust withholding tables to reflect this tax increase. In lieu of only minor increases in January 2011 tax receipts, it is assumed that these taxes owed will be made up in final payments in Spring 2012, which will be receipted in FY 2012. The Commission estimates the value of this timing factor to be approximately \$548 million.

The GOMB’s FY 2012 General Funds estimate on a modified accrual basis is \$34,287 million, which is \$355 million higher than their FY 2012 cash basis estimate.

Methodology for Modified Accrual Basis Revenue Estimates

In general, the Commission on Government Forecasting and Accountability's modified accrual revenue estimates were formulated as follows:

- 1) obtained historical amounts of revenue accrued in a given fiscal but received during July and August of the following fiscal year, or later during the following fiscal year in the case of federal reimbursements associated with Section 25 of the State Finance Act;
- 2) used historical data to calculate the percentage of a fiscal year's cash basis receipts attributable to the previous fiscal year;
- 3) used data described above and additional insight from relevant agencies to formulate estimates of accrued revenue to be received after the close of fiscal years 2011 and 2012;
- 4) used these estimates of accrued revenue received after the close of fiscal years 2011 and 2012 to convert fiscal year 2012 cash basis revenue estimates to modified accrual basis estimates by subtracting fiscal year 2012 cash receipts attributable to fiscal year 2011 and adding fiscal year 2013 cash receipts attributable to fiscal year 2012.

It should also be noted that:

- 1) for federal revenues to the general funds, the Governor's Office of Management and Budget estimates were used given GOMB's role in coordinating federal receipts and the estimates' similarity to such receipts in previous fiscal years;
- 2) in accordance with Public Act 90-0479, the Commission also formulated fund balance estimates – however, GOMB's estimated fiscal year 2012 beginning cash basis fund balances were utilized for the Agricultural Premium Fund, the Road Fund, and the Motor Fuel Tax Fund;
- 3) the Governor's Office of Management and Budget's estimates of expenditures were utilized for fund balance calculations given the Commission does not routinely estimate expenditures.

Background

Each year, the Comptroller's office produces the *Comprehensive Annual Financial Report* (CAFR). The CAFR is the State's official annual report, which provides the readers with the financial position of the State as of June 30 each year, and results of operations during the fiscal year. The report is intended to provide the State's taxpayers, managers, investors, creditors, lawmakers, and other users with information in accordance with GAAP. The State of Illinois' daily activities are operated on a "cash basis," where bills are paid with the available balances of cash on hand.

Cash basis budgets are based on estimates of the cash balance available at the beginning of the fiscal year, the amount of revenue actually received during July through June of the fiscal year, the amount of expenditures actually made during July through June of the fiscal year, and the ending cash balance. Budgeting on a modified accrual basis instead recognizes revenues and expenditures as they accrue.

Funds

Below is a brief description of the funds for which modified accrual estimation is required.

- General Funds - The general funds support operations and programs of numerous State agencies with revenues from various sources, the largest of which include income taxes, sales taxes, and federal sources.
- Agricultural Premium Fund – The Agricultural Premium Fund has been used to meet numerous expenses including those of the Racing Board, the State Fairs, and the Department of Agriculture. Revenues to this fund include a portion of the horse racing privilege tax, transfers from the General Revenue Fund (GRF), and other miscellaneous sources such as proceeds from the sale of advertising at the DuQuoin State Fair and fees paid to the State Police for racetrack investigative services.
- Road Fund – Uses of the Road Fund have included retiring principal and interest on highway construction bonds issued by the State, administering certain chapters of the vehicle code, meeting administrative expenses of the Illinois Department of Transportation, construction of highways and bridges, and patrolling and policing highways. Examples of Road Fund revenue sources are motor vehicle and operator license fees and transfers from the Motor Fuel Tax Fund.
- Motor Fuel Tax Fund – The Motor Fuel Tax Fund is a holding fund for all revenue to the State from the motor fuel tax. Revenue is used for such purposes as deposits to the State Boating Act Fund, deposits to the Grade Crossing Protection Program, and for State and local road programs, including a deposit to the Road Fund.

FY 2012 GAAP REPORT

Supplementary Notes March, 2011

Cash Basis Revenue Estimate vs. Modified Accrual Basis Revenue Estimate

- It is estimated that there will be a relatively small difference between FY 2012 revenue measured on a cash basis and FY 2012 revenue measured on a modified accrual basis. The modified accrual basis general funds estimate is \$37.9 million lower than the cash basis estimate.
- The differential between the two estimates is largely because lapse period collections in FY 2012 are expected to be slightly lower than FY 2011 lapse period collections, particularly in the area of federal sources. Lapse period collections from the income taxes are expected to increase in FY 2012 due to the income tax increases that became effective January 1, 2011. However, this increase from income tax related lapse period spending is offset by the expected decrease in lapse period-related spending from federal sources.
- Fund balance estimates were made utilizing both cash basis and modified accrual basis revenue and expenditure estimates.
 - The cash basis fund balance calculation starts with an estimated FY 2011 beginning cash balance of \$130 million. The FY 2012 beginning cash balance is calculated by adding the Commission's FY 2011 estimated cash basis revenues to the FY 2011 beginning cash balance and by subtracting GOMB's FY 2011 cash basis spending estimate.

FY 2011 Beginning Cash Balance:	\$130 million
FY 2011 CGFA Est. Base Cash Revenue:	\$30,481 million
FY 2011 Est. Cash Spending:	(\$32,787 million)
FY 2011 Ending/FY 2012 Beginning Cash Balance:	(\$2,176 million)

The above beginning cash balance of -\$2,176 million is simply the calculation of the FY 2011 beginning cash balance plus cash basis revenues less cash basis spending. By definition, the Comptroller's Office would not allow the cash balance estimate to fall to negative territory. Instead, unpaid bills would be pushed into the following year. It is unclear, however, how low the Comptroller will allow the end-of-year cash balance to fall.

The “modified accrual basis” fund balance calculation starts by adjusting the estimated FY 2012 beginning balance for outstanding revenues and liabilities not accounted for in the cash basis beginning balance.

FY 2011 Ending/FY 2012	
Beginning Cash Balance:	(\$2,176 million)
FY 2012 Cash Receipts	
Attributable to FY 2011:	\$1,716.9 million
FY 2011 Lapse Period/ Section 25 Spending:	(\$6,444.0 million)
FY 2011 Ending/FY 2012	
Beginning Modified Accrual Balance:	(\$6,903.1 million)

The estimated FY 2012 modified accrual basis ending balance is calculated by adding estimates of FY 2012 modified accrual basis revenue and subtracting GOMB estimated FY 2012 expenditures, adjusted to a modified accrual basis by subtracting estimates of prior year lapse period and Section 25 spending and adding estimates of current year lapse period and Section 25 spending.

FY 2012 Estimated Beginning	
Modified Accrual Balance:	(\$6,903.1 million)
FY 2012 Estimated Modified	
Accrual Revenue:	\$34,844.1 million
FY 2012 Estimated Modified	
Accrual Expenditures:	(\$35,760.0 million)
FY 2012 Estimated Ending	
Modified Accrual Balance*:	(\$7,819.0 million)

The estimated FY 2012 modified accrual basis ending balance results in a deficit of \$7.8 billion. This figure is nearly \$4.8 billion lower than the estimated cash basis ending balance. This is mostly because FY 2011 lapse period / Section 25 spending is anticipated to be much higher than FY 2012 cash receipts attributable to FY 2011.

Budget Deficit Clarification

It should be noted that the Section 25 provision allows the State to pay any remaining Medicaid bills from one fiscal year with monies from next year’s appropriations. Because of this, the budget can still appear balanced on a cash basis (or have a lower reported deficit), even though the State may not have sufficient funding for the Medicaid program. On a modified accrual basis, Section 25 liabilities from one fiscal year that are pushed off into the next fiscal year must be counted in the year that the liability is accrued. As a result, when including these Section 25 liabilities, the modified accrual deficit will be shown to be higher than the cash basis deficit.

CGFA FY 2012 REVENUE ESTIMATE - ANALYSIS OF CASH BASIS VS. MODIFIED ACCRUAL BASIS
 (General Funds - \$'s in Millions)
 March '11

<u>Estimated General Funds Revenue</u>	<u>FY 2012 Cash Basis Collections</u>	<u>FY 2011 Lapse Period Collections</u>	<u>FY 2012 Lapse Period Collections</u>	<u>FY 2012 GAAP Basis</u>		
<u>State Taxes</u>						
Individual Income Tax	\$17,300.0	\$177.8	\$251.9	\$17,374.1		
Corporate Income Tax	\$3,358.0	\$73.4	\$103.2	\$3,387.8		
Sales Taxes	\$6,739.0	\$364.3	\$366.6	\$6,741.3		
Public Utility Taxes	\$1,136.0	\$6.0	\$6.1	\$1,136.1		
Cigarette Tax	\$355.0	\$0.0	\$0.0	\$355.0		
Liquor Gallonage Taxes	\$161.0	\$17.6	\$17.8	\$161.2		
Vehicle Use Tax	\$29.0	\$0.0	\$0.0	\$29.0		
Inheritance Tax	\$196.0	\$0.0	\$0.0	\$196.0		
Insurance Taxes & Fees	\$315.0	\$0.0	\$0.0	\$315.0		
Corporate Franchise Tax & Fees	\$202.0	\$0.0	\$0.0	\$202.0		
Interest on State Funds & Investments	\$35.0	\$0.0	\$0.0	\$35.0		
Cook County Intergovernmental Transfer	\$244.0	\$0.0	\$0.0	\$244.0		
Other Sources	\$379.0	\$6.9	\$7.3	\$379.4		
Subtotal	\$30,449.0	\$645.9	\$752.9	\$30,556.0		
<u>Transfers</u>						
Lottery	\$645.0	\$0.0	\$0.0	\$645.0		
Gaming Fund Transfer	\$357.0	\$0.0	\$0.0	\$357.0		
Proceeds from sale of 10th License	\$75.0	\$0.0	\$0.0	\$75.0		
Other	\$614.0	\$0.0	\$0.0	\$614.0		
Total State Sources	\$32,140.0	\$645.9	\$752.9	\$32,247.0		
Total Federal Sources	\$4,844.0	\$1,101.2	\$968.8	\$4,711.6		
Total Federal & State Sources	\$36,984.0	\$1,747.1	\$1,721.7	\$36,958.6		
<u>Refund Fund</u>						
Personal Income Tax	(\$1,514.0)	(\$17.3)	(\$24.6)	(\$1,521.2)		
Corporate Income Tax	(\$588.0)	(\$12.8)	(\$18.1)	(\$593.2)		
Base General Funds Revenue	\$34,882.0	-	\$1,716.9	\$34,844.1		
Regular and Section 25 Expenditures	(\$35,760.0)	-	(\$6,444.0)	(\$35,760.0)		
FY 2012 Estimated General Funds Balance	Beginning Balance	Revenue	Expenditures	Ending Balance		
Cash Basis	(\$2,176.0)	+	\$34,882.0	+	(\$35,760.0)	(\$3,054.0)
FY 2012 Cash Receipts Attributable to FY 2011	\$1,716.9					
FY 2011 Lapse Period / Section 25 Spending	(\$6,444.0)					
Modified Accrual Basis	(\$6,903.1)	+	\$34,844.1	+	(\$35,760.0)	(\$7,819.0)
NOTES:						
FY 2012 estimated beginning modified accrual balance was derived by subtracting the Governor's Office of Management and Budget's (GOMB) FY 2011 lapse period and other Section 25 spending estimate from the estimated beginning FY 2012 cash balance and adding the estimated FY 2012 cash receipts attributed to FY 2011.						
Fund balances are calculated using the Governor's Office of Management and Budget spending estimates as the Commission on Government Forecasting and Accountability does not formulate estimates of expenditures.						
The GOMB's spending estimates were converted to modified accrual basis by subtracting prior year lapse period and other estimated Section 25 spending and adding current year lapse period and other Section 25 spending. Excluded from the revenue and spending estimates are various revenue/expenditure changes proposed by the Governor. Budget Stabilization Fund transfers are also not included.						

FY 2012 REVENUE ESTIMATES - ANALYSIS OF CASH BASIS VS. MODIFIED ACCRUAL BASIS
Agricultural Premium Fund, Road Fund, & Motor Fuel Tax Fund
 \$'s in Millions

Agricultural Premium Fund

	FY 2012		FY 2012 Cash Receipts Attributable to FY 2011		FY 2013 Cash Receipts		FY 2012	
	<u>Cash Basis</u>	-	<u>\$'s</u>	<u>% of FY 2011 Cash Receipts</u>	+	<u>Attributable to FY 2012 - \$'s</u>	=	<u>Modified Accrual Basis</u>
Estimated Revenue	\$25.9		\$4.0	15.4%		\$4.0		\$25.9
Estimated Fund Balance	FY 2012 Beginning Balance		Revenue			Expenditures		FY 2012 Ending Balance
Cash Basis	\$11.2	+	\$25.9		-	\$22.6	=	\$14.5
Modified Accrual Basis	\$11.2	+	\$25.9		-	\$22.6	=	\$14.5

Road Fund

	FY 2012		FY 2012 Cash Receipts Attributable to FY 2011		FY 2013 Cash Receipts		FY 2012	
	<u>Cash Basis</u>	-	<u>\$'s</u>	<u>% of FY 2011 Cash Receipts</u>	+	<u>Attributable to FY 2012 - \$'s</u>	=	<u>Modified Accrual Basis</u>
Estimated Revenue	\$3,100.0		\$517.0	16.7%		\$517.0		\$3,100.0
Estimated Fund Balance	FY 2012 Beginning Balance		Revenue			Expenditures		FY 2012 Ending Balance
Cash Basis	\$663.6	+	\$3,100.0		-	\$3,315.0	=	\$448.6
Modified Accrual Basis	\$663.6	+	\$3,100.0		-	\$3,315.0	=	\$448.6

Motor Fuel Tax Fund

	FY 2012		FY 2012 Cash Receipts Attributable to FY 2011		FY 2013 Cash Receipts		FY 2012	
	<u>Cash Basis</u>	-	<u>\$'s</u>	<u>% of FY 2011 Cash Receipts</u>	+	<u>Attributable to FY 2012 - \$'s</u>	=	<u>Modified Accrual Basis</u>
Estimated Revenue	\$1,265.0		\$211.2	16.7%		\$211.2		\$1,265.0
Estimated Fund Balance	FY 2012 Beginning Balance		Revenue			Expenditures		FY 2012 Ending Balance
Cash Basis	\$113.0	+	\$1,265.0		-	\$1,240.0	=	\$138.0
Modified Accrual Basis	\$113.0	+	\$1,265.0		-	\$1,240.0	=	\$138.0

NOTES:

- * The Governor's Office of Management and Budget (GOMB) estimated FY 2012 beginning cash balances are utilized for the Agricultural Premium Fund, the Road Fund, and the Motor Fuel Tax Fund.
- * FY 2012 estimated beginning modified accrual balances were assumed to equal FY 2012 estimated beginning cash balances.
- * Fund balance calculations utilize the GOMB's spending estimates as the CGFA does not formulate estimates of expenditures.
- * Estimates of modified accrual basis spending equal the GOMB's estimates of cash basis spending as FY 2011 and FY 2012 lapse period spending are assumed to be equal.

APPENDIX

Synopsis of Public Act 90-0479 (15 ILCS 20/50-5), Pertaining to Budget Formulation

Both Public Act 90-0479 (15 ILCS 20/50-5), effective August of 1997, requires that the State budget, both underlying revenue and spending estimates, for the following funds be formulated on a modified accrual basis in concert with generally accepted accounting principles (GAAP):

- 1) General Funds;
- 2) Agricultural Premium Fund;
- 3) Road Fund;
- 4) Motor Fuel Tax Fund.

Revenue estimates for a fiscal year are to include:

- 1) the estimated beginning fund balance;
- 2) plus the revenues estimated to be received from July through June of the fiscal year;
- 3) plus receipts due to the state as of June 30 but expected to be collected during the lapse period;
- 4) minus the receipts collected during the first two months of the fiscal year that are attributable to the previous fiscal year;
- 5) plus federal reimbursements associated with State expenditures made in accordance with Section 25 of the State Finance Act.

Spending estimates for a fiscal year are to include:

- 1) expenditures estimated to be made from July through June of the fiscal year;
- 2) plus expenditures estimated to be incurred in the fiscal year but paid in the following fiscal year;
- 3) minus costs paid in the fiscal year which were incurred in the previous fiscal year.

Both revenue and expenditure estimates for a fiscal year are to include all transfers between funds that are based on revenues received or costs incurred during the fiscal year.

The Commission on Government Forecasting and Accountability is to prepare revenue and fund transfer estimates in accordance with Public Act 90-0479 each year. These estimates are to be reported to the General Assembly and the Governor.

For other funds not specified in Public Act 90-0479, proposed expenditures and appropriations are not to exceed estimated available funds for the budgeted fiscal year.

BACKGROUND

The Commission on Government Forecasting and Accountability (CGFA), a bipartisan, joint legislative commission, provides the General Assembly with information relevant to the Illinois economy, taxes and other sources of revenue and debt obligations of the State. The Commission's specific responsibilities include:

- 1) Preparation of annual revenue estimates with periodic updates;
- 2) Analysis of the fiscal impact of revenue bills;
- 3) Preparation of "State Debt Impact Notes" on legislation which would appropriate bond funds or increase bond authorization;
- 4) Periodic assessment of capital facility plans;
- 5) Annual estimates of public pension funding requirements and preparation of pension impact notes;
- 6) Annual estimates of the liabilities of the State's group health insurance program and approval of contract renewals promulgated by the Department of Central Management Services;
- 7) Administration of the State Facility Closure Act.

The Commission also has a mandate to report to the General Assembly ". . . on economic trends in relation to long-range planning and budgeting; and to study and make such recommendations as it deems appropriate on local and regional economic and fiscal policies and on federal fiscal policy as it may affect Illinois. . . ." This results in several reports on various economic issues throughout the year.

The Commission publishes several reports each year. In addition to a Monthly Briefing, the Commission publishes the "Revenue Estimate and Economic Outlook" which describes and projects economic conditions and their impact on State revenues. The "Bonded Indebtedness Report" examines the State's debt position as well as other issues directly related to conditions in the financial markets. The "Financial Conditions of the Illinois Public Retirement Systems" provides an overview of the funding condition of the State's retirement systems. Also published are an Annual Fiscal Year Budget Summary; Report on the Liabilities of the State Employees' Group Insurance Program; and Report of the Cost and Savings of the State Employees' Early Retirement Incentive Program. The Commission also publishes each year special topic reports that have or could have an impact on the economic well-being of Illinois. All reports are available on the Commission's website.

These reports are available from:

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<http://www.ilga.gov/commission/cgfa2006/home.aspx>