STATE OF ILLINOIS FY2026 BUDGET ROADMAP

LANDSCAPE, ISSUES, AND RECOMMENDATIONS

THE CIVIC FEDERATION

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February 12, 2025

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EXECUTIVE SUMMARY

The State of Illinois (Illinois or the “State”) faces ongoing financial challenges, including a high tax burden, structural budget deficits, and legacy pension obligations, all of which put a strain on the state’s long-term sustainability. While the State has made progress in stabilizing its budget in recent years, Illinois lacks a long-term strategic framework to ensure consistent revenue growth, efficient spending, and economic competitiveness.

In this report, the Civic Federation presents a comprehensive set of solutions for lawmakers to consider over the next several years—not as immediate fixes for the upcoming fiscal year 2026 (FY2026) budget deficit but as a roadmap for long-term sustainability. Instead of approaching each budget year with a short-term lens, the Civic Federation calls on the Governor and Illinois General Assembly members to conduct a holistic re-evaluation of the State’s fiscal structure and implement a more strategic approach to budgeting. Our recommendations focus on tax modernization, performance-based budgeting improvements, and greater fiscal transparency, with the goals of promoting economic growth and sustainable public investments.

At its core, the State’s outdated tax structure fails to align with the modern economy, placing an excessive burden on certain taxpayers while discouraging business investment. The stagnant revenue base has not kept pace with rising spending demands, exacerbating budgetary pressures. Unclear performance-based budgeting metrics and poor systemic decision-making further complicate spending prioritization. Persistent pension liabilities continue to strain finances, requiring urgent reforms to ensure fiscal stability. Meanwhile, insufficient reserves leave the state vulnerable to economic downturns, and a lack of transparency in policymaking undermines public trust and accountability in the budgeting process. Addressing these issues through strategic tax modernization, improved budgetary planning, and greater fiscal transparency is essential for Illinois’ long-term financial health.

To address these challenges and establish a path toward fiscal sustainability, the Civic Federation urges Illinois lawmakers to consider the following key reforms:

Modernize Illinois' Tax Structure: Illinois’ tax structure must align with the modern economy. As part of a broader examination of the tax structure to generate sustainable revenue growth, Illinois should consider expanding the sales tax base to include services, conduct a systematic review of tax exemptions, evaluate and develop a sustainable revenue structure, and review and consolidate Special Funds.

Strengthen the Budgeting Process through Strategic Financial Planning: The State should improve the transparency of the strategic budget planning process and conduct long-term planning and evaluation. As part of this, the State should:

- **Enhance the performance-based budgeting process** to ensure spending decisions are data-driven and aligned with measurable outcomes;

- **Address pension liabilities responsibly** by avoiding unnecessary Tier 2 benefit enhancements and only enacting changes targeted at compliance with Social Security Safe Harbor guidelines;
- **Increase the level of reserves** to constitute a more robust rainy day fund;
- **Support local governments** by collaborating with local government entities on funding matters; and
- **Improve transparency** in state decision-making to ensure a more cooperative and open policy-making process.

Illinois must move beyond short-term budget fixes and adopt a strategic, long-term approach to fiscal management. By modernizing its tax system, improving budget decision-making, ensuring pension sustainability, and increasing transparency, the State can promote economic growth, attract investment, and ensure financial stability for future generations.

This report is intended to spur legislative discussions and policy actions that will strengthen Illinois' fiscal health for this year and the years ahead.

INTRODUCTION

Over the past several years, the State of Illinois has made significant progress in stabilizing its operating finances, with four of the past five fiscal years ending in budget surpluses. This was largely driven by a strong economic recovery from the pandemic and passing less structurally imbalanced budgets than in previous years. During this timeframe, the State budget benefited from the assistance of federal pandemic funding and stronger than projected revenue performance. Additionally, the State has prioritized payment of outstanding debt, including COVID-related borrowing, interfund borrowing, and obligations to the Unemployment Insurance Trust Fund. The State has also made significant progress in reducing its prior backlog of unpaid bills inherited from the prior Administration, thereby bringing payment schedules closer to normal. At the same time, it has increased pension contributions and gradually built its "rainy day" budgetary reserves.

However, while much progress has been made, there is more that the State must do to address its fiscal challenges through strategic and long-term financial planning to alleviate structural imbalance and budget pressures in future budgets. Potential federal funding shifts due to the new administration's policy priorities is a serious concern for state revenue that supports critical services. But regardless of external factors, the core work the State needs to do remains the same.

The projected $3.2 billion deficit heading into the 2026 fiscal year beginning July 1, 2025,[1] demonstrates the need for a more holistic and strategic approach to the annual budget process. To close the deficit, the State must cut spending and find additional revenues. Several one-time revenues used to close last year's deficit are now exhausted, and without a revenue system set up for growth to keep pace with spending needs, there are no easy or obvious answers.

Instead of approaching each budget year with a short-term lens, the Civic Federation calls on the Governor and Illinois General Assembly members to conduct a holistic re-evaluation of the State's entire fiscal structure and implement a more strategic approach to budgeting. This would involve a more thorough and intentional planning process that reviews Illinois' tax structure, sets up systems to regularly re-examine State tax exemptions, implements accountable and transparent evaluations of performance-based budgeting, increases transparency, and provides sufficient support to local governments whose services are necessary complements to the shared objective of fostering equitable, sustained economic growth and opportunity statewide. To help ensure that spending decisions are made based on evaluation and outcomes, the State should also make more effective and extensive use of its performance-based budgeting system, Budgeting for Results.[2]

[1] Governor's Office of Management and Budget, Illinois Economic and Fiscal Policy Report, November 2024.
[2] Budgeting for Results Commission.

Civic Federation's State Budgeting Principles

The Civic Federation offers the following budgeting principles as a framework to guide State lawmakers and the Governor's Office in a long-term financial planning process. The State budget should:

- Ensure that annual operating budgets are structurally balanced;
- Remain on a normal bill payment schedule;
- Control and contain annual spending growth (for example, by limiting growth to no more than the inflation rate) and ensure that discretionary spending is guided by outcomes-based budgeting;
- Avoid drastic revenue cliffs;
- Broaden the tax base to provide sustainable revenue sources responsive to the economy and business structures;
- Budget to foster stability and capacities for local governments;
- Set aside reserves for an adequate rainy day fund;
- Address Illinois' long-term challenges, such as unfunded pension liabilities and infrastructure needs; and
- Work toward an economic and population growth-oriented tax structure.

STATE FISCAL AND ECONOMIC LANDSCAPE

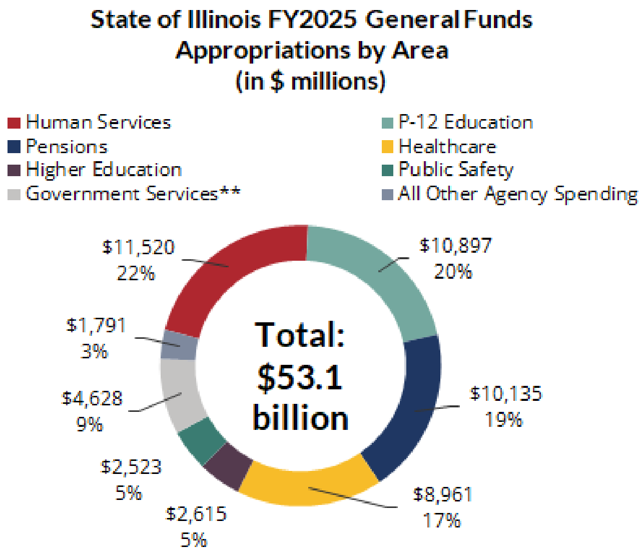
Illinois faces significant financial challenges. In combination with other units of government, the tax burden is comparatively high, with distortions in how that burden is distributed, and its fiscal policies generally lack long-term sustainability. The State's tax structure creates disincentives that hinder efforts to attract new residents, businesses, and expand and diversify economic opportunities. These challenges in part originate from and are compounded by legacy financial problems—most notably pension obligations and structural budget deficits—that require strategic, holistic solutions to ensure future fiscal stability and growth.

To address these issues, Illinois should adopt a comprehensive approach that includes long-term and strategic planning, the expansion of performance-based budgeting, and meaningful tax restructuring. By aligning revenue with the structure of the state's economy, and balancing revenue growth with strategically prioritized spending needs in an accountable, equitable and sustainable manner, the State can reduce distortions in the tax system and avoid disproportionately burdening specific groups or sectors. Such reforms would not only support Illinois' fiscal health but also create an environment that fosters population growth, business investment, and expanded economic opportunity. Together, these measures can resolve existing financial challenges while promoting long-term stability and sustainability at all levels of government.

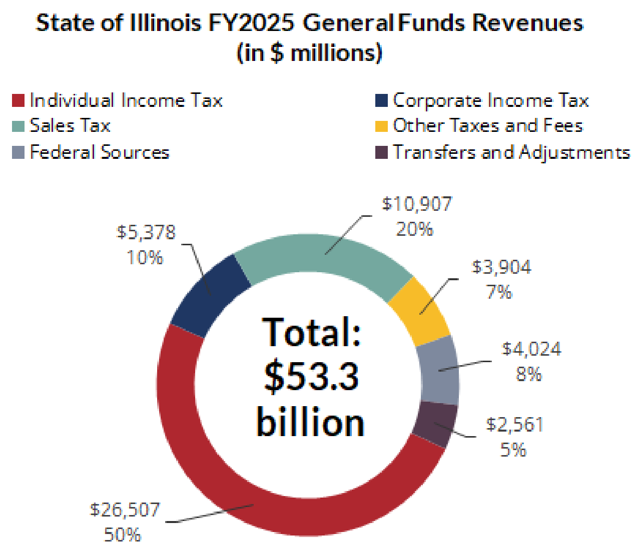
To help inform the discussion of fiscal policy processes and decision-making, the Civic Federation begins with a brief overview of Illinois' current financial situation, economic landscape, and tax structure.

Fiscal Landscape

The State of Illinois adopted a General Funds budget for the current 2025 fiscal year of $53.1 billion.[3] The budget was supported by $53.3 billion in revenues, leaving a surplus of $200 million that was pledged to the State's rainy day reserve fund. The revenue and expenditure breakouts are shown in the following charts.



*Does not include unspent appropriations or transfers out of General Funds.
**Includes employee and group health insurance.
Source: State of Illinois FY2025 Enacted Budget Financial Walkdown.



Source: State of Illinois FY2025 Enacted Budget Financial Walkdown.

For the fifteen fiscal years prior to 2022, the State ran a structural deficit. The FY2025 adopted budget followed three years of budget surpluses funded in part by federal pandemic aid.[4] Some of that one-time federal COVID funding was used to launch new programs and initiatives. With that pandemic relief funding depleted, the State projected a $970 million budget deficit for FY2025, which the Governor's budget ultimately closed through several tax changes and enhancements without any reductions to expenditures (see Appendix 1 for details).

The Governor's Office projects that FY2025 revenues and expenditures will end the year essentially on track with the adopted budget.[5] Both revenues and expenditures are projected to come in about $200 million above budgeted levels, resulting in a $262 million surplus, most of which will be contributed to the rainy day fund (see Appendix 1 for a complete breakdown of FY2025 budgeted and projected year-end revenues and expenditures.)

[3] The General Funds are operating funds that support the regular operating and administrative expenses of most State agencies and are the funds over which the State has the most discretionary control.
[4] For more details on the FY2025 State of Illinois Budget, see the Civic Federation's May 2024 report.
[5] Governor's Office of Management and Budget, Illinois Economic and Fiscal Policy Report, November 2024.

Fiscal year 2026 brings the State to a critical crossroads. After a few years of strong revenue performance, the State faces a General Funds budget deficit of over $3 billion in FY2026 and more significant projected budget deficits over the next five years. The FY2026 projected deficit is driven by significant spending increases of nearly $3.2 billion—many but not all of which are legally mandated—and no net revenue growth. Two of the State's largest revenue sources—individual and corporate income taxes—are expected to increase significantly next year, while sales taxes are expected to decrease. Because it makes up 20% of General Funds revenues, a lack of growth in the sales tax is concerning. The Governor's Office projects very little change in smaller general operating revenue sources including lottery, gaming, cannabis, and sports betting revenues in FY2026.

On the other side of the ledger, the Governor's Office anticipates significant spending increases across key areas, including K-12 education, human services, healthcare (i.e., Medicaid spending), employee health insurance, and contributions to State pension funds.[6]

Given the State's already high tax burden and regressive tax system, options for new revenue sources to close the budget gap and sustain increased spending levels in future years are constricted and politically challenging. In addition to the budget deficit and end of federal pandemic funds, the State is also being called on to fund a number of services at the local and regional level around the State, including public transit, education funding, and pension benefit enhancements. A final looming issue is uncertainty surrounding future federal funding given the new presidential administration.

ECONOMIC LANDSCAPE

Illinois' fiscal policies operate as a drag on economic growth and employment in the state. A recent Civic Federation report on Illinois' economic policy finds that although Illinois has a variety of economic assets and strengths, such as education, healthcare, and energy, economic growth has stagnated relative to the region and the rest of the nation in recent years.[7] This economic weakness is linked to Illinois' tax and fiscal policy measures, many of which are under the state's control.

Overall, Illinois' economic growth has lagged behind other states regionally and nationally. Illinois' November 2024 unemployment rate of 5.3% is one of the highest rates in the nation and a full percentage point higher than the national rate of 4.2%.[8] Employment growth has likewise been sluggish, with November 2024 employment only 0.2% higher than pre-pandemic levels. If Illinois employment had grown at the rate experienced in Wisconsin, for example, over 90,000 additional jobs would have been created since February 2020. Additionally, Illinois' output growth, as measured by gross domestic output, continues to be significantly slower than neighboring states and the nation as a whole.[9]

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[6] Governor's Office of Management and Budget, Illinois Economic and Fiscal Policy Report, November 2024.
[7] Civic Federation, *Illinois Economic Landscape and Fiscal Structure*, January 31 2025.
[8] Bureau of Labor Statistics, *Local Area Unemployment Statistics*, December 2024.
[9] Civic Federation, *Illinois Economic Landscape and Fiscal Structure*, January 31 2025.

Population growth is an important indicator of the State's economic health and its capacity to grow economically, with both critical to the generation of increasing but sustainable tax revenues needed for government services. However, Illinois' population has been flat for several decades, with an annualized growth rate of under 0.1% since 2000.[10] The State saw a net loss of 113,833 residents between 2020 and 2024, with more than 418,000 residents leaving the State; this was partially offset by immigrants coming to the State. Illinois relies heavily on international immigration to keep the population steady—immigrants were the sole reason the population in Illinois increased in 2024. This rate is far below the national average of a 0.8% annual increase.[11]

Though these indicators describe an overall negative economic environment, Illinois has a variety of strengths that can be drawn upon to bolster economic growth. Rankings of the State typically praise its infrastructure including transportation, energy, and water, as well as its higher education system, healthcare, and technology sectors.[12] The Illinois Department of Commerce and Economic Opportunity (DCEO) also identifies the State as having a strong clean energy sector and a highly skilled workforce.[13] Illinois' strengths in workforce, infrastructure, and energy, coupled with the right incentive structure, should make it an attractive location to do business. As the State develops a plan for building economic growth in the future, it should look to maximize these advantages.

TAX STRUCTURE OVERVIEW

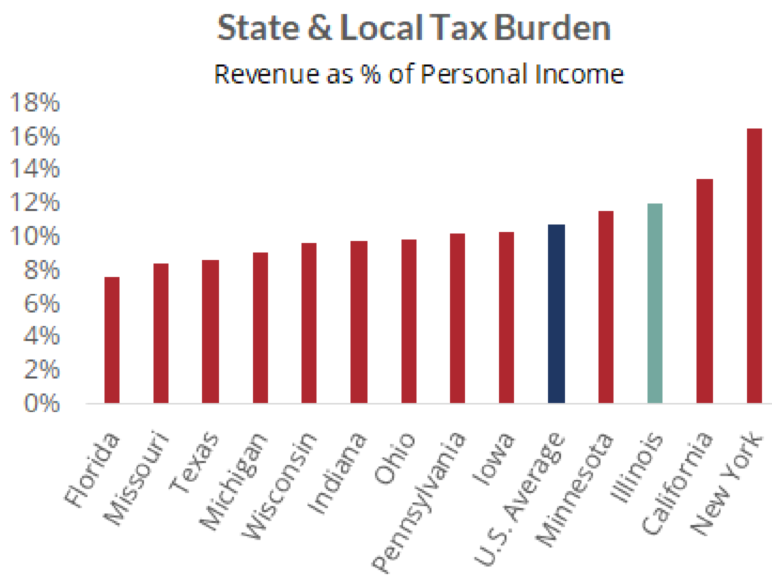
In addition to weak economic conditions, Illinois' high tax burden reinforces the perception that the state hinders economic growth and is unattractive to businesses. Illinois' tax structure is also regressive, meaning lower-income residents pay a higher share of their income in state and local taxes than wealthier individuals.

Looking at tax rates alone, Illinois' rates are at the high end nationally. However, simply comparing tax rates does not factor in the actual burden placed on residents based on their ability to pay. There are two principal ways analysts compare tax burdens across governmental jurisdictions. One approach is to scale dollar amounts to reflect differences in population across states using per capita values. Another approach is to look at taxes paid as a share of total personal income in the state. When comparing tax burden, we compare combined state and local taxes, as different states delegate different amounts of authority and taxation to the local level. Illinois ranks high on both measures of tax burden. On the measure of taxes per capita, Illinois ranked first in terms of state and local tax revenues per capita at $7,350 in 2021, based

[10] U.S. Census Bureau, *Resident Population in the States*, December 2024. Note that recent Census Bureau data for Illinois has notable discrepancies with reported tax revenue by the Illinois Comptroller's Office.
[11] U.S. Census Bureau, *U.S. Population Grows at Fastest Pace in More than Two Decades*, December 19, 2024.
[12] CNBC, *Top States for Business*, 2024.
[13] Department of Commerce and Economic Opportunity, *Open for Business*, August 2024.

on a comparison to nine peer states.[14] The national picture is not much better as Illinois' combined tax burden is among the highest in the country due to elevated property taxes, corporate income taxes, and excise taxes—or taxes on goods and services.

On the measure of taxes as a percentage of personal income, Illinois ranks third highest out of thirteen peer states,[15] with an overall tax burden of 11.96% of total personal income. Although New York and California have higher state and local tax burdens at 13.45% and 16.45% burdens, respectively, Illinois outpaces all of its neighboring states. The average U.S. state has a tax burden of 10.72% of personal income, more than a whole percentage point below that of Illinois. Though not an outlier, Illinois is undoubtedly on the higher end of tax burdens among its peers nationally.



Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

However, there are distinctions when examining each tax source individually as a percent of personal income. Illinois has lower-than-average burdens in individual income taxes and sales taxes. The income tax burden is low because Illinois levies a flat income tax instead of a graduated tax structure, as most other states do. Sales tax burden is low because although Illinois has high sales tax rates, it taxes very few consumer services. Finally, the property tax burden is high compared to peer states; since local governments have a limited ability to raise tax revenue, they lean strongly on property taxes, causing Illinois to have one of the highest property tax burdens in the nation (see Appendix 2 for a more detailed comparison of Illinois' tax burden to other states.)

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[14] Civic Federation, *Illinois Economic Landscape and Fiscal Structure*, January 31 2025. The nine peer states include: Indiana, Michigan, Ohio, and Wisconsin (BEA's "Great Lakes" states); Iowa and Missouri (two additional neighboring states); and Florida and Texas (as examples of strong-growth states).

[15] This report's peer state list includes five high-population states—California, New York, Texas, Florida, and Pennsylvania, and seven neighboring Midwest states—Ohio, Indiana, Wisconsin, Michigan, Missouri, Iowa, and Minnesota.

ISSUES AND RECOMMENDATIONS

The Civic Federation offers the following recommendations to the Governor's administration and the Illinois General Assembly to address the challenges outlined above. The issues and recommendations are rooted in two primary needs:

1) A realignment of the State's tax structure to improve business competitiveness, economic growth, and sustainable revenue growth.
2) A more robust strategic budgeting process to drive budget decisions based on performance outcomes.

Within each of these larger umbrella issues, we provide several concrete recommendations to begin the process of accomplishing these goals. These issues and recommendations are not meant to be immediate solutions to resolve the pressing budget issues this cycle but rather are intended to guide the Governor and General Assembly members toward thinking about long-term solutions to the State's structural budget issues. Simply put, Illinois' core revenue streams have not been keeping pace with spending growth. In addition to a re-evaluation of the State's tax structure, there should be an emphasis on understanding and evaluating the effectiveness of the State's spending. We hope these suggestions spur questions and conversations with state agencies during the 2025 budget session that will continue into future years.

Develop a Tax Structure for a Sustainable Future

The Civic Federation urges the State to re-evaluate its tax structure to align better with the modern economy, make Illinois more competitive with peer states, and set up the State for future revenue growth. The State of Illinois collects the majority of its revenue every fiscal year from three large tax sources—individual income taxes, corporate income taxes, and sales taxes. However, Illinois is one of the few states with a flat income tax, which limits the state's ability to generate additional revenue in a progressive manner that distributes individual tax burden in a way that reflects individual capacity. Additionally, Illinois does not impose a sales tax on services despite the growing shift in the economy toward a service-based market, which limits the amount of revenue the state can obtain. Expanding the sales tax to include services could modernize the tax base and make it more reflective of the current economy.

The State also receives grants and reimbursements from the federal government but relies heavily on the above-mentioned tax sources as operating resources to support ongoing programs and services. Revenues have performed on target over the past few years, but the State's revenue mix has historically shown a high level of volatility due to unexpected economic conditions that impact revenue levels. Going forward, revenue levels are expected to be stagnant. The State has projected budget deficits for fiscal years 2026 through 2029, as expenditures are expected to outpace revenues in future years.

Now that the State has allocated all of its federal pandemic relief funding, it needs to consider how it will continue investing in programs and services with reliable revenue sources. Doing so will position the State to broaden and diversify its tax structure to mitigate regressivity and unintended disincentives in ways that will promote economic (and population) growth.

Recommendation: Illinois should evaluate and develop a more diversified, equitable and sustainable tax structure that would best benefit its economy in future years.

As part of a plan to revamp the State's tax structure, the Civic Federation offers for consideration three concrete steps that the State can take in the near term:

1) Modernize the sales tax;
2) Assess tax exemptions and incentives (i.e., tax expenditures); and
3) Review the need for existing special revenue funds.

Each of these recommendations is discussed further below.

Modernize the Sales Tax to Include Services

Illinois' current sales tax structure is outdated and no longer aligns with consumer spending and the overall structure of the state's economy, which has shifted from goods to services over the past several decades. As part of a path to sustainable state finances, Illinois should expand its sales tax to cover consumer services.

One of the basic principles of government finance is that to be stable and efficient, a tax should generally have as broad a base and as low a rate as possible. Illinois' sales tax does not live up to either ideal. Illinois—to its detriment—has a high sales tax rate with a narrow base.

The State of Illinois levies a 5.0% sales tax to generate revenue for the state government, in addition to a uniform 1.25% sales tax that funds local governments, counties, and mass transit districts, totaling a base 6.25% sales tax rate statewide.[16] Local governments can also choose to levy additional sales taxes. The average combined state and local sales tax rate in Illinois is 8.87%,[17] while the combined sales tax rate in the City of Chicago is the second highest of any major municipality in the United States at 10.25%. Illinois' sales tax rates are some of the highest in the country, failing to meet the principle of maintaining a low tax rate.

Also to its detriment, despite having one of the nation's highest average sales tax rates, Illinois' sales tax base is much narrower than those in other states as it only levies this tax on goods. Most services, such as plumbing, dry cleaning, or haircuts, go entirely untaxed. As one of the three largest sources of revenue for Illinois, it is important to update the sales tax to reflect the modern consumer economy.

[16] Illinois General Assembly Legislative Research Unit, *Illinois Tax Handbook for Legislators*, 38th Ed., April 2022, p. 135.
[17] Tax Foundation, *State and Local Sales Tax Rates, Midyear 2024*, July 9, 2024.

By applying the sales tax only to goods and a small number of services, Illinois is missing the ability to tax much of the spending within its borders. An increasing proportion of consumer spending is on services rather than goods. In 2021, almost 50% of consumer spending was spent on services, excluding housing and healthcare.[18] However, out of the 176 total services taxed by states recognized by the Federation of Tax Administrators, Illinois currently taxes only 29.[19] These mostly include utilities and are special taxes levied separate from the general sales tax. By comparison, the average state taxes 62 services. The State would need to consider how to account for the limited number of services currently taxed in Illinois when designing and implementing a sales tax on services.

Broadening the sales tax base would yield several notable benefits for the State and its residents and consumers. It would bring in increased revenue needed to address immediate cliffs as well as better align sustainable revenue with budgetary expenditures and could be used to fund transit districts or local governments in pressing need of support. Initial modeling estimates show that an extension of the sales tax to an expansive list of services without a rate reduction could raise as much as nearly $2 billion annually for the state alone.[20] A sales tax expansion to services could also be paired with an overall rate reduction to lower the tax burden and increase the political palatability of the policy. Any reduction in the sales tax rate should be part of a comprehensive effort to reevaluate Illinois' tax structure, with the goals of reducing regressivity and maintaining sustainable revenue sources. Finally, a sales tax on both goods and services would be less regressive than the current model. Wealthier households tend to spend a higher proportion of their income on services. Therefore, a services tax would shift more of the sales tax burden onto these high-income spenders.[21] This makes a combined goods and services sales tax more equitable than a goods-only sales tax.

Any sales tax expansion to services should be calibrated to support economic competitiveness. Taxing business-to-business services can result in tax pyramiding when a single good or service is taxed multiple times before it reaches the consumer.[22] For example, tax pyramiding occurs if a supplier is taxed when providing raw materials to a manufacturer. When the manufacturer sells a completed consumer good, the consumer pays a consumer sales tax layered on top of the tax on the raw material, which is passed through in the final price. Tax pyramiding can lead to outsized tax burdens on certain services and can create negative economic distortions. The best way to ensure that an expanded sales tax avoids pyramiding is to only tax consumer services and exempt business-to-business services. The Illinois Department of Revenue already has a sales tax exemption system in place to prevent tax pyramiding on the sale of goods, and this process could be extended to cover services as well.

Recommendation: The State of Illinois should modernize the sales tax by expanding the base to include more consumer services while considering lowering the rate to make it less regressive.

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[18] Chicago Metropolitan Agency for Planning Analysis of U.S. Bureau of Economic Analysis Data.
[19] Federation of Tax Administrators, *By the Numbers Newsletter*, July 2017.
[20] Chicago Metropolitan Agency for Planning, *Plan of Action for Regional Transit*, December 2023
[21] Pew Charitable Trust, *Household Expenditures and Income*, March 2016.
[22] Tax Foundation, *Tax Pyramiding*, 2025

Review and Analysis of State Tax Exemptions

Tax exemptions, or Tax Expenditures

The State of Illinois reduces its operating resources by a significant amount annually to provide individuals and businesses tax benefits through exemptions (technically known as tax expenditures). These take the form of exemptions, deductions, credits, allowances, or abatements that the State of Illinois provides to individuals, businesses, or organizations to further public policy goals. In FY2023, the most recent year that data has been reported on tax expenditures by the State Comptroller, these exemptions totaled $12.3 billion, or a 17.0% reduction from total potential tax revenues of $72.5 billion.[23] Approximately $1.8 billion of the total exemptions, or 14.6% of the total, benefit businesses and agriculture, including:

- Agricultural tax exemptions, worth $717.3 million
- Corporate income tax exemptions, worth $707.4 million
- Sales tax exemptions, worth $437.6 million

The six largest tax expenditures primarily benefit individuals and were nearly $8.7 billion, or 70.2% of the total, in FY2023. They include:

- Income tax exemptions for retirement and social security income, worth $3.3 billion
- Sales tax rate reduction for food and drugs from 6.25% to 1.0%, worth $2.4 billon (the 1% tax was repealed in 2024 but may be reinstated by local governments)
- Standard exemptions for individual income taxes, worth $1.2 billion
- Sales tax exemptions for nonprofit organizations, worth $819 million
- Property tax credits against the individual income tax, worth $556 million
- Earned income tax credits, worth $378 million

Each should be evaluated and reported out on cost-benefit basis and considered for recalibration on that, among other bases. It is important to note that each exemption category has political constituencies who may be expected to resist to efforts at reduction or elimination. One key area of exemptions that ought to be reviewed for effectiveness is economic development incentives.

Economic Development Incentives

In FY2023, a total of $910.9 million was specifically designated as economic development incentives intended to spur job growth and economic activity. The question of whether they accomplish this is an open question as they are not regularly reviewed for efficacy. Therefore, these tax expenditures should be a top priority for review and reconsideration.

The $910.9 million in FY2023 economic development exemptions are shown in the following table. These included $471.2 million in corporate income tax credits or subtractions, $306.2

[23] Office of the State Comptroller. Tax Expenditure Report Illinois for Fiscal Year Ended June 30, 2023, December 12, 2024, p. 4.

million in sales tax exemptions, and $97.9 million in individual income tax credits or subtractions.

State of Illinois FY2023 Economic Development Tax Expenditures

Tax Expenditure Type		FY2023 Amount ($ Millions)
Corporate Income Tax	$	471.2
Sales Tax	$	306.2
Individual Income	$	97.9
Gas Revenue Tax	$	21.4
Electricity Excise Tax	$	13.1
Telecommunications Excise Tax	$	0.8
Gross Receipts Tax (Public Utility Fund)	$	0.3
Total	**$**	**910.9**

Source: Office of the State Comptroller. Tax Expenditure Report Illinois for Fiscal Year Ended June 30, 2023, December 12, 2024, p. 5.

All state governments provide millions of dollars in tax exemptions, deductions, credits, and other incentives for the purpose of promoting economic development. The benefits that are most frequently used as a justification for granting these incentives are job creation and retention. However, few states require regular reviews of the performance of these programs to determine whether they actually achieve their stated goals and objectives. Once provided, these tax expenditures become long-term entitlements that cost treasuries millions of dollars in foregone revenues without adequate public disclosure or regular review of their costs and/or benefits. This is in contrast to budgets, which are subject to regular reviews, debate, and discussion through the appropriations process. Despite incentivizing economic development via tax expenditures and more specific programs, a state often has little idea of the effectiveness of these incentives.[24]

Before proposing changes to economic development tax expenditures, the State of Illinois should commission a comprehensive review of these incentives. The review would clearly identify the goals and objectives of each program, require the transparent reporting of metrics that help determine whether goals are being met, and provide for the reduction or elimination of tax incentives that fail to produce promised results such as job creation.

Models for how to evaluate the effectiveness of tax expenditures exist in other states. For example, the State of Minnesota requires that a tax expenditure budget be submitted in even-numbered years to inform the biennial budget submitted in odd-numbered years. The information required includes the purpose of the expenditure, the incidence of the expenditure, and the revenue-neutral amount if the expenditure was repealed.[25] Similarly, the State of Washington regularly reviews the performance of tax expenditures to determine if they

[24] The Civic Federation, *Illinois Economic Landscape and Fiscal Structure*, January 31, 2025.
[25] Minnesota Department of Revenue. State of Minnesota Tax Expenditure Budget Fiscal Years 2024-2027 p. 1.

meet the goals set forth by the legislature when incentives are adopted. They then make recommendations for changes when needed. Illinois should follow a similar model.[26]

Recommendation: The State of Illinois should undertake a comprehensive review of tax expenditures, with a special focus on economic development tax exemptions to determine if they are meeting stated goals in terms of job creation and economic growth. A potential model could be the annual reports published by the Illinois Department of Commerce for the Economic Development for a Growing Economy (EDGE) tax credit program. Those that do not meet those goals should be considered for termination.

Review Existing Special Revenue Funds

Illinois has over 400 Special State Funds, which were created to receive earmarked revenues that are only used for designated purposes. Special Funds consist of all State accounts *except*:

- General Funds, which pay for the regular operating and administrative expenses of most State agencies
- Highway Funds, which support State and local transportation-related activities
- Bond Financed Funds, which pay for capital improvements
- Debt Service Funds, which accumulate money used to pay interest and principal on debt obligations
- Federal Trust Funds, which support grants and contracts between State agencies and the federal government
- State Trust Funds, which hold funds for other entities or individuals
- Revolving Funds, which finance the operation of State agencies that provide services to other State agencies on a cost-reimbursement basis and support local capital projects.[27]

Special Funds receive resources through transfers or appropriations from General Funds or directly from other sources, such as designated State taxes and fees and federal grants. They account for a large total portion of the state budget; in the FY2025 operating budget they were earmarked at approximately $49.1 billion.[28]

The State should review its Special Funds to determine if (and how well) they serve their stated purpose. Those that do not should be eliminated and funds transferred to the General Funds so that the State can be afforded maximum flexibility in allocating resources to meet policy priorities. In most cases, segregating revenues into special purpose funds is a practice that should be reserved for a few priority or mandatory programs. Certain special funds, including those receiving federal entitlement disbursements such as Medicaid funds, would be exempt from any transfer or elimination.

[26] State of Washington, Citizen Commission for Performance measurement of Tax Preferences.
[27] Illinois State FY2025 Budget, p. 143.
[28] Illinois State FY2025 Budget, p. 143.

Recommendation: Review special purpose funds to ensure that these funds are still necessary and eliminate any that no longer serve a valid purpose, transferring those funds to the General Fund.

DEVELOP A STRATEGIC BUDGETING PROCESS

While the annual budgets under the current gubernatorial administration are guided by budget goals laid out in the FY2020 State budget,[29] the State lacks a clear and transparent strategic budgeting framework. The FY2020 budget, the first under Governor JB Pritzker, included a plan to achieve fiscal stability, which included targets for pension reform, rebuilding the State's "rainy day" fund, implementing performance-based budgeting, supporting local governments, and enhancing transparency in governance. However, this fiscal stability plan does not constitute a long-term strategic plan. The Civic Federation would like to see much more improvement in the State's strategic planning process to ensure consistent revenue growth, efficient spending, and economic competitiveness.

The Governor's plan for achieving fiscal stability laid out a proposal for dealing with pension liabilities, which as executed has helped to stabilize the State pension systems while maintaining commitments to retirees. It also called for rebuilding the Budget Stabilization Fund, or "rainy day" fund, to ensure Illinois has a reserve to help it weather future economic downturns and fiscal emergencies; and highlighted the State's commitment to performance-based budgeting through the Budgeting for Results initiative. It also included a proposal to increase revenues through sources such as video gaming and cannabis taxes.

While there is much to be said for the progress achieved under this administration in addressing long-term fiscal issues, the State needs a more systematic long-term strategic planning process. Addressing pension obligations and other fiscal reforms will not result in the systemic changes needed to grow revenues and meet spending needs. It is true that the tax and revenue changes enacted in the past six years have resulted in some new revenues and have managed to help close budget deficits, but more meaningful structural changes are needed. This should be accomplished through a more robust planning process that meets the criteria for a strategic plan and planning process, as set by best practice guidance from the Government Finance Officers Association (GFOA).[30]

To meet the definition of an actual strategic plan and align with GFOA best practices, the State of Illinois would need to improve in several areas, particularly in terms of strategy, assessment, transparency, and the availability of information about how the plan was created. One major issue with the current fiscal stability plan laid out in FY2020 is the lack of a detailed and systematic analysis of external factors influencing State finances, such as broader economic trends, demographic shifts, technological advancements, and intergovernmental changes. A true strategic plan should examine Illinois' role within broader regional or national contexts to

[29] Illinois State Budget FY2020, 2019, p.32-36.
[30] Government Finance Officers Association, *Best Practices Strategic Planning*, 2023. https://www.gfoa.org/materials/bp-strategicplanning

leverage its strategic positioning. Without clear documentation of how these factors are considered during the planning process, any ability to address these challenges is effectively limited. Additionally, the existing plan has no clear articulation of a comprehensive strategy and vision, making it difficult to understand how goals will be achieved, how they align with long-term objectives, or how these goals were determined.

Stakeholder engagement is another area in need of improvement, as the Governor's current plan has little information about who is consulted and how their perspectives are incorporated into goal setting. Moreover, an effective strategic plan should go through a formal approval process that will afford it clear authority and legitimacy as a guiding document. If these processes are currently being done, they are not communicated transparently, and the process for evaluating and addressing these issues is unclear.

Finally, there is limited information on how performance-based budgeting is utilized in crafting the State's budget or how it is assessed to ensure accountability. Improving the clarity and transparency of the planning process, including providing detailed explanations of how decisions were made and who was involved, will enhance the plan's credibility, effectiveness, and transparency.

In summary, Illinois should enhance its strategic budget planning by implementing an iterative process for long-term planning that includes conducting a systematic analysis of external factors, articulating a clear long-term vision and strategy, prioritizing stakeholder engagement, improving transparency, and a process for outcomes-based evaluation. Additionally, the plan should consider Illinois' position within regional and national contexts to leverage collaboration and best practices, ensuring a more effective and responsive approach to addressing the state's needs.

Recommendation: Illinois should develop a strategic budget plan that aligns with GFOA's best practices**.** This will help promote economic growth, attract investment, and ensure financial stability for future generations.

As part of a strategic planning process, the Civic Federation offers five concrete steps that the State can take in the near term:

1) Enhance the performance-based budgeting process;
2) Avoid unnecessary Tier 2 pension benefit enhancements;
3) Build up the reserve fund;
4) Align state support of local governments with their needs; and
5) Improve transparency within the budget and lawmaking process.

Each of these recommendations is discussed further below.

Enhance the Performance-Based Budgeting Process

The State of Illinois has had a performance-based budgeting (PBB) process in place for 15 years, but it is currently not fully utilized, and it lacks transparency and clarity around whether and how metrics help direct funding during the budgeting process. The State's Budgeting for Results Commission, established in 2010 and is presently housed within the Governor's Office of Management and Budget (GOMB), works to help Illinois government agencies set their priorities, meet their goals, and deliver services.[31] The Commission is comprised of Illinois legislators, executive staff, outside experts, and stakeholders. It gathers data and performs comprehensive program assessments to help inform the state's budget.

The Budgeting For Results comprehensive program assessment framework includes the Illinois Performance Reporting System (IPRS), the Illinois Benefit-Cost Model (IBCM), and the State Program Assessment Rating Tool (SPART).[32] These tools assess 369 State programs from 64 departments across 11 policy domains, including education, healthcare, public safety, and workforce development.[33] The number of programs being assessed is variable as different programs are started and ended, and each department is required to set a minimum of one performance measure for each program. New State departments and programs, such as the Department of Early Childhood, should prioritize setting these metrics.

While data on performance metrics is collected through the IPRS system, there are no legal requirements for this data to be used in the strategic planning and budgeting processes. [34] The IPRS is the central tool for collecting and analyzing performance data year over year, and the results are primarily used to inform the Governor's Office of Management and Budget (GOMB) and legislators during the preparation of the state's budget. However, there is no direction in how much weight these results should be given or how they should be considered, and it is unclear if these metrics are considered.

Illinois' performance-based budgeting has several positive aspects that contribute to its success. By focusing on outcomes as part of the budgeting process, State programs have ensured that resources are used effectively to address key priorities. This success is apparent in the tangible positive results, such as a reduction in juvenile recidivism rates, as reported by the Illinois Department of Juvenile Justice.[35] Additionally, Illinois has strengthened accountability and transparency by clearly communicating its goals and priorities to the public through the Budgeting for Results Interactive Performance Dashboard. This open communication fosters trust and allows residents to better understand how public funds are being utilized to drive progress and deliver meaningful results.

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[31] Illinois Budgeting for Results, *Budgeting for Results 14th Annual Commission Report*, November 1, 2024.
[32] Illinois Budgeting for Results, *Budgeting for Results 14th Annual Commission Report*, November 1, 2024, p.6.
[33] Illinois Budgeting for Results Interactive Performance Dashboard.
[34] Melkers & Willoughby, *The State of the States: Performance-Based Budgeting Requirements in 47 out of 50,* 1998.
[35] Melkers & Willoughby, *The State of the States: Performance-Based Budgeting Requirements in 47 out of 50,* 1998.

Despite its benefits, performance-based budgeting faces several challenges in Illinois. The first is departmental buy-in. While the Budgeting for Results Commission encourages Departments to evaluate and report on their programs, some agencies have resisted setting performance goals. For example, in 2019, the Department of Corrections resisted setting performance goals for electronic monitoring.[36] The second challenge is resource constraints, as the Budgeting for Results Commission is short-staffed. The Budgeting for Results Commission's current resources limit the frequency of program assessments, which occur infrequently. Ideally, this would occur on a five-year cadence, which would be the Commission's goal if it was properly staffed. Third, the legislative process often prioritizes traditional line-item budgeting over performance outcomes, [37] and some agencies resist the cultural changes required to implement PBB effectively. Fourth, the IBCM currently only includes 11 policy areas, which limits the programs that can be analyzed with the model. Fifth, collecting multiple measures for programs, rather than relying on a single metric, would provide a more comprehensive understanding of program impacts. For instance, while the Department of Corrections tracks the number of individuals who obtain a GED, there is limited data on their post-release outcomes, such as employment or continued education, which are critical for evaluating long-term success. Finally, performance data is not consistently used at higher levels of decision-making, which would be necessary to ensure alignment with the State's strategic goals. The State should use performance data from the Budgeting for Results Commission to demonstrate how its programs and initiatives drive meaningful outcomes and deliver value to its residents.

Illinois can look to several states for models to enhance its performance-based budgeting practices.[38] North Carolina[39] and Texas[40] are often cited as best in class exemplars for successfully integrating performance measures into their strategic planning and budgeting processes. These states demonstrate how aligning performance metrics with budgetary decisions can drive accountability and efficiency. Washington State provides another valuable model by highlighting the direct relationship between performance measures and the quality of government services, emphasizing the importance of measuring outcomes to improve public programs. Connecticut[41] also offers a strong example, particularly in setting and analyzing performance measures. In Connecticut, measures are developed collaboratively by state agency staff and private providers, with the analysis process incorporating input from consumers, as well as agencies and providers. This inclusive approach ensures that performance metrics are comprehensive and reflective of stakeholder priorities and offers a robust framework that Illinois could adapt to its own needs.

Best practices for performance-based budgeting, developed by the Organization for Economic Co-operation and Development, focus on creating a system that is transparent, strategic, and adaptable to changing circumstances. These practices include clear documentation of the rationale and objectives of PBB to ensure they reflect stakeholders' interests and align

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[36] NPR Illinois, "Will Illinois Ever Embrace 'Budgeting For Results'?," July 4, 2019.
[37] Melkers & Willoughby, *The State of the States: Performance-Based Budgeting Requirements in 47 out of 50,* 1998.
[38] Melkers & Willoughby, *The State of the States: Performance-Based Budgeting Requirements in 47 out of 50,* 1998.
[39] Governor's Advisory Committee on Performance Management
[40] Legislative Budget Board
[41] Results First Connecticut

expenditures with strategic goals and priorities. Effective PBB systems also incorporate flexibility to account for variations in government activities and economic conditions, ensuring responsiveness and resilience. Investing in human resources, data systems, and infrastructure is critical to supporting the implementation and sustainability of PBB. Additionally, PBB best practices should facilitate oversight by both the legislature and civil society, enhancing accountability and trust. Ultimately, well-designed performance-based budgeting should complement tools that improve performance orientation and be supported by incentives that encourage performance-driven behavior and continuous learning. By integrating these elements, PBB promotes efficiency, effectiveness, and a focus on outcomes in government budgeting processes. [42]

Recommendation: The Budgeting for Results Commission should: 1) expand its program assessment framework to increase the number of programs that can be assessed; 2) establish ongoing collaboration between the Governor's Office and other State agencies and departments to set clear benchmarks and outcome measures for programs; 3) provide a more comprehensive understanding of program impacts; and 4) ensure the consistent use of performance data at higher levels of decision-making.

Avoid Unnecessary Tier 2 Pension Benefit Enhancements

The extraordinarily high cost of paying down state pension liabilities remains a major challenge for the State of Illinois. In addition to contributing to the State's high overall tax burden that serves as a disincentive to population and economic growth, it diverts funding away from other priorities such as education, healthcare, and human services. However, not directly addressing pension debt would only exacerbate pension liabilities owed over time. The State must continue to make progress in paying down pension debt and avoid adding to existing costs by enhancing benefits.

Pension obligations for the State's five pension plans[43] make up an extraordinarily high portion of total State spending, comprising approximately 19% of General Funds spending. The amount the State is required to contribute to the funds annually has increased from $1.8 billion in FY2005[44] to $11.3 billion in FY2025 pursuant to a statutory mandate. The contribution is projected to increase to $18.6 billion by FY2045 in order to reach the State's existing funding goal of 90% funded by FY2045.[45] Recent projections show that the increased contributions are helping to tamp down the growth in unfunded liabilities; beginning in FY2026, the State will be

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[42] Organization for Economic Co-operation and Development, *OECD Good Practices for Performance Budgeting,* 2019.

[43] The State's five pension systems are: the Teachers' Retirement System, which covers public school teachers outside Chicago; the State Employees' Retirement System, for most State employees who are not eligible for another State plan; the State Universities Retirement System, for faculty and staff of universities and community colleges; the Judges' Retirement System; and the General Assembly Retirement System.

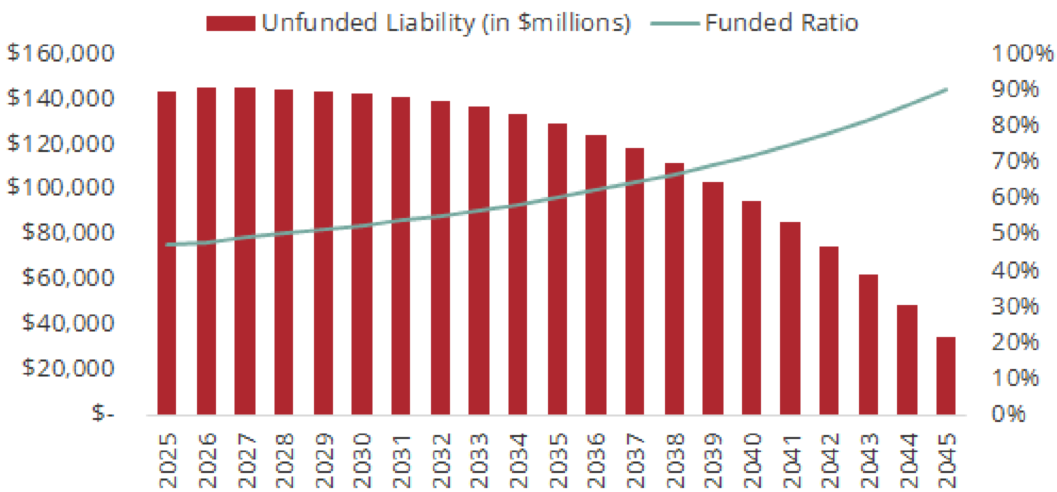
[44] Illinois Economic and Fiscal Commission, Fiscal Year 2005 Budget Summary: P.A. 93-0842 (SB 3340).

[45] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Special Pension Briefing*, November 2024, p. 12.

contributing enough annually to stop the unfunded liability from growing every year (referred to as the "tread water" contribution).[46]

Despite this progress, Illinois' retirement systems are among the most poorly funded of any state in the U.S. The unfunded liabilities for the State's five pension funds totaled $144.3 billion, and the combined funded ratio stood at 45.8%[47]—near the bottom of almost every national ranking by state. It is important to remember that these estimates account only for the State's five pension funds. They do not include the unfunded liabilities of local pension funds throughout Illinois, many of which are struggling with their own underfunding issues, the four City of Chicago pension funds foremost among them.

State of Illinois Retirement Systems Projected Financial Condition: FY2025 to FY2045



Source: Illinois General Assembly, Commission on Government Forecasting and Accountability, *Special Pension Briefing*, November 2024, p. 12.

There are two sides to the pension equation: how much goes into the pension funds in the form of employer and employee contributions and earned interest, and how much goes out in the form of benefit payments. On the funding side, the State must continue increasing pension contributions and paying down unfunded liabilities. On the spending side, the State must avoid increasing the cost of pensions, which brings up the issue of Tier 2 pensions.

The State of Illinois created a new pension benefit structure effective in 2011 to address budgetary pressures due to the rising cost of pension benefits. This less generous benefit

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[46] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Special Pension Briefing*, November 2024, p. 12.
[47] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Special Pension Briefing*, November 2024, p. 2

structure is known as "Tier 2" and applies to employees hired on or after January 1, 2011.[48] The change in benefits for new Tier 2 employees includes an increase in the retirement age to qualify for full benefits and reduced annual automatic benefit increases. Tier 2 employees also receive annual benefit increases upon retirement of 3% or one-half of the rise in the Consumer Price Index (CPI), whichever is less, on a simple-interest basis. In contrast, the increase for most workers hired before 2011 is 3% on a compounded basis—this does not include Chicago police officers, firefighters, and some other employees. Additionally, Tier 2 reduced the final average salary on which a pension is based. Previously, the final average salary, which is used to calculate a pension benefit, was the average of the highest four of the last five years of service. Tier 2 employees' final average salary is now calculated using the average of the highest eight of the last ten years of service. A limit was also imposed on the amount of earnings used to calculate the final average salary, with a salary cap starting at $106,800, the Social Security wage base in 2010.[49] This salary cap increases at the rate of the lesser of 3% or half of the annual increase in CPI.

The purpose of enacting a less generous tier of benefits (Tier 2) for new employees was to curb unsustainable growth in pension costs. At the time, some pension experts warned as early as 2010 that the new benefit structure was so low that it might force certain government employees to pay into the Social Security system in addition to their pension plans[50] due to IRS "Safe Harbor" rules. Social Security Safe Harbor rules require that government workers who participate in a pension plan and not in Social Security must receive certain minimum benefits that are deemed equivalent to Social Security.[51] Of the State of Illinois' five pension plans, most members of the Teachers' Retirement System (TRS) and State Universities Retirement System (SURS), and some of the State Employees' Retirement System (SERS) members, are not covered by Social Security, so those plans must meet Safe Harbor requirements.

If the Tier 2 benefit structure does not meet the Safe Harbor tests, either the benefits must be increased, or employees would have to pay 6.2% of their salary to Social Security, matched by an equal employer (i.e., government-funded) contribution in addition to paying into their pension plan. This would be far more costly than proactively adjusting Tier 2 plans to ensure continued compliance.[52] There is a general consensus that Illinois pension plans will eventually fail the Safe Harbor test within the next few years, but precisely when is not known.

Several bills have been introduced in the Illinois General Assembly over the past several years to restore benefits for Tier 2 employees back to the same benefit levels provided for employees

[48] Public Act 96-0889, enacted on April 14, 2010. The new tier applied to most State and local public pension funds in Illinois, with the exception of police and fire pension funds and the Chicago Transit Authority, which already had a second tier added in legislation passed in 2008
[49] Commission on Government Forecasting and Accountability, Illinois State Retirement Systems Financial Condition as of June 30, 2021, September 2022.
[50] Teachers' Retirement System of Illinois, Tier 2 Issues, Updated December 13, 2019.
[51] See the Civic Federation's issue brief, "Tier 2 Pensions and the Safe Harbor Issue: Explained," November 7, 2023.
[52] Civic Federation, "Tier 2 Pensions and the Safe Harbor Issue: Explained," November 7, 2023.

before Tier 2 was enacted. These have been billed as "Safe Harbor fixes." Despite the moniker, they are no such thing. "Safe Harbor" is specific to the level of benefits needed to be consonant with Social Security benefits. The benefits proposed go far beyond the benefit enhancements needed to comply with Internal Revenue Service rules. In their worst form, they obliterate the Tier 2 distinction.

The most recent of these bills, House Bill 5909 (HB5909), makes several sweeping benefit enhancements that are projected to cost the State an additional $29.8 billion in state pension contributions through FY2045, with an additional $1.1 billion in the first year alone.[53] Adjusting the pensionable salary cap to match the Social Security Wage Base alone—which the Civic Federation has advocated as the most direct way to ensure compliance with Safe Harbor rules—is projected to cost $6.2 billion through FY2045 for the State's three largest pension funds, with $78 million in the first year. Additional benefit enhancements proposed in HB5909, including a revision to the way the final average salary is calculated, an automatic annual cost of living adjustment of 3% per year, and reducing the retirement age, would be far more costly than simply addressing the pensionable salary cap.

The simplest and least costly way to assure Illinois' pension plans meet Safe Harbor tests is to adjust the maximum pensionable salary to match the Social Security Wage Base, ensuring that both grow at the same rate over time. Enacting any other Tier 2 pension benefit enhancements would be far more costly and could undo much of the progress that Tier 2 benefits have made to curb unsustainable growth in pension costs.

Recommendation: The State of Illinois should refrain from unnecessary increases to pension liabilities and enact only those benefit enhancements to Tier 2 pensions necessary to comply with Social Security Safe Harbor guidelines. The most direct and efficient way to handle this would be to increase the pensionable salary cap to align with the Social Security Wage Base.

Increase Reserve Fund to Align with Best Practice Standards

Building a financial cushion to deal with future economic downturns or unforeseen shortfalls in revenue is a key element in maintaining fiscal stability. According to public finance experts, all governments should place a portion of their general operating revenues in a general fund reserve or "rainy day" fund.[54] Reserve funds are savings accounts that governments can use to address revenue shortfalls or unanticipated expenditures and to help stabilize tax rates. Governments that maintain adequate reserves are better positioned to deal with funding issues in times of financial stress, such as when revenues underperform or when there are unexpected expenditures. Putting money into reserves is more fiscally prudent than spending surplus funds on new or expanded programs. In FY2024, the median reserve fund balance

[53] Actuarial Impact Study – House Bill 5909, commissioned by the Commission on Government Forecasting and Accountability and completed by Segal, January 8, 2025.
[54] Government Finance Officers Association, *Best Practices: Fund Balance Guidelines for the General Fund*, September 2015.

among states was 13.5% of General Funds expenditures, according to a survey by the National Association of State Budget Officers.[55] That average is itself less than the 16.67% (equal to two months of operating costs) recommended as best practice by the Government Finance Officers Association (GFOA).[56] By comparison, Illinois' fund balance is only 4%.

In 2000, Illinois established its Budget Stabilization Fund with money from the State's portion of a 1998 lawsuit against tobacco companies.[57] In 2004, the state enacted a law establishing a goal of maintaining 5% of General Funds revenues in the Fund. According to the law, the Fund would be used to reduce the need for future tax increases or short-term borrowing, maintain high credit ratings, and address budgetary shortfalls. Withdrawals from the Fund were to prioritize services for children, while deposits into the Fund would be triggered by projected revenue growth of more than 4% from the prior year. The State added about $250 million in 2001 from the tobacco settlement and made few changes after that point. The Fund never exceeded $277 million, which is less than 1% of the general fund and far below the 5% goal.[58]

Prior to FY2017, instead of being used to withstand fiscal emergencies as originally intended, the Fund was used for cash flow problems resulting from timing variations between receipt and disbursement of funds in a given fiscal year.[59] By law, any cash flow borrowings transferred during a fiscal year from the Budget Stabilization Fund to the General Funds are to be reimbursed by a transfer back by the end of that fiscal year.[60]

Amid the State's financial crisis in 2017, this provision was changed to allow the Budget Stabilization Fund to be used to pay expenses without requiring repayment that year.[61] As part of the stopgap spending plan passed in June 2016, the Fund's entire balance was appropriated to pay for State operations in FY2017.[62] Since FY2022, the State has been replenishing the fund. Additionally, in FY2023, a law was enacted that raised the targeted balance for the Fund from 5% of revenues to 7.5%.[63] As of FY2024, the reserve fund was at approximately $2.1 billion, or 4.0% of General Funds revenues.[64]

The Civic Federation recommends that the State aim for a Budget Stabilization Fund funding goal of 10% of General Funds revenues. This goal was suggested by the General Assembly's Commission on Government Forecasting and Accountability (COGFA) in 2015 in light of the

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[55] National Association of State Budget Officers, *The Fiscal Survey of States Fall 2024*, p. 68.
[56] Government Finance Officers Association, Best Practices: Fund Balance Guidelines for the General Fund, September 2015.
[57] Illinois State Comptroller, *Rainy Day Fund*, Updated January 2025.
[58] Illinois State Comptroller, *Rainy Day Fund*, Updated January 2025.
[59] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Illinois Revenue Volatility Study, Public Act 98-0682*, Updated February 17, 2015, p. 88.
[60] 30 ILCS 105/6z-51(b). The law was amended to defer cash repayment for FY2011 until July 15, 2011.
[61] Public Act 99-0523, signed on June 30, 2016.
[62] State of Illinois Governor's Office of Management and Budget, *Illinois Economic and Fiscal Policy Report*, November 1, 2024, p. 12.
[63] Public Act 102-1115.
[64] National Association of State Budget Officers, *The Fiscal Survey of States Fall 2024*, p. 68.

State's revenue volatility.[65] COGFA examined two funding strategies for the Fund: making deposits into the fund only when revenues are growing rapidly or making regular deposits regardless of revenue growth. They determined that both approaches presented challenges; relying on excess revenues can lead to wide variations in annual funding, while regular funding puts annual pressure on the budget by reducing available resources for annual expenses.[66] The Civic Federation recommendation of 10% is an interim goal because, as noted, the GFOA recommends a best practice standard of two months of funding, or 16.67%.[67] However, GFOA acknowledges that this goal is not attainable for all states and recommends that governments take into account specific circumstances such as public trust and resource constraints.[68][69]

In the last few years, as part of its effort to replenish the Budget Stabilization Fund, Illinois has designated several sources of regular deposits, including a portion of cannabis taxes, monthly transfers of $3.75 million from the General Fund, repayment on a loan to the State's Unemployment Insurance Trust Fund, and interest on the money in the reserve fund. Approximately $205 million was contributed to the reserve fund in FY2024.[70] The State also plans to contribute $246 million in FY2025.[71] The State is to be commended for committing regular contributions of revenue to the reserve fund. However, to reach the recommended goal of 10% of general fund revenues, or about $5 billion, the State should increase the rate at which it grows the reserve fund.

Recommendation: The State of Illinois should work toward building a reserve fund equal to 10% of General Funds revenues to better cushion the budget from the next economic downturn.

Collaboratively Align State Support with Local Government Needs

It is critical for the State to recognize how its decisions impact local governments and to provide local governments with the necessary resources to support their own operations and foster economic stability at the local level. There are many funding needs at the local and regional levels that need to be considered as part of a strategic spending plan. Several competing interests are currently asking the State of Illinois for massive influxes in funding, including Chicago Public Schools and the Chicago regional transportation agencies. Chicago Public

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[65] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Illinois Revenue Volatility Study Public Act 98-0682*, Updated February 17, 2015, p. 99.
[66] Illinois General Assembly, Commission on Government Forecasting and Accountability, *Illinois Revenue Volatility Study Public Act 98-0682*, Updated February 17, 2015, p. 103.
[67] Government Finance Officers Association, *Best Practices: Fund Balance Guidelines for the General Fund*, September 2015.
[68] Civic Federation, *GOFA Recommends Governments Rethink Their Reserve Policies*, September 15, 2023
[69] Government Finance Officers Association, *Should we Rethink Reserves?*, May 2023.
[70] State of Illinois Governor's Office of Management and Budget, *Illinois State Budget Fiscal Year 2025*, February 21, 2024
[71] State of Illinois Governor's Office of Management and Budget, *Illinois Economic and Fiscal Policy Report*, November 1, 2024, p. 12.

Schools (CPS) is calling on the State for additional funding of $1.1 billion annually,[72] and the Regional Transportation Authority, which oversees Chicago-region public transit, is calling for additional funding of $1.5 billion, including $770 million needed to close a projected FY2026 budget gap.[73]

Support for municipalities through the Local Government Distributive Fund (LGDF)—the fund through which the local share of State income tax collections is distributed to municipalities—has declined.[74] In 2011, as part of a temporary income tax increase, the percentage share of the LGDF to local governments was reduced from 10% to 6%. Though the local share percentage has undergone various revisions through the years, it has never been restored to the full 10%. The rates for FY2025 were 6.47% for individual income taxes and 6.845% for corporate income taxes.[75] An increase in the rate warrants consideration for both existing taxes and any new taxes the State may impose.

Compounding this challenge, in recent years, the State has made decisions without consultation with local governments. For example, the FY2025 budget eliminated the 1% retailer's occupation tax applied to food purchased for consumption at home, referred to as the grocery tax, starting in 2026.[76] This loss in revenue could mean significant budget holes for many municipalities. Local governments were allowed to enact their own locally imposed version of the grocery tax but were not involved in the decision-making process for this change.

As the State continues to address a number of funding needs at the local level and considers the pension enhancements needed to comply with Safe Harbor rules, the Civic Federation urges the State to consider several principles. First, the State should refrain from imposing unfunded mandates, such as pension benefit enhancements or new debt obligations, without consultation from local government entities and a clear plan to fund those additional costs. The State should also consider calibrating support for municipalities through the Local Government Distributive Fund in ways that mitigate inequitable and regressive fiscal and taxpayer burden and incentivize economic and population growth. Doing so should be effected through the use of a collaboratively formulated strategic framework to guide State funding decisions that includes parameters for helping financially distressed local governments.

Recommendation: Illinois should adopt a more collaborative approach to policy-making that impacts funding for local government entities to ensure adequate funding to support local service needs.

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[72] Samantha Smylie, "Report: Illinois schools won't be 'adequately funded' by 2027," *Chalkbeat Chicago*, May 15, 2024.
[73] Regional Transportation Authority, *Transforming Transit: Our Vision for Chicago's Future*.
[74] Illinois Department of Revenue, Income Tax Distributions to Local Governments.
[75] Illinois Municipal League, "LGDF – Local Share of State Income Tax Revenue: A Critical Investment in Illinois Communities," August 14, 2024.
[76] Todd Feurer, "Gov. JB Pritzker signs legislation ending Illinois grocery tax in 2026," *CBS News Chicago*, August 5, 2024.

Improve Transparency in the Budgeting and Legislative Process

Budget and Budgeting Process

There are deficiencies in the transparency and availability of information regarding the State budget and budgeting process, which hinders public understanding and trust. Currently, many Illinois residents lack access to clear, comprehensive details about how their governments' budgets are developed, funded, and allocated. To improve transparency in State government and legislative process, a variety of steps can be taken to enhance access to information and public understanding.

To begin to enhance fiscal transparency, the State should provide a clear, detailed breakdown of the fiscal year's personnel budget, such as Colorado does.[77] This should begin with guidance on how to interpret the budget, including explanations of common terms, charts, and categories, which would further empower the public to analyze and assess State spending decisions.

This should be accompanied by an accessible and user-friendly explanation of the foundational aspects of the budgeting process to foster greater public understanding and transparency. This explanation should outline the budget development timeline, from initial planning to final approval. It should detail how the State identifies the key sources of revenue, such as income taxes, sales taxes, and federal funding to provide clarity on where the State's funds originate. It should also provide an in-depth analysis of State revenue streams, such as the specific allocation of tax dollars to various programs and services. Ultimately, this level of detail would promote accountability and provide citizens with the tools they need to evaluate the State's fiscal priorities and performance and when they can engage in the budgeting process.

While Illinois has taken steps to include metrics in the State budget as part of its performance-based budgeting efforts, there is a lack of clarity about whether these metrics are truly meaningful. To enhance transparency and effectiveness, the State should focus on ensuring that performance metrics included in the budget are directly tied to resource allocation decisions and measurable outcomes. Metrics should be clearly defined, consistently monitored, and explicitly linked to the State's strategic goals. By improving the quality and relevance of the performance data in the budget, Illinois can better demonstrate how taxpayer dollars are being used to achieve desired outcomes. Providing detailed explanations of how these metrics are developed, analyzed, and used to guide decision-making would further enhance public trust and understanding of the budgeting process. These steps would make performance-based budgeting more impactful for driving accountability and improving the efficiency of public programs.

Illinois General Assembly

In terms of legislative transparency, the Illinois General Assembly (ILGA) can take several steps to make its process more open and user-friendly. First, the ILGA should offer free access to an online archive of legislative hearings, with links to recordings and platforms for viewing or

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[77] Colorado State Budget.

listening, which would allow residents to follow legislative discussions more closely. According to the National Conference of State Legislatures (NCSL), all 50 states now livestream floor proceedings, and most legislatures, including Illinois, also livestream all or selected committee hearings.[78] Several states archive and provide on-demand recordings of floor and committee proceedings at no charge, but Illinois is one of only four states that do not offer this service. In Illinois, the third-party platform BlueRoomStream live-streams selected hearings, press conferences, and Illinois Supreme Court proceedings, and some videos remain online. An expensive subscription is required to access these videos.

Additionally, the ILGA website should publicly post meeting materials, such as presentations, testimony copies, and other related documents provided to legislators but not made available to the public. Making information about the budget and audits available online would further enhance financial transparency. By adopting these measures, Illinois could significantly improve access to legislative proceedings and documents, fostering a more transparent and accessible government.

Another step towards enhancing transparency and accessibility in Illinois' legislative process is ensuring all legislators' email addresses are readily available on the Illinois General Assembly website. Currently, not all legislators' emails are listed, making it difficult for constituents to communicate directly with their representatives. This lack of uniform access to contact information undermines public engagement and limits opportunities for constituents to provide input or seek assistance on legislative matters. Improved access to contact information fosters transparency, strengthens the relationship between lawmakers and their constituents, and ensures that the voices of Illinois residents are heard in the legislative process.

A dedicated webpage for ballot initiatives would be a valuable resource for fostering civic engagement and empowering citizens to actively participate in shaping State policy. This webpage should provide a step-by-step guide to the process of getting an initiative on the ballot, including eligibility requirements, deadlines, signature collection guidelines, and submission procedures. Additionally, it should include a searchable database of current and past ballot initiatives, allowing citizens to easily track the progress of existing proposals, review their content, and understand their potential impact. This would enhance transparency by providing clear and accessible information about one of the most direct forms of democratic participation.

Moreover, addressing the lack of a search function for legislation prior to 1971 would fill a significant gap in historical accessibility and support State legislative history research. Currently, individuals seeking to research or reference legislative actions from before this period face significant challenges due to the lack of readily available information. Creating a comprehensive, searchable archive of pre-1971 legislation would support scholars, policymakers, journalists, and the public in understanding Illinois' legislative history. This resource would also provide valuable context for evaluating the evolution of State laws and policies, offering insights that can inform present and future decision-making. Together, these

[78] National Conference of State Legislatures, "Legislative Broadcasts and Webcasts," May 27, 2022.

measures would promote greater accessibility, transparency, and engagement in Illinois' legislative and electoral process.

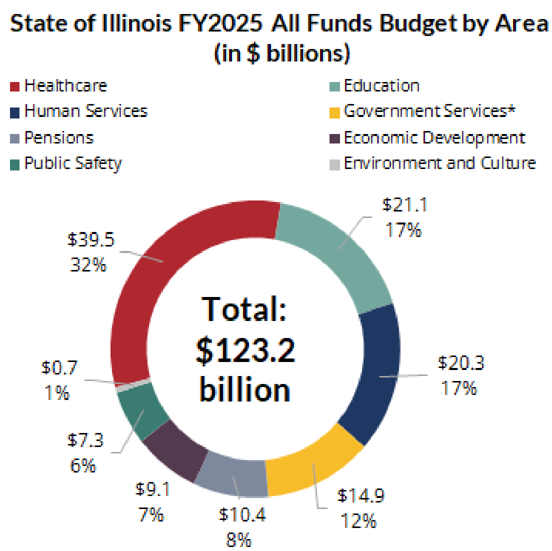
Recommendation: Illinois should provide a detailed breakdown and a clear explanation of the budgeting process. Additionally, the State should update the general assembly website so that it includes free access to the archive of legislative hearings, all legislator's email addresses, a webpage about ballot initiatives, and a search function for legislation prior to 1971.

APPENDIX

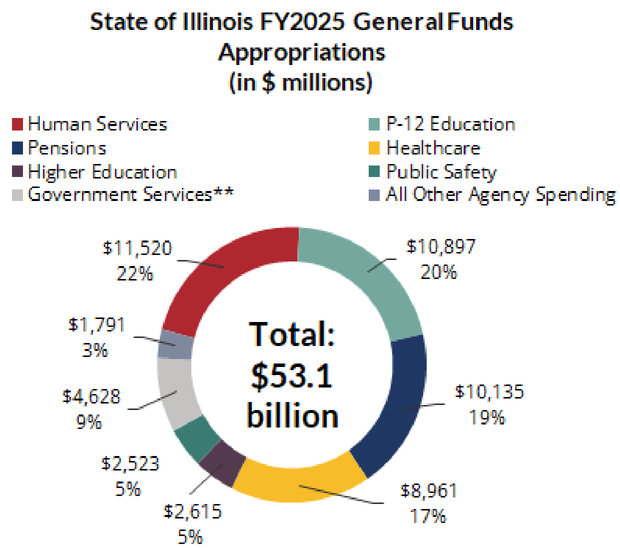
APPENDIX 1: ILLINOIS' FINANCIAL LANDSCAPE

FY2025 Budget

The State's FY2025 operating budget totaled $123.2 billion across all funds and $53.1 billion in the General Funds (which cover general operations). The charts below show the budget by program area. The General Funds support the regular operating and administrative expenses of most State agencies and are the funds over which the State has the most discretionary control. The total operating budget also includes Other State Funds, which account for activities funded by revenue sources that may only be used for specific purposes, and federal funds, which support a variety of State programs through federal revenue.



*Includes employee group health insurance.
Source: Illinois State FY2025 Proposed Budget, p. 89.



*Does not include unspent appropriations or transfers out of General Funds.
**Includes employee and group health insurance.
Source: State of Illinois FY2025 Enacted Budget Financial Walkdown.

The General Funds budget for FY2025 originally projected a $970 million budget gap, which was closed through the following tax changes and enhancements:

- Extending the limit on corporate net operating loss deductions, which were set to expire, through tax year 2027, at a new threshold of $500,000 compared to the current limit of $100,000. This is projected to yield $526 million.

- Capping the Retailers' Discount of 1.75% that Illinois retailers are allowed to recoup for the cost of collecting sales taxes on behalf of the state. The proposed cap is $1,000 per month, which would only impact 1% of retailers. This is expected to generate $101 million for the State's General Funds and $85 million for local governments.

- Increasing the Sports Wagering Tax rate from 15% to 35%, of which the increased portion of the tax collected above 15% would be transferred to the General Fund. This is expected to generate an additional $200 million in revenue.

- Setting the standard personal income tax deduction at $2,250, which reflects a one-year Consumer Price Index (CPI) adjustment but is a lower deduction than would otherwise occur under existing state statute. This change would increase General Funds revenue by $93 million.

- Making a supplemental $175 million deposit into the Public Transportation Fund from the Road Fund, thereby reducing the need for General Funds to be diverted.

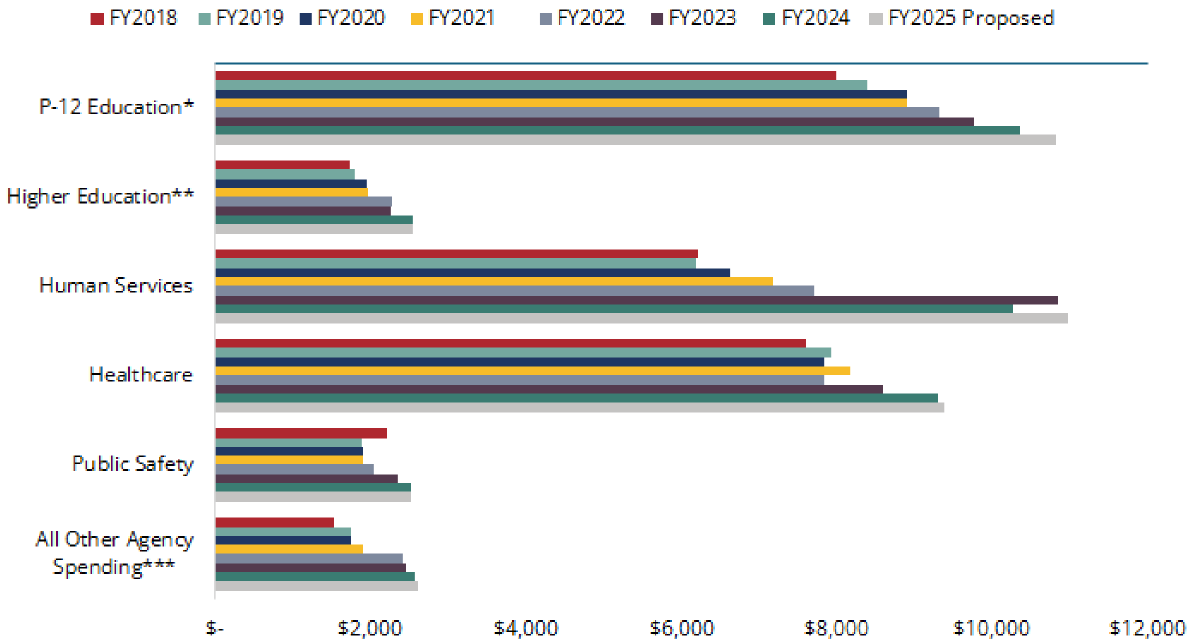
- Directing a $25 million increase in the distribution of part of the Real Estate Transfer Tax to the General Fund, rather than the Open Space Lands Acquisition and Development Act (only for FY2025).

The State has enacted large spending increases in recent years. The chart below shows the progression of spending by agency area from FY2018 to FY2025 within the General Funds. State agency spending consistently increased over this period, particularly during the years of federal aid, which resulted in the creation of several new programs and initiatives. Over the eight-year period shown, State agency spending increased by $11.6 billion, or 42.4%, which includes the following increases by agency:

- $2.8 billion (45.4%) for P-12 Education;
- $181 million (47.2%) for Higher Education;
- $4.8 billion (76.6%) for Human Services;
- $1.8 billion (23.2%) for Healthcare;[79]
- $312 million (14.1%) for Public Safety; and
- $1.1 billion (70.4%) for All Other Agency Spending.

[79] The State's healthcare category refers to the Department of Healthcare and Family Services (HFS), which is the Illinois agency mainly responsible for Medicaid, the joint federal-state program that pays for healthcare for low-income people.

State of Illinois General Funds Agency Expenditures and Appropriations by Area (in $ millions)



*P-12 Education does not include contributions to the Teachers' Retirement System or the Teachers' Retirement Insurance Program.
**Higher Education does not include contributions to the State Universities Retirement System or the College Insurance Program.
***All Other Agency Spending includes the State contribution to the Chicago Teachers' Pension Fund and the areas of Economic Development, Environment and Culture and Government Services (excluding group insurance).
Source: Illinois State FY2018-FY2025 Proposed Budgets.

Unfortunately, despite the State's strong post-pandemic recovery, revenue growth has been insufficient to account for these annual increases. Most of the State's revenue derives from individual income tax, corporate income tax, and (as discussed earlier, a narrowly structured) sales tax—each of which is susceptible to economic fluctuations and may limit the State's future growth. In the upcoming 2026 fiscal year, the State now faces a preliminarily projected budget deficit of over $3 billion, driven by a $74 million decrease in total revenue and a $3.2 billion increase in expenditures.

FY2025 and FY2026 Projections

Illinois plans its budget each year based on estimates of revenue performance and current-year spending that are adjusted over time as revenue performance is observed throughout the year. This provides a framework of the State's finances that ultimately sets the stage for the following year's budget.

The table on page 33 shows the General Fund revenue and expenditure estimates from the enacted FY2025 budget (adopted in June 2024),[80] the most recent estimates for year-end

[80] Governor's Office of Management and Budget, State of Illinois General Funds Financial Walk Down, June 4, 2024.

FY2025 (released in November 2024),[81] and projections for FY2026 based on the Governor's Office of Management and Budget's Economic and Fiscal Policy Report.

FY2025 year-end estimates are generally on target with revenues and expenditures in the FY2025 adopted budget. The enacted FY2025 Budget anticipated a General Funds surplus of $211 million, of which $198 million would be contributed to the Budget Stabilization Fund ("rainy day" fund), leaving an adjusted surplus for FY2025 totaled $13 million. The Governor's Office of Management and Budget expects both revenues and expenditures to end the current 2025 fiscal year slightly higher than budgeted levels, resulting in a $262 million surplus.[82] As noted in a monthly report released by the Commission on Government Forecasting and Accountability in November,[83] the economy has performed better than expected, which is reflected in the State's revenue results.

The FY2026 projection, however, shows a nearly $3.3 billion budget deficit that will need to be closed. The budget gap is driven by a $74 million decrease in resources and a $3.2 billion increase in projected expenditures. Revenue from State sources (excluding federal) is expected to see a net increase of $228 million, or 0.5%. While individual and corporate income taxes are expected to increase cumulatively by $1 billion, sales tax, public utility taxes, and all other sources are projected to collectively decrease by $782 million. This is in part due to the ongoing shift of revenues generated by the state sales tax on motor fuel from the General Funds to the Road Fund (5% of the total share). Concurrently, expenditures are projected to balloon by nearly $3.2 billion due to significant spending increases across a number of key areas, including K-12 education, human services, healthcare spending (i.e. Medicaid spending), employee health insurance, and contributions to State pension funds.[84]

The Governor's proposed FY2026 budget, expected to be released on February 19, 2025, will show updated projections for both FY2025 and FY2026 based on additional data that have come in since the release of the Economic and Policy report in November 2024.

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[81] Governor's Office of Management and Budget, Illinois Economic and Fiscal Policy Report, November 1, 2024.
[82] Governor's Office of Management and Budget, Economic and Fiscal Policy Report, November 1, 2024.
[83] Commission on Government Forecasting and Accountability, Monthly Briefing For the Month Ended: November 2024, 2024.
[84] Governor's Office of Management and Budget, Illinois Economic and Fiscal Policy Report, November 2024.

FY2025 and Projected FY2026 General Funds Financial Walkdown
(in $ millions)[1]

	FY2025 Enacted (June 2024)	Year-End FY2025 Estimates (Nov. 2024)	FY2026 Projected (Nov. 2024)	Year-End FY2025 - Projected FY2026 $ Change	Year-End FY2025 - Projected FY2026 % Change
RESOURCES					
State Sources: Revenues					
Net Individual Income Taxes	$ 26,507	$ 26,992	$ 27,776	$ 784	2.9%
Net Corporate Income Taxes	$ 5,378	$ 5,299	$ 5,525	$ 226	4.3%
Net Sales Taxes	$ 10,907	$ 10,696	$ 10,369	$ (327)	-3.1%
Public Utility Taxes	$ 701	$ 691	$ 684	$ (7)	-1.0%
All Other Sources	$ 3,203	$ 3,280	$ 2,832	$ (448)	-13.7%
Total State Sources: Revenues	**$ 46,696**	**$ 46,958**	**$ 47,186**	**$ 228**	**0.5%**
State Sources: Transfers In					
Lottery	$ 902	$ 902	$ 906	$ 4	0.4%
Gaming	$ 177	$ 177	$ 182	$ 5	2.8%
Adult-Use Cannabis	$ 123	$ 123	$ 123	$ -	0.0%
Sports Wagering	$ 200	$ 200	$ 204	$ 4	2.0%
Other Transfers	$ 1,159	$ 1,095	$ 700	$ (395)	-36.1%
Total State Sources	**$ 49,257**	**$ 49,455**	**$ 49,301**	**$ (154)**	**-0.3%**
Federal Sources	$ 4,024	$ 4,024	$ 4,104	$ 80	2.0%
TOTAL RESOURCES	**$ 53,281**	**$ 53,479**	**$ 53,405**	**$ (74)**	**-0.1%**
EXPENDITURES					
1. Education	**$ 13,513**	**$ 13,513**	**$ 14,035**	**$ 522**	**3.9%**
PreK-12 Education	$ 10,897	$ 10,897	$ 11,341	$ 444	4.1%
Higher Education	$ 2,615	$ 2,616	$ 2,694	$ 78	3.0%
2. Economic Development	**$ 387**	**$ 382**	**$ 388**	**$ 6**	**1.6%**
3. Public Safety	**$ 2,523**	**$ 2,522**	**$ 2,613**	**$ 91**	**3.6%**
4. Human Services	**$ 11,520**	**$ 11,519**	**$ 12,093**	**$ 574**	**5.0%**
5. Healthcare	**$ 8,961**	**$ 8,961**	**$ 10,061**	**$ 1,100**	**12.3%**
6. Environment and Culture	**$ 133**	**$ 132**	**$ 136**	**$ 4**	**3.0%**
7. Government Services	**$ 4,628**	**$ 4,888**	**$ 5,243**	**$ 355**	**7.3%**
Group Health Insurance	$ 2,327	$ 2,327	$ 2,877	$ 550	23.6%
Chicago Teachers' Pension Fund	$ 354	$ 354	$ 363	$ 9	2.5%
Government Services	$ 1,947	$ 2,207	$ 2,003	$ (204)	-9.2%
9. Unspent Appropriations	**$ (895)**	**$ (950)**	**$ (990)**	**$ (40)**	**4.2%**
Total Operating Budget	**$ 40,770**	**$ 40,967**	**$ 43,579**	**$ 2,612**	**6.4%**
EXPENDITURES: PENSIONS					
K-12 Education Pensions	$ 6,204	$ 6,204	$ 6,496	$ 292	4.7%
State Universities' Pensions	$ 1,998	$ 1,998	$ 2,106	$ 108	5.4%
State Employees' Pensions	$ 1,933	$ 1,933	$ 1,971	$ 38	2.0%
Total Pension Costs	**$ 10,135**	**$ 10,135**	**$ 10,573**	**$ 438**	**4.3%**
EXPENDITURES: TRANSFERS OUT OF GENERAL FUNDS					
Statutory Transfers Out	$ 445	$ 445	$ 454	$ 9	2.0%
Debt Service	$ 1,720	$ 1,670	$ 1,788	$ 118	7.1%
Total Transfers Out	**$ 2,165**	**$ 2,115**	**$ 2,242**	**$ 127**	**6.0%**
TOTAL EXPENDITURES	**$ 53,070**	**$ 53,217**	**$ 56,394**	**$ 3,177**	**6.0%**
General Funds Surplus/Defecit	**$ 211**	**$ 262**	**$ (2,989)**	**$ (3,251)**	**-1240.8%**
Budget Stabilization Fund Contribution	**$ (198)**	**$ (246)**	**$ (186)**	**$ 60**	**-24.4%**
Adjusted General Funds Surplus/(Deficit)	**$ 13**	**$ 16**	**$ (3,175)**	**$ (3,191)**	**-19943.8%**

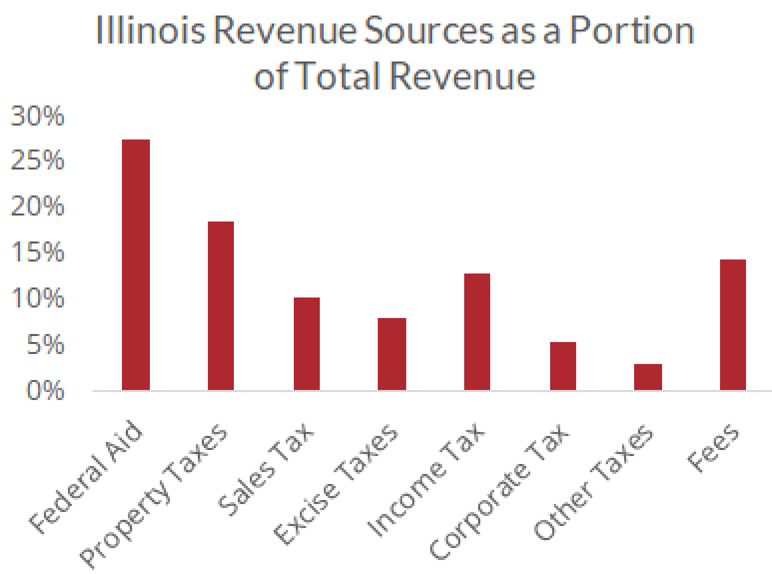
Source: GOMB FY2025 Enacted Budget General Funds Walk Down and 2024 Illinois Economic and Fiscal Policy Report.

[1]Totals may differ slightly due to rounding.

APPENDIX 2: TAX BURDEN LANDSCAPE

This appendix provides additional details about Illinois' tax burden as measured by revenues as a percentage of the state's total personal income—the total of all income earned by individual residents of the state—based on data collected by the Census Bureau for 2022.

Rather than comparing Illinois to all 50 states, which have a variety of different economies and needs, a selection of peer states is used for comparison here based on their similarities in geography and population size. This group includes the top five states by population (Illinois is ranked 6th) and a set of neighboring midwestern states. The list of peer states is as follows: California, New York, Texas, Florida, Pennsylvania, Ohio, Michigan, Indiana, Wisconsin, Missouri, Iowa, and Minnesota.



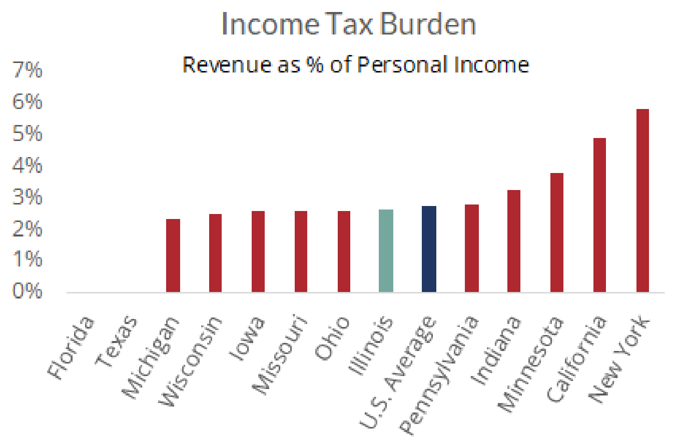
Source: Census Bureau, Annual Survey of State and Local Finances

Individual Income Tax

With a tax burden of 2.63% of total personal income—for the tax that every income earner pays annually to both federal and state governments—Illinois ranks sixth highest among the 13-member peer group.[85] This puts it close to the national average of 2.72% and far below New York's high of 5.76%. It is also worth noting that seven states levy no income tax, including two from the peer group: Texas and Florida.[86]

[85] U.S. Census Bureau, *Resident Population in the States*, December 2024. Note that there are notable discrepancies on reported Illinois tax revenue between recent Census Bureau data and the Illinois Comptroller's Office, especially in individual income tax revenue and corporate income tax revenue.
[86] Civic Federation, *Individual Income Tax Structures in Selected States*, March 27, 2020.

With such a high overall tax burden, it might seem anachronous that Illinois' income tax burden is average for what is the largest source of revenue for most states. This fact owes itself largely to Illinois' flat income tax rate. While many states, especially larger states such as New York and California, have graduated income taxes like the federal tax bracket structure, Illinois instead levies a flat 4.95% tax on all income earners regardless of their level of income.[87] This tax is not progressive, which means that it extracts more tax revenue from low-income earners than graduated tax structures do but takes less revenue from high-income earners. Due to its low flat rate income tax, Illinois is less reliant on income taxes than on other forms of taxation for revenue. Although this means that Illinois residents face a comparatively low income tax burden, state and local governments make up for this with other taxes that impose higher burdens.

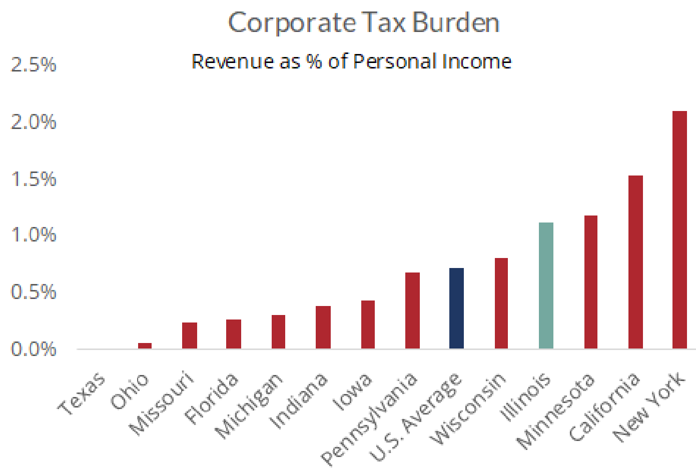


Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

Corporate Income Tax

Most states use flat tax rates to structure their corporate taxes, but fifteen use graduated systems instead. Six states levy no corporate income tax. However, four of those states, including Texas, levy gross receipts taxes instead. Gross receipts taxes levy a tax on every transaction made by a business and are generally considered more harmful than corporate income taxes as they create a larger economic disruption, along with perverse incentives toward vertical integration.[88] A handful of states also allow local governments to levy corporate income taxes.[89] Illinois levies a flat corporate income tax of 9.50%.[90] With corporate tax revenues equal to 1.12% of total personal income, Illinois is the fourth highest state among its peer group. It is also notably 55% above the national average of 0.72%.[91]

[87] Tax Foundation, *State Individual Income Tax Rates and Brackets, 2024*, February 20, 2024.
[88] Vertical integration happens with companies internalize parts of their supply chain. Gross receipts tax can create an artificial incentive for businesses to buy up suppliers or retailers to reduce the total number of transactions with other businesses they are taxed for.
[89] Tax Policy Center, *How do State and Local Corporate Income Taxes work?*, Updated January 2024.
[90] Tax Foundation, *State Corporate Income Tax Rates and Brackets, 2024*, January 23, 2024.
[91] The majority of corporations in Illinois are pass-through entities, which only pay replacement taxes and are not taxed under the corporate income tax. Most of the state's largest corporations, however, do pay this tax.



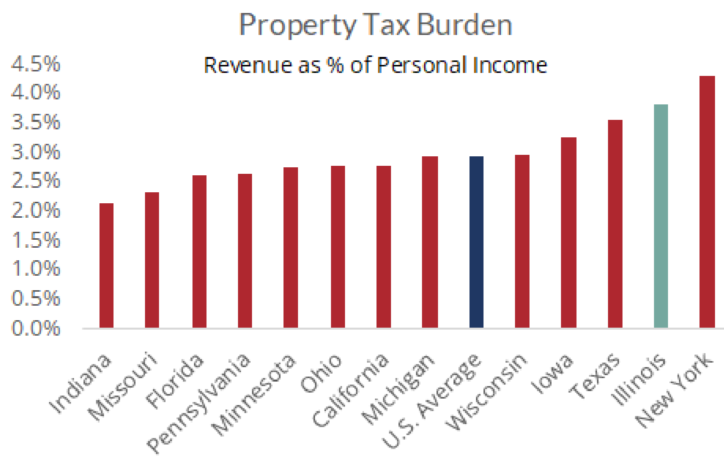
Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

Property Tax

Illinois ranks second highest among the peer group, with a property tax burden of 3.81% of total personal income. While a few other states have similarly high tax burdens, most notably New York at 4.28%, the average burden among all 50 states is 2.94%, and most peer states are more than a full percentage point lower than Illinois.

Property taxes are predominantly a revenue tool utilized by local governments rather than state governments.[92] Illinois is no exception to this rule. Illinois shifts responsibility for a variety of government services onto localities, which respond by levying taxes to make up for revenue not accounted for by state assistance. Illinois' relatively low state income tax means that the State has less revenue, so it provides less support to localities, forcing local governments to make up the difference by levying high property tax rates. The disproportionately high rate of property tax revenue in Illinois is likely also related to Illinois' high number of unique local governments. As of 2021, the Civic Federation counted 8,924 local governments in the State, a far higher number than any other state.[93]

[92] Lincoln Institute of Land Policy, *50-state Property Tax Comparison Study*, August 2023.
[93] Civic Federation, An Inventory of Local Governments in Illinois, February 25, 2021, pp. 3-6 and 10-11.

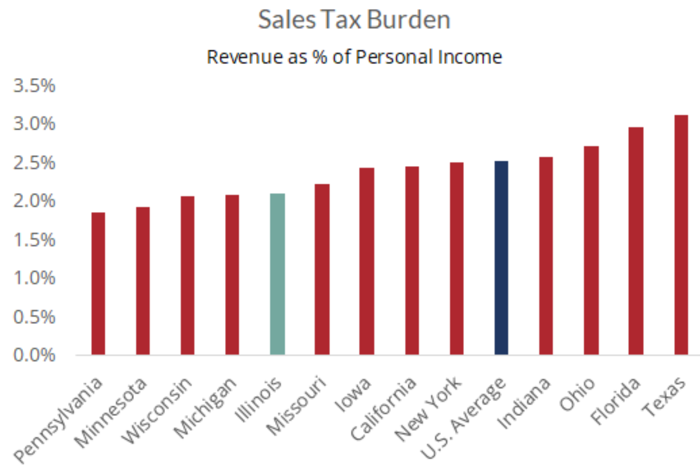


Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

Sales Tax

In most states, both state and local governments levy sales taxes, and consumers pay the combined tax on their purchases. Illinois levies a 6.25% statewide sales tax on general merchandise, of which 1.25% is remitted to local governments.[94] Local taxes vary widely, but the average aggregate tax in Illinois is 8.87%, while Chicago has a total tax of 10.25%, one of the highest municipal rates in the nation.[95] Illinois has the highest aggregate average sales tax rate among the peer group selected for this report. However, it has only the ninth highest tax burden out of the peer group, at 2.10% of total personal income. This is notably below the national average of 2.52%. While this fact may seem counterintuitive, it is due to the narrow tax base for sales taxes in Illinois, as Illinois is among the minority of states that do not tax most services under the sales tax. Thus, though Illinois has an aberrantly high sales tax rate, it imposes a lower tax burden on residents through this tax than would be expected.

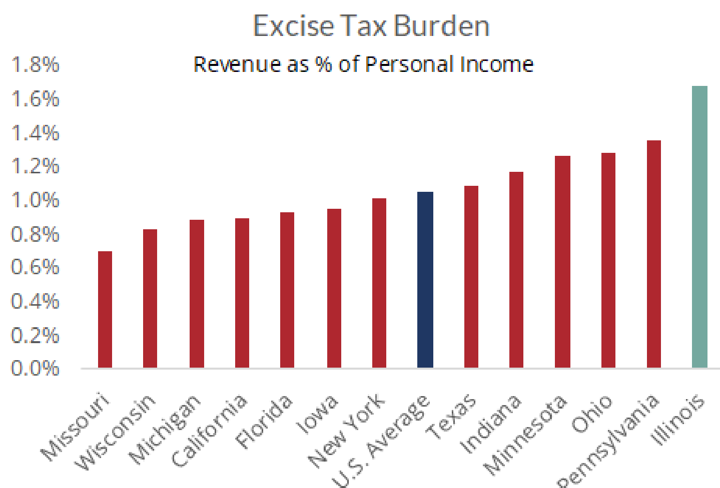
[94] Tax Foundation, *State and Local Sales Tax Rates, Midyear 2024*, July 9, 2024.
[95] Civic Federation, *Consumer Taxes in Chicago: A Compilation of Selected Taxes in Place in the City of Chicago as of January 1, 2024*, April 18, 2024.



Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

Excise Taxes

Illinois imposes a variety of excise taxes on specific goods including alcohol, cigarettes, motor fuel, and marijuana.[96] Although all states tax these goods, Illinois taxes most of them at rates notably higher than average. This contributes to an overall excise tax burden that is first among peer states at 1.68% of personal income and is far above the national average of 1.05%.



Source: Census Bureau, Annual Survey of State and Local Finances; U.S. Bureau of Economic Analysis, Personal Income Inlays and Outlays

[96] Illinois Department of Revenue, *Excise Tax Rates and Fees*, 2025.