Comptroller Mendoza's Plan Aims To Rebuild Illinois' Rainy-Day Fund

by Adam Schuster
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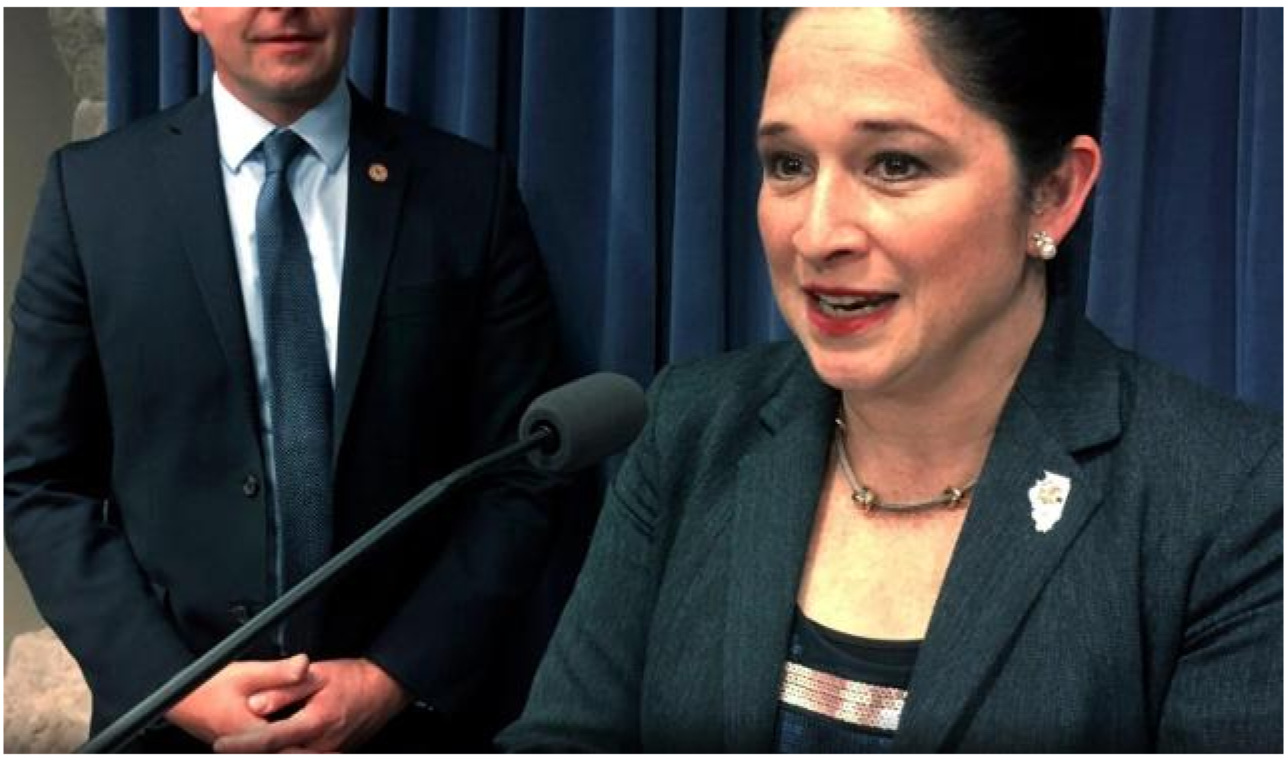

SPRINGFIELD - Automatic transfers into Illinois' rainy-day reserves could help when another fiscal crisis similar to COVID-19 happens.

When COVID-19 hit Illinois, there was enough emergency cash on hand to run the state for about 15 minutes. Illinois' Comptroller Susana Mendoza is pushing House Bill 4118 to work toward making sure the rainy-day fund has something in it during the next crisis.

"It's the fiscally responsible thing to do," Mendoza said in a statement reported by Bond Buyer.

Illinois and New Jersey were the states least prepared for a recession prior to the COVID-19 crisis, Illinois after decades of poor financial performance. Mendoza said Illinois must do a better job to prepare for future emergencies and rebuild its rainy-day fund.

The bill to implement her plan was filed on Aug. 5 by state Rep. Michael Halpin, D-Rock Island. It would trigger monthly transfers into the Budget Stabilization Fund and Pension Stabilization Fund whenever the bill backlog is less than $3 billion and the state's reserves are less than 5% of the general funds budget. Mendoza estimates a backlog lower than $3 billion is the point when the state pays its bills within a 30-day cycle, a customary business practice.

The bill creates an identical requirement to make a $200 million payment to the state's pension stabilization fund when the backlog drops below $3 billion. The pension stabilization fund was created in 2006 based on the premise the state could solve its pension crisis by making supplemental payments whenever the legislature produced a budget surplus of at least 1%. The state has run deficits each year since 2001 and the fund currently sits empty.

While an automatic trigger for rainy-day fund deposits is fiscally responsible, an automatic trigger for higher pension payments is the wrong way to address that crisis.

Illinois state and local governments already spend the largest share of their revenue on pensions of all 50 states, more than double the national average. But despite its first-in-the-nation spending, Illinois also carries the largest pension debt burden and has the biggest gap between what it currently pays and what it would take to stop the debt from growing.

The solution to Illinois' pension crisis is a constitutional amendment to allow the growth of future benefits to be brought in line with what Illinois' governments, and their taxpayers, can truly afford. Throwing more money at a broken system will simply mean further crowd out of valuable government services that have already been cut by 14% as pension spending has exploded by 533%.

On its own, the new rainy-day fund procedures proposed in Mendoza's legislation would be a big improvement.

Illinois has historically struggled with its finances in multiple ways: rising pension debt, fund sweeps and borrowing schemes, and run-away spending because of unsustainable pension costs. Those are a few of the contributing reasons for the state's 21 years of unbalanced budgets and poorest-in-the-nation credit rating, despite recent upgrades.

Another manifestation of the state's financial woes is its poor preparation for emergencies such as the COVID-19 pandemic. In March, fiscal watchdog the Volcker Alliance gave Illinois a D for reserve funds. The report noted the state's minimal rainy-day fund balances left it especially vulnerable to financial disasters. During the COVID-19 pandemic, Illinois was the only state to borrow from the Federal Reserve; it had to do so twice for a total of $3.2 billion.

When the crisis first hit in March 2020, Illinois had $1.19 million in emergency funds: enough to run the state for about 15 minutes. At one point in 2020, the reserve fund was down to $60,000, less than a single state household's median income and enough for 30 seconds. Mendoza said the fund increased to $9.3 million currently but noted it was minuscule in comparison to Illinois' $42 billion budget for fiscal year 2022 and enough to operate for a little less than two hours.

The U.S. state median was 28.5 days' worth of general fund spending at the start of fiscal year 2021, a Pew Charitable Trusts article in May found. Experts recommend states save 5 to 10% of their annual general revenues in their rainy day funds. HB 4118 keeps the state goal of having 5% of its general fund's revenues held in the budget stabilization fund, but strengthens procedures for reaching that goal.

Judging by the state's financial record, maintaining a bill backlog of less than $3 billion will be a challenge. The $16.7 billion record for the bill backlog was reached in 2017 during the state budget impasse. Mendoza told rating agencies in April Illinois' backlog reached a years-long low of $3.5 billion, but it would still not be enough to trigger rainy-day deposits under the proposed legislation. As of Aug. 27, the backlog was again growing and reached $3.85 billion.

The drop in the bill backlog is less meaningful than it might seem for two reasons. First, much of the debt has been moved to other forms of short-term debt through bonds sold to lower the bill backlog, inter-fund borrowing, and recent borrowing from the Federal Reserve. Second, the improvement rests on the back of a flood of federal aid that will run dry within a few years.

With related debt added to the bill backlog, state projections show short-term debt on track to exceed the prior $16.7 billion peak by June 2023.

Reducing the bill backlog is still a positive development, because it means vendors won't be left waiting without payment as long and because the state will pay lower interest on other forms of short-term debt than it does on the backlog. Under state law, most bills not paid within 90 days accrue interest of 1% per month and health care bills accrue 9% interest per year if not paid within 30 days.

Illinois must adopt significant financial reforms, starting with allowing people to vote on an amendment for structural pension reform. If enacted, the rainy-day fund rules will not take effect until fiscal year 2024. This would allow lawmakers time to adopt pension reform and other budget measures needed to end the state's two decades of spending beyond its means.

Only when the state is responsibly aligning its revenues and expenditures in the long term can it hope to end short-term debt and give taxpayers confidence it is ready to face the next unknown emergency.