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# Report of the **Taxpayer Action Board**

**June 2009**

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## TAXPAYER ACTION BOARD

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President, Taxpayers' Federation of Illinois

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Former State Legislator

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## **EXECUTIVE SUMMARY**

On March 18, 2009, Governor Pat Quinn appointed the Taxpayer Action Board, or TAB, to identify opportunities that can guide Illinois toward long-term, sustainable fiscal health. Within the context of the three pillars of his 2010 budget proposal – reform, responsibility, and recovery – the Governor charged the TAB with exploring ideas and identifying new approaches that will bring substantial efficiencies to State government and thus enable it to better meet its commitment to its constituents.

Hailing from many locations throughout Illinois, the 33 individuals named to the TAB by Governor Quinn represent a diverse group of experience and expertise in both the private and public sectors. Given the importance and immediacy of the issues at hand, the TAB was asked to deliver its final report by the end of May, a two-month period.

### **The Context Defining the TAB's Work**

Projected to spend approximately \$53 billion in FY10, the State of Illinois is facing an extraordinary challenge: Without action, the projected budget deficit for FY09 and FY10 combined is at least \$11.6 billion. While today's recession exacerbates the challenge by forcing revenues lower, the budget gap is not a new or one-time problem. Costs have been rising faster than revenues for years, and now the State's fiscal problem has reached a crisis. In the same period (FY08 to FY10) during which revenues are expected to decline by 9% (\$2.7 billion), spending in the State's general fund is projected to jump from \$30.5 billion to \$34.3 billion, a 12.5% increase, unless radical steps are taken. All told, Illinois' total liabilities and unfunded commitments are now in excess of \$110 billion, and growing rapidly. Without bold action, the services our taxpayers depend on will continue to be squeezed, while we leave to future generations an ever-increasing mountain of debt.

Furthermore, in the FY10 budget, much of the roughly \$2 billion increase over FY09 will be funded by increased federal funding through the American Recovery and Reinvestment Act (ARRA), otherwise known as the stimulus bill. That funding ceases in 18 months on December 31, 2010, and will leave a tremendous hole in the funding of State programs.

Waiting for the recession to end will not bring relief. The problems started well before the recession, and now are of such a magnitude that only large-scale, fundamental rethinking of State government will solve them. Inaction will only result in accelerated deterioration of services and larger burdens for our children, and for future generations.

Thus, as members of the TAB, we took as our charge a mandate to think innovatively, to consider best practices from other states and, where appropriate, from the private sector, and to look critically at whether underlying structures, processes, and federal funding mechanisms are set up as efficiently and effectively as possible. Ideas to add or increase net State costs were not considered. Nor were ideas to increase State revenues, as our explicit charge was to examine costs.

## The TAB's Process

Led by Tom Johnson of the Taxpayers' Federation of Illinois, the TAB organized itself into subcommittees to consider ideas in six focus areas: human services; Medicaid; State employees' retirement and healthcare benefits; education; government operations; and public safety. Each subcommittee considered opportunities for efficiencies and improvements within its area of focus, and then advanced its ideas to the full TAB for discussion, deliberation, and refinement. Meetings were public and open, and a number of individuals and organizations attended, presented at, and actively participated in these sessions frequently. Additionally, a web site was established that enabled members of the public to comment and submit their own ideas: 23 such ideas were submitted via the web site, all of which were then shared with the subcommittees. A handful of organizations also submitted full papers for review by the subcommittees.

For the past two months, the 33 members of the TAB have met five times in full board sessions and in numerous subcommittee meetings to shape the ideas included in this report. We would particularly like to commend the many State agency staff that provided data and made presentations to subcommittees, often on short notice.

The work of the TAB was also supported by the efforts of 15 consultants, all of whom participated on a *pro bono* basis. The consultants acted as subcommittee "conveners," identifying best practices and examples of efforts in other states, interviewing approximately 120 State staff and external experts, and supporting subcommittee and full TAB deliberations.

The accelerated, two-month timeframe necessitated an often fast-paced review of potential opportunities and limited the TAB's ability to assess fully all of the factors necessary to implement the ideas it has generated. As a result, we expect that ideas in this report will be refined as our elected representatives and State staff work out their implementation. Also, this timeframe did not allow us to review some significant State programs (such as public health or certain aspects of transportation, among others) sufficiently to allow us to make recommendations or identify opportunities in those categories. In other areas, such as payroll, education, and local government revenue sharing, certain areas of spending are so large that they necessitate a deep look. While we touch on these areas in this report, we know they merit further scrutiny. As such, other opportunities for reducing costs are no doubt feasible. Because they do not appear in this report, does not mean they do not exist.

Our deliberations were driven by consensus. As a result, while the opportunities identified in this report represent the consensus opinion of the TAB, some ideas are not supported by individual members. Where feelings were strong, TAB members were encouraged to write minority opinions. Those opinions are included in the supplemental materials of the report. Additionally, we include in this report a few other ideas, which were brought to the TAB but for which we did not have adequate time or information to assess. Rather than omit potentially valuable ideas, we have included in the report brief mentions of those possibilities, but we are not in a position to endorse or reject them.

Throughout, we tried not to let political concerns enter our deliberations. Rather we focused on new ways to reduce the State's severe fiscal imbalance. As the opportunities outlined in this report make their way

through legislative debate, collective bargaining, or other relevant vetting, those processes will weigh the arguments of competing interests and navigate toward hopefully reasonable compromise. That is what those vetting processes are designed to do. What those processes aren't so well-equipped to do is to come up with dramatic remedies for a problem that may require strong medicine and demanding changes to the operation of State government and the delivery of services. That has been our charge for the past two months.

### **Summary: Opportunities Identified by the TAB**

To focus our analysis, we established a set of guiding principles for the TAB's work, noting that discussions should identify and develop opportunities that:

- Cut significant costs to the State
- Maintain or, where possible, improve service levels
- Are feasible either immediately, within the 18-month stimulus time horizon, or within five years
- Evaluate government structures (e.g., Are State functions currently located in the right department or segment of government?)
- Consider new methods of delivery and operations to assess whether the current practice is the best way to provide services
- Include a review of direct operations as well as awards, grants and contracts

The TAB was driven by a commitment to ensure that taxpayers' dollars are being spent well and effectively. The TAB strongly believes that substantial efficiencies can be gained by introducing new approaches, best practices, and sometimes simple modifications – with minimal if any change to the services enjoyed by constituents.

### **State Services and Programs**

As the TAB considered specific opportunities for efficiencies within the State's systems, we placed critical importance on the need to maintain service levels experienced by recipients of State programs. Changing government systems and identifying efficiencies both run the risk of impacting service levels, but we sought to identify those opportunities for savings that would not impact program eligibility.

However, if by the time that the stimulus funds run out, the types of actions outlined in this report are not taken or are not producing the levels of savings we have identified, the State will have no choice but to make dramatic cuts in eligibility and probably in service levels. We can't underscore this enough: when stimulus funding ends, the State will face a crisis so much more severe than today's that it will have no choice but to drastically reduce the services it offers. That time will come in just 18 months. To avoid that fate, the State must take bold steps – today.

## **Cost Savings**

Throughout this report, we have tried to identify areas that hold opportunity for significant, achievable cost savings. We have quantified those potential savings where we could, using data provided by State agencies and the Office of Management and Budget; making projections based on trends observed; and studying comparable experiences and efforts in other states.

Each opportunity is presented independently in this report, with a chapter dedicated to ideas for improvements and efficiencies in each of the following areas: human services, Medicaid, State employees' pensions and health care, education, government operations, and public safety. We have also included a section on State-wide opportunities – those ideas that cut across all State agencies and, while perhaps less refined in their approach, can enable the State to save significant costs very quickly during this critical time.

We caution against simply sum-totaling our list of identified opportunities, as some of the ideas could be mutually exclusive, or some may overlap.

That said, we believe that the full set of these opportunities provides the State with an idea pool of several billion dollars in potential annual savings that could be implemented within the next five years – or in many cases, much sooner.

## **A Final Word**

We know there are impediments to implementing these ideas. Where we know the impediments, we have highlighted them in the text. Our challenge and recommendation to the State is this: Don't focus on the reasons why these ideas won't work – they are, by definition, difficult and challenging, and you will find myriad reasons not to pursue them. Rather, find a way to make these ideas work. We would all fall short of our obligation to the people of Illinois to do anything less.



## Overview of potential annual savings

The following table summarizes potential savings associated with the opportunities and ideas generated by the TAB. It is important to recognize that these numbers are rough approximations and should serve more as targets than as concrete calculations of savings.

The TAB developed these estimations through a number of means: some are based on our analyses of data provided by State agency staff; others are estimated from historical and projected trends, the experiences of other states, and best practices. We present our ideas with three time horizons in mind:

- Immediate savings (FY10): What can be put into place within the FY10 budget, to help the State address its current budgetary issues?
- Completion of the stimulus period (FY11): What is possible within the stimulus funding cycle, which concludes December 31, 2010?
- Two to five years (FY12, FY13, and FY14): What will take more time to implement but allows bolder cost reductions to be realized?

The numbers are the approximate *annual* savings potential of each opportunity within the designated time period below. Again, we caution against simply sum-totaling the numbers in this list, as the implementation of one idea may preclude the idea of another, or there may be overlap between certain areas. The purpose here is to provide a menu of significant opportunities for the State to explore.

Potential Annual Savings (\$ Millions)	Achievable in:		
	FY10	FY11	FY12, 13, 14
<b>State-wide</b>			
Make uniform, 2-3% across-the-board operating cuts, from 2009 levels	180-270		
Freeze operational spending at 2009 levels	240		
Limit payroll burden	data not available		
Additional cost reduction opportunities	40	-	-
<b>Human Services</b>			
Adopt an integrated service delivery model	-	20	155-400
Improve approaches to long-term care	-	40	95
Enhance foster care management	-	15	40
Adjust select eligibility levels and rules	-	n/a	n/a
<b>Medicaid<sup>1</sup></b>			
Promote cost-effective care management strategies that focus on the health of the person, promote prevention and wellness, and provide a medical home <sup>2</sup>	95	110	325-850
Reverse the bias toward institutional care in long-term care	70	80	285-635
Enhance pharmacy cost containment efforts	45	55	190-425
Additional cost reduction opportunities	15	15	90-110

<sup>1</sup> Medicaid expenditures receive federal matching fund reimbursement. Savings from changes to Medicaid programs should be discounted accordingly (roughly, half state, half federal). For details, see the Medicaid chapter.

<sup>2</sup> Estimates reflect cost savings created by a decrease in the projected growth rate of Medicaid expenditures, not a spending cut from the current budget level.

## Overview of potential annual savings (cont.)

### Potential Annual Savings (\$ Millions)

Pensions	Achievable in:		
	FY10	FY11	FY12, 13, 14
Introduce a new pension plan for new hires & increase employee contributions for current employees	— see below* —		
Additional opportunity: Change future benefits for current employees	— see below* —		
Consolidate plan administration and service providers			30
Begin reducing unfunded liabilities now		n/a	n/a

### Employee and Retiree Health Care

Restructure premiums	175-200	175-200	
Modify plan design	165	165	
Maximize purchasing efficiencies	50	50	
Modify prescription drug program	35	35	
Change the model for purchasing health care	50-60	50-60	
Manage the health of the covered population			n/a
Additional opportunity: Fund retiree medical obligations	n/a	n/a	n/a

### Education

Consolidate K-12 school districts in Illinois			60-120
Freeze the PTELL adjustment and amend the GSA formula			
Sunset the hold harmless provisions	90	90	90
Block grant the Special Education categorical and move to a common funding formula		15-75	15-75
Consolidate K-12 intermediate service agencies		5-10	5-10

### Public Safety

Reduce low-risk inmate populations	30-65	100-200	200-400
Reduce salary burden	10-40	10-60	15-65
Modernize information technology	1-3	5-25	5-30

### Government Operations

Analyze spending to improve procurement processes		500	500
Manage real estate and facilities as part of asset portfolio	20-60	20-60	20-60
Review local government revenue sharing			n/a
Improve infrastructure financing and development			>100
Minimize costs associated with boards and commissions	3	3	3

\* The time horizon for savings due to changes in the pensions system is very different from that of the other ideas presented here. To introduce a new plan for new hires, the savings begin to be realized as new hires are brought on and the State starts funding their associated pension liability. Thus the savings accrue over a longer period of time. The estimated cumulative savings from the Governor's proposed pension changes are a reduction in the pension liability of \$150 billion by 2045.

Similarly, savings from changes to pension liabilities for current employees would be realized across a longer time horizon. The data were not available for us to be able to calculate a specific amount by which the pension liability would be reduced for this idea.

## STATE-WIDE OPPORTUNITIES

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### MAKE A UNIFORM OPERATING SPENDING CUT ACROSS-THE-BOARD

While across-the-board operating cuts are often criticized as a sledgehammer approach, which can miss large opportunities for cost reductions and penalize disproportionately those programs that are already operating efficiently, a cut of 2-3% in all budget lines from the FY09 appropriation level would save considerable costs and is an option the State should review. An across-the-board cut would in some ways be easier and quicker to implement than targeted reductions, which require detailed analyses of the State's service delivery.

If this is a direction the State takes, we suggest that (1) exceptions be made only for payment of debt and pension obligations and in the case where cuts would result in the direct loss of federal stimulus funds or other federal matching programs; and (2) the legislature increase the agencies' ability to transfer funds amongst agency budget line items, so each agency has maximum leeway to determine, within each of their agency budgets, where it is most appropriate to make the needed cuts.

Finally, we point out that where cuts impact salaries or benefits, the changes will be subject to collective bargaining with the State's employee unions.

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### FREEZE OPERATIONAL SPENDING AT 2009 LEVELS

Short of making across-the-board cuts, the State could consider freezing operating spending at last year's levels for all departments where reductions have not been mandated in the draft FY10 budget. While this action retains some of the problems with across-the-board cuts (i.e., penalizes some programs that are already efficient and misses opportunities for larger savings), the need to renegotiate union contracts will be lessened, and implementation could be easier.

As with an across-the-board cut, we suggest that (1) exceptions be made only in the case where freezing would result in the direct loss of federal stimulus funds or other federal matching programs; and (2) that the legislature increase the agencies' ability to transfer funds amongst agency budget line items, so each agency has maximum leeway to determine, what to cut and what to retain, subject to the requirement that total spend should remain constant.

As with across-the-board cuts, we point out that where freezing impacts already-agreed to salary adjustments or benefits, the changes will be subject to collective bargaining with the State's employee unions.

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## LIMIT PAYROLL BURDEN

The seriousness of the State's economic problems requires serious measures. Given that the majority of operating funds support personnel costs, no comprehensive solution to the State's financial problems can expect to avoid addressing payroll costs. The steps outlined below, and any like them should be made equitably, with consideration for the sacrifices and circumstances of the Illinois workforce.

- **Introduce State-wide pay freeze**

The State could implement a pay freeze for all positions (management, collective-bargained, and exempt positions). Any pay freeze should include all merit-related or step/grade increases, until the State's economic environment can support a reversal of the freeze.

While the TAB did not have the time to conduct a detailed analysis, we believe that this is an opportunity that could save significant funds and the State should consider. Again, any universal pay freeze would be subject to collective bargaining with the State's employee unions.

- **Eliminate certain paid holidays**

The State offers its workforce a significant cadre of paid holidays as part of the total employee benefits package. The current scope of this generous benefit is out of line with the private sector, and should be reduced accordingly. The State should consider eliminating pay for some holidays. This opportunity would represent a substantial savings to the State. Alternatively, the State may also consider converting these paid holidays to work days. Although this choice would not generate savings, it would increase the productivity of State employees and the State's availability to serve the public by providing an increased number of work days. As the majority of the State's positions are classified under collective bargaining agreements, the State will need to work with appropriate representation to realize this opportunity.

- **Move towards amending work rules and re-classifying certain positions**

The vast majority of the State's workforce is subject to defined work rules and position classifications that govern, guide and limit the extent to which employees can support operational needs. The State should consider amending work rules and re-classifying certain positions in order to: (1) help bring positions and salaries in line with comparable private sector compensation levels, and (2) bring work rules in line with modern business practices and needs.

The State should work with the Labor Relations Board and all necessary parties involved in collective bargaining to implement a targeted approach to this effort. Here, too, the State will need to work with appropriate representation to realize this opportunity.

- **Measure the success of the State's shared services centers before further investment to ensure improved customer service and efficiency gains are being achieved**

The State is engaged in a large, multi-year initiative to establish Shared Service Centers across State agencies in an effort to group agencies by similar function to share administrative personnel and duties, improve efficiency, reduce costs and enhance service. The State has currently implemented two of five Shared Service Centers to date. Some have questioned the success of the effort to date,

but its intended application, if implemented effectively, has merit. Before further investments are made, the TAB believes that the State should measure the success of Shared Service Centers, focusing on 1) improvement in customer satisfaction, and 2) gains in efficiency that ensure decreased aggregate costs.

It should be noted that the implementation of the Shared Service Centers may provide an organizational structure that better and more easily enables the implementation of a new Enterprise Resource Planning system, an effort currently in the planning phase.

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## **COORDINATE AND EVALUATE TECHNOLOGY INVESTMENTS THROUGH CAPITAL PLANNING**

Technology is a high priority for many of the State’s executive agencies. Whether a system-wide enterprise resource planning initiative or sustainable energy technologies or an integrated criminal offender tracking system, there is no shortage of identifiable opportunities where the State could improve its operations, service delivery, and efficiency through technology. For example, the State’s current provision of health and human services is spread across five agencies – the Department of Children and Family Services, the Illinois Department of Employment Security, Department of Healthcare and Family Services, Department of Human Services, and Department of Public Health – each with disparate technology that does not enable easy, accessible or consolidated access to services. Each of these agencies sees the benefit of a coordinated technology solution.<sup>3</sup>

Yet the current structure of technology procurement could hinder the ability to develop a coordinated multi-agency technology solution: the State currently acquires new technology through its operating budget where new investment competes with operating cost needs for services delivery within each agency. And contrary to most operating budget expenditures, investment in technology is specifically intended to produce multi-year benefits that increase productivity, as well as the ability to track service delivery and outcomes more effectively. Unlike the State’s operating budgeting, the capital planning process requires a full evaluation of the expected return on a proposed investment, including annual cost savings. For these reasons, the TAB believes that incorporating technology procurement and investment with the capital planning process may produce significant benefits to the State, including better coordination in the use of technology across agencies.<sup>4</sup> This approach would also allow the State to evaluate each project independently and to prioritize the various technology “wants/needs” from a State-wide perspective to produce the greatest impact.

Significant federal stimulus and other federal program funds provide funding for state technology investment. The State should work to maximize Illinois’ share of those funds.

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<sup>3</sup> See page 19 for a discussion of the proposed Healthcare and Human Services Framework.

<sup>4</sup> While bond proceeds may not be suitable for technology investments, capital budgets often include projects acquired from current revenues.

The TAB further notes that there are many sources for technology acquisition: the State may develop customized technology, or it may opt to acquire and adapt existing software through licensing or purchase. Since all states provide similar types of basic services and are required to report information under the same federal funding programs, any centralized technology acquisition function should be charged to determine whether another state has already developed an existing “best practice” solution that could be licensed economically by Illinois.

Lastly, the State may want to lead a multi-state development of a technology solution to address a common need. We would expect the federal government funding programs to look favorably on these types of multi-state efforts.

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## EXPLORE MULTI-STATE TECHNOLOGY CONSORTIA

Cloud computing is an internet-based style of computing that provides common applications that users access from a web browser (with software and data stored on host servers). A new trend that is still in its infancy but gaining momentum in the private sector, cloud computing may insulate the State from the fixed expense and maintenance required to run applications in the State system. The State should explore whether creating a consortium of other states in the region might feasibly develop systems that can be accessed in a cloud environment. As a potential host, the State might be able to build its IT software and infrastructure through cloud computing. Agreements between states on certain standards about how data is stored and formatted would facilitate building these systems.

The State should determine which department is an appropriate first pilot for a multi-state technology consortium. There is already a similar initiative in healthcare to store data in a common format to make it easier to share among systems to realize greater cost savings. The federal CIO is a proponent of cloud computing, and the University of Illinois is a leading cloud computing research site, which may be an asset to the State.

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## OTHER IDEAS

During the course of the TAB’s review, the following ideas were raised. While we did not sufficiently review these ideas – and thus we neither endorse nor oppose them – we include them here as additional ideas that the Governor and his staff might want to look into further. Rather than leave potentially valuable ideas off the table, we decided to include a small set of such ideas in our report.

- **Freeze positions State-wide**

The State could freeze positions, and mandate that total headcount not exceed the current, FY09 level of 54,809. With exceptions only for those positions required to receive ARRA funds, we estimate that freezing headcount at FY09 levels would reduce personnel by more than 500, and provide an annual operating savings of more than \$40 million.

- **Regionalize pay**

In addition to seniority and job function, another way that the State could consider making targeted salary cuts would be to review pay scales according to geography and local cost of living. Currently, pay in a number of functional areas is standard for employees across the State despite dramatically different costs of living in different areas. In these departments, an employee living in Chicago may be earning a salary commensurate with his peer group (same education, same experience level), whereas a corrections officer in rural Illinois who is earning the same as his Chicago colleague may well be earning above-market rate. The State would still likely face staunch union opposition to such a proposal, but such salary reductions might be seen as more equitable than an across-the-board cut.

- **Launch an internal change management group**

The State could further develop its concept of a taxpayer action board by creating an internal change management group within State government. Such a group could be charged with identifying new ways to think about old problems and with generating creative thinking throughout and across the agencies. Not an audit group, rather, an internal change management group could develop new approaches, consider the State's assets collectively (rather than by departmental home), and look at system-wide improvements that could generate even greater efficiencies. With staff on loan from key departments, this group could develop new opportunities and approaches that would potentially pay back significantly within a matter of a few years.

- **Focus on governmental transparency**

In addition to the specific ideas laid out in this report, certain practices identified in our deliberations deserve comment. In effect, the TAB has concerns about a range of practices that degrade the public's confidence in our how State funds are spent and in our elected and appointed officials. These concerns relate to practices such as filling employment rolls with unnecessary and politically-connected individuals, special perquisites for legislators, marketing subsidies for legacy industries, and expenditures that are hidden behind multiple (and sometimes changing) budget categories.

These practices also hinder the ability of thousands of hard-working State employees, who come to work every day with the goal of improving the quality of life of fellow citizens, from doing their important work.

Eliminating abuses in hiring practices and abolishing other questionable practices won't in and of themselves solve a multi-billion dollar budget hole. But reducing these practices will help increase public confidence in our government and will assist front-line employees in doing their work. To these ends, we encourage a fundamental review of State hiring and staffing practices and procedures. We further encourage all branches and levels of State government to become more transparent. By communicating clearly how all of our tax dollars are spent and what we get for each expenditure, we believe everyone will be served better.

## HUMAN SERVICES

### Overview and Imperative for Change

A thriving Illinois presupposes a healthy populace. Accordingly, the state government allocates tremendous resources to support its citizens in need of physical, mental, and social services.

Present economic conditions in Illinois suggest that the State's human services safety net will be asked to serve more clients in the near-term – with or without adequate cash infusions. Unemployment rates in Illinois are expected to rise to 15-year highs in 2010; this amid an unprecedented wave of real estate foreclosures, and an aging population. These scenarios threaten to rupture families and increase the need for federal- and State-provided human services. In this landscape, future thinking about the management of human services must include rigorous debate on issues of cost containment, efficiency, and technology infrastructure solutions.

There are reasons for optimism. First, consensus is growing among major stakeholders about the need for reform. Second, there is a greater willingness to explore new ideas, some of which can be implemented rapidly. Third, states do hold some discretion in setting or adjusting eligibility criteria. Illinois has opportunities to better orient its existing programs and unlock substantially more federal funds. Finally, technology offers the promise of improved services together with real cost savings. Florida, for instance, reports that its new robust online ACCESS program is saving the state \$83 million annually. Human service departments in Illinois are already piloting a few “best practice” models in this arena.

There are three departments in the State that primarily support these basic needs. To complete their work, these departments operate a complex network of service centers across Illinois and largely adopt traditional (face-to-face) case management methods.

These departments requested a combined \$8.13 billion in appropriations for fiscal year 2010. Of this, 70% comes from General Fund revenues, 18% from federal funds, and 12% from other State sources. Illinois' structure presently demands a headcount of over 17,000 employees, which represents a net decrease of almost 19% from five years ago, primarily due to hiring and position management - rather than reduced caseload demand.

The human services departments conduct over 145 distinct programs, ranging broadly from children's foster care; to mental health; to disability determination; to daily nutrition, to seniors' adult day care programs. The 10 most significant programs represent almost \$6.1 billion, or 74% of total annual human services spending.

The three primary Illinois human services departments are:

- **Department of Human Services (DHS)** – (\$5.82 billion total budget, including federal funds). A 13,500-person staff operates 200 offices and customer facilities and oversees contracts with 1,500 community-based agencies. DHS serves more than 1.5 million Illinois residents each year through core programs addressing developmental disabilities, substance abuse and mental health



issues, community health/prevention efforts, and rehabilitation services. DHS also administers direct aid vehicles such nutrition and cash assistance.

- **Department of Children and Family Services (DCFS)** – (\$1.33 billion total budget). A 2,900-person staff operates roughly 80 offices and customer facilities. DCFS acts as the state’s child-welfare agency providing for the direct well-being of 16,000 children and investigating 100,000 reports of abuse each year. DCFS also licenses 10,000 day care homes, 3,000 day care centers, and nearly 500 group day care homes.
- **Department on Aging (DoA)** – (\$622 million total budget). A 160-person staff oversees contracted services with 13 Area Agencies on Aging to serve 1.3 million older adults. DoA’s major programs include Community Care, providing in-home care, adult day services, and case management services to low-income older adults; and Circuit Breaker Pharmaceutical Assistance, assisting low-income seniors with prescription drugs and property tax relief.

An understanding of these departments is not complete without also recognizing customers’ frequent needs for coordinated care from additional state entities overseeing Medicaid (Department of Healthcare and Family Services), unemployment insurance (Department of Employment Security), and job training/readiness (Department of Commerce and Economic Opportunity).

The wide variety of human service programs and populations served has brought about many operational silos, especially as each department must consider and manage an assortment of different funding formulas. By comparison to its neighboring states, Illinois operates a more complicated network of service departments, with some overlapping or redundant services. The State of Ohio, for example, recently consolidated its human and labor service delivery into a single department, effectively placing customers at the center of the structure, which not only emphasizes information sharing across divisions/personnel but also drives cost efficiencies.

In assessing the environment in which our Illinois human services agencies operate, the TAB observed several persistent issues and conditions that hamper the departments’ overall effectiveness. There are 25 court-ordered consent decrees, requiring new procedures or structure. Auditor General reports list many internal control and compliance deficiencies, some citations recurring for as many as 10 years, and potentially limiting Illinois’ access to future federal awards. Antiquated mainframe computer systems that are on average 20-30 years old require manual processing, demand heavy maintenance support, and limit management reporting – inhibiting information sharing to serve customers and reducing worker productivity.

A few central themes held constant throughout the TAB’s inquiry. Consideration was given to whether groups outside government could perform the State’s work equally well or better; whether existing services – from registration to discharge – are patient-centric enough to fit modern business applications; and if service cuts or reductions were needed, whether the root cause was a performance or a policy issue.

An effective cost containment plan that minimizes customer impact must incorporate small solutions on any number of fronts, from driving more business to community providers, to expanding prevention-

based care options, to empowering clients to self-register or complete other basic tasks. With this in mind, we identified four opportunities as areas of highest priority for State leadership to study and take action.

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## ADOPT AN INTEGRATED SERVICE DELIVERY MODEL

### Background

The State of Illinois delivers human services through federal- and State-funded programs delivered directly by State personnel and through contracts with community-based or local government entities. Various State agencies deliver aspects of Illinois' human services programs: Department of Human Services (DHS), Department of Children and Family Services (DCFS), Department on Aging (DoA), and Department of Healthcare and Family Services (DHFS).

The wide variety of programs and the different departments involved in human service delivery have encouraged service delivery through separate silos. Each department relies on its own legacy information technology systems to support its business processes. These systems were built with little thought to other programs and have limited integration. This increases maintenance costs and complicates efforts to change how departments serve Illinois' human services customers.

States across the country have been revamping their approach to delivering human services. These solutions range from renewing technology infrastructure for particular program areas, to changing service delivery models within or across program areas. Some states have outsourced functions such as call centers, while others have re-aligned state departments to more accurately reflect the populations they serve and the services they provide. These initiatives have primarily been initiated by state legislatures or governors, but also by departments. The examples below illustrate alternative models for human services delivery integration.<sup>5</sup>

- **Florida** revamped its process for receiving applications for programs such as Medicaid, Temporary Cash Assistance, and Supplemental Nutritional Assistance Program (SNAP, formerly Food Stamps). It receives over 90% of its benefit applications electronically via its My Access self-service website, and has set up agreements with community partners to facilitate application submission.
- **Texas** moved to statewide call centers for handling processing of benefit applications, utilizing an outsourcing approach for staffing. It also built a web-based, eligibility determination system. Texas' efforts were initiated by a legislative request for a cost/benefit analysis of electronic customer service models.
- **Wisconsin** has incrementally renewed its technology infrastructure over a five-year period. A department began by developing self-service features for screening and applying for assistance, implementing statewide imaging and scanning for document management, and replacing the state's

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<sup>5</sup> American Public Human Services Association (APHSA) and individual states' web sites.

15 -year-old eligibility and case management system with a web-based solution that has reduced worker training time by 60%.

- **Massachusetts** has used both technology and organizational changes to streamline multiple state agencies responsible for providing human services. Upon the Governor’s direction, the “Virtual Gateway” was created, providing a self-service site to support citizens, providers, and community partners. An Executive Office of Health and Human Services was established to coordinate activities across human service agencies.

### Strategy

The following areas were identified as specific opportunities. Also, the Illinois human service departments are in the initial stages of developing a collective Healthcare and Human Services “Framework” to support state-wide service integration. The TAB believes that this broad, long-term initiative should be supported and federal funding sought.

- **Co-location** – Illinois’ human service agencies maintain over 300 different locations to provide services to often similar populations. Revamping the service delivery model to both co-locate customer service locations, as well as improve data-sharing across programs to coordinate services, will result in better customer outcomes. DHS is currently piloting an “Open Door” project that is exploring use of this approach. This program should be expanded and considered for cross-departmental roll-out.

- **Department and Mission Alignment** – To facilitate this process, Illinois should assess its large program portfolio and how staff aligns to similar programs and their missions. Illinois has at least double the number of agencies dedicated to human services programs than our neighboring states. For example, compared with neighboring states, both DHS and DoA have a hand in serving the health care needs of elderly clients. Cross-department changes may reduce administrative overhead (such as HR, payroll, management) by redeploying resources to higher-need, customer-facing areas.

Number of Human Services Agencies - Illinois versus Neighboring States



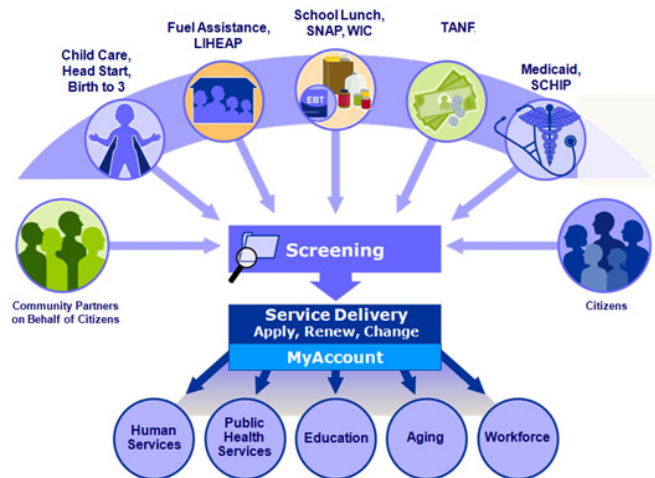
IA – DHS; IN – FSSA, DCS; KY – HFS; MI – DHS; MN – DHS, DOH; MO – DHSS, DSS; OH – JFS; WI – DHS, DCF,

- **Technology Streamlining** – Illinois’ human service departments have dozens of legacy computer systems (excluding HR/payroll functions), many of which are 30-40 years old. These antiquated systems inhibit worker productivity, prevent Illinois from reducing costs, and challenge cross-department collaboration. For example, DHS now has over 50 technology initiatives underway. Reducing the number of systems, standardizing under a common technology platform, and implementing a unique customer identifier system will have numerous benefits beyond information sharing. These include 1) reducing costs by consolidating software licensing fees across divisions and by retiring licenses used by legacy computer systems; 2) requiring a lesser variety and number of technical systems to

support staff than currently employed across the five health and human services departments; and 3) consolidation of hardware purchasing and server maintenance across departments.

- Self-Service Channels** – The State has an opportunity to reduce and shift costs by expanding self-service channels via the internet and automated phone. These channels can (1) provide more convenient times for customers to search, apply, and maintain benefits; (2) shift data-entry work and inquiries from front-line State workers to customers and partners; and (3) increase the productivity of existing workers. To further reduce costs, these new service channels, if interfaced with re-engineered systems that share information, can be augmented by a centralized call center that can answer questions across different programs. This may allow for further consolidation of service locations.

### Use of Internet to Channel Customer Inquiries on programs



### Benefits

Determining the ultimate cost savings of this opportunity depends on the level of integration that occurs. Innovation and consolidation across front-line service locations, systems, benefit programs, and departments would provide the maximum cost savings to the State. Implementing these actions will require an initial capital investment, causing the net short-term savings to the State to be an estimated \$20 million annually. The return on this investment can be substantial in the long-term. For example, the State of Florida estimated a return of \$4 for each \$1 it spent on its My Access initiative. Within a five- to 10-year time horizon and assuming maximum adoption across Illinois’ human services agencies, savings could range from \$155 million to \$400 million annually.

The goal of integrated service delivery is to enable the State to serve more people within a similar or smaller budget – without adversely impacting the quality of care. Reducing workloads by providing tools to workers and customers will (1) allow workers to be more efficient and (2) encourage customers and community partners to perform actions previously done by State employees. The ultimate goal is to improve information-sharing across programs to yield better customer outcomes, while at the same time reducing dependence on the State’s human services network.

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## IMPROVE APPROACHES TO LONG-TERM CARE

Illinois' human service agencies can achieve significant savings if the State can better coordinate approaches for assessing customer needs and prioritize care toward less restrictive community settings. The State must quickly transition from being a *provider* of generous, uninterrupted, institutionalized care (partially through contracted, outsourced services) to a *locator* of rapid, varied, and sustained pathways to quality community vendors – caregivers able to work in or near clients' homes.

*(Note: Transitioning to more community-based long-term care is an idea also relevant to other Medicaid-funded programs in the State, which are administered by the Department of Healthcare and Family Services. See the separate Medicaid section for further examination of the Medicaid-related aspects of this idea.)*

### Background

The State's provision of human services is funded by a variety of sources, including Medicaid and State funds. Currently it costs \$36-140,000 (or more) per year to serve a typical client in a nursing facility as compared with \$8,400-17,000 per year to coordinate Medicaid home- or community-based services. At these rates, it is imperative that only those people who truly need long-term facility-based care – the most dependent – be placed in these situations. Projections for the aging Baby Boomer generation foresee increasing needs for states to manage customers' access to Medicaid and other services; while the opportunities and complexities of modern life and their implications on traditional nuclear family structures likely mean an increasing need for a dense matrix of community-based care outlets. Not only do basic trends and cost analyses show a challenging road ahead, but in several respects Illinois will need to start from a standstill. A look at national statistics shows that our system has not fully embraced the community-based service model:

- Illinois operates a total of 104,000 licensed nursing facility beds; however, just over 81,000 beds were occupied at year end 2008 – a costly inventory that needs to be cleared.
- An estimated 14,000 nursing facility beds are occupied by individuals aged 18-59 years old.
- Illinois ranks 51<sup>st</sup> in total number of adults served in settings of six persons or fewer.

It would be an unrealistic assumption to consider that all elderly citizens and individuals with developmental or mental impairments can be reintegrated into community settings. Still, many people placed in institutional settings do not require that level of care; others may need such care only temporarily and should later move to a community setting. The availability of institutionalized care presents an immediate opportunity for a case manager wishing to provide quick relief to a client, with or without a demonstrated need for that level of service. It is easier still to leave a client in institutional care, potentially denying that individual the opportunity to lead a more dignified life, in a less restrictive setting.

Recently, the states of Oregon and Pennsylvania have each enacted successful programs for lowering institutional bed counts without major disruption or undue harm to customers. Illinois' Department of Aging has experienced success with its "Home Again, Enhanced Transition" program, an effort that identifies and moves able customers living in State-run institutions to less restrictive community care

environments. The State should give support to ramp up these efforts, while also eyeing ways to improve the overall stock and portfolio of qualified community partners.

### Strategy

Weighting human services delivery toward community-based providers will provide relief to the budget. First, it can deliver immediate cost savings. If the targeted programs are thoroughly vetted, it can do so without compromising care to existing customers who would then be diverted to services outside State management (but not outside federal oversight and standards). Second, it presents an opportunity to freeze or discontinue previous State-run efforts, and more easily enable case managers to locate customers within less restrictive, community-based settings. Third, it can strengthen longer-term goals, such as efforts to improve information access. Further, the smaller scale of most community-level operations is such that a double bottom line – quality care and cost-effective care – is more plainly evident and able to be managed without risking systemic threats to the overall safety net.

The following were identified as priority opportunities:

- **Accelerate the capacity of DoA case workers to receive individuals from institutions** or those waitlisted for institutional care and to find them alternate care settings.
- **Reduce institutional bed counts** to prevent back-filling by waitlisted clients.
- **Shift demand for institutional care** by identifying high-risk populations and proactively offering services needed to maintain these individuals in (less costly) community care settings.
- **Expand the use of bridge rental subsidies** such as supportive housing ventures, which allow individuals to move out of institutional care, particularly in the mental health and developmental disability areas. The degree to which the state opens new or rehabbed housing developments dictates potential savings.
- **Improve information access** to support coordinated community care across health care and economic security/economic opportunity programs.
- **Close Howe Development Center** – This 289-bed facility has been de-certified by the federal government and therefore DHS is unable to receive matching funds from Medicaid of \$2.2 million each month.

### Benefits to Addressing Existing Long-Term Care

The range of potential reduction in spending through this strategy is approximately \$40 million annually in the short-term (12 to 18 months) to \$95 million annually in the long-term (two to five years).

Considering the sustained success of many not-for-profit and faith-based direct care givers and supportive housing providers, there is precedent for long-term care customers to continue to receive vital services and to make improvements in their overall quality of life.

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## ENHANCE FOSTER CARE MANAGEMENT

### Background

The Title IV-E foster care program is an entitlement program under which the federal government reimburses states for a portion of the costs they incur on behalf of children in foster care who meet statutorily prescribed eligibility criteria. Under this program, Illinois incurs costs and receives federal financial participation reimbursement (FFP) as a result of meeting the board and care needs of children in foster care and performing certain administrative functions on behalf of eligible children. Foster care maintenance payments are matched at a rate that is equal to the State's Federal Medical Assistance Percentage (FMAP) of 50.32% (the national range is between 50% and 77% depending on the state). For all states, administrative costs are matched at a rate of 50% and training costs up to 75%.

The foster care program is an entitlement in which there are no limits to the amount of Title IV-E federal funds that states can receive for allowable costs so long as those costs are incurred on behalf of children who meet Title IV-E eligibility rules.<sup>6</sup> Not all children in DCFS' foster care program will be eligible.

The Administration for Children and Families (ACF) within the U.S. Department of Health and Human Services (HHS) conducts foster care eligibility reviews to determine states' degree of compliance with applicable eligibility provisions. States can incur substantial penalties should ACF determine that a state has inappropriately claimed federal aid for children who are not Title IV-E eligible.

DCFS is also required to obtain federal approval of its cost allocation plans as a basis for claiming federal funds. This can be a complex undertaking as the expenditure of funds must be allocated to the programs that benefit from them. For example, a social worker may be working in foster care with both Title IV-E eligible children as well as non-eligible children, but only the percentage of time that the worker is working with IV-E eligible children can be charged to the foster care program.

### Strategy

The following were identified as priority opportunities:

- **Maximize federal revenue by increasing the number of children in foster care who are Title IV-E eligible.** Any increase in the percentage of children in foster care who are enrolled under Title IV-E – the State's penetration rate – would increase the amount of funds that the State can draw down from the federal government because (1) it increases the number of children in foster care eligible for Title IV-E maintenance payments and (2) every percentage point increase in the penetration rate increases the percentage of agency overhead expenses that can be claimed under the Title IV-E Administrative Costs Program.

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<sup>6</sup> Title IV-E eligibility rules include having been physically removed from a home that met certain income-level thresholds at the time of removal; having been removed from their home as a result of a judicial determination that to remain in the home was contrary to the welfare of the child or pursuant to a voluntary placement agreement; being placed under the legal authority of DCFS; and having been placed in a licensed or approved facility or family foster care home.

- **Enhance the State’s SACWIS system.** The U.S. Department of Health and Human Services (HHS) funds Statewide Automated Child Welfare Information Systems (SACWIS), which are expected to be comprehensive, automated case management tools. Illinois is one of nine states identified by HHS as having a non-certified SACWIS model. DCFS should enhance its SACWIS system by (1) improving information exchange between SACWIS and other data systems; and (2) capturing caseworker information relevant to Title IV-E eligibility determination, thus “unbundling” these costs from other programmatic data to permit separate billing.
- **Reduce the length of stay for children who are removed from their homes of origin.** DCFS has a low intake rate for children, compared to the national average. After preventative services programs, the children who are screened into the program have a relatively longer length of stay. DCFS could achieve savings by reducing the lengths of stay in foster care by ensuring that children who are not able to be reunited with their families of origin are expeditiously moved to adoption. The State should enhance strategies to recruit, assess, prepare and retain families who are able to provide permanent homes for children in foster care. For example, increasing the participation of faith-based organizations and private entities in the linking of waiting children with approved and waiting families can decrease the length of time that children spend in foster care after parental rights have been terminated.

Caseworkers are often responsible for managing a full caseload of children in foster care whose needs vary from reunification to placement, and for recruiting and screening potential parents. Specialized caseworker teams can accelerate timely adoptions for children who cannot be safely returned to their homes of origin and can manage the recruitment of potential adoptive families.

- **Determine the appropriate balance of funding for family preservation, family reunification and adoption services.** DCFS has historically focused on family preservation and reunification, as the best outcome for a child is to remain with their family of origin. However, this focus at times comes at the expense of adoption services. DCFS should continue to assess how it is providing support to families to ensure that adoptions work well. Such services might include psychological and family counseling, or training in parenting skills.

## Benefits

Increasing DCFS’ foster care program penetration rate, unbundling of costs to allow separate billing, and streamlining the adoption process for children in foster care, could result in short-term (12 to 18 months) savings of \$15 million annually and long-term savings (between two and five years) of \$40 million annually.

The savings and federal reimbursement estimates above do not include results from other strategies that DCFS is undertaking, including (1) Title IV-E rules allowing retroactive claiming for two years, and (2) The American Recovery and Reinvestment Act’s (stimulus bill) temporarily enhanced federal medical assistance dollars, based upon penetration rate improvements made before October 1, 2010.



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## ADJUST SELECT ELIGIBILITY CRITERIA AND RULES

### Background

The citizens of Illinois are served through a wide variety of human services programs. Different federal and State funding allocations support each program. For example, the *benefits* paid through the SNAP program (formerly Food Stamps) program are 100% federal dollars – no state money is used for the actual SNAP benefit. However, the State is required to contribute approximately 50% of the cost for *administering* the SNAP program by processing applications, verifying information, and issuing benefits. In comparison, Medicaid, which provides health care coverage to low-income, elderly, and disabled populations, requires states to contribute to both the benefit and administration of the program.

The FY09 Federal Medical Assistance Percentage (FMAP) for Illinois was 50.32% - which means Illinois paid for 49.68% of the benefits for the programs. Certain programs qualify for enhanced FMAP (e.g., Illinois' enhanced FMAP in FY09 was 65.22%), and different categories of expenses can qualify for different rates of reimbursement. Of the programs run by Illinois human services agencies, roughly 50% are State- and federally-funded, 40% are State-funded only, and 10% are funded primarily with federal dollars.

In addition, each human service program has different eligibility criteria used to determine who qualifies for the particular program. Criteria include levels of income, U.S. residency rules, limits on the amount of assets owned, diagnosed medical conditions, disability, ability to perform daily living activities, and many others. The State has varying levels of control over these eligibility and administration rules, depending on whether it is a federal or State program.

Several federal programs are funded via block grants that set high-level rules but give states the flexibility to adjust and set additional criteria. Examples of block grant programs include the Temporary Assistance for Needy Families (TANF) program, which provides temporary financial assistance for pregnant women and families with one or more dependent children, and Illinois' Child Care Assistance Program (CCAP), which provides low-income, working families with access to quality, affordable child care. Additionally, states can apply to the federal government for a Waiver to change certain rules, for example, in Medicaid and nutrition programs.

### Strategy

The State should carefully consider several strategies for altering eligibility criteria and rules. Promising examples include:

- **Shifting clients to programs that have greater federal funding participation** – Many of Illinois' human services programs have overlapping missions. The State could make policy changes to steer clients into programs with better federal participation. For example, the State could allow more elderly clients to qualify for Medicaid coverage by implementing less stringent income spend-down policies. This would prevent elderly clients from having to utilize other State- and county-funded health care programs that have less federal funds participation.

- **Reducing burdensome administrative rules** – Some programs have rules that create workload burdens for staff. Removing these rules can lead to overall service improvements, although it can also increase the benefit cost. For example, adopting what are known as “categorical eligibility rules” can remove the requirement that asset tests be done in order for an individual to be eligible for the SNAP (food stamps) program. This could increase program participation and reduce potential errors, which might allow Illinois to qualify for more Food and Nutrition Service bonuses. Food stamp benefits are 100% federally-funded, so the cost to the State for administration would be offset by not having to verify assets for the population at large.

### **Benefits**

Illinois has more than 145 distinct human services programs that are tailored to different segments of the population. As a result, the TAB did not have sufficient information to quantify or estimate realistic savings or federal reimbursements at this time. We encourage the State to conduct an in-depth comparison of programs and populations served to arrive at a reasonable estimate of net savings and an implementation plan.

## MEDICAID

The Medicaid program was created in 1965 as an addition to the Medicare program, and was intended to cover the health care costs of those receiving welfare benefits. No longer a simple safety net for “the poorest of the poor,” Medicaid is now a public health insurance program covering roughly one in five Illinois residents.

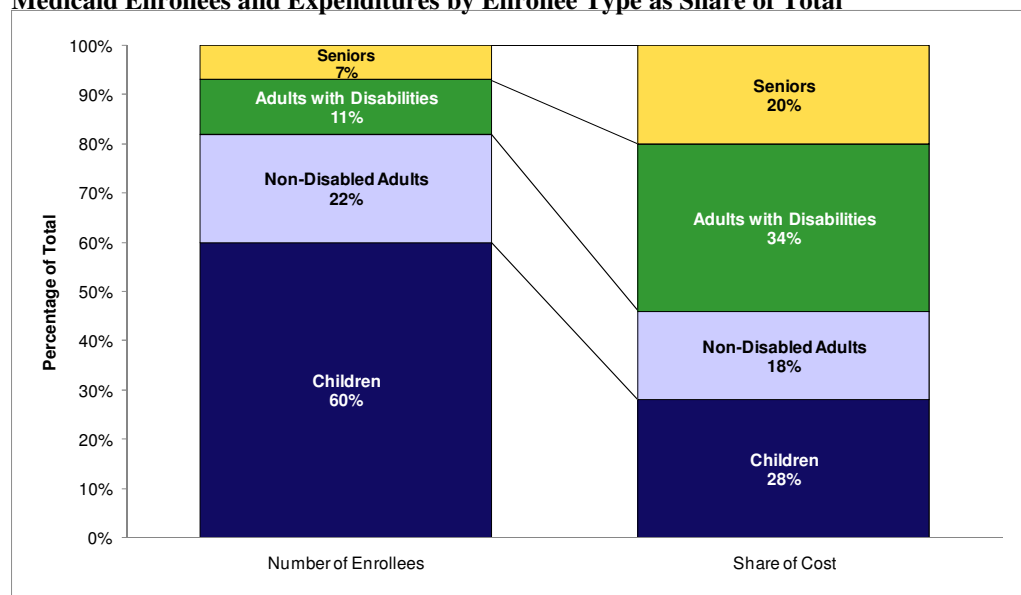
Medicaid is financed by a unique federal and state partnership through which the federal government reimburses states from 50% to 77% of the costs of services provided to Medicaid recipients. The federal medical assistance percentage, or FMAP, is based on a state’s wealth (as measured by personal income); Illinois generally receives a 50% federal match for most Medicaid services (under the federal stimulus plan the current match is 60.48% until January 2011). The federal match has a number of implications in terms of the discussion below. First, it should be noted that Illinois is responsible for roughly half of the Medicaid liabilities described in this section (with the federal match covering the remainder). In addition, the TAB recognizes that for every reduction in State Medicaid expenditures, there will be a corresponding reduction in federal match – however, this consideration should not be used as a rationale for failing to identify cost savings that will provide value to all taxpayers.

### Medicaid Enrollment

The number of Illinoisans enrolled in Medicaid has been steadily increasing. From 2003 to 2008 the Medicaid population grew at an average rate of 7.8% per year, while the population of Illinois grew at only 0.5% during the same time period (see Medicaid Appendix 1, page 45). Today, over 2.45 million people, or more than 19% of the entire Illinois population, are enrolled in Medicaid, which is higher than the national average.

Five major groups are eligible for Medicaid: (1) low-income seniors, aged 65 and older; (2) adults with disabilities who meet the Social Security definition of having a disability; (3) children under 19 years of

**Medicaid Enrollees and Expenditures by Enrollee Type as Share of Total**



age; (4) parents and other caretakers of dependent children; and (5) pregnant women. Children, non-disabled adults, and low-income pregnant women together represent over 80% of the people that receive Medicaid services at some point during the year. The number of beneficiaries is

broken down as follows: low-income seniors (160,000); adults with disabilities (241,000); other adults and caretakers without disabilities (537,000); and children (1,550,000).

Although children as a group are the largest component of beneficiaries in Illinois, they do not account for the majority of the spending. The elderly, blind and disabled that are in poorer health and need more services comprise only 18% of beneficiaries, but account for over 50% of Medicaid spending.

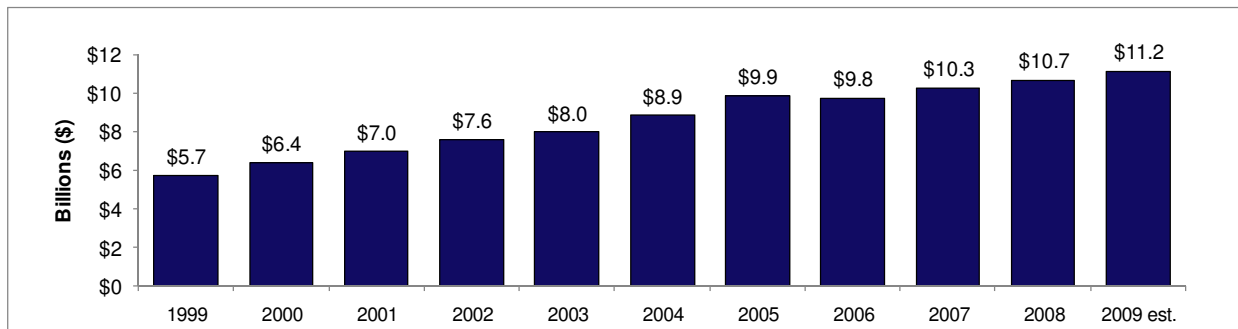
## Medicaid Spending

Medicaid is now the largest single State expense in Illinois, accounting for over 40% of general fund appropriations.

For FY09, spending on hospitals comprises the largest portion of Medicaid liabilities, approximately 33% of all Medicaid spending in Illinois. The remaining segments of Medicaid liabilities are prescription drugs (20.2%), long-term care (17.7%), physicians and other practitioners (12.3%), and all others (11.1%). Capitated managed care spending accounts for only 2.5% of all Medicaid liabilities.

From 1993 to 1999, Medicaid liabilities grew at an annual rate of only 1.4%. But over the last 10 years, Medicaid liabilities have been increasing at an average rate of 6.9% per year.

**Total Medicaid Liability  
(1999 – 2009 est.)**



Much of this growth has been driven by Medicaid eligibility changes over the last few years that have led to substantial increases in the number of enrollees. For example, in July 2000 the income eligibility threshold for the aged and disabled population was increased. This change alone has resulted in approximately 136,000 new enrollees in this category. In October 2002, the income standards for parents of low-income children, already eligible for coverage, were also increased, adding another 170,000 enrollees to the program. Then in June 2004, the State began a federal demonstration Waiver to provide family planning and related services to women of child-bearing age that were above the previous income standards. Finally, beginning with the enactment of legislation covering all uninsured children of any income level in November 2005, Illinois began an aggressive public relations campaign to promote enrollment of children in the All Kids health insurance program. This campaign has resulted in 68,600 additional children being added to the Medicaid program.

In addition, the increasing cost of services – such as drugs, physician services and nursing homes – have had a significant impact, as well as changes in the types of services used by Medicaid beneficiaries and overall service utilization.

The Illinois Department of Healthcare and Family Services (HFS) projects an increase of 7% in Medicaid spending from FY09 to FY10. This 7% growth in spending for the next fiscal year is a reasonable estimate when compared with national Medicaid spending growth projections by the Centers for Medicare and Medicaid Services (CMS), which are estimated to be 7.9% per year over the next 10 years. However, if Medicaid liabilities continue to grow at a 7% rate in Illinois, Medicaid spending will reach approximately \$22 billion in 2019, which could represent roughly 50% of the entire State budget and would begin to crowd out other State spending priorities, such as public safety and education. If that growth rate can be reduced to 3% per year, Medicaid liabilities in 2019 would be substantially less – around \$15 billion (See Medicaid Appendix 2, page 45).

### **Impact of Savings Opportunities**

Because liabilities over the last 10 years have increased at an average rate of 6.9%, we adopted HFS's projected FY10 7% rate of Medicaid liability growth for each of the next five years (assuming no cost-cutting or change efforts) as the baseline against which to compare potential savings.

As described above, this baseline growth rate is unsustainably high, which means that savings opportunities must cut costs in the short term (while maintaining or improving service effectiveness and quality) *and* substantially slow this growth rate going forward. To accomplish these goals, we have identified significant savings opportunities, which fall into five broad categories: care management; long-term care; pharmacy; technology; and revenue maximization.

The following analysis estimates the savings that could be achieved over the next five years if the State implements the opportunities we have identified, as well as the impact on the future Medicaid growth rate. Two different sets of projections are included in the analysis. The first was made, at the TAB's request, by HFS staff, in conjunction with other relevant State agencies. The second is our own, more aggressive, estimate of potential savings in these areas. The intention is to preserve the ARRA funds associated with these programs by maintaining program eligibility.

### **Savings projections identified by the Department of Healthcare and Family Services**

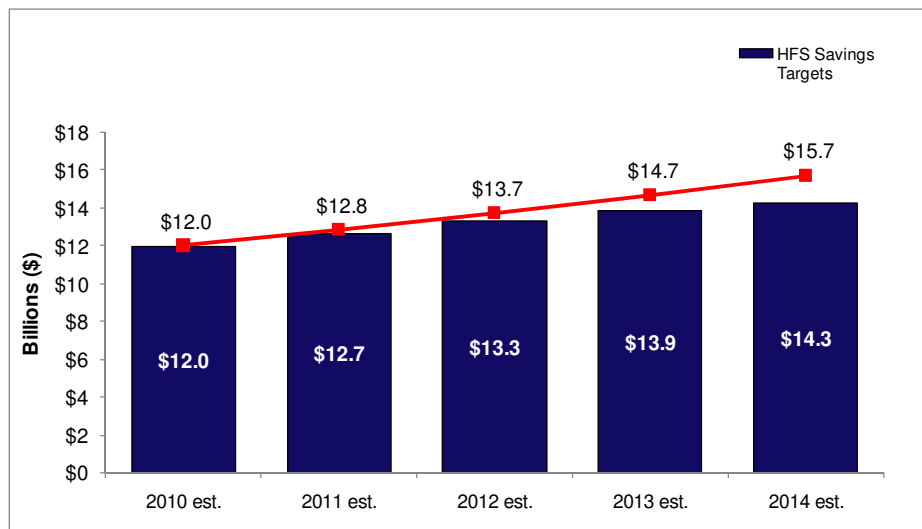
At the TAB's request, the Department of Healthcare and Family Services (HFS) estimated the level of cost savings that could be achieved in year one, year three, and year five of implementation of the five opportunity areas identified in this report. We include below the numbers that HFS provided, based on their assumptions of how quickly change could be introduced and the level of resources that would be required:

(\$ in Millions)	Year 1 2010	Year 2 2011	Year 3 2012	Year 4 2013	Year 5 2014
Liability assuming 7% annual growth	\$12,000.0	\$12,84.0	\$13,738.8	\$14,700.5	\$15,729.6
Bending the trend					
Revised growth assumption	6.50%	6.00%	5.00%	4.25%	3.00%
Revised liability	11,952.7	12,669.9	13,303.3	13,868.7	14,284.8
Annual savings v. 7% growth	(47.3)		(265.3)		(613.0)
Cumulative savings v. 7% growth	(47.3)		(435.5)		(1,444.8)
<b>Estimated cost/saving for recommendations, by cost reduction opportunity and fiscal year</b>					
I. Care management	\$(40.0)		\$(130.0)		\$(310.0)
II. Long-term care rebalancing	10.0		(80.0)		(200.0)
III. Pharmacy	(18.0)		(55.0)		(100.0)
IV. Technology*	5.0		40		10.0
V. Revenue maximization	<u>0.0</u>		<u>0.0</u>		<u>0.0</u>
Total additional savings**	(43.0)		(222.50)		(600.0)

\* Appropriations necessary to support MMIS upgrades. The federal match on these expenditures is 90%.

\*\* Data and projections provided by HFS. Individual categories do not add to total savings; the balance will come from other savings TBD.

### Projected Total Medicaid Liability (2009 – 2019 est.)



### Savings projections identified by the TAB

The TAB assumed that the State would be able to contain the growth of Medicaid liabilities more aggressively and suggested the following savings targets for the next five years. Both the TAB and HFS project that the State will be able to reduce the growth of Medicaid liabilities to a 3% rate by year five, but the TAB projections include lower rates of growth in years one through four. As a result, the TAB's projections decrease costs more quickly. While we believe that more aggressive savings rates are

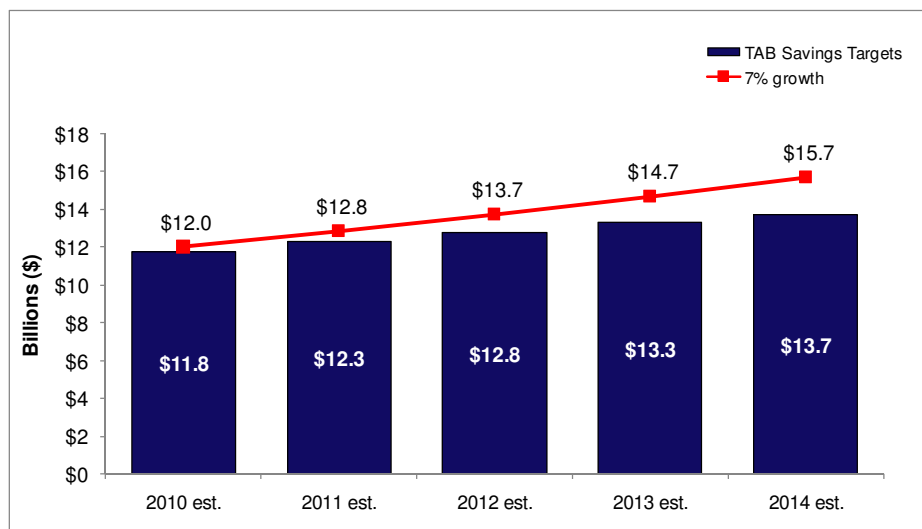
attainable quickly, we encourage the State to conduct a more intensive review to identify the appropriate targets and set bold goals for cost reductions in these areas.

(\$ in Millions)	Year 1 2010	Year 2 2011	Year 3 2012	Year 4 2013	Year 5 2014
Liability assuming 7% annual growth	\$12,000.0	\$12,84.0	\$13,738.8	\$14,700.5	\$15,729.6
<b>Bending the trend</b>					
Revised growth assumption	5.00%	4.50%	4.00%	4.00%	3.00%
Revised liability	11,775.7	12,305.6	12,797.8	13,309.7	13,709.0
Annual savings v. 7% growth	(224.3)	(534.4)	(941.0)	(1,390.8)	(2,020.6)
Cumulative savings v. 7% growth	(224.3)	(758.7)	(1,669.7)	(3,090.4)	(5,111.0)
<b>Estimated cost/saving for recommendations, by cost reduction opportunity and fiscal year</b>					
I. Care management	\$(95.0)	\$(225.0)	\$(405.0)	\$(595.0)	\$(855.0)
II. Long-term care rebalancing	(75.0)	(170.0)	(305.0)	(445.0)	(645.0)
III. Pharmacy	(50.0)	(115.0)	(205.0)	(300.0)	(430.0)
IV. Technology*	5.0	5.0	25.0	25.0	10.0
V. Revenue maximization**	<u>(10.0)</u>	<u>(30.0)</u>	<u>(50.0)</u>	<u>(75.0)</u>	<u>(100.0)</u>
Total additional savings	(225.0)	(535.0)	(940.0)	(1,390.0)	(2,020.0)

\* Appropriations necessary to support MMIS upgrades. The federal match on these expenditures is 90%.

\*\* The TAB has not had sufficient time to thoroughly review all revenue maximization opportunities, but is aware of a substantial amount of State-only programs, using State-only dollars, that provide additional match opportunities.

**Projected Total Medicaid Liability (2009 – 2019 est.)**



## Description of Savings Opportunities

In the following pages we describe each of the five broad categories included in these savings estimates, as well as some detail regarding the opportunities identified by the TAB in each category.

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**PROMOTE COST-EFFECTIVE CARE MANAGEMENT STRATEGIES THAT FOCUS ON THE HEALTH OF THE PERSON, PROMOTE PREVENTION AND WELLNESS, AND PROVIDE A “MEDICAL HOME”**

### **Current System**

The cost and utilization of hospital inpatient and outpatient procedures, including the use of emergency rooms for the delivery of primary care, drive much of the near doubling of Medicaid liabilities in Illinois over the last 10 years.

When compared to national data, Illinois Medicaid relies far too heavily on costly inpatient hospital procedures, laboratory tests, outpatient procedures, and emergency rooms. According to a Kaiser Foundation study, in 2006 and 2007 inpatient hospital procedures comprised over 45% of Medicaid acute care spending in Illinois, compared to the national average of 25%<sup>7</sup>. Moreover, there is a high rate of emergency room usage in Illinois for all Medicaid beneficiaries.

To reduce costs, incentives must be aligned to ensure that care be delivered in the most efficient setting. Towards this end, in 2007, HFS launched Illinois Healthy Connect, a primary care case management (PCCM) system that provides a primary care doctor, coordinated care and preventative care to Medicaid-eligible children and adults without disabilities. HFS has contracted with a provider to enroll these beneficiaries, and, to date, has enrolled over 1.7 million individuals into PCCM.

HFS has also contracted with another provider to implement a disease management program that provides a more focused case management system for enrollees with chronic conditions, such as diabetes and asthma. HFS has indicated that there are currently 200,000 beneficiaries in this disease management program. While the program is voluntary, HFS has reported substantial savings attributed to this program in the first two years.

Illinois Medicaid has additional opportunities to expand on the current PCCM model by implementing the following coordinated care management strategies:

- **Enhance the Primary Care Case Management (PCCM) system so beneficiaries are given a true medical home, with adequate provider incentives to drive quality of care, prevention and wellness, as well as appropriate patient disciplines to ensure proper health outcomes. Monitor health outcomes to ensure quality of care, prevention and wellness**

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<sup>7</sup> The inpatient rate also takes into consideration the hospital provider tax and the intergovernmental transfers to Cook County and the University of Illinois. Thus, the fact that these funding mechanisms are different among states makes it difficult to make a clear comparison.



The current PCCM system offers children and adults without disabilities access to primary care physicians, but it could be significantly strengthened. For example, the current system rewards physicians with a small per member per month (PMPM) fee. The State should tie this PMPM to specific outcomes that require the physician to actively engage and provide appropriate primary care to the Medicaid beneficiary. Co-pays or other disincentives would discourage patients from using the health care system in a costly manner; and disciplines, incorporating provider risk-sharing such as reductions in PMPM payments, would encourage physicians to provide top care, including adequate hours and access for Medicaid patients. True incentives for the provider and patient could reward healthy lifestyles. HFS also needs to ensure that primary care physicians are making only proper referrals, and it needs to limit doctor shopping within the PCCM system, since having a stable medical home will be best for proper care management.

Additionally, HFS must ensure that the PCCM network operates as a true medical home. A medical home is one that allows for (1) accessibility; (2) guidance/education; (3) continuous monitoring of individuals' health status; and (4) appropriate management of resources. In addition, a true medical home provides 24-hour accessibility, much like a hospital or a community health center. HFS should begin to demand this type of accountability for any PMPM payment.

- **Evaluate the opportunity to expand the capitated managed care program, in which managed care organizations assume the full risk for medical care, provide beneficiaries with a quality network of medical providers, and monitor health outcomes to ensure quality of care, prevention and wellness**

This year, only about 2.5% of all Illinois Medicaid liabilities will be for full-risk capitated managed care providers. In such a system, the capitated managed care provider negotiates a per member per month (PMPM) contract with the State, which is set by an actuarial assessment of what the predicted costs will be for the covered population of beneficiaries. The managed care company is at risk for any costs above the negotiated PMPM contract, which provides an incentive to keep costs in control, and encourages the use of best-practice health, wellness and prevention strategies to limit unnecessary medical costs for beneficiaries. Other states have had significant success in implementing a broad-based capitated managed care program, including North Carolina<sup>8</sup>, Pennsylvania<sup>9</sup>, and Wisconsin.

If used appropriately and coupled with improved primary and preventive care, capitated managed care can be a substantial cost saver for the Medicaid program, while, at the same time, ensuring quality of care for the person.<sup>10</sup> We believe that the State should expand its capitated managed care network for the same Medicaid beneficiaries that are eligible for the PCCM program today, and include the aged, blind and disabled populations (see discussion later in this section), where the higher fee-for-service structure allows for more significant savings. We believe that, while HFS enhances its PCCM program, it can also move towards additional capitated managed care for all beneficiaries, not just those covered by the PCCM program today.

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<sup>8</sup> <http://www.statecoverage.org/node/1349>

<sup>9</sup> [http://www.rockinst.org/pdf/health\\_care/2003-management\\_success\\_story\\_the\\_pennsylvania\\_medicaid\\_managed\\_care\\_program.pdf](http://www.rockinst.org/pdf/health_care/2003-management_success_story_the_pennsylvania_medicaid_managed_care_program.pdf)

<sup>10</sup> "Medicaid Managed Care Cost Savings – A Synthesis of 24 Studies," The Lewin Group, March 2009

- **Enhance disease management and care coordination of beneficiaries that are in the high-cost category, or at risk of joining the high-cost category. Payment for service should be contingent on meeting performance metrics and improving health outcomes**

The disabled population is the most expensive population covered by HFS: although comprising only 11% of the population, disabled beneficiaries account for over 34% of costs in the HFS budget. HFS has already launched a disease management program to manage the care of this high-cost population, and substantial savings have already been attributed to the program in the first two years. However, the program is voluntary, and HFS should consider ways to require participation and create incentives for appropriate beneficiary outcomes. HFS should also enhance its efforts and, in the future, tie payments to the program's vendor to savings and health outcomes.

- **Explore the cost-effectiveness of competitively bidding certain non-emergent, elective, hospital procedures, as well as durable medical equipment (DME), in areas outside of the capitated managed care program, provided that there is access and quality is not compromised**

Other states have negotiated with preferred providers for lower rates for non-emergent surgical procedures. For example, California passed legislation in 1982 allowing Medi-Cal to negotiate with selected hospitals to compete for Medicaid inpatient services. California obtained a Waiver and saved an estimated \$300 million per year. Rhode Island is the most recent state to obtain a federal Waiver for selective contracting of inpatient and outpatient services. Some states have also explored selective contracting systems that allow for competitive bids from DME companies to serve a certain segment of the population.

Currently, Illinois Medicaid pays hospitals the lower of their charges or a specific rate that is set by the State. When exploring this issue regarding hospital inpatient and outpatient services, policy makers should ensure that any successful bid establishes a lower rate than what the State would be paying in the absence of such a selective network. We believe that competition, in this regard, may promote a lower cost and higher quality.

- **Expand procedures at low-cost outpatient and ambulatory care settings, and review the reimbursement methodology to more properly align provider incentives**
- **Reduce reliance on high-cost emergency rooms for primary care through effective, best-practice diversion strategies**

When Medicaid patients use the emergency room for primary care needs, it not only costs the system more, but also makes the emergency department (ED) less able to serve the needs of truly emergent cases. The PCCM/managed care system could address the overuse of emergency room care by ensuring adequate, convenient, local primary care access and by establishing a medical home – a primary care physician – for Medicaid participants. Illinois could also adopt additional strategies to decrease emergency room use, including:

- Requiring a co-payment for patients that inappropriately use emergent care
- Assisting clinics and physicians in supporting off-hour access
- Financially supporting the expansion of clinics and physicians offices in convenient locations, with convenient hours of operation
- Providing ask-a-nurse phone support to handle questions that do not require physical presence

- **Support interconceptional care management strategies to significantly improve birth outcomes**

The Medicaid program covers about one-half of all births in Illinois and about one-half of teen births. Two-thirds of these births are second babies or higher, with 17% of the subsequent births having an interpregnancy interval of less than eighteen months. A number of these births result in complications that have very costly consequences for the Medicaid program. HFS has begun an intervention program of interconceptional care that has real promise in providing quality care management and intervention for those high-risk pregnancies; this program should be supported and expanded.

- **Implement mandatory care management for all eligible seniors, adults with disabilities and those with mental illness**

Today in Illinois, other than those that voluntarily participate in a disease management program, no Medicaid beneficiaries with disabilities or mental illness have a “medical home.” The State should develop care management options for adults with disabilities and seniors with chronic conditions, as well as those with mental illness, to enhance cost effectiveness, care coordination, wellness, and quality of care. Some other states have already had success in finding private sector entities that will contract to care for people with specific types of disabilities. Florida, for example, has had such success and recently Hawaii has moved to cover all Medicaid populations within its managed care system. Illinois could seek a demonstration Waiver from CMS to include a segment of this beneficiary population in a mandatory managed care-type system. All departments should work together and consider mandatory enrollment in a care management system an important opportunity to integrate prevention, wellness, person-centered, and pay-for-performance principles into the Medicaid program.

- **Expand Federally Qualified Health Centers (FQHC) as a component of care management**

- **Consider including low-cost pharmacy clinics in the care management network, especially for areas where access to appropriate medical care can be an issue**

- **Implement pay-for-performance strategies that will align incentives with health outcomes**

- **Provide regular reports to policy makers and the public on the status (quality, savings and implementation) of the State care management program**

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## REVERSE THE BIAS TOWARD INSTITUTIONAL CARE IN THE LONG-TERM CARE SYSTEM

**Prioritize a unified, state-wide commitment to reduce the reliance on institutional care in the Medicaid long-term care system, so individuals who are aged or living with a disability or serious mental illness can remain in the communities in which they live with quality services as long as it is medically practical and cost-effective**

*(Note: The long-term care issue was also raised in the earlier Human Services section of this report. While both sections deal with overlapping populations, the ideas below apply to those individuals who are eligible for Medicaid based on their income level, assets and medical diagnosis.)*

### Current System

Medicaid beneficiaries in the long-term care system in Illinois are primarily low-income older adults (160,000 individuals) and adults with physical and developmental disabilities (241,000 individuals). Many of these beneficiaries are in high-cost nursing facilities and institutions, and, with appropriate support services, could live in a less expensive community setting.

However, Illinois' long-term care system is marked by an imbalance between the resources devoted to institutional care (nursing facilities, institutions for those with developmental disabilities or mental illness and psychiatric hospitals) and those devoted to less costly community care options. A recent AARP report showed that in 2009, Illinois had a rate of older adult institutionalization of 5.0 per thousand compared to the national average of 3.8 per thousand. Another study by the Human Services Research Institute found that in 2006, only 56.9% of Medicaid individuals with developmental disabilities were supported through Illinois community programs (compared with 82.9% nationwide). In sum, in Illinois Medicaid beneficiaries are in more expensive institutional settings at a greater rate rather than in alternative independent-living community environments, despite the fact that community settings are both less costly and preferred by older adults<sup>11</sup> and the physically disabled.

Many states have successfully reversed this institutional bias and provided meaningful choices for Medicaid beneficiaries to live independently in less-costly community settings – we suggest that Illinois could do the same by implementing the strategies described below.

- **Pursue a comprehensive and coordinated agency-wide approach to reduce the reliance on high cost institutional care in the Medicaid long-term care system, and offer meaningful choice to individuals with physical and developmental disabilities and all seniors in institutional care on Medicaid to live in a community setting. Enhance diversion and transition strategies to make community-based care the primary option**

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<sup>11</sup> [http://assets.aarp.org/rgcenter/health/fs\\_hcbs\\_hcr.pdf](http://assets.aarp.org/rgcenter/health/fs_hcbs_hcr.pdf)

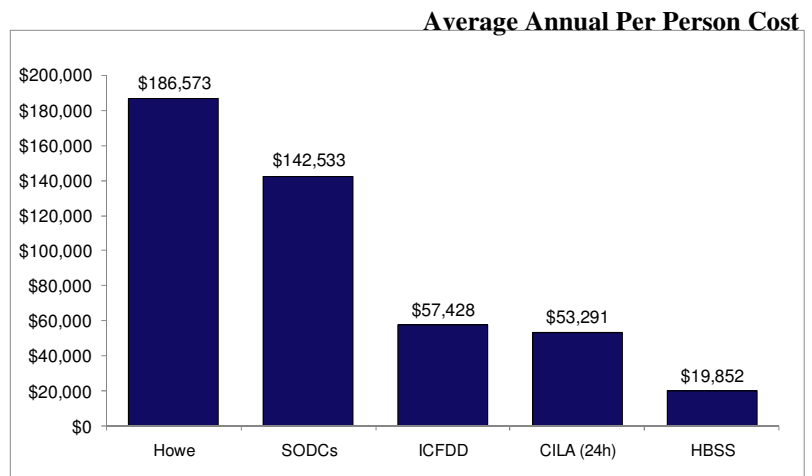
**Enhance the Community Care Program for Medicaid-eligible seniors:** The Community Care Program (CCP) prevents premature and unnecessary institutionalization of seniors by providing in-home and community services. CCP provides home-based services for over 55,000 adults each month and nearly 70,000 during the course of a year. The average cost per CCP beneficiary is \$8,400 per year, while the average annual cost of nursing home placement is close to three times that amount.

The CCP has been very successful in reducing nursing home utilization, and the program should be expanded. We believe that a goal of reducing nursing home placements by 10% per year, over the next five years, is desirable and achievable. Such a reduction could result in a net Medicaid liability decrease of roughly \$70 million a year, provided the necessary resources are available in the community to serve these seniors.

**Enhance community options for people with developmental disabilities that are living in State- or privately-run institutions:** The Division of Developmental Disabilities (DDD) provides services to adults with developmental disabilities who are living in their homes and communities, or in institutional settings. Currently, there are 2,385 individuals served in nine State-Operated Developmental Centers (SODCs), which provide residential and program services to those with developmental disabilities needing active treatment programs and intensive supervision.

One of the SODCs, the Howe Development Center, is a de-certified facility, serving approximately 289 adults at an average annual cost per beneficiary of \$186,573.

The average cost per individual of the remaining SODCs is \$142,533. In addition, there are over 300 private intermediate care facilities for persons with disabilities (ICF/DD) that are currently serving 5,648 adults at an average annual cost per beneficiary of \$57,428. Both SODCs and private ICF/DDs are certified and operate under the same federal regulations.



There is also a network of Community Integrated Living Arrangements (CILA), in which approximately 200 community-based organizations provide services to 7,240 people with disabilities on a 24-hour basis, at an average annual cost of \$53,291. Services provided by these centers include advocacy, peer counseling, skills training, information and referral.

Finally, there are 3,055 people with disabilities that currently receive home-based services at an annual individual cost of \$19,852. All other individuals with disabilities are being served on a

Waiver program, in which they receive day services at an average cost of approximately \$12,000 per year.<sup>12</sup>

Illinois relies disproportionately on high-cost institutional settings rather than less costly community settings or shared living environments to serve the needs of these individuals. According to recent state comparisons,<sup>13</sup> Illinois ranks at the very bottom - 51<sup>st</sup> - out of all states, including the District of Columbia, in serving adults with disabilities in settings of six persons or less.

We believe that every individual with developmental disabilities should be given a meaningful choice to live and remain in his or her community. Many of the beneficiaries who are currently being served in high-cost institutions in Illinois could be served in the community with quality services at a much lower price. States such as New Hampshire, Maine, Florida, Oregon, and Wisconsin have developed shared living environments that serve individuals in an independent foster care-like setting. In 2006, 70.5% of all persons nationwide were supported in living arrangements for six or fewer people - Illinois can take advantage of these best practices to make successful community transitions.

The State should immediately begin pursuing aggressive strategies to reduce the number of individuals with developmental disabilities in institutional care, including:

- Exploring the potential closure of some of Illinois' State-Operated Developmental Centers (SODCs).
  - Pursuing the immediate closure of Howe Developmental Center. The Department of Human Services has recommended to the TAB the closure of this facility, and the TAB supports this department's recommendation. The decision was based on a number of factors: concerns from the U.S. Department of Justice, the need to ensure quality of care for all residents, the decertification of the facility under the federal Medicaid program, the facility's inability to regain certification, and the continued loss of over \$2 million of federal matching funds per month.
  - Investing some of the savings from closing these facilities in enhancing the capacity and services available in the community.
- **Support the "consumer recovery" movement and provide proper community supports for those that are currently in nursing facilities or institutions with mental illness, and for those that are being considered for such placement:**
    - The TAB supports the "consumer recovery" model, in which consumers of mental health services receive greater choice to live in a community with proper supports, and also have access to broader evidence-based community treatment options.

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<sup>12</sup> It should be noted that the CILA, home-based services and private ICF/DD annual costs reflected above do not include pharmacy or other medical services funded through the Medicaid State Plan. The ICF/DD and CILA costs do include some nursing services provided at the residential settings. Nevertheless, the large disparity in costs associated with private and community services versus those delivered by the State, even after taking into consideration additional Medicaid medical services, clearly supports the TAB strategy addressed below.

<sup>13</sup> "The State of the States in Developmental Disabilities: 2008," Washington, DE. American Association on Intellectual and Developmental Disabilities. Braddock, D., Hemp, R. and Rizzolo, M.C. (2008)

- The State should consider moving certain long-term care patients (those who have a diagnosed mental illness, are clinically appropriate and do not require daily skilled nursing care) to more appropriate community-based settings, provided there are a sufficient quality and quantity of services available. This could make a large portion of the funds spent in general funds by DHS’s Division of Mental Health annually eligible for federal matching funds.
  - For those individuals who have serious mental illnesses, the State should pursue placement in the least restrictive setting possible, in the best interest of that individual and public safety. Nursing facility care should be the last resort, when it is clear that only this level of 24-hour nursing care is appropriate to support and ensure the individual’s health, safety and/or quality of life.
- **Assess the feasibility of outsourcing State-run psychiatric hospitals and move forward with the Tinley Park Mental Health Center Renaissance Plan:**

On the acute care side of mental health services, the TAB supports a State-wide assessment of the feasibility of outsourcing State-run psychiatric hospitals, or at least using a hybrid model with contracted staff and support services. In this regard, we support the plan to replace the Tinley Park Mental Health Center (TPMHC).

In February 2007, TPMHC was decertified by the Center for Medicare Services (CMS). As a result, TPMHC currently cannot bill the federal government for Medicare and Medicaid services, which results in a \$547,000 per year loss in revenue. According to the Department of Human Services (DHS), TPMHC continues to have significant life safety concerns directly related to the physical plant, and continues to experience difficulties recruiting and retaining professional staff. DHS has announced a plan to replace the TPMHC with a new, state-of-the-art private hospital. The plan is expected to result in a higher quality of care and significant savings, beginning in 2012. In Florida, a similar project yielded a 15% per year savings to the general fund.

### **Additional strategies to enhance community based services goals**

- **Create an effective and efficient screening process, before and after any institutional placement, to ensure that Medicaid meets the goal of doing all it can to provide the least restrictive setting for beneficiaries that want to remain in the community**

Under this strategy, the Division of Rehabilitation Services will need additional resources for effective post-screening. Policy makers should recognize that these additional resources will save substantial amounts in the long-run by appropriately transitioning and diverting individuals to community settings.

- **Ensure that discharge planning supports the State’s priorities and re-align resources to reflect this focus effectively**
- **Manage admissions to ensure a short institutionalization period and to facilitate rapid reintegration to a community setting**

- **Adopt a unified and coordinated “Money Follows the Person” approach to allow beneficiaries to transition to the community from a nursing home or institution**

The current federal Money Follows the Person (MFP) Demonstration grant in Illinois is a great opportunity for the State to work together in an integrated manner towards a common goal of giving all beneficiaries the choice of living in a community setting. All departments involved in this strategy can use the Demonstration to share ideas and work collaboratively. The key objective of the MFP Demonstration, as stated in the grant, is the “creation of an equitable, clinically sound and cost-effective system for identification and review of community transition candidates across all long-term care systems; including the improvement of prescreening, assessment for rapid reintegration and targeted review of longer stay residents, training and outreach education for providers and consumers on community alternatives across all long-term care systems.”

We see MFP as an integral part of initiating that interagency process. We also recognize that HFS, as the single State agency responsible to the federal government for Medicaid program financing and operations, and as the lead agency under the MFP grant, should be intimately engaged and involved in any of these decisions.

*Note: There were some concerns raised during TAB discussions of this issue that a lack of community capacity for appropriate services, providers, and housing would make an aggressive community-based care strategy difficult. As a result, we believe that the State should immediately undertake an assessment of community capacity to determine whether there are significant issues, and develop a plan to address any identified issues*

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## **ENHANCE PHARMACY COST CONTAINMENT EFFORTS**

### **Current System**

Prescription drugs are an expensive optional Medicaid benefit that Illinois, like most states, has chosen to extend to all beneficiaries. Illinois Medicaid currently reimburses pharmacies for the cost of prescription drugs in the amount of approximately \$2 billion dollars. The State then receives rebates from drug companies that total approximately \$700 million - a net cost of approximately \$1.3 billion.

The State has been very aggressive and effective in controlling some of these rising costs. Specifically, the Department of Healthcare and Family Services (HFS) has instituted the following procedures: extensive use of prior approval, prescription quantity limits, daily dose limits, a unique refill-too-soon calculator, age restrictions for some drugs, reduction in reimbursement rates, aggressive use of maximum allowable cost (MAC) pricing, a three-brand limit, tiered co-pays and dispensing fees that encourage generic drugs usage, and a preferred drug list which produces substantial rebates. These measures combine to save over \$250 million annually in prescription drug costs.



Notwithstanding these efforts, the cost of brand drugs in Illinois Medicaid has grown 8.8% per year over the last five years (from \$118.31 to \$180.39). Moreover, 30% of all prescriptions continued to be filled with brand drugs. Additionally, the cost of mental health drugs is excessively high, and the prescribed drug list does not provide, as a first option, some of the lower-cost alternatives to the brand mental health drugs. Finally, the dispensing fee that pharmacies receive from the Medicaid program for brand and generic drugs appears to be higher than the fees paid to the pharmacies by private insurance companies.

The TAB has identified the following opportunities for additional savings:

- **Consider enhancing State purchasing power: Pool all State prescription drug purchases, and combine administrative resources to reduce duplication of effort and to maximize savings**

There are a number of additional ideas that HFS and the State could explore to further its already effective cost containment efforts. First, HFS could work with other State agencies and explore the idea of developing a first-in-the-nation, State-wide government pharmacy purchasing pool that maximizes savings and rebate opportunities to the government by negotiating with drug companies for the best price through supplemental rebates. In this pharmacy purchasing pool, the State would look to pool all prescription drug purchases where the State is a payor, including Medicaid, State employees, State retirees, and Corrections. The State could also negotiate with county and local governments to join the pool. The larger the pool of government payors, the greater the bargaining power and value of discounts and rebates will be.

We recognize that such a purchasing pool has not included Medicaid prescription drugs in the past because of the rebates and supplemental rebates allowed states in the Medicaid program only. If this becomes an issue, we believe that the Governor and policy leaders across State government should work with their congressional delegation to lift legal restrictions if possible.

- **Continue to ensure the effectiveness of the Preferred Drug List (PDL), including reviewing options for lower cost drugs and adding aggressive management of mental health drugs**

A close look at the State's current PDL shows some higher-cost brand mental health drugs. In FY08, the total liability for these drugs after rebate was about \$146 million. Some of these mental health drugs may have lower-cost alternatives that could be listed instead of the high-cost brand name, provided a physician has the ability to override any such restriction based on medical necessity.

- **Review the dispensing fee charged by pharmacies to State Medicaid to determine whether it needs to be modified**

Currently, the State is paying pharmacies a fee of \$3.40 for brand-name drugs and \$4.60 for generics to dispense prescription drugs to Medicaid beneficiaries. The total amount paid to pharmacies through these fees in FY08 was approximately \$91 million. The State ought to look at the level of dispensing fees paid to pharmacies dispensing drugs to Medicaid beneficiaries to make sure that they are

appropriate in relation to the level paid in other states and paid to private insurers in Illinois, recognizing there may be differences in the collectability of copayments.

- **Review best practices in other states and strategies for high-cost medication management**
- **Work with the federal delegation to expand the availability of rebates to Medicaid managed care companies**

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#### **USE TECHNOLOGY TO ENSURE THAT MEDICAID CLAIMS DATA CAN BE USED BY THE STATE AND THE PUBLIC TO DRIVE COST SAVINGS AND BETTER HEALTH OUTCOMES**

- **Provide privacy-protected access to the public regarding State Medicaid claims information, with all unique, identifying information removed**
- **Support a Medicaid Management Information System (MMIS) re-design that will improve claims processing and data analysis**
- **Continue to plan for Health Information Technology (HIT) improvements**

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#### **MAXIMIZE FEDERAL MATCHING FUNDS**

The State of Illinois has not maximized its efforts to receive a federal match for the cost of care to certain beneficiaries. Some of these beneficiaries are in institutional settings and are not covered under federal Medicaid guidelines because of the facility in which they are placed. In other areas, Illinois has expanded eligibility for programs beyond federal guidelines - these are commonly referred to as “expansion populations.” The State is then responsible for all funding, without any federal match.

Other states have sought Waivers from the federal government to cover some of these programs and expansion populations. In some states, CMS has allowed matching funds for beneficiaries that do not receive a match today in Illinois. In those states, Waivers were tailored to keep low-income beneficiaries out of high-cost institutional settings.

Moreover, as the federal government looks to reform health care, the timing may be right for Illinois to approach its congressional delegation to explore issues of revenue maximization. For example, the federal government might be persuaded to change its restriction against allowing Medicaid matching funds for those individuals with mental illness currently in nursing homes.

The TAB has not had sufficient time to explore all aspects of potential opportunities for additional federal match, but we see an opportunity for the State to explore. Whether through an institutional setting not

currently receiving a federal match, or a non-Medicaid-covered expansion population, the State may be forgoing several millions of dollars for services provided to these low-income, at-risk populations. We urge the State to explore all available opportunities to maximize federal revenue in order to minimize the burden to the general fund.

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## OTHER IDEAS

During the course of the TAB’s review, the following additional ideas were raised. While we did not sufficiently review these ideas – and thus we neither endorse nor oppose them – we include them here as additional ideas that the Governor and his staff might want to look into further. Rather than leave potentially valuable ideas off the table, we decided to include a small set of such ideas in our report.

- **Federal Medical Assistance Percentage (FMAP):** The current federal stimulus package has given all states an 18-month across-the-board increase in the FMAP rate. However, the methodology that provides the basis for the determination of the FMAP baseline has not had a comprehensive and thorough review by Congress for a number of years. At the time the FMAP rate was set for all states – and the methodology determined for rewarding states with a lower per capita income per population base – Illinois was experiencing much higher growth and was not facing today’s high unemployment and the loss of critical economic infrastructure and revenue base. Given the change in the State’s economy, the Governor and policymakers should encourage Congress to closely scrutinize the FMAP methodology and tailor it to today’s economic situation. Such a review should be made prior to the expiration of current stimulus programs.
- **Global Budgeting:** In Illinois, department heads are too often focused on particular line items within a department, or even a division, budget. In this situation, decisions are made based on available funding in a given line item, instead of available funding in the entire system. A number of states have begun to coordinate all Medicaid-eligible expenditures to remove them from departmental or agency silos, and to introduce a more global approach that considers “what is best for the person” receiving services.

States that have global budgeting use various means – such as fund transfers with legislative approval and authority of a federal Waiver – to transfer Medicaid funds to needed areas to ensure that cost-effective services are given to beneficiaries in the right place at the right time.

Oregon and Washington each pool state and federal funds for both institutional and home- and community-based services into one budget with an overall spending cap. The federal government has recently embraced this type of approach in its “money follows the person” demonstrations.

Additionally, the idea of global budgeting was recommended in 2007 by the Illinois Older Americans Act Advisory Committee.<sup>14</sup>

- **Section 1115 Waiver:** The State should undertake a comprehensive review of recent Section 1115 Waivers to identify whether it is a good opportunity for Illinois. A Section 1115 could allow for additional matching opportunities and provide for fiscal responsibility over the period of a Waiver demonstration. Because Section 1115 Waivers are major demonstration projects and involve a number of stakeholders' interests, the State should reach out to stakeholders and consumers if it chooses to begin planning for any such transformation.

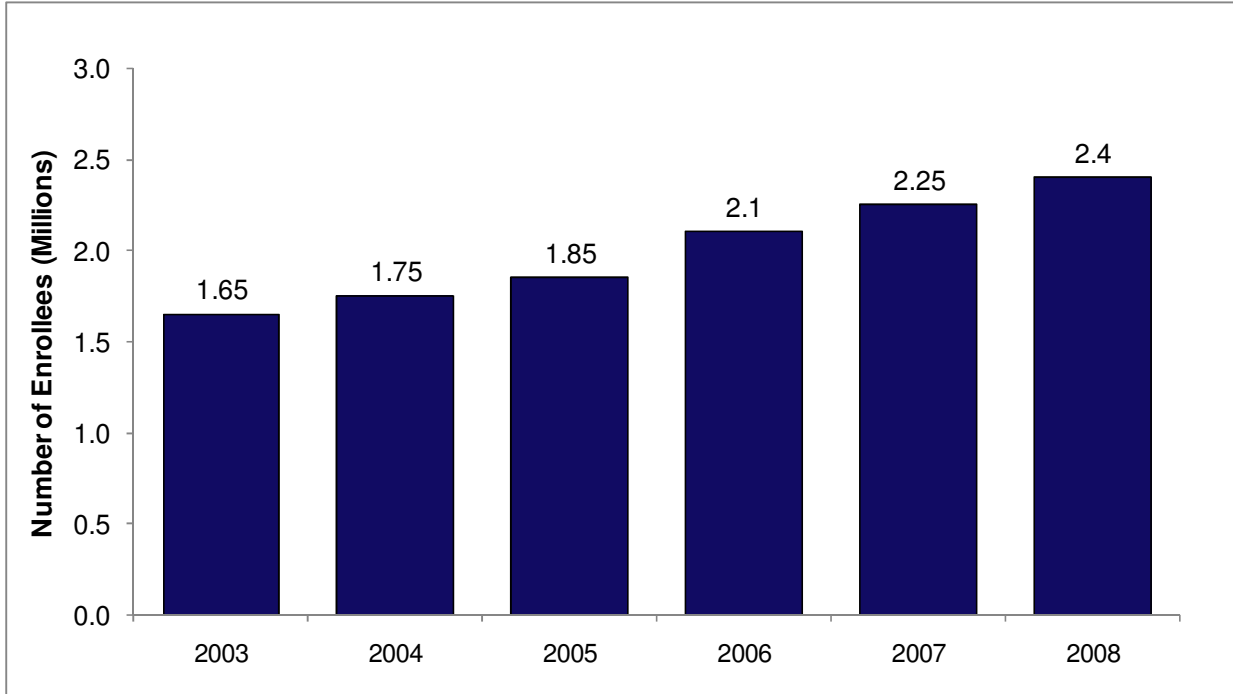
In planning for a Waiver, the State could consider an approach sometimes referred to as a Global Waiver, which was recently approved by CMS for the State of Rhode Island, where the entire Medicaid population is covered under one demonstration, with maximum state flexibility. Alternatively, the State of Vermont received a Waiver a few years ago for its entire long-term care population, which has reduced costs by ensuring that beneficiaries are given a meaningful choice to remain in a community setting rather than a nursing home or institution. The State could also follow the examples of several other states that have received approval for successful best practices demonstration Waivers that have reduced costs and provided quality services.

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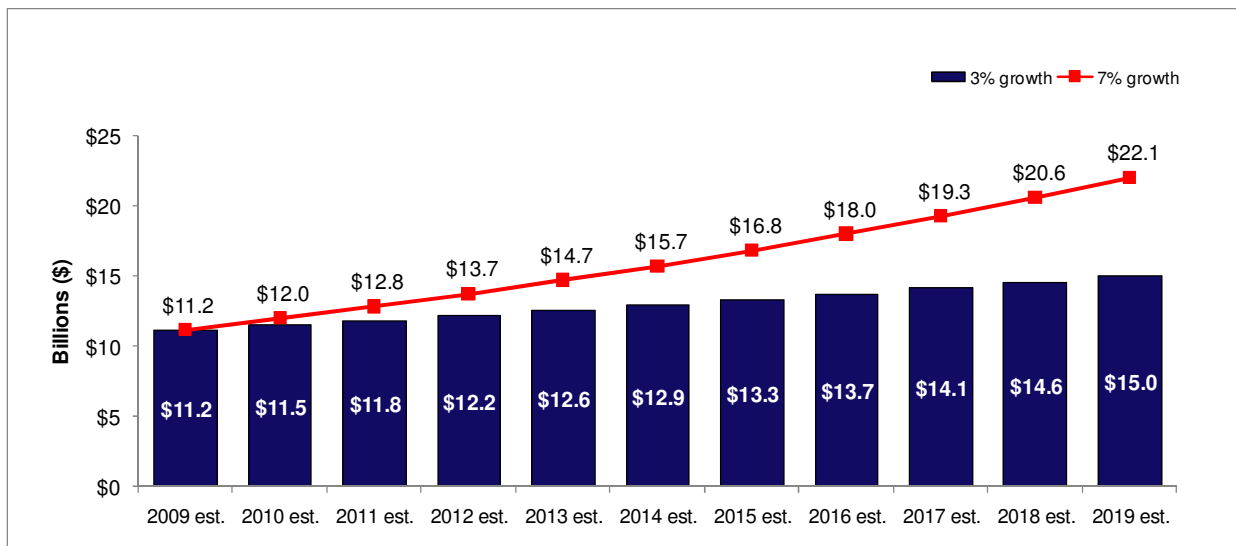
<sup>14</sup> Older Americans Service Act, 2008 Report to the General Assembly

## Medicaid Appendices

**Appendix 1 -- Historical Medicaid Enrollment in Illinois  
(2003 – 2008)**



**Appendix 2 -- Projected Total Medicaid Liability  
(2009 – 2019 est.)**



## PENSIONS

The State of Illinois currently maintains five separate defined benefit pension plans. In aggregate, these plans cover over 300,000 active employees and almost 400,000 retirees, surviving spouses and terminated former employees. These pension plans are seriously underfunded, and the need to fund the benefits that have already accrued under these plans represents a serious drain on State finances.

Below is an overview of the State pension plans; all data is as of June 30, 2008 (All dollar amounts have 000's omitted and represent millions of dollars.):

Plan	Teachers' Retirement System of The State of Illinois (TRS)	State Employees' Retirement System of Illinois (SERS)	State Universities Retirement System of Illinois (SURS)	Judges' Retirement System of Illinois (JRS)	General Assembly Retirement System of Illinois (GARS)	Totals
Liabilities	\$ 68,632	\$23,841	\$24,918	\$1,457	\$ 236	\$ 119,084
Assets	\$ 38,431	\$10,995	\$14,586	\$ 612	\$ 75	\$ 64,699
<b>Unfunded Liability</b>	<b>\$ 30,202</b>	<b>\$12,846</b>	<b>\$10,331</b>	<b>\$ 844</b>	<b>\$ 160</b>	<b>\$ 54,383</b>
Funded Ratio	56.00%	46.10%	58.50%	42.00%	32.00%	45.67%
Active Employees Covered	160,801	66,237	83,074	957	182	311,251
Retirees, Other Terminated Vested Participants and Surviving Spouses	196,431	77,790	122,067	981	470	397,921
Total Membership	357,232	144,027	205,141	1,938	652	709,172

In assessing the funded status of these plans, it is important to note that the assets contained in this table represent amounts as of June 30, 2008. Based on the market declines that have occurred since that date, it is reasonable to anticipate that asset values have declined by at least 20%; this would increase the unfunded liability to over \$65 billion and decrease the funded ratio to approximately 43%. It is also important to note that the liabilities are valued using an 8.5% discount rate. This rate is higher than that used to fund plans in the private sector (whose actuarial assumptions are regulated by the Internal Revenue Service), so the current 8.5% rate may serve to understate the liabilities. Accordingly if a lower

rate is utilized (one that is perhaps more realistic in light of economic circumstances), the liabilities will increase and the plans' under-funding would be even worse. For example, use of a discount rate between 6.0%-7.0% is anticipated to increase the plans' liabilities by an amount estimated to be between \$10 billion and \$20 billion.

**Plan Design.** In considering opportunities available with respect to these pensions, it is important to understand the underlying benefit structure. These comments will focus on the three main plans and not address all details of the Judges' Retirement System of Illinois or the General Assembly Retirement System of Illinois.

Each of the plans is a defined benefit pension plan that provides participants with lifetime payments upon retirement. The basic accrual under each of the three main plans is 2.2% of final average salary per year of credited service.<sup>15</sup> Accordingly, a member who completes 30 years of service with a final average pay of \$50,000 would receive a normal retirement benefit of \$33,000/year ( $\$50,000 \times .022 \times 30$ ). The plans also have provisions capping maximum benefits payable; generally, the plans cap out at 75%-80% of final pay.

The 2.2% formula applies only to members who are not covered by Social Security. There are approximately 240,000 active members who are not covered by Social Security, distributed as follows:

	<b>Covered By Social Security</b>	<b>Not Covered by Social Security</b>
TRS	n/a	165, 572 (all active members)
SERS	63,418	2,819
SURS	n/a	73,086 (all active members)
JRS	n/a	1,938 (all active members)
GARS	n/a	652 (all active members)

For the members not covered by Social Security, the Illinois State plans represent both a benefit in lieu of Social Security plus an additional employer-sponsored amount. For the 63,000 employees who are covered by Social Security, the basic accrual rate is 1.67% of final average salary per year of credited service.

In applying the formulas under the three main plans (to all covered employees), the definition of compensation used is important. Compensation based on total salary is based on the average of highest consecutive four years within last 10 years of employment.

<sup>15</sup> The formula under JRS is 3.5% of final salary for the first 10 years of service and 5.0% of pay for each additional year of service. The formula under GARS is between 3.0% and 4.5% of final salary per year of service for the first 12 years of service and 5.0% of final salary per year of service in excess of 12.

Both SERS and SURS have alternative formulas for employees deemed to be in dangerous jobs. Although these alternative formulas are associated with jobs such as police and firefighting, the availability of the special alternative formulas under SERS has been expanded to cover a wide range of other personnel. These alternative-formula employees receive a benefit of 3.0% of final average salary times service (for alternative-formula personnel not covered by Social Security) or 2.5% of final average salary times service (for alternative-formula personnel covered by Social Security). Currently, SERS has almost 17,000 personnel covered by the alternative formula and SURS has 250 active members covered by the alternative formula.

Members who retire before their normal retirement date can receive a reduced early retirement benefit. The key normal and early retirement provisions under the plans are as follows:

<b>Plan</b>	<b>Unreduced Benefits Available</b>	<b>Key Early Retirement Provisions</b>
TRS	<ul style="list-style-type: none"> <li>■ Age 60 and 10 years of service, or</li> <li>■ Age 62 and 5 years of service, or</li> <li>■ 35 years of service.</li> </ul>	<p>Early retirement available at age 55 and 20 years of service; benefits are reduced by 0.5% per month that retirement precedes age 60.</p> <p>However, a member (and his or her employer) can make a one-time payment to the plan to avoid the early retirement reduction.</p>
SERS	<ul style="list-style-type: none"> <li>■ Age 60 and 8 years of service, or</li> <li>■ 35 years of service, or</li> <li>■ Rule of 85 (85 combined age and service points).</li> </ul>	<p>Early retirement available at age 55 and 25 years of service; benefits are reduced by 0.5% per month that retirement precedes age 60.</p>
SURS	<ul style="list-style-type: none"> <li>■ Age 60 and 8 years of service, or</li> <li>■ Age 62 and 5 years of service, or</li> <li>■ 30 years of service.</li> </ul>	<p>Early retirement available at age 55 and 8 years of service; benefits are reduced by 0.5% per month that retirement precedes age 60.</p>
JRS	<ul style="list-style-type: none"> <li>■ Age 60 and 10 years of service, or</li> <li>■ Age 62 and 6 years of service.</li> </ul>	<p>Early retirement available at age 55 and 10 years of service; benefits are reduced by 0.5% per month that retirement precedes age 60 (if member has 28 years of service), but early retirement benefits are increased for retirees with more than 20 years of service.</p>
GARS	<ul style="list-style-type: none"> <li>■ Age 55 and 8 years of service, or</li> <li>■ Age 62 and 4 years of service.</li> </ul>	NA

Employees make contributions to the plans as follows:



	TRS	SERS	SURS	JRS	GARS
Not Covered by Social Security	9.4% of salary	8.0% of salary	8.0% of salary	11.0% of salary	11.5% of salary
Covered by Social Security	NA	4.0% of salary	NA	NA	NA
Alternative Formula/Not Covered by Social Security	NA	12.5% of salary	11.0% of salary	NA	NA
Alternative Formula/Covered by Social Security	NA	8.5% of salary	N/A	NA	NA

Retirees receive annual increases to their pensions intended to offset increases in the cost of living (COLA). These increases are 3% per year, compounded.

**Funding.** For a number of years the State has systematically underfunded the pension plans. The most common measure of funding considers the annual contribution needed to fund (1) current year accruals, plus (2) amortization of previously accrued unfunded liabilities. Excluding contributions to the plans in 2004 attributable to pension obligation bonds (which represent both an influx of cash and the creation of additional debt obligations), in the last 10 years State contributions to the plans have been over \$20 billion less than the amount that would be required to simply allow the plans to fund current year accruals and amortize previously accrued unfunded liabilities – in effect, the State has contributed over \$20 billion less than the amount needed to allow the plans to “stand still.”

It is in this context that we identify the following opportunities for savings and increased efficiency:

### Pension Structure

Many of the problems with the current retirement plan structure are attributed to problems considered inherent in all defined benefit plans; however, the TAB believes that virtually all of the problems are attributable to aspects of the Illinois plans that can be remedied while retaining a defined benefit plan structure. Accordingly, the TAB believes that the State should continue to provide a defined benefit plan as the primary retirement vehicle for State employees – albeit one with significant changes (as described below).

The TAB is aware that there has been much discussion of moving governmental plans away from the defined benefit model and towards the defined contribution model that is dominant in the private sector. However, moving to a pure defined contribution model loses much of its attractiveness upon examination of several key points.

Most significantly, it should be noted that the majority of State employees do not have Social Security coverage, unlike the private sector where employees really have two retirement programs—Social Security and the employer-sponsored program (such as the 401(k) plan). If Illinois moved to a pure defined contribution plan, the absence of Social Security benefits would render over 75% of State employees without a minimum life annuity upon retirement. This is a significant difference from private sector employees who, as noted, have both Social Security and employer-sponsored plans.

Also, transition to a defined contribution program would not be financially advantageous to the State (especially in the short-term):

- In the short- and mid-term, a transition to a defined contribution plan does not reduce costs (for newly hired employees). The annual pension costs associated with younger, newly hired employees is fairly low (approximately 1% of pay) and gradually builds up over time. By contrast, virtually all of the annual cost for a defined contribution plan is recognized immediately upon entry into the plan. (A defined contribution plan providing 5% of pay costs the employer almost the full 5% for all participants – even for newly hired employees.)
- Employees contribute a substantial component of the costs of the State plans.
- In aggregate, the “normal” cost to the State (reflecting the value of accruals earned in a single year) for the current pension plans represents approximately 9% of covered payroll. In light of the fact that Social Security alone would represent a cost of 6.4% of payroll, the net incremental cost to the State (after consideration of Social Security contributions) of maintaining defined benefit plans is less than 3% of covered payroll.

We are aware of other states that have addressed this problem. To date, very few states have moved to a pure defined contribution structure (most notably Alaska, Michigan, and West Virginia). Even then, the transition to defined contribution has been problematic. In fact, West Virginia has recently reopened its defined benefit plan and given defined contribution plan participants the opportunity to transfer to the defined benefit plan. Likewise, Alaska currently has legislation pending to reopen its defined benefit plan.

Instead, many other states that have addressed these issues have created programs that retain a defined benefit element but try to better balance defined contribution and defined benefit features.

- A number of states including Ohio, Georgia, Indiana, and Oregon have defined benefit plans with more modest formulas (with annual accruals of between 1.0 and 1.5% of pay) and a defined contribution element.
- Other states (including Colorado, Ohio, and South Carolina) have programs that allow employees to choose between a defined benefit and a defined contribution structure.
- Other approaches are also being adopted in isolated instances, such as the hybrid, cash-balance formula adopted by Nebraska, and the Arizona approach in which employer contributions, employee contributions and annual COLAs are tied to the plan investment results.

Although these different approaches may merit consideration, for purposes of the TAB initiative the most important points to note are that (1) state governments are, for the most part, preserving some defined benefit structure; and (2) none of these other approaches inherently offers the kind of cost savings so important to Illinois at this time.

That said, even if the State retains a defined benefit plan, there are several aspects of the State’s pension system that should be changed in order to render the plans less costly and less susceptible to manipulation:

- **Retirement age:** The current normal and early retirement provisions of the plans are costly and not justifiable. The current plans permit employees to receive “normal” (unreduced) retirement at or before attainment of age 60. In a period of increasing life expectancy and longer productive careers, the current plan provisions encourage retirement at an age that is simply too early.

The current normal retirement age provisions create an environment that encourages retirement at age 60—incurring both pension and medical costs. For example, under TRS, of the 132,000 full-time employees and regular substitute teachers covered by the plan—fewer than 3,000 are over age 60. By contrast, TRS has over 26,000 retirees age 65 or younger. Similarly, SERS has over 18,000 retirees (out of 44,000 total retirees) age 65 or younger. This is a loss of resources that Illinois cannot afford.

In the case of a participant retiring at a plan’s “normal” (unreduced) retirement age, a plan with a normal retirement age of 67 is approximately 40% less costly than a plan using age 60 for unreduced benefits. Also, retirements taken before normal retirement age should reflect true actuarial equivalent reductions. It should be noted that early retirement should still be available to employees—but it is the employees who should bear the cost of any decision to retire early.

- **Final average salary and compensation:** The formula for determining pensionable earnings should be reformed. Such reform would include lengthening the period used to determine final average salary and using a definition of compensation (such as base pay) that is not susceptible to artificial inflation near retirement.
- **Alternative formula:** The use of the special benefit formula (as noted, currently covering almost 17,000 employees) must be reviewed and restricted. For example, in 2004, highway maintenance workers were added to the special formula; this seems to be a significant distortion of a special formula intended for police officers and firefighters.
- **Full funding:** A binding formula for fully funding the pensions, and any future changes thereto, must be put into place. One of the greatest flaws in the current Illinois system is the “moral hazard” that the State increases benefits and/or skip payments today, recognizing that the cost of those decisions are borne by future generations.

With these principles in mind, the Board sees the following savings opportunities for the State.

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**INTRODUCE A NEW PENSION PLAN FOR NEW HIRES AND INCREASE  
EMPLOYEE CONTRIBUTIONS FOR CURRENT EMPLOYEES**

Governor Quinn has proposed revising the State employees’ pension system going forward and increasing contributions for current employees. The TAB believes that a revised State pension system for newly-hired employees, using a design substantially similar to the design proposed by Governor Quinn, represents a long-term savings opportunity for the State.

Under the Governor’s proposal, the new pension plan would have the following key provisions:

- Unified benefit formula for all employees
  - Benefit equal to 2% of final average compensation, per year of service, for employees not covered by Social Security and 1.5% per year for employees covered by Social Security. Service would be capped at 35 years, creating a maximum benefit of 70% of final average pay (for employees not covered by Social Security) and 52.5% of final average pay (for employees covered by Social Security).
  - Unreduced benefits at Social Security normal retirement age (67) and 10 years of service. Reduced benefits available at age 62 plus 10 years of Service, with 6% reduction per year for benefit commencement before Social Security normal retirement age.
  - Benefits would be based solely on base salary (up to Social Security Covered Wage Base; this was \$106,800 in 2009), indexed for annual increases in the SSWB. Final average salary is average of highest consecutive eight years out of last ten years, with raises limited to 3% each year.
  
- New contribution schedule to be paid into pension plans by new employees:

	<b>TRS</b>	<b>SERS</b>	<b>SURS</b>	<b>JRS</b>	<b>GARS</b>
Not Covered by Social Security	8.0% of salary (currently 9.4%) <sup>16</sup>	7.0% of salary (currently 8.0%)	7.0% of salary (currently 8.0%)	7.0% of salary (currently 11.0%)	7.0% of salary (currently 11.5%)
Covered by Social Security	NA	3% of salary (currently 4%)	NA	NA	NA

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<sup>16</sup> The higher rates for TRS reflect provisions allowing employees to “purchase” increased access to early retirement subsidies.

- New contribution schedule for current employees:

	TRS	SERS	SURS	JRS	GARS
Not Covered by Social Security	11.0% of salary (currently 9.4%)	10.0% of salary (currently 8.0%)	10.0% of salary (currently 8.0%)	13.0% of salary (currently 11.0%)	13.5% of salary (currently 11.5%)
Covered by Social Security	NA	6% of salary (currently 4%)	NA	NA	NA

- Service Limits: 35-year limit creating a 70% maximum benefit for employees not covered by Social Security, with no ability to “purchase” additional credited service, except two years of military service, and with no conversion of vacation or sick time.
- COLA: Simple-interest COLA equal to the lesser of 3% or one-half of increases to the consumer price index(CPI).

### TAB Reaction to Governor’s Pension Proposals

The Governor’s proposal represents a more modest, but substantial defined benefit structure. Most importantly, the Governor’s proposal eliminates a number of secondary features within the current system that are costly and that encourage behaviors that are contrary to prudent management of the State’s finances. These features include:

- The proposed rate of benefit accrual (2.0% of pay for employees not covered by Social Security and 1.5% for employees covered by Social Security) represents approximately a 10% reduction in the overall benefit level provided by the new plans, yet continues to allow a meaningful level of retirement income. According to a 2006 study by the State of Wisconsin of 68 major public employee plans, 28 had accrual rates between 1.3% and 1.9% of final pay and 24 plans had accrual rates between 1.9% and 2.1% of final pay. By way of contrast, only eight plans had accrual rates over 2.1% of final average pay. When Social Security coordination is reflected, the average accrual rate for plans in this study that were coordinated with Social Security was approximately 1.97% of pay and the average accrual rate for plans not coordinated with Social Security was approximately 2.3% of pay.

The TAB notes that this reduction in benefit accrual rates in Governor Quinn’s proposal is accompanied by a reduction in employee contribution levels. While the TAB understands the appeal of lower employee contributions for a lower benefit level, the TAB believes that the State’s current financial circumstances do not justify lowering employee contributions and disagrees with the lower employee contribution levels included in the Governor’s proposal.

- As noted, the current plans permit employees to receive “normal” (unreduced) retirement at or before attainment of age 60. Moving to an age 67 normal retirement date is an important feature that should

be put into place for the State's plans. Currently, 25 states use age 65 or Social Security Normal Retirement Age as their "normal" retirement age for one or more of their statewide employee plans.

- The Governor's proposal contains a number of ancillary provisions that will limit manipulation of the benefit formula. The TAB supports these efforts to reduce the opportunity for manipulation of the pension formula under the plans. The provisions in the Governor's proposal that reduce the opportunity for manipulation include the use of eight years of compensation (out of the last 10 years of service) in the definition of final average compensation, limiting raises recognized by the plans to 3%, limiting employees' ability to "purchase" additional years of credited service, and limiting compensation recognized under the plans to the Social Security Wage Base.
- The Governor's proposal limits cost-of-living adjustments to the lesser of 3% or ½ of the consumer price index (CPI). The TAB supports this limitation.

The Governor's proposal represents a prudent long-term design, and the TAB supports its basic direction. The Governor's proposal would reduce the taxpayers' pension liability by over \$150 billion in 2045.

Even if adopted immediately, the Governor's proposal would achieve only minimal short-term cost savings. This occurs because the Governor's proposal covers only employees hired after the adoption of the new provisions. Although a significant portion of those savings are not realized until after the timeframe established for the TAB's focus, these represent significant and noteworthy savings that should be pursued. Because the Governor's proposal is limited to employees hired in the future, the current formula will be the predominant formula under the State's plans for many years to come. For this reason, the TAB believes the State should build on the direction taken by the Governor's proposal and go farther.

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## **CHANGE FUTURE BENEFITS FOR CURRENT EMPLOYEES**

The Governor's pension proposal includes an increased employee contribution, but no other changes for current employees. As a result, the shortcomings in the current plans (such as the ability to receive a full benefit at age 60) will continue to apply to the 300,000 active employees currently in the plans. The strategy for current employees reflects current interpretations of the Illinois constitution that recognizes pension benefits as contractual undertakings by the State that cannot be "impaired." Specifically, the Constitution states that:

Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

This impairment provision is seen as limiting the State to increasing employee contributions as the sole action available to the State with respect to current employees.

The approach of preserving plan provisions for all current employees and this concept of impairment are common in governmental plans. However, in the private sector (where ERISA and the Internal Revenue Code protect previously accrued benefits – but do not prevent changes applicable to future accruals), it is more common for employers to modify benefit formulas applicable to future service performed by current employees.

In order to accelerate the impact of the Governor’s proposed pension changes, the TAB supports aggressive action by the State to apply some or all of the Governor’s proposed pension changes to current State employees with respect to service performed in the future. The TAB recognizes that a shift of this nature would be too dramatic for those employees nearing retirement eligibility. Accordingly, the TAB supports aggressive action by the State to move to a new pension formula and/or reduced subsidies for retirement before age 67 (both changes being substantially similar to the changes proposed by Governor Quinn) for all future service for all current employees who have sufficient opportunity to revise their retirement planning in response to these changes, for example, by applying new provisions only to those employees who have completed fewer than 20 years of service, or some other provision designed to address employees who are nearing retirement age.

The TAB recognizes the obstacles to the implementation of this change. However, we feel that it is important to move away from the current pension formula – and toward a fundamental design that is more sustainable – as soon as possible. There are no savings estimates available for this opportunity.

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## **CONSOLIDATE PLAN ADMINISTRATION AND SERVICE PROVIDERS**

The State’s pensions are currently administered using three different administrative structures and systems: TRS, SERS (which also administers GARS and JRS) and SURS. Total administrative costs for the three systems are over \$45 million per year and the current administrative structure requires approximately 500 employees.

The TAB encourages the State to consolidate these entities into a single program, with unified administration, investment management and actuarial services. The current fragmented approach to administration cannot be justified, particularly as the State moves to a unified formula (although consolidation makes sense even if differences in the provisions of the five plans remain). Once implemented, we estimate that consolidation of plan administration will generate savings of at least \$10 million per year. Such savings would only be available after consolidation is complete; this process would take several years.

The TAB did not address the issue of whether plan administration should continue to be done by State employees or should be outsourced to a third party. We anticipate that outsourcing may present additional

savings opportunities. Accordingly, the State should undertake a feasibility study to assess whether the consolidated plan administration should be performed in-house or whether it should be outsourced.

In addition to consolidation of plan administration, the TAB believes the State should review, restructure, and rebid all major contracts for plan services, particularly contracts for investment management and actuarial services. This process should occur in the normal course of the plan consolidation discussed above but is also an independent idea even if the plan consolidation does not occur. The Commission on Government Forecasting and Accountability recently projected that the consolidation of investment managers is likely to save the State approximately \$21 million per year (once such consolidation is implemented).

The current, fragmented approach limits the ability of the State to engage in comprehensive management of these programs. The State currently receives five different actuarial reports and does not receive consistent and comprehensive data or other analyses regarding these plans. Similarly, the current fragmentation of investment management adds costs and renders it virtually impossible for the State to develop an integrated and strategic approach to investment management and risk management. Although we cannot attribute a cost savings to this opportunity, we believe it to be a fundamental component of prudent plan management.

It should be noted that the issue of having too many separate plans is not limited to the five State-wide plans discussed in this report. According to the U.S. Census Bureau, Illinois has 370 separate State and local pension plans, the second highest number of such plans in the country. By contrast, California maintains 59 state and local plans and Indiana maintains 71 state and local plans.

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## **BEGIN REDUCING UNFUNDED LIABILITIES NOW**

To date, there has been much focus on the unfunded liabilities under the State's pension plans and discussion about how to reduce that liability. Any discussion of the unfunded liability must start with the acknowledgement of an unpleasant fact: the liabilities for the State pensions represent benefits that have already been accrued, for services already rendered, by retirees and State employees. None of the design changes described above will reduce that liability; they will only affect the rate of growth of those liabilities in the future. Correspondingly, it must be recognized that the only way to reduce the current unfunded liabilities is to fund them.

As stated above, over the past decade the State has underfunded the retirement plans by over \$20 billion. As a result, the contributions needed simply to finance current accruals and pay "interest" on the unfunded benefits will be approximately \$6 billion per year for the next few years (gradually increasing). Each year that the State fails to meet its funding obligations to the plans, it is simply adding to the burden that will be imposed on future generations.



In managing current needs and priorities, it is inconsistent with sound governance – of the plans and of the State’s finances – to continue deferring these payments. Similarly, the State needs to cease the practice of making plan changes that will achieve savings in the future – and use those savings as an offset to current contributions.

Continuing to defer payments represents a vicious financial trap for the State. If the State continues following the funding policies of the last decade, the unfunded liability is projected to double in the next ten years to over \$120 billion.

Accordingly, the TAB believes that the process of fully funding the plans’ liabilities should begin now and that deferral of these obligations should cease. Governor Quinn’s proposal regarding the State pensions contains funding recommendations that can serve as the beginning of a dialogue on this need. We recognize that this idea is beyond the formal scope of the TAB mandate; however, we believe that the ongoing and persistent underfunding of these plans undermines the State’s overall finances. We also believe that such funding is an integral component of the comprehensive pension restructuring described elsewhere in this section. The State’s employees have made their contributions to the plans while the State has systematically underpaid its contributions. It will be difficult to gain acceptance of the plan design changes described above without convincing plan participants that the State is serious about making good on its obligations.

The State needs some mechanism that ensures that funding for pension liabilities is addressed. One opportunity might be the creation of a spending cap on State expenditures that creates a funding pool for pension liabilities. Under this idea the State would maintain an operating budget that balances in recessions and specifically directs that any higher levels (of boom-time revenues) be dedicated to reducing the pension obligations. This idea would require setting a base-level of expenditures during a recession and limiting spending growth to inflation plus growth in population and a small percentage to reflect rising real per-capita wealth. Any effort to exceed the formula expenditures would require some supermajority vote to protect funding of pension liabilities.

## **Constraints and Considerations**

There are several constraints on the ability of the State to realize the savings opportunities described above. Most notably, most of the savings opportunities described herein are subject to collective bargaining and will require difficult negotiations with the unions representing the State’s employees. Additionally, some of the changes (such as consolidation of pension administration) will require legislative approval and are likely to meet resistance from the current plan administrators. Also, any effort to modify retirement benefits for current employees is likely to generate legal challenges; indeed, if this matter is resolved in the courts, it is not clear whether such changes will be permitted. Nonetheless, this is an effort worth pursuing.

The TAB is cognizant of the fact that these obstacles are significant. Nonetheless, the savings opportunities identified can have a significant impact on the State’s finances, and the State’s current financial circumstance necessitates pursuit of these opportunities.

## RETIREE HEALTH CARE AND EMPLOYEE HEALTH CARE

### Current Program

The State currently sponsors health care plans covering approximately 350,000 individuals, including active employees, retirees, and dependents. The structure of the “core” health care plans (excluding ancillary coverages such as dental and vision plans) is set out below. All of these programs are offered both to active employees and retirees.

- Quality Health Care Plan (QCHP), administered by CIGNA. The QCHP is considered a preferred provider organization (PPO) and offers two tiers of benefits: higher coverage levels (generally 90% of “usual and customary,” or U&C, charges) for care by a provider in the CIGNA network and lower coverage levels (generally 70% of U&C charges) for care received outside the CIGNA network.
- A variety of HMO plans, offered in different regions of the State
- An Open Access plan (OAP), administered by HealthLink, a subsidiary of WellPoint. The OAP offers three tiers of benefits:
  - The highest coverage levels (generally 100% of U&C charges) for care received under a program that is structured much like a traditional HMO plan;
  - The middle tier (generally 90% of U&C charges) for care received from a provider in the WellPoint network; and
  - The lowest tier (generally 70% of U&C charges) for care received outside the WellPoint network.

Distribution of participation is as follows:

	Active	Retiree	Total
<b>QCHP</b>			
Member	26,981	54,405	81,386
Dependent	21,817	18,094	39,911
Total	48,798	72,499	121,297
<b>HMO</b>			
Member	69,789	20,525	90,314
Dependent	86,212	9,644	95,856
Total	156,001	30,169	186,170
<b>Open Access Plan</b>			
Member	14,911	3,254	18,165
Dependent	18,844	2,042	20,886
Total	33,755	5,296	39,051
<b>Total Program</b>			
Member	111,681	78,184	189,865
Dependent	126,873	29,780	156,653
Total	238,554	107,964	346,518

The prescription drug program for several of the HMOs, OAP and QCHP is administered by Medco. Other HMOs administer prescription drugs through the health plan.

The premiums for these programs differ based on:

- Whether the employee selects (1) the QCHP or (2) the OAP and the HMOs;
- The employee’s salary level (with five different tiers); and
- Coverage selected (with different tiers for employee only, one dependent, or two or more dependents).

Retiree premiums differ based on service: Retirees with 20 or more years of service pay no health care premiums, while retirees with less than 20 years of service pay a percentage of the cost.

The aggregate cost for the health care plans is approximately \$2 billion per year, with retirees (and their dependents) representing one-third of this annual cost and active employees and their dependents representing the remaining two-thirds. In aggregate, employee premiums represent approximately 20% of the cost of the active plans, and retiree premiums represent less than 10% of the cost of the retiree plans. Thus, the share of premiums borne by retirees is far lower than the share borne by active employees, and the greatest savings available to the State by changing premiums (as described below) will occur through changes to the retiree premium structure.

It should also be noted that the State’s costs are higher than those of virtually all other states. According to the National Conference of State Legislators, for 2006 Illinois had the 6<sup>th</sup> highest total average cost for state employee health premiums.

In assessing these programs, there is one more issue that should be addressed. Currently, aggregate costs per covered individual are relatively close for the OAP and the HMOs. (For FY2009, it is estimated that OAP costs will be \$4,517 per covered life and the HMOs average \$4,415 per covered life). By contrast, the cost for the QCHP is \$6,409 per covered life. This differential is addressed in the opportunities described below.

## **Savings and Efficiency Opportunities**

The current health care structure represents a number of opportunities for cost savings to the State and to fundamentally change the way health care is delivered and financed. In reviewing the items discussed below, it is important to note that many of the items overlap and cannot simply be added together. For example, modifying plan design will affect the savings opportunities generated by changing the employee and retiree premium structure. Also, some of the changes represent a shifting of costs from the State to employees and retirees (and do not reduce overall costs), while other items described below represent an opportunity to truly reduce the State’s health care expenditures.

Many of the opportunities identified below – reducing health costs by improving quality of care, improving the health of plan participants, and restructuring how health care is purchased to reward better outcomes – overlap with the opportunities described in the Medicaid section of this report.

Correspondingly, many of the initiatives described in this section and in the Medicaid sections can be combined. This movement – toward better coordination of State health care programs – is beginning to take effect in other states. For example, Kansas has established a single entity (the Kansas Health Policy Authority) to promote effective purchasing and administration across a number of the state’s health plans. Such an agency can be used to develop consistent quality standards, wellness initiatives, and claims analysis.

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## RESTRUCTURE PREMIUMS

The current premium structure presents an opportunity for improved cost management within a short-term timeframe. Overall, the State should pursue the following changes:

- **Require that employees pay premiums more consistent with overall market trends.** For example, employee premiums covering 15% of plan costs (for employee-only coverage) and 22% of plan costs for dependent/family coverage has been cited as a “typical” premium structure for large employers in the private sector and represents a good benchmark for evaluating the impact of premium changes. This is also consistent with data available from the National Conference of State Legislators, showing employees paying an average of 19% of the total health care premiums for family coverage.
- **Address the significant cost differential between the QCHP and the other plan offerings.** At this point, we do not yet have sufficient data to assess whether this cost differential is generated by (1) differences in the health status of covered individuals; (2) excess utilization in the QCHP (which represents the lowest level of “managed” care offered by the State; (3) excess provider charges; or (4) some combination of these (and other) factors.

In the short-term, the cost difference between the QCHP and the other plan offerings can be addressed through the premium structure. However we believe this represents a stopgap measure until more fundamental plan changes (discussed below) can be made.

The Governor’s budget proposal recommends that employees covered by QHCP pay the entire value of the differential between the other health care offerings and the QCHP. Accordingly, a single employee covered by an HMO or the OAP would pay a monthly premium of approximately \$60 (representing 15% of the average cost of the HMO and OAP offerings), while a participant electing single coverage under the QCHP would pay a monthly premium of approximately \$310 (reflecting the \$60 premium for other coverages plus the full incremental cost of the QCHP). The TAB believes that premium changes similar to those proposed in the Governor’s budget do indeed represent an appropriate savings opportunity, subject to some critical caveats. As noted earlier, it is not yet clear why QCHP costs are higher than those of the other health care plans. If the higher QHCP costs are the result of higher claims experience, then steep premium increases that drive those claims into the other health care plans will simply increase costs in those plans. Accordingly, any attempt to increase premiums in the QHCP will be effective only if the premiums are increased in a way that reflects the

risk/claims experience of each plan and that creates incentives for members to move toward more cost-efficient plans (as discussed below).

- **Require all retirees (and especially early retirees) to pay a greater share of total plan costs through increased premiums.** Many private sector employers are eliminating post-65 coverage (once Medicare and Medigap coverage are available) and requiring pre-65 retirees to pay much (or all) of the cost of coverage. Indeed, these trends are starting to permeate governmental plans; the State of Idaho recently eliminated retiree benefits for all retirees over age 65.

The Governor's budget proposal would continue offering State-subsidized health care to all retirees, but pre-65 retirees would be required to pay the full differential between the cost of their coverage and the subsidy provided by the State to Medicare-eligible retirees. This would represent a substantial premium increase for these individuals of between \$400-\$600/month. The TAB believes that premium changes for retirees similar to those proposed in the Governor's budget do indeed represent an appropriate savings opportunity.

When the State is revising premiums, it also has an opportunity to modify behaviors in ways that produce further benefits. For example, retirees with 20 years of service receive the same subsidy as retirees with 30 or 35 years of service. In effect, the State could use changes to the premium structure to encourage employees to lengthen their period of employment with the State, defer retirement, and otherwise shift the responsibility to paying for early retirement to plan participants. This approach is already in place in a number of states, including Nebraska, Ohio and Oregon.

Pricing / contribution changes consistent with these three objectives could yield savings to the State in excess of \$200 million per year. However, there are a number of alternative structures that could be considered. It is important to note that identifying the available cost savings is really only the first step in a design process that will enable the State to achieve these savings in a way that also realizes strategic objectives regarding the utilization and delivery of health care to employees, retirees and dependents.

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## MODIFY PLAN DESIGN

Premium increases represent the least nuanced approach to shifting costs; such increases affect all participants equally (irrespective of whether they are high or low users of health care). In addition to premium increases, however, the State can also modify plan design (such as changing deductible amounts, copayments, and out-of-pocket maximums). This reduces the overall coverage provided by—and the cost of—the plans and shifts these costs to those that use health care.

In reviewing the design of the State's health care programs, it would be feasible to modify a range of the plan provisions and reduce the cost to the State of its health plans by approximately 10%. These changes would not turn the State plans into a minimalist catastrophic program. Rather, they would retain

significant coverage levels and would be consistent with prevailing trends at most large private sector employers. Thus, by modifying deductible, out-of-pocket and coinsurance levels, we believe the State can reduce health care expenditures (excluding prescription drugs) by approximately \$165 million per year. The TAB is not recommending a specific plan design or premium structure. However, the materials we have reviewed cause us to believe that some combination of premium and plan design changes can generate savings to the State in excess of 15% of total health care expenditures (or \$300 million per year).

At the same time the State is revising plan structure, the State also has an opportunity to modify behaviors in ways that further benefit the State and covered individuals. For example, the new design could encourage use of primary care physicians; such increased use of primary physicians is generally seen as an important step in reducing long-term health care costs. Thus, in structuring plan design changes, the State should be mindful of changes that do more than simply shift costs to employees.

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## MAXIMIZE PURCHASING EFFICIENCIES

As described earlier, the State provides a range of programs, including QCHP, OAP and a range of HMOs. This basic structure creates some inherent limitations in the State's ability to maximize discount value and medical management opportunities:

- **Provider discounts:** Although we have not had an opportunity to analyze the specific discounts achieved by the State, given the current carrier relationships in place, we would anticipate that it would be possible for the State to realize savings of up to \$20 million per year by maximizing provider discounts.
- **Self-insurance and insured coverages:** Currently 200,000 individuals (of the total of 350,000 covered lives) under the State's health care program are insured through HMOs. This means that the State is paying risk charges and other HMO-related costs for a population that can be completely self-insured by the State. Even if the State wishes to continue using these HMO networks, it can do so on a self-insured basis. Although we have not had an opportunity to analyze the specific benefits of moving to self-insurance, we would anticipate that it would be possible for the State to realize annual savings of up to \$30 million by eliminating insured coverages.

We recognize that this differs from opportunities regarding increases in the use of capitated programs for the State's Medicaid population. However, in the case of the State's employee and retiree plans, we believe that control of participant and provider behaviors and improvement of quality, utilization of care and health outcomes can be managed by an insurance carrier without the need to pay the fees associated with capitation. On the other hand, the nature of the Medicaid program and population may render a capitated approach more effective for Medicaid.

- **Generic drugs and prescription drug management contracts:** Prescription drugs represent approximately 15-18% of health care costs. Under the current program, the State offers relatively mild financial incentives for participants to utilize generic drugs. As a result, the State has an opportunity to move to a design that provides much stronger incentives for participants to purchase generic drugs (such as a \$5 or \$10 copayment for generic drugs and a 20% coinsurance for branded drugs). Currently, generic use by participants in the State’s plans is approximately 62%. Increasing the generic utilization through plan design and other incentives represents the greatest single opportunity for savings in the prescription drug program. Additionally, market conditions currently enable large employers to obtain more favorable terms with pharmacy benefit managers (PBMs) by rebidding prescription drug management contracts. Between these two areas, we anticipate that the State could obtain savings of approximately 10% on its prescription drug costs (or approximately \$35 million per year).

In 2004 the State of Wisconsin initiated revisions to its employee prescription drug program that focused on issues similar to those described above. Specifically, the Wisconsin program focused on maximizing the state’s leverage as a purchaser, transparency in purchasing prescription drugs and elimination of rebates from drug manufacturers to the pharmacy benefit manager, and the increased use of generic drugs. These changes have reduced Wisconsin’s spending on prescription drugs by \$160-\$200 million over a four-year period (for a savings of approximately 20%). Such savings, if realized by Illinois, would save the State up to \$70 million per year.

Further savings may be realized by consolidation of the State’s prescription drug purchases with Medicaid and other populations served by the State. This opportunity is raised in the Medicaid section of this report, and will not be repeated here. Still, the State should integrate those Medicaid-related efforts with its purchases of prescription drugs under the employee and retiree programs.

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## **CHANGE THE MODEL FOR PURCHASING HEALTH CARE**

As noted earlier, the State’s underlying structure for purchasing health care is fragmented across a number of HMOs, QCHP, and OAP. Generally, cost savings and fee negotiations are primarily centered on discounts and network utilization. However, there is little focus on managing the health of participants or on the efficiency of the care provided. Focusing on these areas creates savings opportunities. Examples of these opportunities are as follows:

- **Carrier incentives for cost reduction, wellness, and prevention:** Under the State’s current approach to purchasing health care, none of the carriers utilized by the State is responsible for health outcomes or increased efficiency of health care expenditures. Current performance guarantees center around traditional measures, such as volume of services provided in-network. An alternative approach to purchasing health care that has emerged among large employers in the private sector is to hold carriers accountable for health outcomes and utilization levels – with the carriers responsible for reducing health care cost increases and managing the health status of members. This strategy does

present an opportunity for short- and medium-term cost reduction; however, we have not been able to quantify these savings.

- **Premiums linked to coverage levels:** As described earlier, the State offers programs with three different coverage levels (HMO benefits, the PPO levels provided under the QCHP and the three-tiered coverage options under the OAP). Also, as noted earlier, 200,000 individuals covered by State health care plans are insured through HMOs. As an alternative to this current structure, the State could self-insure the entire covered population and restructure the plan offerings to provide “high,” “medium” and “low” options. The “high” option could resemble the current OAP design, and the medium and low options could contain higher deductible, copayment and out of pocket features than the current plans. In effect, the State could give employees a choice between higher premiums for higher levels of coverage or lower premiums with more responsibility for costs. This approach could then be the basis for implementing the proposed strategy (described above) for increasing overall premiums.
- **Managed competition:** A number of other states have adopted different approaches to purchasing health care under a concept referred to as managed competition. Under this model, providers still compete for participants—but within defined parameters. Moreover, the parameters often focus on efficiency and quality, rather than on price or plan features. For example:
  - Under the **Wisconsin** model, all carriers offering health care coverage to state employees must offer the same plan design. However, the state subsidy (and, accordingly, the employee premium) is not based on plan cost. Rather Wisconsin purchases health care by focusing on quality and efficiency. Specifically, Wisconsin arrays all the plans in one of three tiers and the tiers generate different employee monthly premiums contributions. Placement of a plan into a tier is based on the risk-adjusted per-member-per-month (PMPM) cost of each plan; the use of risk-adjusted PMPM cost allows Wisconsin to measure the relative efficiency with which a plan is able to provide care. The theory underpinning this contribution model is that care should be directed to the most efficient plans, and not just the least expensive. Employees are encouraged to choose an efficient plan, even if that plan has higher overall costs due to the make-up of its risk pool. In this way, plans are not penalized for having a high-risk population as long as they manage care for that risk appropriately. Conversely, a plan is not unduly rewarded merely for having a better risk profile if they fail to manage that risk appropriately.

It is difficult to quantify the financial impact of the Wisconsin approach. However, in the five years preceding adoption of this program Wisconsin saw annual increases of 12.9% per year and in the five years since the adoption of this program Wisconsin’s annual rate of increase has been 7% per year. This 5.9% decline in the rate of annual “trend” increases is in contrast with decline in annual increases for other public plans (during this same period) of 2%. Thus, Wisconsin can be seen as saving approximately 4% per year in health care costs through this approach. If Illinois could achieve comparable results, the annual savings to the State would be approximately \$50-\$60 million per year.



**Minnesota** also uses a managed competition model – but focuses on providers, rather than insurers. The Minnesota program uses a risk-adjustment methodology to classify providers into three levels using risk-adjusted costs. To encourage employees to select risk-adjusted low-cost providers and to decrease unnecessary utilization, the state expanded requirements for co-pays, deductibles, and co-insurance. Further, employees who choose providers in risk-adjusted lower cost levels face lower out-of-pocket expenses than those who choose providers in higher levels. Finally, to allow employees the option of changing providers throughout the year, all health plans now have the same premiums for individual and family coverage respectively. Minnesota’s approach resulted in zero percent premium increase in 2006 and approximately \$20 million in savings that was returned to employees through a premium holiday.

Both Wisconsin and Minnesota have seen positive results from these designs, both in terms of managing overall health care costs and in steering participation towards more efficient providers. These savings are realized as overall health care costs rise at a rate lower than that under typical trend rates. Similar initiatives are occurring elsewhere. For example Massachusetts has also adopted a program for state employees that tiers providers based on quality measures, and Oregon is moving to evaluate carrier proposals based on quality.

- The State of Illinois currently purchases health care by either reimbursing for care provided (for QCHP, OAP and self-insured HMOs) or on a capitated basis (insured HMOs). There is a growing concern that both models are flawed in that they are based primarily on volume of services, rather than the value and effectiveness of services. A project supported by the Robert Wood Johnson Foundation, the PROMETHEUS project, is developing a payment method for certain conditions that hold providers accountable for potentially avoidable complications. This methodology is currently being piloted in Rockford, Illinois and by the State of Utah and holds promise as a new strategy for purchasing health care – one that presents an opportunity to save money by actually reducing health care costs.
- In addition to placing responsibility on carriers to manage outcomes and efficiencies, other mechanisms can place more responsibility on employees to manage their own health. Examples of such programs include smoker surcharges for employees who smoke and fail to take smoking cessation programs and surcharges on employees who fail to participate in a health risk appraisal to allow the identification of at-risk individuals. At least 10 states already impose smoker surcharges on employees. Other states have used financial motivations to increase use of health risk appraisals and encourage other healthy behaviors, including Alabama, Arkansas, Missouri and Ohio. Illinois currently maintains voluntary programs intended to address the issues of participant management of their health; however, it is unlikely that significant savings can be achieved unless more aggressive designs are put into place. At this time we are unable to develop cost savings projections for these approaches.

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## **MANAGE THE HEALTH OF THE COVERED POPULATION**

The State currently uses relatively low-key, voluntary efforts by participants to manage their health conditions. However, there are a range of more proactive initiatives available to the State to help participants actively manage their health. Although private sector employers have led the way on many of these efforts, in many ways the State (which maintains a long-term relationship with employees and retirees) is ideally suited to realize the gains available from such initiatives.

Substantial savings are available over the longer-term through better management of the health status of the covered population. Such management entails a number of different initiatives, including condition management, disease management programs, health coaching programs, health information programs and wellness programs (discussed in the previous section). The purpose of these programs is to help a plan sponsor avoid or delay future health care costs, particularly those precipitated by poor lifestyle choices and those associated with chronic conditions. In general, the impact on health care costs for these programs will emerge over a period of five to seven years, resulting in cost trend decrements during this entire period.

The general idea is to target specific plan members for appropriate interventions (using a third party to ensure confidentiality). These interventions can include a range of activities such as providing general health information, providing a member with specific education and coaching about ways to manage their clinical condition, completing regularly scheduled calls to discuss a member's status and needs, and specific calls initiated by identified gaps in evidence-based care. The goal of these programs is to improve health outcomes and decrease the cost of medical care for the selected populations of members.

Although the State currently offers some initiatives within the rubric of population health management and case management, these efforts are fragmented across the different vendors and rely on participant initiative and voluntary action. We believe that more aggressive, integrated efforts to provide population health management and case management initiatives have the opportunity to decrease health care costs by 1%-2% (or \$20-\$40 million) per year.

Enhanced use of health information technology offers the promise of long-term health care cost reductions. Indeed, the increased use of this technology is supported with funding available under the American Recovery and Reinvestment Act. The use of health information technology and ARRA funds are raised in the Medicaid section of this report and will not be repeated here. However, those efforts should be integrated with the State's cost savings strategy for the employee and retiree health plans.

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## **FUND RETIREE MEDICAL OBLIGATIONS**

The present value of the retiree medical obligations (for both existing retirees and current employees) is approximately \$24 billion. This amount represents an additional unfunded obligation of the State (in

addition to the \$65 billion of unfunded pension liabilities). Under Statement No. 45 issued by the Governmental Accounting Standards Board (GASB), governmental employers are now required to calculate and disclose their retiree medical obligations. This has prompted increased focus, by many governmental employers, on these plans.

In Illinois, there are currently no assets set aside to fund these liabilities. As a matter of prudent sponsorship, there is significant merit to prefunding these obligations. There is an additional reason to prefund these liabilities: under GASB rules, prefunding effectively reduces the amount of the underlying liability via an increase in the discount rate used to calculate the liability. In effect, if the State were to set aside some amount now (probably in the range of \$12 billion), the entire \$24 billion unfunded liability would be considered eliminated. Accordingly, prefunding of the retiree medical liabilities does represent a short-term cash cost to the State—but ultimately represents an opportunity to reduce the State’s unfunded liabilities.

### **Constraints and considerations**

There are constraints on the ability of the State to realize the savings opportunities described above. Most notably, most of the savings opportunities described herein are subject to collective bargaining and will require difficult negotiations with the unions representing the State’s employees.

The TAB is cognizant of the fact that these obstacles are significant. Nonetheless, the savings opportunities identified can have a significant impact on the State’s finances, and the State’s current financial circumstance necessitates pursuit of these opportunities.

## EDUCATION

Education is a major obligation of the State. The fact that it consumes almost a quarter of the State's budget testifies to the seriousness with which that obligation is taken. In the coming fiscal year the State will spend over \$10 billion on the education of more than 2.75 million students enrolled in its public elementary and secondary schools and institutions of higher education. As large as that expenditure is, it represents less than one-third of the total cost of educating these students.

Because their organizational structures, sizes and roles are so different, we examined primary and secondary education (K–12) separately from higher education.

### K-12 Education

In Illinois, 870 local school districts provide primary and secondary education to more than 2 million students. School districts range in size from fewer than 100 students to more than 400,000 in the case of the Chicago Public Schools District (District 299). Districts are overseen by the Illinois State Board of Education (ISBE), which sets educational policies and guidelines for public and private schools, as well as for vocational education. The State Board analyzes the aims, needs and requirements of education and recommends legislation to the General Assembly and Governor to benefit the students in its charge.

Funding of K–12 education comes from three sources: State appropriations, local funding (primarily through property taxes), and federal grants. Over the years the relative amounts contributed by these sources has stayed strikingly constant: 37.8%, 54.2% and 8.0%, respectively in FY89, compared with 34.6%, 56.5% and 8.8%, respectively, in FY08.

While K-12 enrollment has increased modestly in 20 years (by 18%, from 1,790,566 to 2,113,435 students), costs have grown remarkably (by 62%, from \$10.7 billion to \$17.33 billion, in constant 2000 dollars). Correspondingly the cost per pupil increased in current dollars by 162% (from \$4,438 to \$11,634) and in constant 2000 dollars by 37.9% (from \$5,974 to \$8,199).

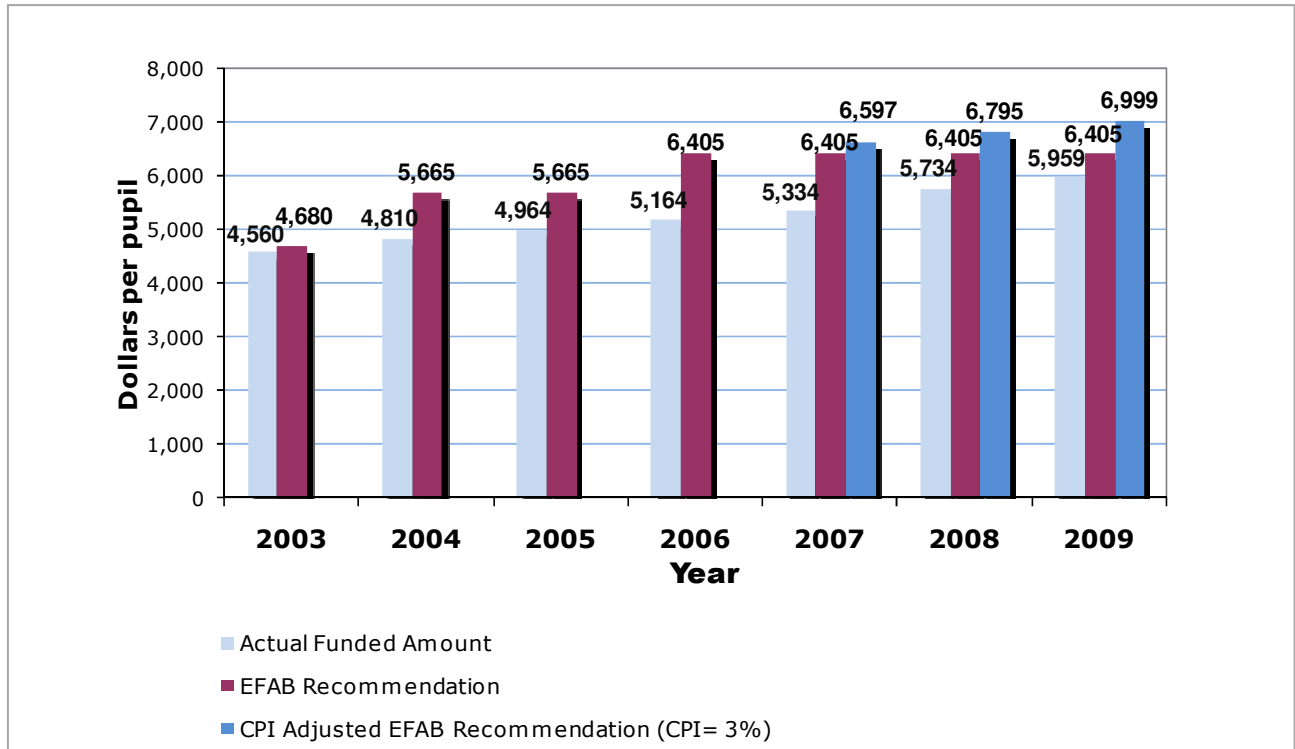
The goal of providing all students access to a sound education guides the amount of the State's appropriation for K-12 education. To that end the State determines what the cost per pupil would be to reach that goal, the so-called foundation level. In 1997, Educational Funding Advisory Board (EFAB) was created to set the foundation levels.

Once EFAB establishes the foundation level, the State then determines how much each school district should be able to collect, based on the assessed valuation of property within the district and an assumed, reasonable tax rate. If the available local resources derived from this "reasonable tax" per pupil are lower than the foundation level, the State is supposed to make up the difference according to a formula where the poorest districts (those with the fewest available local resources) get the most State money per pupil.

Until FY02 the foundation level grants were funded as defined in the 1997 statute. Then in 2003 the foundation level was set at \$4,680 per pupil, but only \$4,560 was funded (Exhibit 1). This trend of

underfunding has continued in every year since FY03. In FY06 the foundation level was determined to be \$6,405, but only \$5,164 was appropriated, a gap of approximately \$1,240 per pupil. The foundation level has not been adjusted since 2006, but assuming a consumer price index (CPI) of 3%, it should have been roughly \$7,000 in 2009, when the State funded just under \$6,000 (see Exhibit 1).

**Exhibit 1 -- EFAB Recommendations and Actual Funding Level**



In addition to leaving the foundation level unchanged for the past three years, modifications to the formula’s straightforward application have survived long after they were needed and pose a threat to the fairness of future funding.

### Higher Education

More than 820,000 students participate in Illinois’ higher education system through nine public universities, 48 community colleges and 1,223 private universities.<sup>17</sup> In 2007, 202,493 students enrolled in the State’s public universities and 347, 277 in community colleges, figures that reflect only modest increases over the prior decade. In 2007 the public universities conferred 47,422 bachelor, master, professional, and doctoral degrees, and the community colleges conferred 25,708 associate degrees and 25,614 certificates.

Each of the public universities and community colleges is accountable to its own board. Members of the public university boards are appointed by the Governor. Except for Chicago, where members of the

<sup>17</sup> The Illinois Report 2008 - Higher Education and Illinois’ Future, S. Ikenberry, D. Lazell, W. R. Kangas, Institute of Government & Public Policy, Univ. of Ill., Jan. 30, 2009.

community college board are appointed by the Mayor of Chicago, community college board members are elected locally. The Illinois Board of Higher Education (IBHE) coordinates the actions of university boards, determines higher education policy and allocates state appropriations among the higher education institutions. The Illinois Community College Board (ICCB) plays a similar coordinating role with the state community colleges.

Funding for the public universities comes from three principal sources: tuition, federal grants, and State appropriations. Total operating expenses for these universities for FY10 is expected to be \$6.1 billion, including \$1.4 billion from the State. The remaining costs are paid for by grants and tuition, which, in turn, is supported by State and federal student aid.

Funding for community colleges comes from local tax levies, tuition, State appropriations (primarily through the Illinois Community College Board, ICCB), and the federal government. In FY07 total operating expenses of the community colleges were \$2.245 billion, to which the State contributed \$330 million through the ICCB and \$121 million from other State sources (excluding student assistance). ICCB grants to community colleges are based upon the colleges' relative credit hours of education provided. In general State support for higher education has increased modestly in current dollars and gone down materially in constant dollars over the past 10 years. Thus, both the public universities and community colleges have had to increase tuition over the recent period to keep pace with rising costs. At the same time, community colleges have increased reliance on local taxes.

The remaining \$1.16 billion of the State's higher education budget includes appropriations for student assistance, the Illinois Math & Science Academy and the State University Retirement System. Of these, the last is by far the largest and is discussed in the Pensions section of this report.

## **The Context for the TAB's Analysis**

As we began to examine education spending, we discovered several themes, which ultimately shaped the opportunities we cite in this report. We believe that to achieve the best opportunities to increase efficiency and reduce costs in State-funded education – while not threatening educational outcomes – the State should:

- Create administrative and funding efficiencies
- Re-align K-12 spending formulas with their original intent
- Reduce costs through a more effective execution of sunset provisions in K-12 education
- Introduce a common methodology to distribute funds to institutions of higher education

Of necessity, our examination could reach only the broadest issues given the urgency of the report. Thus, we set our priorities by the potential dollar amount involved. Smaller dollar items that arose in the course of the examination, that nonetheless show promise for cost savings, are mentioned but in less detail.

Given structural misalignments in the State's major funding formulas and practices, we conclude that a holistic review and restructuring of Illinois' education finance, both K-12 and higher education, is critical.

## CONSOLIDATE K-12 SCHOOL DISTRICTS

Illinois supports 870 separate school districts. Consolidating small districts and those with multiple elementary feeder districts could lower administrative costs, reduce the level of bureaucracy, and in some cases improve curricular alignment among the elementary, middle, and high schools.

We estimate that taxpayers could save, conservatively, \$60-\$120 million by such consolidations. Importantly, our estimates are based on administrative consolidations only, not school consolidations. We did not consider merging schools.

### Background

Compared to other states in the nation, Illinois has the third highest number of school districts (Table 1). On average, school districts in Illinois serve only 2,407 students, the second lowest of the 14 states with school populations over 1 million. Florida, by comparison, averages 37,709 students per district, while North Carolina averages more than 11,000 students per district. As shown in Table 2, Illinois supports 129 districts with fewer than 300 students, 163 districts with 300-599 students, and 156 districts with 600-999 students.

**Table 1 –  
2006-2007 Enrollment Data  
from NCES**

Rank by No. of Districts	State or Jurisdiction	Total No. of districts	Total No. of students	Average Students per District
	<b>USA</b>	<b>13,862</b>	<b>48,105,937</b>	3,470
1	Texas	1,033	4,513,835	4,370
2	California	989	6,211,439	6,281
<b>3</b>	<b>Illinois*</b>	<b>873</b>	<b>2,100,994</b>	<b>2,407</b>
4	New York	697	2,757,907	3,957
5	Ohio	614	1,758,645	2,864

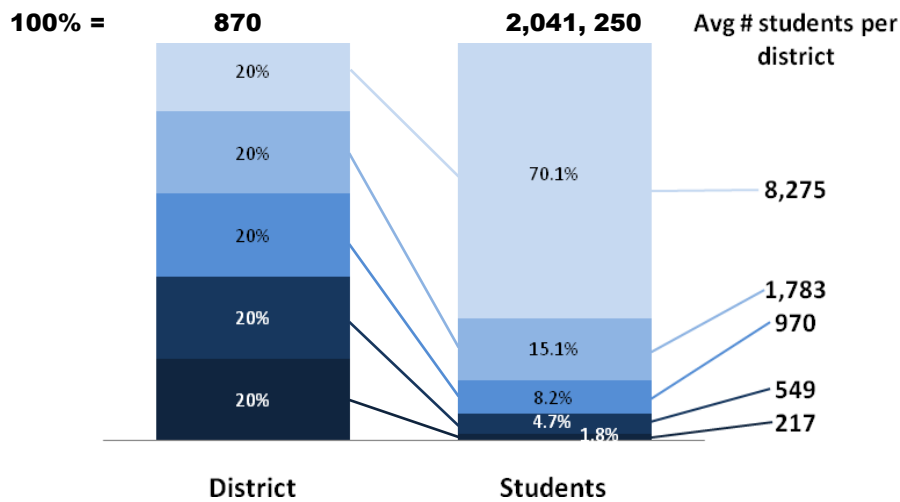
\* Illinois ranks 34th in terms of average number of students per district

**Table 2 --  
Number of Districts by  
Enrollment Size**

District Enrollment	2007-2008
25,000 or more	5
10,000 to 24,999	18
5,000 to 9,999	47
2,500 to 4,999	112
1,000 to 2,499	239
600 to 999	156
300 to 599	163
Fewer than 300	129

Of the 870 Illinois districts, roughly 200 are single-school districts. Many regions have multiple school districts, and in many cases, several separate elementary districts feed into a single high school district. As can be seen in Exhibit 2, 60% of the districts in Illinois teach only 14.7% of the total student enrollment.

**Exhibit 2**



All told, this fragmentation is highly inefficient financially and does not necessarily contribute to better educational outcomes.

**Benefits of District Consolidation**

District consolidation would at a minimum reduce the number of duplicative administrative staffs (e.g., superintendents, secretaries, HR, business management staff, technology staff) that exist in all districts, regardless of size or structure.

If half of all districts with fewer than 1,000 students were eliminated, and half of all single elementary school feeder districts were consolidated into common feeder systems, the State could eliminate approximately 400 districts. Assuming, further, that two to four administrative staff positions could be eliminated in each consolidation, taxpayers could save, conservatively, \$60-\$120 million per year.

The rate at which these savings could be captured would be determined by the speed of decision-making and the decisions on severance, if offered, to departing administrative staff. Equally important is for consolidated districts to manage costs stringently, so benefits gained through consolidation are not quickly dissipated over time. Also, when districts with differing pay scales are consolidated, they must resist the temptation to negotiate to the higher pay scale. Rather, a pay scale should be mandated that makes total pay constant, across the entire, new district.

**Action Steps**

While attempts have been made to consolidate districts, success has been mixed at best. From 1986 to 2009, \$175 million in incentives was paid by the State for district annexations, school consolidations, district consolidations, and other reorganizations, but only 125 districts have been eliminated in the past 23 years. Most recently in 2006, Public Act 94-1019 consolidated several Articles of the School Code to provide more flexibility and efficiency in the consolidation process. However, over the past 10 years, the number of districts has fallen by only 28, from 898 to 870. Significant district consolidation will require new legislation that mandates action if Illinois is to generate the necessary budgetary savings.



Legislation creating a District Consolidation Commission should be introduced immediately. The Commission should set consolidation and reorganization guidelines, select candidate districts and establish a process for implementation. It should further support the creation of legislation that mandates the consolidation recommendations it makes. The Commission should consider all cost, tax, and legal considerations facing consolidating districts.

Savings from school consolidations are likely to begin no earlier than two to three years from now, after the Commission has fully completed its consolidation report and consolidations are rolled out. Full savings will only be realized once all consolidations are completed and transition payments are finalized.

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## **CAP THE PTELL ADJUSTMENT AND AMEND THE GSA FORMULA**

Illinois' General State Aid (GSA) for primary and secondary education was originally intended to help equalize school spending across all districts. The GSA formula was structured to supplement each district's available local property tax resources with additional State funds, depending on need, with the intent of enabling all districts to reach a targeted foundation level of educational spending per student, so all students would have access to a sound education. In 2008/09 the foundation level was \$5,959 per student.

The GSA formula assumes that each district has local available resources for school funding based on a fixed percentage of that district's local property tax base. The State then aims to provide funding equal to the foundation level, less the assumed local available resources. For those property-poor districts unable to fully reach the foundation level with local resources, the GSA provides the necessary differential, or "equalization." For those property-rich districts capable of reaching and exceeding the foundation level, the GSA makes correspondingly smaller per student payments.

Over time, the GSA has been altered to include three components: Equalization (the portion intended to move all districts to the foundation level); the Poverty Grant; and the PTELL adjustment.

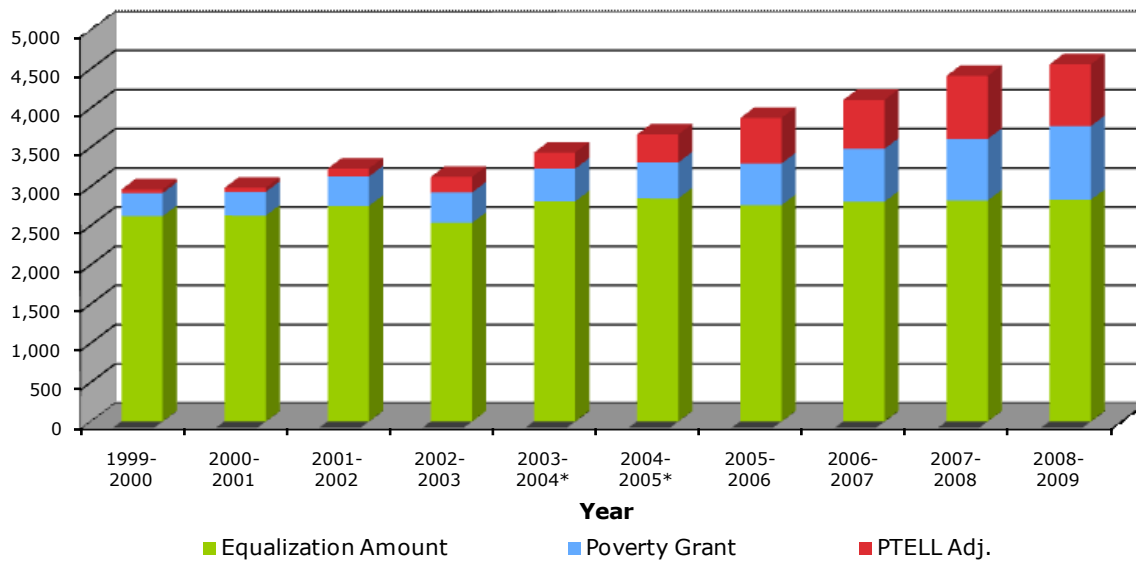
In the late 1990s, caps on property tax levies (PTELL) in selected districts limited their ability to increase local tax sources for school funding without referendum approval. In 2000, to compensate those districts affected by PTELL caps, GSA funds were redirected from their traditional purpose of equalization and toward the districts needing PTELL relief. Since then, GSA funds have been used first to fund PTELL adjustments and then, what is left, to fund equalization. As PTELL adjustments have grown, less remains every year for equalization. What began as a \$46 million PTELL adjustment in 2000 has grown to \$789 million in 2009. The PTELL adjustment is now a significant fraction of the GSA total.

On top of the PTELL adjustment, GSA funds are also earmarked for Poverty Grants, an expenditure that has also grown significantly in the past few years. The Poverty Grant is distributed to districts based on their proportion of low-income students. In 2009, Poverty Grants will total \$941 million.

Over the past nine years, Poverty Grant and PTELL payments have grown at double digit rates (PTELL at 37% per annum), leaving concomitantly less GSA funding for equalization. Thus, only 62% or \$2.9 billion out of \$4.6 billion in total GSA spending is now going to equalization, its original intent (see Exhibit 3). While PTELL, Poverty Grants, and equalization payments are all arguably worthy and important goals, they are now working at cross-purposes, one against the other.

Without PTELL adjustments in 2009, the State could have increased its contribution to the foundation level in 2009 by over \$700, from \$5,959 to \$6,678 per pupil, coming close to the recommended level of \$7,000 per student.

**Exhibit 3 -- General State Aid Components (Dollars per pupil)**



PTELL and Poverty Grants are now, in effect, competing with the goal of equalization.

We believe that the State should cap the PTELL adjustment and immediately begin a review of all education formulas, with the goal of realigning actual distributions with their original intent.

### **Impediments to implementation**

As shown in Table 3 below, the impact of PTELL varies greatly from one region of the state to another. From a financial standpoint, PTELL has had a significant impact on the distribution of funds across Illinois. Any piecemeal change to PTELL without a holistic approach to restructuring the school funding formula, would create immediate winners and losers and impede a proper resolution.

**Table 3 -- 2008-2009 Financial Impact of PTELL on key Regions (amounts in millions)**

Region	Total Gross GSA*	PTELL Adj. Received	Total GSA if PTELL Adjustment Eliminated**	Net Impact of Eliminating PTELL Adjustment
Chicago	1,140	505	658	(482)
Other Cook	642	126	624	(18)
Collar	724	131	819	95
Downstate	2,055	27	2,484	429
Adj.	21		-3	(24)
	<b>4,582</b>	<b>789</b>	<b>4,582</b>	<b>0</b>

\* Foundation Level at \$5,959

\*\* Foundation Level at \$6,678

For that reason, we encourage the State to cap – not eliminate – the PTELL Adjustment, and examine the entire school funding formulas, so funds can be directed towards their intended uses.

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## SUNSET HOLD HARMLESS PROVISIONS

Hold Harmless provisions help districts transition through the negative impacts of restructured funding formulas. Though Hold Harmless provisions are usually mandated to expire at a specified date, several provisions in school finance have failed to end as prescribed. As a result, the intent of the original funding formula changes have not been realized, and the funds being used for Hold Harmless provisions continue to drain state coffers.

Allowing current Hold Harmless provisions to expire would save approximately \$90 million annually. These funds could be reinvested in other education programs or returned to the taxpayers.

### Background

School funding formulas are often restructured for reasons of efficiency or shifts in population. For districts negatively affected by changes in a formula, a transition period to make necessary adjustments is usually allowed. During this “Hold Harmless” period, the State continues to provide funding under the old formula. A “sunset provision,” defining the date on which the transition period ends, typically accompanies the Hold Harmless provision. If a Hold Harmless provision never sunsets, however, the State continues to pay for the provision, plus the commitments of the new formula.

Currently, four Hold Harmless provisions fall into this category: Supplemental General State Aid (Poverty Grant) Hold Harmless; Transitional Assistance; and Special Education – Funding for Children Requiring Special Education Services Hold Harmless; and General State Aid Hold Harmless. Of these, the first three have continued past the allowed transition period, yet continue to be appropriated each year via budget implementation bills. The fourth, GSA Hold Harmless, does not contain a sunset provision.

## Benefits of Phasing out the Hold Harmless Provisions

As shown in Table 4, the State could save nearly \$90 million per year by sunseting Hold Harmless provisions, funds that could be reinvested in other education programs or returned to the taxpayers.

**Table 4 -- Summary of the Costs of the Four "Hold Harmless" Provisions in ISBE Programs**

Hold Harmless Type	Preliminary	
	FY2009	FY2010
General State Aid HH*	26,449,225	38,647,203
Poverty HH	8,447,148	6,754,393
Transitional Assistance**	36,763,600	TBD
Special Ed Extraordinary HH***	17,553,676	TBD

\* FY 09 amount is actual claim. Appropriation was \$26,106,400 so the payments were prorated.

FY 10 amount assumes a \$130 increase to the foundation level.

\*\* FY 09 Transitional Assistance is the appropriated amount. Actual claims have not been calculated.

\*\*\* Special Education Extraordinary Hold Harmless is dependent upon the foundation level for FY10.

The State should perform an immediate review of the programs scheduled to sunset, re-establish firm sunset dates, and allow phase-outs to occur. Likely, this would take two to three years, and could be done in conjunction with the establishment of a new GSA formula, as suggested above.

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## BLOCK GRANT THE SPECIAL EDUCATION CATEGORICALS AND MOVE TO A COMMON FUNDING FORMULA

By converting all Special Education categorical grants into a single block grant and using a common formula for all school districts, Illinois has an opportunity to increase both the effectiveness of spending on special education and, potentially, to reduce the overall cost, which in 2009 exceeded \$1.5 billion. Assuming the conversion to block grants generates from 1-5% in administrative efficiencies, the State could save \$15-\$75 million annually.

### Block Grants

Special Education spending, appropriated at \$1.525 billion for FY2010, represents one of the State's fastest growing education expenditures. With the exception of District 299 (Chicago), Illinois has six special education programs (Table 5) that are distributed to school districts as categorical mandates.<sup>18</sup> Each is earmarked for a particular population or purpose and subject to audit. Each district must file separate claims for reimbursement to access each of the categorical funds.

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<sup>18</sup> Since 1995 the Chicago Public Schools has received its special education funding in one block grant, allowing it to use funds more effectively, with a broader ability to prioritize spending.

**Table 5 -- Special Education Mandated Categoricals (in millions of \$)**

Program Name	FY01	FY09	FY10 Request	'01 vs '10 Pct Change	'01 vs '10 Pct CAGR	'09 vs '10 Pct Change
Personnel	300	426	460	53%	5%	8%
Transportation	206	383	430	109%	9%	12%
Funding for Children	228	331	334	46%	4%	1%
Private Tuition	48	152	181	277%	16%	19%
Orphanage	127	102	120	-6%	-1%	18%
Summer School	7	11	12	71%	6%	9%
<b>Totals</b>	<b>916</b>	<b>1,405</b>	<b>1,537</b>	<b>68%</b>	<b>6%</b>	<b>9%</b>

An opportunity exists to convert these categorical funds into one block grant. By eliminating significant reporting, tracking, and reimbursement processes throughout the entire school system, administrative savings could be realized. In addition, flexibility to prioritize spending where it is most effective for each child could lead to better outcomes.

### **Funding formula**

For District 299/Chicago, spending for each category of special education is based on a static share of the State's total special education expenditure by category. Those percentages (weighted average approximately 28%) are based on the proportions of the State's various special education categories in District 299 in 1995.<sup>19</sup> The rest of the state, on the other hand, is budgeted based on the number of students who are identified as needing special education services and associated costs. Once the non-District 299 budget is determined, that number is grossed up to fund the percentage that goes to District 299, and to generate the overall State budget.

Due to changes in demographics, this process leads to widely different special education spending, on a per student basis, between Chicago and the remainder of the State. According to the Senate Task Force currently reviewing Special Education Spending (HJR 24), if *actual* District 299 populations were funded based on the other districts' funding-per-student methodology, total Special Education spending would fall by \$241 million in FY2010. On the contrary, if District 299's funding-per-student amount were used to fund the other districts' actual populations, the total cost would rise by approximately \$1.3 billion (see Table 6). We encourage the State to develop a new approach to determining the level of special education spending, based on the number of students needing service and a reasonable cost per student.

<sup>19</sup> In August 2004, the distribution methodology for Special Education Funding for Children Requiring Special Education Services was changed. It is no longer based on 1995 percentages and is now distributed statewide based on ADA and Poverty counts.

**Table 6 -- Special Education Spending by District 299 and the Remainder of the State\***

	Spending per Student		Population Count		Actual Expenditures		Pro-Forma Expenditures	
	District 299	Non-District 299	District 299	Non-District 299	District 299	Non-District 299	District 299**	Non-District 299***
Private Facilities	62,928	9,637	1,166	8,397	73,374,048	80,921,889	11,236,742	528,406,416
Personnel	9,596	4,825	8,481	74,130	81,383,676	357,677,250	40,920,825	711,351,480
Transportation	10,535	3,518	11,170	78,082	117,675,950	274,692,476	39,296,060	822,593,870
Summer School	616	88	9,714	55,385	5,983,824	4,873,880	854,832	34,117,160
<b>Totals</b>			<b>30,531</b>	<b>215,994</b>	<b>278,417,498</b>	<b>718,165,495</b>	<b>92,308,459</b>	<b>2,096,468,926</b>

\* Amounts are approximate, as population counts are from 2007-2008, while expenditures are from 2009. Special Ed Funding for Children excluded per footnote

\*\* Assumes that District 299 spends the Non-299 District amount per student

\*\*\* Assumes that Non-District 299 spends the District 299 amount per student

Before moving to block granting, the State should assess what level of reporting will be sufficient to ensure funds are well spent and students are well served by the resulting programs. Because changes to the current formula will create winners and losers, a transition period will, in all likelihood, be necessary before fully implementing a common funding formula.

The State should review the opportunity to immediately block grant the special education grants and to create one combined State-wide block. An analysis of the efficiencies gained throughout the system should then be determined in order to allow for a reduction in the block grant total. If the block grant can be legislated within the next year, savings could occur within the 2010/2011 fiscal year.

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## CONSOLIDATE K-12 INTERMEDIATE SERVICE AGENCIES

Illinois maintains five types of Intermediate Service Agencies for education: Regional Offices of Education (ROE); Education for Employment Systems (EFE); Learning Technology Centers (LTC); Professional Development Centers (PDC); and Intermediate Service Centers (ISC).

The Regional Offices of Education (ROE) are remnants of the early County Superintendent of Schools, once maintained by every county. These ROEs support School Improvement Plans and monitor compliance with administrative rules. Over the last 60 years consolidations and legislation have reduced the number of ROEs from 102 to 45. Legislation existed that would have further reduced the number of ROEs to 35 over a few years, but it was not enacted.

Education for Employment Systems (EFEs), created in 1985, are charged with supporting and developing school to work programs. Today, the State supports 55 EFES. They work mostly with high school vocational programs to develop vocational plans, and with middle schools to provide career awareness. EFE boundaries do not align with those of the ROEs.

Six Learning Technology Centers (LTCs) were created as Technology Hubs in 1996 and later were divided into 15 centers serving the same schools. Their formation coincided with the Internet boom, a

period in which Illinois provided substantial funding to schools for Internet hookups. Since then, State funds for internet support have been moved to Central Management Services, while State grants for classroom technology no longer exist. The LTCs, however, continue to operate, providing support for Technology Plans in districts.

These three intermediate service agencies overlap with one another in the services provided to the school system. The agencies provide support to administrators and program directors in K-12 schools in the form of technical assistance, professional development, compliance monitoring, and flow of State and federal funds to the schools. In many cases, these services are duplicative of what local districts are already providing. Moreover, for an intermediate service agency to provide its services, each individual agency must maintain appropriate operational and support functions, including directors and staff, bookkeepers, clerical staff, as well as office space and equipment. A separate budget must be created for each one, while some also negotiate separate employee health contracts.

### **Benefits of Consolidation and Streamlining**

The independent evolution of these agencies has created a duplication and overlap of services throughout Illinois. The State has an opportunity to consolidate the Intermediate Service Agencies under the ROEs, eliminating duplicative administrative and service functions. Taking into account only the administrative savings (75-150 FTE) associated with eliminating duplicative administrative functions, we estimate that the State could save approximately \$5-\$10 million per year. If consolidation resulted in elimination of duplicative services, the savings could be substantially higher.

The State should align boundaries for each of these Intermediate Agencies, and then mandate consolidation of EFEs and LTCs under ROEs. Ultimately, the State might also consider consolidating ROEs.

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## **OTHER ISSUES FOR CONSIDERATION**

### **Higher Education Spending**

The State plans to spend \$2.4 billion on higher education in FY10. Nevertheless, the TAB did not find opportunities for significant cost savings without adversely affecting the delivery of services. Indeed, the TAB observed that, in 2007 dollars, State general revenue funds for our nine public universities actually declined by 17.9% from FY98 to FY08 while spending for K-12 education increased 46.8%. Operating costs of the public universities and community colleges have increased steadily over the same period, and the difference has been made up by significant increases in tuition and, in the case of the community colleges, increases in property taxes. The State's need-based aid, while generous by national standards, has failed to keep up with rising costs.<sup>20</sup> Thus, our institutions of higher education are less affordable for many now than they were a decade ago.

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<sup>20</sup> The Illinois Report 2008 - Higher Education and Illinois' Future, S. Ikenberry, D. Lazell, W. R. Kangas, Institute of Government & Public Policy, Univ. of Ill., Jan. 30, 2009.

Although the Board does not suggest reductions in the State’s funding of higher education, we urge the IBHE and the ICCB to work closely with the boards of the universities and community colleges to improve the efficiencies of their operations. For example, improving articulation agreements and curricular alignment between community colleges and universities would speed students’ attainment of educational goals while reducing the systems’ expenditures. Universities and community colleges should combine programs or courses offered at two or more institutions where enrollment and practical considerations suggest one institution would suffice. If sharing services or facilities reduces costs, institutions should seek them out aggressively, free of political or other considerations.

While overall spending might not decline, we believe revisions in the way funds are distributed to higher educational institutions could improve efficiency and accountability significantly. Today, public universities and community colleges are allocated funding based on very different criteria. Community colleges receive funding based on credit hours provided, and are measured against the average cost of delivering that credit hour. Public universities, on the other hand, receive funding that has little, if any, basis on enrollment or any other metric. Rather, they each receive similar increases or decreases annually, dependent on the overall appropriation. We encourage rethinking the approach to funding higher education, with the goal of tying funds more consistently to enrollment and other rational drivers.

### **Mandate Reductions and Elimination**

The TAB has learned that one of the largest contributors to inefficiency is the overuse of unfunded and partially funded mandates from the State. While many of those mandates may serve useful purposes, today’s budget and economic realities do not allow for the education system to be continuously burdened by a growth in mandates. The TAB believes that all current and future mandates contain a sunset provision. This would ensure that any mandates that move away from their original purpose or significance be automatically retired. Other mandates that need to be preserved would then have to be reinstated by the legislature.



## PUBLIC SAFETY

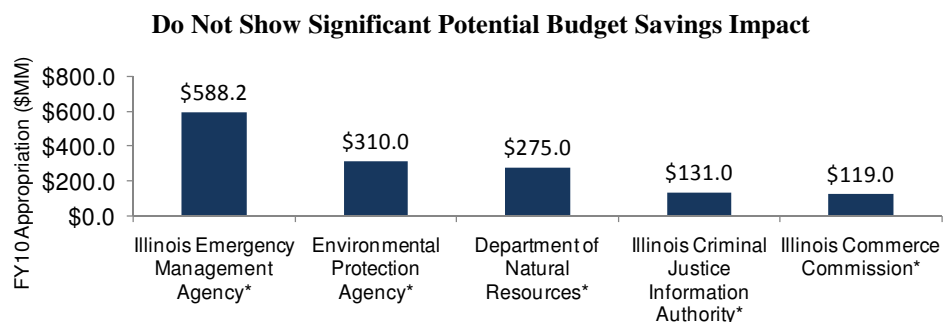
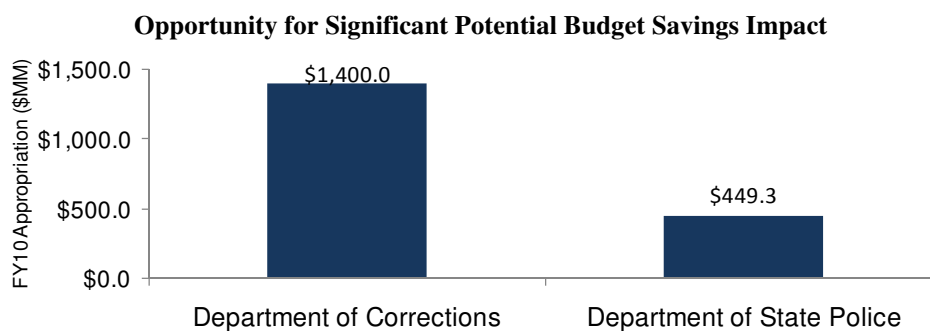
The TAB examined the areas of Public Safety and Business and Environmental Regulations to find significant operational savings that could be realized the coming five year period and to do so without impacting current levels of taxpayer safety and services.

To help fulfill this vision and mandate, we quickly and systematically narrowed our focus to the agencies that met two main criteria:

1. Operating budgets large enough to be able to realize significant operational savings without dramatically impacting the agency. (This threshold was defined as an agency with an annual budget of at least \$100 million.)
2. A majority of their operating budget received from the State’s General Fund.

When we looked across the nine agencies within Public Safety and the nine agencies within Business and Environmental Regulations, we found only seven agencies that met our first requirement, with only two of those meeting the second criteria – as it turned out, both were in the area of public safety: the Department of Corrections and the Department of State Police.

### The Potential Opportunity for Significant Budget Savings Impacts Can Only Be Realized in The Department of Corrections and Illinois Department of State Police



\* These agencies receive little or no General Budget Funds and are mainly funded through Federal Funds and Program Fees.

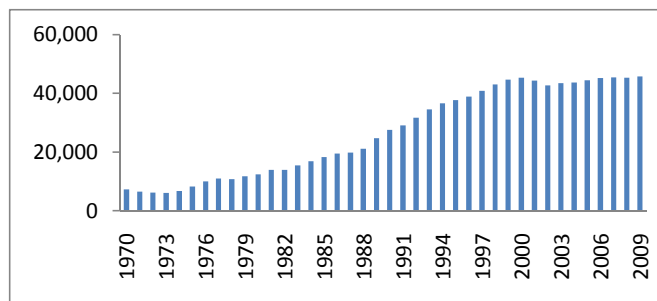
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## REDUCE LOW-RISK INMATE POPULATIONS

**To dramatically reduce the prison population by reviewing the prisoners' records to identify inmates that may no longer represent a significant risk to society, and to allow those individuals to re-enter society under state supervision.**

The prison population in Illinois has experienced a dramatic increase over the past generation. In 1970, the State's prisons held 7,326 inmates. By 2000, the prison population had grown to over 45,000 inmates, an increase of more than 600% (Figure 1).<sup>21</sup> During this same period, the State's total general population grew only 11%. The increase in prisoner population was not the result of a dramatic increase in crime in Illinois, or a demographic shift in the population. Rather, as with many other states, this increase was driven principally by changes that encouraged longer sentences, and enhanced efforts to incarcerate criminals for minor offenses.

**Figure 1: Illinois Prison Population (1970-2009)**



It is worth considering how the State's prison population got so large in the first place. While a variety of factors have contributed to this trend, three in particular are notable. First, starting in 1974, Illinois courts began sentencing Murder, Class X, and Class 1 offenders to longer prison sentences as part of a "get tough on crime" initiative. Second, in 1978 Illinois instituted a policy of determinate sentencing, whereby each crime was assigned a particular range of suitable punishments. This was meant to standardize prison sentences across the State and to present a deterrent for potential criminals. The result, however, dramatically drove up the prison population as all criminals began receiving longer sentences with fewer opportunities for parole. Third, in 1983 the State discontinued a policy of "forced release" which had been instituted in 1979 to control the prison population. Under forced release, a significant number of offenders were released from prison prior to serving their full sentences, a practice which had effectively slowed the growth of the prison population. In the 10 years after the policy was repealed, the prison population more than doubled.

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<sup>21</sup> Illinois Department of Corrections, 2002 Statistical Presentation, online at <[http://www.idoc.state.il.us/subsections/reports/statistical\\_presentation\\_2002/part1.shtml](http://www.idoc.state.il.us/subsections/reports/statistical_presentation_2002/part1.shtml)>

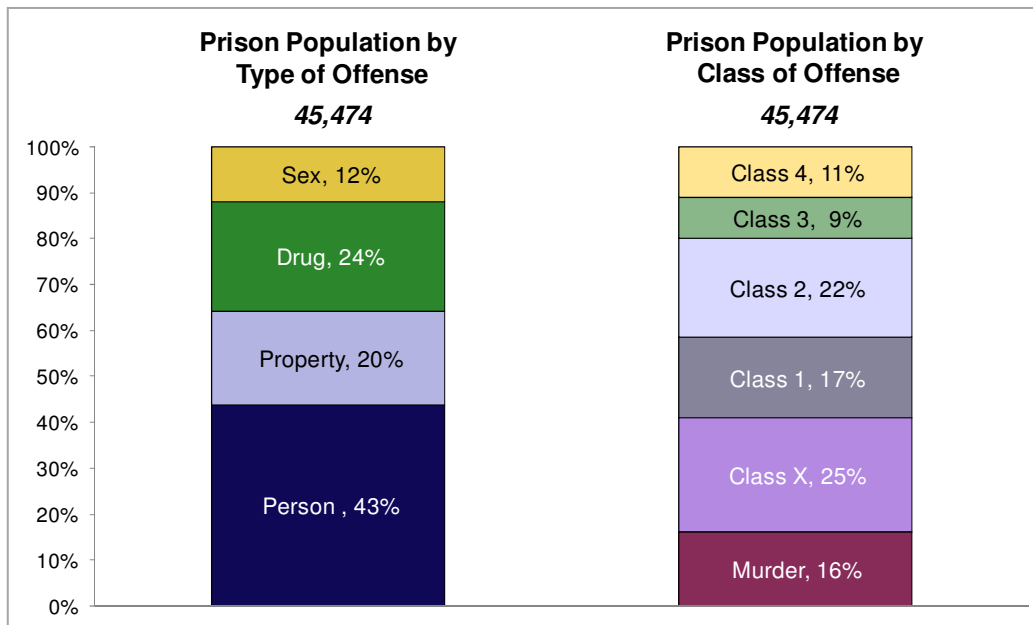
The increased prison population presents myriad problems, including the costs associated with housing, clothing, feeding, caring for, and overseeing this large and growing population. The DOC budget is nearly \$1.4 billion, or 6% of the State’s total budget. These costs might be justified were they yielding a reduction in violent crimes. However, between 1970 and 2000, Illinois’ crime rate increased from 468 to 657 incidents per 100,000 residents.<sup>22</sup> While it is impossible to say what crime rates might have been without increased incarceration efforts, we believe it is worth examining further whether the State could reduce its prison population without compromising the safety of Illinois residents. We believe that a variety of measures could be undertaken to effectively reduce Illinois’ prison population without increasing crime rates.

**Action Steps: Short-Term**

Over the short-term, we believe the State should initiate a review of individual prisoners’ cases of for parole and early-release consideration. This effort should conduct risk assessments to determine which prisoners do not pose a threat to society, for example those prisoners who are elderly, infirm, or those who have been incarcerated for non-violent drug or property-related crimes. This group is of substantial size: there are 4,400 inmates who are 50 or older, nearly 10% of all inmates in Illinois. Inmates serving time for drug or property-related crimes represent nearly 44% of all prisoners.<sup>23</sup>

Another way to look at this data is by class of offense, which divides the prison population according to the severity of crimes committed. As of December 31, 2008 nearly 20% of the prisoners in Illinois were incarcerated for Class 3 or Class 4 offenses (Figure 2). This represents the least severe type of offense, and yet it is estimated that this group costs the state over \$250 million annually.

**Figure 2: Prison Population Breakdown**



<sup>22</sup> FBI, Uniform Crime Rates, and The Disaster Center, <http://www.disastercenter.com/crime/ilcrime.htm>

<sup>23</sup> Illinois Department of Corrections, Internal Data

Unfortunately, recidivism rates among drug and property offenders have not historically been substantively lower than the rates for other types of offenders. A 1998 DOC study showed that 41.9% and 50.6% of drug and property offenders, respectively, had returned to prison within three years of their release,<sup>24</sup> similar to the average 44.1% for all prisoners released in 1998. However, with appropriate treatment programs and an effective parole program it may be possible to lower this rate for drug and property criminals. The State is already spending a significant amount of money treating substance abusers in prison, yet does very little monitoring of program effectiveness. We believe the State should evaluate which programs are working and which are not, and based on this assessment, invest in the highest impact programs. The State may actually experience greater success treating substance abusers outside of prison.

Enhanced measures to reduce recidivism should focus on a mixture of sentencing practices, monitoring and tracking techniques, and educational and rehabilitation opportunities. In particular, the State should consider redefining Judicial Sentencing Guidelines. Currently, judges receive social data on convicted offenders prior to sentencing, but they do not receive any data regarding the costs of incarceration. The TAB believes the costs should be considered as part of the sentencing process so judges may determine whether incarceration is truly the most effective and cost-efficient manner to both punish and rehabilitate an offender. Judges should have greater discretion in deciding if an offender may be better served by home confinement, community service, work-release programs, fines, or other punitive measures that do not involve incarceration. Such discretion would allow judges to balance more equitably the interests of the offender, the State, and the taxpayers of Illinois.

In response to these changes, the State could increase the number of parole officers who provide guidance and support for the increased number of parolees. The parole program could be further aided by electronic monitoring of prisoners. Advances in technology over the past several decades offers the State heightened ability to track the movements and activity of ex-offenders at minimal cost. These punitive measures could help offenders stay on the right side of the law by making them more cognizant of the risks associated with breaking the law and making them more aware of the likelihood that they will be caught for any future indiscretions. To support recently-released prisoners, the State should continue to partner with non-profit organizations that offer educational, job-training, and employment opportunities to offenders. By expanding the reach and scope of these programs, Illinois could become a national leader in controlling prison populations and reducing recidivism rates.

In addition to the potential societal benefits from reducing the prison population, there are also considerable financial benefits. The average annual cost to incarcerate an inmate in Illinois is approximately \$30,200 per year, compared with \$4,000 per parolee per year. For every inmate that Illinois releases, there is a potential net savings of roughly \$26,000. Assuming half of the nearly 5,000 inmates incarcerated for Class 4 offenses were released under the prisoner review program, the State could realize savings of nearly \$65 million. Furthermore, these individuals could re-enter society as productive, tax-paying individuals giving a further boost to State finances. Given the economic benefits coupled with the humanitarian and social benefits to be gained from this measure, we encourage the State to examine ways to reduce the number of low-risk prisoners.

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<sup>24</sup> Illinois Department of Corrections, 2001 Statistical Presentation, [http://www.idoc.state.il.us/subsections/reports/statistical\\_presentation\\_2001/part2.shtml](http://www.idoc.state.il.us/subsections/reports/statistical_presentation_2001/part2.shtml)

It is worth noting that other states, including New York and North Carolina have taken similar steps successfully, and California is engaged in a similar process.<sup>25</sup>

Finally, the State should also work to identify those persons incarcerated in Illinois facilities who are in the United States illegally. A DOC study suggests that there could be as many as 1,700 undocumented immigrants in Illinois correctional centers.<sup>26</sup> Deporting these individuals may pose a logistical and political hurdle. However, we believe that the residents of Illinois should not continue to be responsible for supporting these undocumented persons. The State should immediately begin to identify these individuals and open negotiations with their home countries to have them deported and incarcerated in their nation of citizenship. To prevent the return of these offenders, Illinois should enact measures that impose the strongest possible sanctions against deportees who return to the state.

It is exceedingly difficult to justify the dramatic increase in Illinois' prison population over the past 30 years. While trends have certainly flattened out over the past several years, we believe it is time for the State to begin looking into ways to reduce the overall number.

### **Action Steps: Medium-Term**

In the medium-term, we believe the State should strive towards a deeper reduction in its prison population from 45,000 inmates and 35,000 parolees to a population of 30,000 inmates and (at a minimum) 50,000

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<sup>25</sup> In North Carolina, the General Assembly created a Sentencing and Policy Advisory Commission to review sentencing laws and policies. They produced a system to classify criminal offenses into different categories based on the severity of the offense. The Structured Sentencing Act (1993) offered judges a "felony punishment chart" to determine appropriate sentences for a given crime. Included in the chart was the amount of available prison space in North Carolina prisons. The combined purpose of these efforts was to (1) ensure that prison space was reserved for the most violent, frequent offenders, (2) avoid unnecessary prison sentences for non-violent offenders, and (3) reduce costs for the state. As a result, prison admissions for certain categories of crime fall by more than 50%, and total prison admissions fall by approximately 25%. (National Institute of Justice, "Managing Prison Growth in North Carolina Through Structured Sentencing," online at <http://www.ncjrs.gov/pdffiles/168944.pdf>)

In the mid-1980s, New York State created 175 new Alternative to Incarceration (ATI) programs, including work release and "shock incarceration," were created, serving 50,000 individuals annually. In New York City, prosecutors and courts agreed to release a higher number of offenders on their own recognizance at their first court appearance. As a result, New York experienced an 8% decrease in its prison population at the same time that most states were increasing their prison populations. Meanwhile, crime rates in the city declined by 44% for property crime; 54% for robbery; and 47% for violent crimes.

Earlier this year, Governor Arnold Schwarzenegger forced the California Department of Corrections to reduce its spending by \$400 million. In response, the department proposed reducing its prison population by 8,000 inmates by the middle of 2010 through more time off for good behavior, more lenient parole guidelines (including GPS monitoring), and a higher dollar limit on grand theft. The impact of these actions on crime rates has yet to be seen.

<sup>26</sup> Illinois Department of Corrections, Internal Data

parolees. Given the changes being proposed here, it may be necessary to keep a larger number of people on parole for longer periods of time, especially individuals with a history of criminal activity. By enacting these changes, the State could potentially save hundreds of millions of dollars.

Additionally, no entity or process exists to consider the net impact on the penal system of actions taken by any particular agency involved in the criminal justice process. To counter this, we believe the State should begin a process with representatives from the court system, the Department of State Police, the Department of Corrections, the governor's office, the state legislature, and any other stakeholders who warrant inclusion. This effort should conduct a detailed review of the cost, structure, and effectiveness of the current criminal justice system, with the goal of determining how to reduce the State's prison population while creating an effective system to monitor criminal activity, provide treatment and education to drug users, and assist offenders in the process of re-entering society. We expect that this review would take 12 to 18 months to complete. It would likely take another 12 months for the State legislature to enact any necessary changes in sentencing and parole guidelines. In this time, the State could begin to consider, in conjunction with DOC, the logistics of how to enact the proposals and how to handle the transition in prison population.

To realize the cost savings associated with reducing the prison population, the State will need to consider how it could reduce DOC costs commensurate with the reduction in the prison population. This will likely require collective bargaining with AFSCME, the union representing DOC employees, to negotiate the terms of a reduction in headcount.

The State should also consider undertaking full-scale facility closures to realize even greater savings. We believe there are a variety of positive direct and indirect benefits that could be realized by reducing the prison population and closing certain facilities.

### **Action Steps: Long-Term**

Over the long-term, the State should review prison design and construction, as well as DOC organizational structure and staffing policies regularly, to ensure that the department is designed in such a way as to reduce operating costs. If the State can effectively minimize the prison population, it will have considerable positive financial and social implications for the State.

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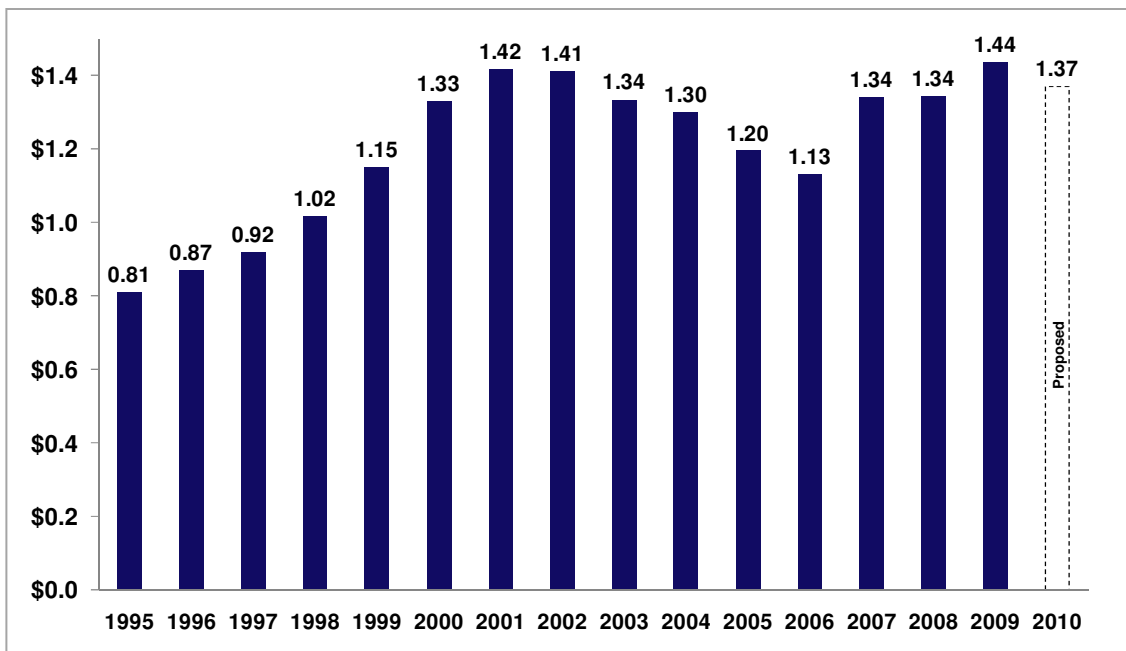
## **REDUCE SALARY BURDEN**

**To reduce State expenditures on salaries and benefits for Department of Corrections and Department of State Police employees without significantly compromising on quality of service**

*(Note: The topic of reducing the overall salary burden to the State is discussed in the preceding State-wide chapter. We take a further look at the salary burden in public safety here because (1) it represents a significant portion of the State workforce and (2) more importantly, there are issues and potential opportunities within public safety that are not relevant to the greater State workforce.)*

A dramatic reduction in public safety spending is not unprecedented. For example, over the past 15 years DOC has seen costs fluctuate considerably, from \$810 million in 1995 to \$1.4 billion in 2001.<sup>27</sup> Following 2002, however, DOC spending fell for several consecutive years, shrinking by over 20% through 2006(Figure 1).

**Figure 1: Department of Corrections Spending, (\$ in billions)**

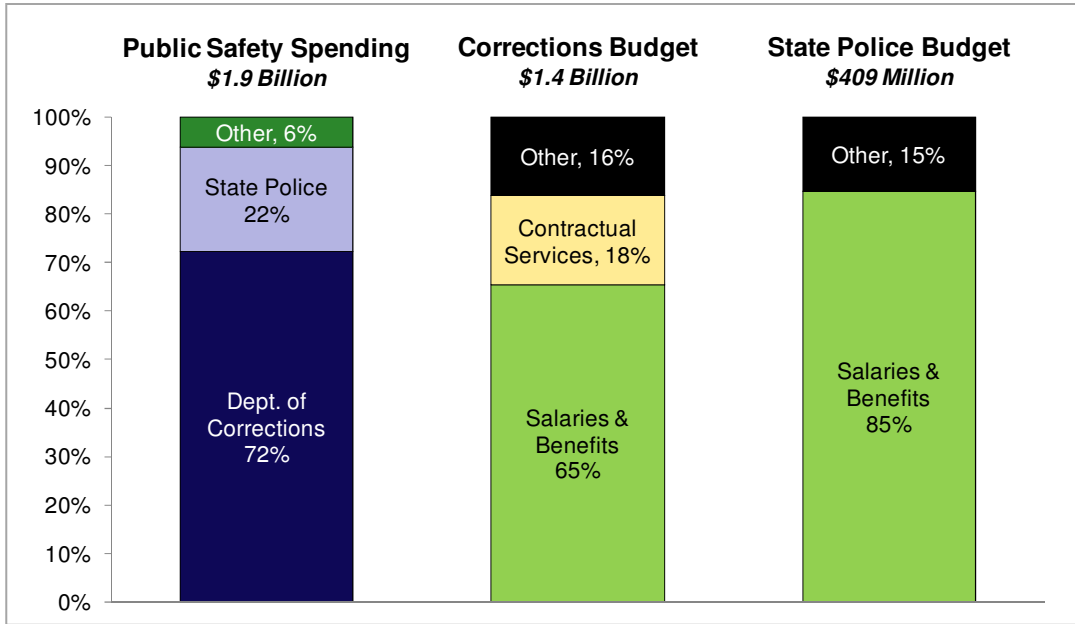


The reductions in spending achieved during the first half of this decade were realized in part by aggressively controlling costs, such as commodities spending, food menu changes, and decreased spending on repairs, prison maintenance, and inmates clothing. The bulk of the savings through 2006, however, was realized through an FY02 early retirement initiative by DOC, which resulted in the loss of approximately 2,500 employees, most of whom were on the higher end of the salary spectrum. This measure alone has saved the State well over \$100 million annually. More recently, higher prisoner populations have contributed to higher department spending.

The only way to significantly reduce State costs associated with public safety is to reduce total salaries and benefits expenditures. In FY10, the appropriated budget for public safety in Illinois is approximately \$2.6 billion, divided among nine agencies. The federal government is expected to contribute \$738 million, leaving Illinois responsible for \$1.9 billion of expenditures. Of that \$1.9 billion, nearly 95% (\$1.8 billion) is dedicated to two departments, the Department of Corrections, at \$1.4 billion, and the Department of State Police, at \$409 million (Figure 2). These two departments represent the overwhelming share of State spending on public safety.

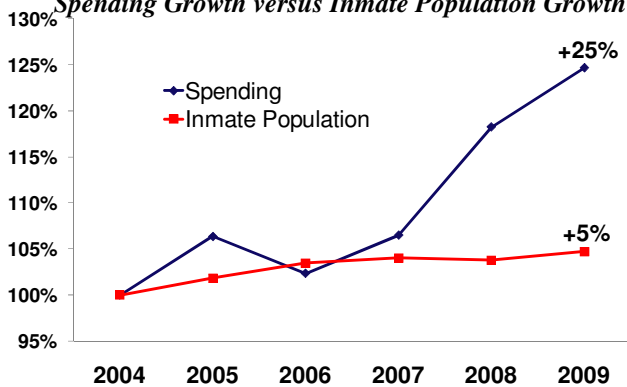
<sup>27</sup> National Association of State Budget Officers, State Expenditure Report 2007, and Illinois Department of Corrections, internal data.

**Figure 2: Illinois Public Safety Spending and Operating Budgets**

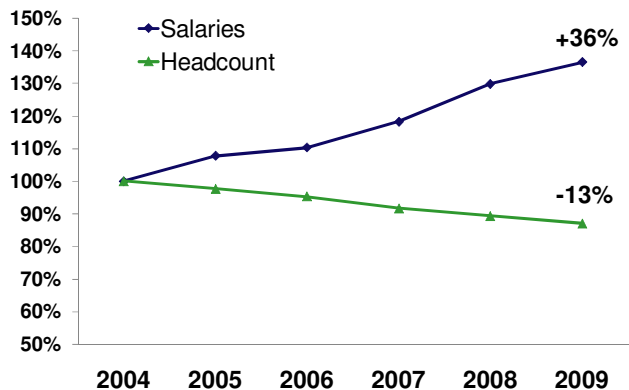


Spending on these two departments has been growing rapidly over the past several years. Since 2004, total spending on the DOC has increased 25%. Over this same period, the inmate population has increased only 5% (Figure 3). The single largest budget item for both DOC and the Department of State Police is salaries and benefits, at 65% and 85%, respectively. The primary driver of the increase in spending has been the cost of personnel, which increased 19%. Remarkably, these increases happened concurrently with a significant reduction in headcount. Between 2004 and 2009, the number of people employed by DOC fell 13%, from 12,689 to 11,039, but the average salary per employee increased 36% (Figure 4).

**Figure 3: Department of Corrections – Spending Growth versus Inmate Population Growth**



**Figure 4: Department of Corrections – Change in Salaries and Headcount**





The increase in spending on salaries was not mirrored by other areas. For instance, spending on items such as food, clothing, and repairs and maintenance decreased by 3%, 27% and 38%, respectively over the same period of time. The fact that salaries and benefits represent both the largest and the fastest growing items in the budgets for the Department of Corrections and the State Police leads to a clear conclusion – if Illinois is going to meaningfully control spending on public safety, something must be done about compensation for corrections officers and State Police.

Additionally, over the past several years, overtime expenses have grown considerably, going from \$19.4 million in FY06 to more than \$67 million in FY09. There is a significant opportunity to realize savings if the State could more effectively manage the overtime it offers its workers. In addition to the \$67 million of DOC overtime expenses, the State Police incurred \$22 million of overtime in FY09. Much of this overtime is accrued by senior DOC and State Police employees, who command a higher rate of pay.

Under the current structure, some DOC employees work two consecutive eight-hour shifts. In a high-stress environment like a correctional center, this is almost certainly a cause for concern for DOC, as a single individual working for such an extended period of time presents a potential liability to the State.

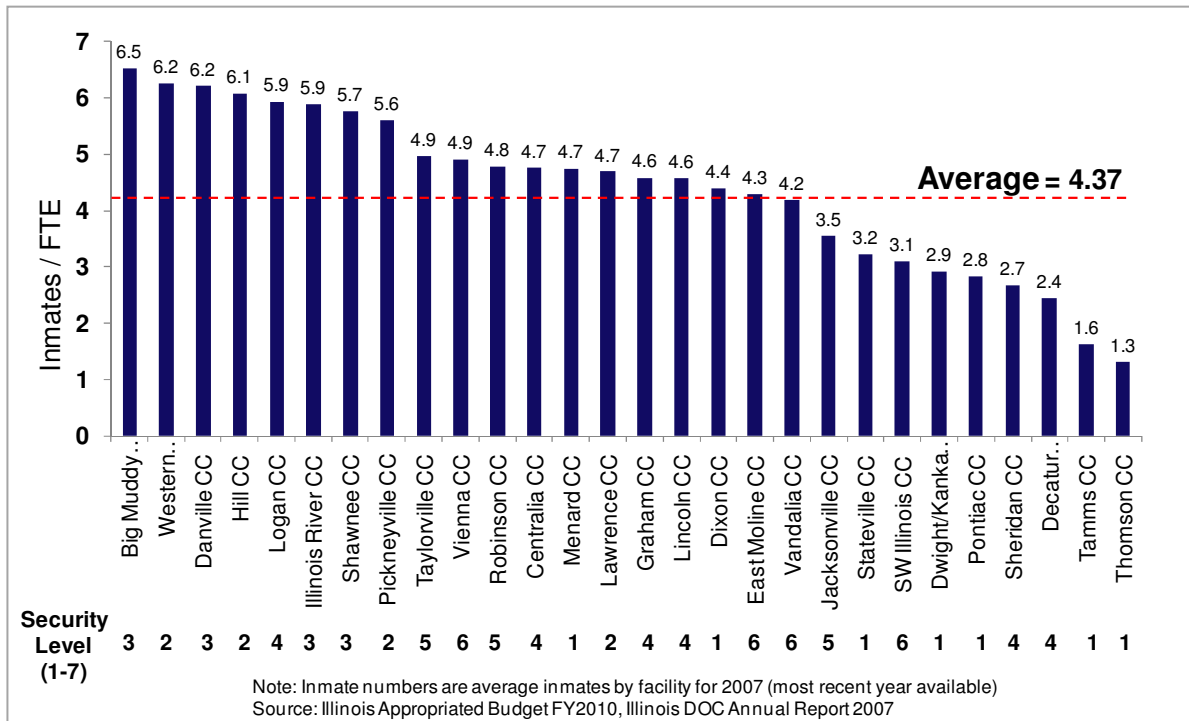
### **Action Steps: Short-Term**

There are several options for reducing salary and benefit costs which might deliver short-term benefits to the State. Some may be more feasible than others.

- **Conduct a full review of staffing and schedules for DOC and State Police employees**  
Given the size of the State’s correctional and police payroll, the State should undertake a comprehensive review of its staffing, including compensation levels, scheduling, allocation among facilities, and other measures. Some of the strategies to reduce the State’s public safety payroll might include the following approaches:
  - **Manage overtime by hiring more staff**  
The State could undertake to reduce public safety expenditures would be to hire more workers for the Department of Corrections and State Police. Though the idea of hiring more workers as a means to reduce costs may seem counterintuitive, the headcount reductions in these departments over the past several years have led to ballooning overtime expenditures. According to an internal study by DOC, hiring an additional 500 frontline employees could result in a \$37.2 million reduction in overtime expenses. The cost associated with hiring these additional employees is estimated to be roughly \$27.9 million. Therefore, DOC believes this measure could save the State approximately \$9 million annually. Hiring this additional staff would also likely improve the quality of work in DOC facilities.
  - **Reallocate corrections officers to under-staffed facilities**  
DOC has already experienced a 13% net reduction in headcount since 2004 and staffing levels in DOC and in the State Police do not indicate heavier staffing in Illinois than in other states. Instead of headcount reductions, therefore, reconfiguring the allocation of corrections officers may be a more promising opportunity. An analysis of Illinois correctional centers

revealed significant variance in employees per inmate, ranging between 6.5 inmates per employee to 1.3 inmates per employee depending on the facility (Figure 5) – while partially related to the severity of the crimes committed and the mental health of the inmates housed at these facilities, security-level and other support factors do not appear to explain the full difference. DOC may be able to more efficiently allocate corrections officers away from facilities that appear over-staffed. Such a measure would have to be done by the State on a facility-by-facility basis, given the specific needs of each facility, but a high-level analysis suggests there may be opportunities in this arena.

**Figure 5: Department of Corrections – Inmates per Employee by Facility**



– **Establish longer shifts and shorter weeks:**

A final measure to reduce costs involves shifting DOC employees to a 12-hour, four-days per week schedule. According to DOC, it requires fewer employees to operate a facility with 12-hour shifts than with the current eight-hour shift structure. DOC anticipates that such a measure would result in \$31.5 million in savings. Such a measure would require union support. Additionally, DOC would have to hire 236 new security officers to staff prisons (as compared with the 500 that would need to be hired if current shift schedules are maintained). Given the high-stress level that working in correctional centers imposes on employees, DOC would have to assess whether a 12-hour work day would compromise job performance. Several states, including Indiana, Montana, Alabama, Louisiana, and California (pilot), have enacted some form of a 12-hour work day, and they do not appear to have experienced significant problems. DOC, the State, and AFSCME should consider whether this shift would be appropriate for Illinois. To date, the union has generally been opposed to enacting such a measure.

### **Action Steps: Long-Term**

We believe enacting targeted prison closures provides a significant opportunity over the long-term. In the past few years, several large facilities such as Stateville and Pontiac were considered for closure. Both of these facilities were deemed outdated and in need of massive capital injections. Furthermore, according to DOC, these facilities have experienced problems in terms of employee attrition, which has increased personnel costs, mostly in the form of increased overtime pay. These proposals were eventually discarded, partly due to a threat of litigation.

Closing a facility would offer opportunities to reduce headcount and overtime expenditures while also saving on fixed costs such as utility and facility-specific expenses. Prison closures might be difficult to enact logistically due to concerns related to the transfer of prisoners and corrections officers to other facilities, as well as the impact to local communities in which the prisons are located. Targeted prison closures appear to be an attractive option, however, particularly if combined with a reduction in the State's inmate population. An internal analysis by DOC has suggested that closing a facility could save between \$30 to \$40 million annually. Much of this amount would be offset by the cost of housing the inmates in another facility: the net benefit is estimated to be between \$4 and \$6 million.

If the State is going to substantively reduce public safety costs, it must confront salary and benefit expenses in the Department of Corrections and the Department of State Police.

The only way to significantly reduce State costs associated with public safety is to reduce salaries and benefits expenditures. There are a number of ways to realize this goal, and we encourage the State to pursue any and all avenues as expediently as possible to move towards a smaller prison population and a more manageable public safety budget.

Lastly, the TAB believes that every effort should be made to communicate to State employees that these reductions, while necessary due to the State's current fiscal crisis, should not be perceived as a punitive action for poor performance. While we have only discussed Public Safety Departments in this section, we believe the State should undertake a review of the salaries and benefits of all State employees (as stated in the earlier State-wide section), not only DOC or State Police employees. Certainly these individuals have served the State of Illinois well, but in difficult times, difficult measures must be undertaken.

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## **MODERNIZE INFORMATION TECHNOLOGY**

**To modernize and integrate a limited 25-year-old system that presently negatively impacts productivity and most importantly does not efficiently track offender program outcomes designed to reduce recidivism and the inmate population**

Hampered by budgetary constraints, the Department of Corrections (DOC) struggles with systems that are not integrated and impede adequate case management tracking. For example, the American Management System (AMS), which tracks parolees, is not sufficiently linked to the Offender Tracking System (OTS):

when an offender becomes a parolee, that person's information cannot be shared with the OTS system. If the systems were better able to share information, DOC could better track and potentially rehabilitate offenders. Additionally, under the current system, case management data cannot be stored for more than two years, despite the need to reach back farther for case data.

Severe IT, telecom, and radio infrastructure problems will ultimately require a significant capital outlay yet will save considerable personnel time. In DOC's IT system, there are about 1,000 workstations that are eight to 10 years old and do not support new, more efficient software applications. These workstations are extremely slow with log-on times taking upwards of 30 minutes. Routing systems backups require nearly an entire weekend.

Without an upgraded IT system, DOC cannot measure or be held accountable for transitioning inmates back into society or for lowering recidivism. DOC believes that in-house modernization of the IT systems would be more cost-effective and less risky. Without hard estimates, a system upgrade might be in the \$5-10 million range, if conducted in-house with support from consultants.

### **Action Steps: Short-Term**

**Implement an automated pay system:** An automated pay system will require roughly \$1-2 million and six months to implement. (A State-wide system would cost an estimated \$10 million.) DOC is likely to save \$1-2 million per year in reduced errors alone. Automation can result in further savings of \$1-3 million a year.<sup>28</sup>

**Upgrade outdated workstations:** The 1,000 outdated workstations throughout the DOC system can dramatically slow personnel productivity. We estimate that the average worker loses an hour each day due to poor response time. At an average cost per worker of \$50 per hour, this lost productivity can amount to \$20 million a year.

**Integrate DOC's IT system with county systems, especially Cook County:** Approximately 30,000 of the 39,000 new offenders that enter the prison system each year are from Cook County. When an offender is processed in Cook County, the system collects medical records, DNA tests, and other costly tests. Since there is no way currently to share this information among systems, these tests are duplicated at the State level. We estimate the savings to be approximately \$2 million a year, after an initial investment of roughly \$25,000.

### **Action Steps: Medium-Term**

**Review DOC's systems:** In addition to the OTS, DOC operates about 60 Windows-based applications, to cover gang-level intelligence, personnel rosters, and case management, for example. Three case management systems are not integrated in any meaningful way with either each other or with OTS. The TAB encourages DOC to conduct a systems assessment to determine which can be replaced, combined, or

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<sup>28</sup> Department of Corrections

retired. We also believe that DOC should move the OTS system to a Windows-based system using an SQL server. Such an effort would likely cost approximately \$10 million and could be conducted within an 18-month period. Through a similar exercise, Marin County California has been able to reduce mainframe operating and personnel costs by 91%.<sup>29</sup> Using this benchmark, the potential annual operating savings to the State would be \$2.5 to \$5.5 million. However, the real savings lie in being able to consistently and efficiently track incarcerated and paroled offenders.

**Enable remote video-conferencing for non-essential court appearances:** Many of the 30,000 new inmates that enter the system from Cook County are placed in facilities in southern Illinois. An inmate may make multiple trips (six hours or longer) to Cook County for non-essential hearings or to serve as a witness in others' hearings. These trips often require one to four corrections officers to accompany the inmate. With the systems upgrades noted above, video conferencing offers an opportunity to reduce expenditures for procedural and non-essential hearings.

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<sup>29</sup> Lewis Wire, May 13, 2009

## **GOVERNMENT OPERATIONS**

### **Drive improvement and savings across the State's internal operations**

Because of the magnitude of the State's spending on running the "business of government in Illinois – procurement, facilities, technology and the like – it is important to look within the State's internal operations to effect important though likely difficult, long-term improvements in efficiency and spending reductions across more than 40 State agencies.

As the TAB looked across the State's internal operations to identify efficiencies, we kept our focus on ideas that offered the best opportunities to: decrease spending; improve the value of dollars passed through to local governments; improve financing; encourage more efficient management and delivery; and encourage investments in the State that add value and, as a means to increase efficiency, support necessary expenditures, retain revenue and promote new economic development.

The TAB examined a broad range of the State's internal support functions managed by State agencies. Our goal has been to identify best practices that enhance productivity, yield substantial returns, and improve the ability of other agencies to deliver direct service.

It must be noted that these State operational functions support the efficient administration of all areas of State government. Without effective support in place, the State could hamper the ability of other agencies and programs to be efficient in their direct service to taxpayers. Thus, any changes to internal operational functions must be made with careful thought given to the potential impact agencies throughout the State. Many of these changes have been historically difficult to change, but perhaps represent the greatest single opportunities for efficiency across the State.

It is vital that the State look within its own operations to introduce internal changes that are significant, creative, flexible and in line with best practices in other governments and in business. As an employer of more than 55,000 full-time equivalents, the State should demand professional management in all aspects of its business. In addition, through the improvement of its functions and ongoing identification of efficiencies, the State becomes better equipped and able to deliver direct services to its external customers, namely, Illinois' residents, businesses, visitors and taxpayers.

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### **MINIMIZE COSTS ASSOCIATED WITH BOARDS AND COMMISSIONS**

The State currently has more than 300 Boards and Commissions that have varying levels of decision-making authority and provide guidance to various State agencies and elected officials. Depending on the role and commitment of the body, Board and Commission members may either be compensated for full-time or part-time roles, or serve in a voluntary, unpaid capacity. For those full-time Boards and

Commissions, the State compensates members commensurate with equivalent salaries, due to the full-time commitment required of these members and certain rules prohibiting outside employment.

Members of the State's part-time Boards and Commissions, however, participate within a more limited time commitment and are allowed to retain external employment. To compensate these members, the State currently expends approximately \$3.1 million annually, not including the cost of additional benefits to certain members such as pension and health-care benefits, which should also be considered as a part of the overall cost savings. The State should eliminate all pay and benefits for part-time Board and Commission Members. Service on part-time Boards and Commissions should be considered a part of Illinoisans' commitment to serve the public.

In addition, the State should review the need to continue maintaining and supporting each of the 300-plus existing Boards and Commissions. Supporting and managing Boards and Commissions often requires a significant time commitment from State employees. The State should seek opportunities to consolidate or eliminate or transfer duties of all Boards and Commissions, or at least consider reducing the size of some larger Boards and Commissions, where possible, thus reducing added layers of government and refocusing staff time on core duties.

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## **ANALYZE SPENDING TO IMPROVE PROCUREMENT PROCESSES**

The State spends almost \$10 billion annually on goods and services – which affords it tremendous buying power. In fact, the State's purchasing authority rivals that of some of the nation's largest private corporations.

In general, the manner in which goods and services are bought and sold is an increasingly specialized process, progressively incorporating new practices in sourcing, technology, inventory, competitive negotiating, contracting, payment and other services. Governments today are dependent on external goods and services – placing ever more importance and pressure on the State's procurement function.

Based on the condition of the State's current procurement processes, the State could achieve substantial long-term savings by adopting private-sector standards. Presently, not only do the State's procurement processes fail to capitalize on the State's buying power, but in fact, negatively impact the State's working capital. The effectiveness of the procurement processes is impeded by a variety of factors: the system does not maximize coordination across the 40 disparate agencies; are separated under six separate authorities; are supported by insufficient and outdated technology; and fail to take advantage of money-saving practices. The TAB believes that the State should undertake the following major opportunities to transform its procurement process, addressing both internal and external impediments.

- **Conduct an analysis of State spending**  
Currently, the State spends approximately \$10 billion annually procuring goods and services, spread across the authority of six chief purchasing officers (CPO), half of this spending is

coordinated through authority granted to Central Management Services' Bureau of Strategic Sourcing and Procurement. The other \$5 billion is conducted under the authorities of five other CPOs, which includes the Department of Transportation, Capital Development Board, Department of Healthcare and Family Services, Illinois Power Authority, and the University system.

Even though the authority of the Procurement Policy Board governs the manner in which these goods and services are procured, the State does not have a consolidated procurement system across the six separate CPOs and over 40 separate agencies. This results in a lack of visibility into the agencies' spending needs, behaviors, and patterns and renders the State unable to improve coordination, reduce costs, or make strategic procurement decisions.

The State should conduct a "spend analysis," a common business practice to help achieve significant cost savings, across \$10 billion in spending. Typically costing about \$500,000, which is a relatively nominal investment given the resulting savings, a spend analysis looks at third-party expenditures to identify cost savings opportunities and to enable improved cost-optimization programs, including:

- Better information about how the State is spending, across multiple agencies and/or the entire State
- Opportunities to consolidate vendors, source strategically, and renegotiate vendor relationships
- Comparisons between the State's major spend categories and industry benchmarks
- Opportunities for improved processes and policy compliance
- Identification of targeted outsourcing opportunities for select business functions

If the State had one procurement system, this information could be readily available to help the State make smart, efficient purchasing decisions. Since it is not the case with many governments, and may not be the case with the State for many years, the TAB encourages the State to conduct a spend analysis, typically a six-month endeavor, to produce this type of valuable information. Other states have conducted such analyses with success, including Virginia, Delaware and Oregon.

Commonly, a spending analysis identifies opportunities that, when implemented, can result in savings of around 5% of total spend. Implementing the recommendations of a spend analysis to drive strategic purchasing decisions could save the State of Illinois up to \$500 million.

- **Improve existing contracts**

In the current economic climate, the State has an opportunity to use its substantial purchasing power to re-open and adjust its existing contracts to renegotiate or rebid them as a means of obtaining more advantageous terms, such as asking vendors to provide a contractual 2% rebate or rate reduction. For vendors that are not interested in participating, the contracts and agreements can be rebid competitively.

- **Introduce procurement cards**

In addition, the State's method of paying for goods and services fails to take advantage of certain modern practices and benefits. For example, the State does not currently employ the use of



procurement cards or “p-cards.” Numerous industries, including governments, are now using p-cards, which can decrease costs through purchase rebates (negotiated with card issuers) and increase efficiency in the payment process through electronic transactions.

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## MANAGE REAL ESTATE AND FACILITIES AS PART OF ASSET PORTFOLIO

- **Outsource management of the State’s real estate assets to a professional services firm**

Despite the significant size and value of the State’s vast real estate portfolio, the State does not approach its real estate holdings as a strategic asset and investment portfolio. Currently, much of the State’s real estate and facilities are primarily coordinated through Central Management Services, Bureau of Property Management (CMS, BPM). However, the largest real estate owners within the State system, which include programmatic agencies, such as the Departments of Human Services, Corrections, and Historic Preservation, manage their own facilities.

In addition to the fragmented management and oversight of its holdings, no comprehensive real estate strategy exists. No single asset inventory exists, nor does the State have a comprehensive inventory of all current leases. Dedicated resources are not assigned to the strategic or financial management of the portfolio; instead the limited resources must focus on reactive management of expired or expiring leases.

The size and potential value of the State’s real estate assets necessitate a dedicated focus that manages these holdings as investment assets. The TAB therefore believes that the State should develop a comprehensive real estate strategy and asset inventory, under the guidance of a professional services firm that would be competitively sought, given responsibility for strategic planning, portfolio management and information management, and held accountable for the performance of the portfolio. CMS, BPM should retain responsibility for maintenance and operations.

With the appropriate partner, the State will be better able to reap the benefits of its investments long-term; to manage against market swings; to identify savings opportunities across its owned, leased, surplus, and abandoned properties; and to more easily recognize opportunities for use, development, and new revenue generation through its real estate assets. Such a change in strategy, focus, and management will require an upfront investment of time and resources, but has the potential to generate significant cost savings, new revenue, and asset gains in years to come.

- **Reduce excess space**

The State estimates that it currently holds 60 million square feet of space, through ownership of 50 million square feet and lease of another 10 million square feet. The State also has an estimated two million square feet or 3%, in excess space. Currently, the State pays an estimated \$10 to \$30 per square foot depending on the use and location of the property.

We encourage the State to take advantage of the opportunity to generate potential cost savings by divesting its excess space, a strategy that could yield the State \$20-60 million (based on average cost of \$10-\$30 per square foot at the time of sale). The specific cost savings will be affected by market conditions. In addition, the State should review its usage – analyzing full-time equivalent (FTE) staffing levels against trends in space availability and use – to determine whether it has further excess capacity.

- **Sell surplus properties or allow related revenue generation from held properties**

Currently, programmatic agencies have authority over the use of their real estate. When deemed “abandoned,” agencies turn over their property to CMS, who then holds the properties until they are divested through sale at fair market price (a statutorily-defined calculation) or at auction.

Due to the lack of a centralized real estate inventory and the disparate authority over agency real estate, there is no way to tell how long surplus or abandoned properties are being held by programmatic agencies before they are turned over to CMS. In fact, current policies create an inherent disincentive for agencies to relinquish this property to CMS in a timely fashion for sale or other purpose.

We believe that the State should change the current real estate holding policy to allow for a swifter identification of possible properties for sale or reassignment. In addition, the State should sell or otherwise divest of abandoned properties, or allow increased uses on property deemed abandoned. For example, allowing temporary advertising on abandoned properties can generate new revenue while the State holds these properties. Specific cost savings will be determined by market conditions.

- **Eliminate hold-over leases**

The State has approximately 100-110 real property leases that are in hold-over status – leases that have expired and are in “hold” status until re-negotiated or cancelled. Although the level of hold-over leases has declined – from 357 in 2005 to current levels, hold-over leases continue to be tremendously inefficient and costly. Once the regular lease has expired, the lessor is able to charge the State less favorable month-to-month rates. The State is also penalized by decreased deferred maintenance on these properties and has less leverage in re-negotiating current and new leases. Pending legislation seeks to end hold-over leases by June 30, 2010, however at the current rate of decline, such leases will not be eliminated until 2011. In order to reduce the costs of maintaining hold-over leases, we urge the State to more quickly eliminate such leases. The swift elimination of hold-over leases may require a short-term staffing increase, and the State should analyze the cost/benefit of accelerating the elimination of such hold-over leases.

- **Outsource facilities maintenance**

The State currently employs a significant number of personnel to perform maintenance on State facilities. The State should consider outsourcing these maintenance responsibilities to an appropriately-skilled and competitively-bid vendor. As part of its review of the opportunity, the State should undertake a cost-benefit analysis that considers the continuing payment of prevailing wage to vendors where applicable. We estimate that the State can save at least the amount dedicated to the overhead and benefits provided to State employees. As the majority of the State’s positions are

classified under collective bargaining agreements, the State will need to work with the appropriate parties to remove impediments to realizing this opportunity.

- **Invest in sustainable energy technology for State facilities and operations**

The introduction of sustainable energy technology in State facilities and operations presents an opportunity to achieve cost savings, generate growth in revenues, and to realize positive benefits on the environment and the health of Illinoisans. Such technology enables governments to move away from increasingly costly and regulated fossil fuel. In addition to reduced energy costs, many governments have seen investment in this technology provide long-term savings that outpace the upfront cost of initial investment. The State should examine which measures – such as design standards for State buildings and fuel requirements for motor vehicle fleets – would be most appropriate and would best generate worthwhile savings.

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## REVIEW LOCAL GOVERNMENT REVENUE SHARING

Illinois' 7,000 units of local governments, or 8% of all the local government in the United States, support a State-wide population that represents 4.24% of the total U.S. population. The State provides significant support for these units of local government, beyond that provided for education entitlements. During FY08, the state provided general, non-education financial support to these local governments close to \$6 billion through multiple fund transfer programs, a significant use of the State's own revenues.

The TAB recognizes that the formulas have not been reviewed or adjusted in some time, and the current economic climate provides a strong impetus for undertaking this initiative. The timeframe of the TAB did not provide a sufficient opportunity to undertake such an analysis.

The intent of a review should not be aimed at balancing the State government budget to the detriment of local governments. Rather, any adjustments made as the result of such a review should encourage regional, unified and inter-jurisdictional cooperation (versus competition) among local governments to gain greater local government efficiencies. The following tax sharing programs should be included in the review:

- Local Share of State Income Tax (\$1.2 billion): 10% of net income tax collections is distributed by the State to municipal and county governments in proportion to their population as compared to the total state population. (The unincorporated population of a county is allocated to counties.)
- Motor Fuel Tax (\$631 million): 54.4% of all collections from the State tax after certain specific set-asides is distributed by IDOT to municipalities, counties, and road districts based on three separate formulas.

- Local Share of State Sales Tax (\$2 billion): The Local Government Tax Fund is derived from 20% of the 6.25% state Retailer’s Occupation Tax on general merchandise purchases and 100% of the 1% tax on sales of food and drugs. The fund is allocated based on the following formula: 84% of the tax on general merchandise is distributed to the municipality or county where sales occurred, and 16% is distributed to the county where the sale occurred (other than in Cook County, where it is distributed to the RTA; 100% of the state sales tax on food and drugs is distributed to the municipality or county where the sale occurred.
  
- Local Share of State Use Tax (\$200 million): 20% is allocated to Chicago, and 10% to the RTA. After minor other set-asides, the remainder is allocated to cities (other than Chicago) and counties, based on population.
  
- Corporate Personal Property Replacement Taxes (\$1.6 billion): 51.65% is allocated to taxing districts in Cook County (including schools) based on each district’s percentage of total personal property tax collections in 1976. The remaining 48.35% is allocated to the taxing districts in the other 101 counties based on each district’s percentage of total downstate personal property taxes collected in all counties other than Cook in 1977. (The formula to determine the allocation balance between Cook and elsewhere in the state was based on the distribution of the collections between Cook and other counties in 1977. The personal property tax was abolished in 1979.)
  
- RTA and Downstate Transit Funds (\$292 million): The RTA is allocated a portion of the 5% State sales tax to match 25% of the amount collected by the RTA under its separate authority to impose sales taxes. The Downstate Transit Fund is allocated 3/32nds of the amount generated by the State’s sales tax.

In addition, there are several other smaller grant and reimbursement programs made to various units of Illinois local government that may also be considered for review.

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## **IMPROVE INFRASTRUCTURE FINANCING AND DEVELOPMENT**

The State’s infrastructure developments are primarily coordinated through two agencies: the Department of Transportation (IDOT) and the Capital Development Board (CDB). Both agencies represent relatively small shares of the State’s operating budget, with most of their spending conducted from the capital budget. In FY10, the State proposes approximately \$26 billion in capital expenditures for large, long-term infrastructure projects. The sheer size of the long-term resources required for infrastructure projects suggests that a focus on improved infrastructure financing and more efficient operations may elicit cost savings for the State. Some opportunities that the TAB has identified include:

- **Utilize public-private financing for large-asset, capital investments**

Historically, the State has supported capital projects through a dedicated capital budget which is funded through the issuance of municipal bonds. Correspondingly, the operating budget then encompasses the debt service on these bonds and any new maintenance required after the completion of the infrastructure development.

In recent years, many state and local governments have begun financing large infrastructure developments through public-private partnerships, in lieu of traditional municipal bonds. Such public-private partnerships can reduce the State's long-term liability, providing lower development costs and decreasing operating and capital expenditures on the whole life cost of the asset, and also decrease short-term liability on the State's operating budget by defraying typical debt service costs on capital expenditures. Often, they also enable infrastructure projects to begin and finish sooner, and if structured correctly, they can reduce risk to the State.

Governments are typically able to realize a 10-30% savings on the whole life cost of the asset through the use of public-private partnerships. To estimate the potential savings, the State should review the cost of FY10 major capital projects, specifically examining the State's match (which is required to receive federal funding for capital projects). Legislation would be required to formalize the State's ability to utilize this approach.

Based on the size of investment required for the development of infrastructure assets, the potential savings to the State is significant. The timeframe for these savings is long-term, due to the lead time to analyze opportunities and how financing should best be structured.

The State should support legislation (currently proposed) to authorize the use of public-private partnerships in large-asset capital developments and utilize this method when appropriate, going forward. Many projects currently under consideration might lend themselves well to a public-private partnership, such as schools, expressway construction or expansion, toll bridges, truck corridors, airport development, rail initiatives, and congestion reduction projects, including high-occupancy vehicle tolling, managed lanes, and/or bus rapid transit.

Other states that have passed public-private financing legislation include Indiana, Virginia, Nevada, North Carolina, South Carolina, Georgia, Oregon, Texas, California, Florida, and Minnesota.

- **Utilize Design-Build-Finance-Maintain-Operate (DBFMO) approach for large projects**

Many of the traditional procurement methods that the State uses in the development of new construction projects are considered inefficient by industry standards. Current procurement regulations require the State to separately bid multiple aspects of every infrastructure development. This practice typically increases the overall length of the procurement process, and fails to take advantage of economies across a project's design (architectural, technical), construction, financing, maintenance, and operations.

Design-Build-Finance-Maintain-Operate (DBFMO) is a leading industry practice that consolidates significant portions of the original bid with a single firm for the lifecycle of the project. The benefits

of this method, which can be parsed in multiple ways to fit the needs of each project (for example, DB, DBFM, or DBFMO), have been shown to increase the overall quality of the project, shorten project turnaround, increase continuity and reduce cost of the project by 5-10% over the lifecycle of the project. Legislation would be required to formalize the State's ability to utilize DBFMO (also currently proposed) and should be supported by the State. Going forward, the State should employ DBFMO in the procurement of major construction projects.

- **Outsource maintenance of public roadways**

IDOT's full-time workforce represents approximately 10% of the State's overall position count. Due to the nature of their work, IDOT's workforce is comprised of full-time, part-time and seasonal personnel, totaling nearly 6,400 personnel in FY09. About 97% of IDOT's workforce is covered by a collective-bargaining agreement, and there is a current petition to subsume most of the remaining IDOT workforce under the same agreement (excepting executive leadership that would fall outside of the related work rules and position classifications).

Half of IDOT's workforce, and thus approximately half of IDOT's total personnel expenditure, is dedicated to the maintenance of State-maintained public roadways. We encourage the State to consider outsourcing IDOT's maintenance responsibilities to appropriately-skilled and competitively-bid vendors. In doing so, the State should compare competitive bids against the total cost of maintenance personnel, which is estimated at \$243 million in FY09. The State should seek bids that continue payment of prevailing wage. The cost savings from such outsourcing most likely lie in the transfer of overhead and benefits (from the State to the outside vendor) for the approximately 3,100 full-time, part-time and seasonal positions covered by the collective bargaining agreement. Not only will this produce cost savings in two to three years, but it will also decrease the State's growing pension burden in years to come.

As the majority of the State's positions are classified under collective bargaining agreements, the State will need to work with appropriate representation in order to remove impediments to realizing this opportunity.

- **Employ more efficient procurement methods for small and medium construction projects**

**Unit price contracting:** Currently, the State requires construction projects to be bid separately, regardless of the project size or task at hand. For small and medium construction projects, the result is that vendors must bid again and again for the same types of projects year after year. With each small and medium project moving through the procurement process the same way that a large project does, the procurement process is extended unnecessarily, and similarities between projects or among different aspects of the same project are largely ignored.

Instead, the State should adopt expedited or standardized procurement methods that take advantage of such potential efficiencies. For example, job-order contracting (JOC) prequalifies vendors so that each vendor's rates and qualified tasks are established in advance. The State essentially develops a master contract with each vendor under JOC, and then when specific task orders arise, the State can

tap the appropriate vendor to fulfill the task. By prequalifying and setting parameters for each vendor, the State can move projects ahead much more quickly.

The use of JOC and similar methods is a standard practice in the construction industry and is used by many state and local governments. Such practices typically reduce costs by 5% (over the current method) because vendors can offer more competitive rates and because the State is better able to predict and plan expenditures, shorten procurement cycles, and provide more consistency in vendors.

**Single-prime contracting:** CDB is currently required to use “multi-prime contracting” for capital construction projects. This is highly inefficient method that requires CDB to procure all vendors and trades separately for a single project. Through legislation, CDB was able to pilot the use of “single-prime contracting” – which engages a single contractor that is given responsibility for the completion of an entire project – on a select number of projects. The pilot generated notable efficiencies: the projects were delivered on-time and on-budget, experienced fewer change orders and modifications, and enjoyed a shorter and easier contracting process.

Given the success of this pilot, and the potential to expand the gains to a broader range of projects, the TAB urges the State to support the adoption of single-prime contracting.

- **Support the development of alternative energy (wind, hydro, solar) infrastructure and uses, including the sale of energy credits and similar carbon-reduction incentives**

Alternative energy infrastructure, such as wind, hydro and solar, can generate long-term savings for the State and yield important environmental improvements, and health benefits. It also has the potential to generate new revenue for the State through the sale of energy credits or similar carbon-reduction initiatives. The State has the opportunity to become a leader in this area, and has thus far shown particular interest in wind energy infrastructure. Aggressive pursuit of energy-efficient, sustainable strategies will help grow Illinois in a responsible, new economic direction.

- **Evaluate criteria and contributions for local school construction grants**

The State’s proposed FY10 capital budget includes \$1.5 billion in capital grants for local school construction projects. When the local K-12 school construction program was first developed, the State only provided funding for local school construction in emergency situations, where the need was urgent and assistance was critical. Since then, the level of State assistance has increased to fund many local schools in various districts. The roster of “entitled” schools is determined by the Illinois State Board of Education in conjunction with the Governor’s Office of Management and Budget (GOMB). The approved list, when funded through a Capital Plan, is then referred to CDB for completion of construction projects. The State is not currently required to provide this funding.

In lieu of eliminating this non-mandated function, TAB encourages a thorough review of the criteria for approving a local school to receive these funds, emphasizing the State’s original intent to offer support in emergency circumstances. We believe that the State’s decision-making criteria should be closely aligned to its investment.

- **Consolidate Capital Planning Liaisons across agencies**

The State currently has Capital Planning Liaisons in multiple agencies that use CDB's capital construction services. The TAB believes this to be an inefficient duplication or distribution of resources, and we encourage the State to make appropriate consolidations of resources within CDB, and once consolidated. Furthermore, the size and need of the Capital Budget should dictate the quantity of resources in accordance with the size and need generated by the Capital Budget.



## CONCLUSION

The Taxpayer Action Board believes that these ideas, taken together, represent the potential to save several billion dollars per year without radically altering service levels, and in some cases increasing service to our fellow citizens. As important, the opportunities offer the chance to help the State operate more efficiently and to direct its resources more effectively.

Many of the opportunities identified in this report will be challenging to implement and will require a new and very different approach. Most will need further exploration and development. We generated the more than 100 ideas described here in a rapid, two-month period, and we are aware that much more work will need to be done to test the viability and to shape the implementation of these ideas.

For example, during our review of State financial reports, we identified a need to significantly improve the transparency of government expenditures – in particular, the myriad and complex movement of funds through the State system. Currently, receipt and expenditures out of General Funds are prominently reported. However, roughly one-third of operational spending is conducted through many of the over 600 special funds of State government. These expenditures occur out of independent revenue sources (e.g. federal reimbursements) and are neither reported nor as visible as they are in the General Funds. While the TAB's review touched on many of these topics, we strongly believe that these areas should be given greater scrutiny and that attempts to make them transparent, comprehensible, and visible to the public should be prioritized.

The State demonstrated a commitment to making tough changes when it formed this Taxpayer Action Board. We see little choice but to implement some difficult, challenging, perhaps painful ideas. Our ever-growing budget gaps and the conclusion of stimulus funding at the end of next year threaten the financial viability of the State and the services it offers.

Through the implementation of the opportunities developed in this report, we look forward to a State government that is effective, efficient, far-thinking, and innovative. We envision fewer duplicated services and more effective overall operations. We look forward to an even stronger culture of transparency and accountability throughout State government. In short, we look forward to the State of Illinois moving beyond its current financial crisis to adopt healthy fiscal practices that enable it to support and strengthen its services to the people of Illinois, our children, and future generations.

## APPENDIX: SUBCOMMITTEE ASSIGNMENTS

### *Human Services*

John W. Casey  
Ruth Munson  
Dory Rand  
Hipolito (Paul) Roldan  
Cheryl Vanderford

### *Medicaid*

Barb Giolitto  
David Hiller  
James Nowlan  
Richard Sewell  
Dan Silverthorn

### *Pensions & Healthcare*

Tom Caliper  
Lester McKeever  
David Mosena  
Zach Mottl  
Deborah Seale

### *Education*

H. Woods Bowman  
Dale Chapman  
Jeff Mays  
Jake Rendleman  
Terence Sullivan

### *Government Operations*

MarySue Barrett  
George Camille  
John Norquist  
Daniel Pierce  
Stephen Schnorf  
Mark Schwiebert

### *Public Safety*

Christine Cegelis  
Dan Donohoo  
Richard Guebert, Jr.  
Chuck Scholz  
Sanford Stein  
William Wolfe

## APPENDIX: MINORITY OPINIONS

Author	Co-signors	Page number
John Norquist	William Wolfe	108
Dory Rand		109
Stephen B. Schnorf	H. Woods Bowman Dory Rand Richard H. Sewell	121
Mark W. Schwiebert		127

## MINORITY OPINION

**Author: John Norquist**

**Co-Signor: William Wolfe**

Dear Governor,

You inherited a fiscal mess. As Lt. Governor you played only a small role in creating the mess and for a while you can avoid blame for its creation. Yet, you will not be viewed as an innocent bystander.

However long you serve as Governor of Illinois, you will be held responsible for putting the state's finances back in order. This will require relentless determination with no guarantee of success and little immediate public appreciation if you are successful.

This report contains "opportunities" to reduce spending. The word recommendations was avoided for reasons I don't quite understand, but the report contains action items that can save money and improve processes. It also contains items that are easily proposed like across the board cuts, but much harder to implement. I'll leave that to you and your staff to sort out. I want to draw one item to your attention that can not only save money and improve service, but if you get started on it soon, also please state employees.

Specifically the TAB report discusses the state employee health plan in Wisconsin. It identifies \$60 million in potential savings if the Wisconsin mechanism were implemented in Illinois. The plan has been in place for more than twenty years and while initially opposed by AFSCME and other state unions, they eventually came to see its advantages in both efficiency and better service. Unlike the other potential savings identified in the TAB Report state employee benefits section, this proposal, sometimes referred to as the Enthoven plan (after Alain Enthoven, a Stanford economist) does not involve diminishing employee benefits. I recommend that you and your staff soon contact Governor Jim Doyle and his staff to explore this option. The Illinois state employee union leadership should be encouraged to confer with their brothers and sisters in Wisconsin. The plan was also adopted by the City of Milwaukee when I served as Mayor. It utilizes the purchasing power of government employees to improve quality and restrain price. It will obviously take time to join all parties and interests behind this change, but it is one of the few items in the TAB Report that can actually make people happier and save money at the same time. Change almost never comes easily. It requires leadership qualities that you've already demonstrated by tackling the budget crises head on. But with this one proposal, you may actually achieve success without enduring or imposing acute pain.

Thanks for the opportunity to offer advice to you.

John Norquist  
President  
Congress for the New Urbanism  
Chicago, Illinois

# TAB MINORITY REPORT ON MEDICAID AND EXECUTIVE SUMMARY

**Author: Dory Rand**

## **Comments regarding the Executive Summary:**

These comments relate to the last version of the Executive Summary that was circulated. It may have been edited since then, but it was not circulated with the final draft of the full report. In “A Final Word” in the Executive Summary, the language used conveys that the Taxpayer Action Board (TAB) is making recommendations rather than proposing opportunities for consideration. The term “recommendation” is even used. Additionally, the Governor is exhorted to “find a way to make these ideas work. We would all fall short of our obligations to the people of Illinois to do anything less.” This language conveys in strong terms that the TAB “opportunities” are fully researched and endorsed action items the Governor must undertake or else the Illinois will suffer. This seems contradictory to the earlier consensus that we only have enough information about the opportunities to know that they have enough merit to be further explored. We cannot in conscience take a strong position at this time. The TAB would be irresponsible in urging the Governor to “find a way to make these ideas work” after earlier conceding that the two-month process was “accelerated” and “fast-paced,” and that TAB members were “limited [in their] ability to assess fully all the factors necessary to implement the ideas it has generated.” [Executive Summary, “The TAB’s Process” p. 2, fourth paragraph from top.] Moreover, these members were a “diverse group of experience and expertise” but were not issue experts on the large subject matters they were charged with evaluating; indeed, many of them lack any familiarity with the subject matter topic of their subcommittee. Thus, the paragraph in “A Final Word” should be much more careful and deliberate to acknowledge these circumstances.

## **Comments on Medicaid Section:**

The TAB was charged with bringing to the Governor’s attention cost efficiencies in state government that will result in maintenance of or a net gain in services for Illinoisans. I have specific comments, stated below, about a number of aspects of the TAB report on Medicaid issues. But I need to preface those specifics with a general comment. The Medicaid report reaches far beyond the charge given to the TAB – to identify efficiencies without reducing care or significantly altering our policy direction in Illinois. The Medicaid report is a departure from the TAB's charge; it recommends significant policy reversals and new directions. It exalts saving money over carefully debated and voted upon state policies. I think reasonable people can have those ideas but it was not TAB’s job to do that. The members of TAB who support those ideas are free to pursue them, but they should not expect all of us to sign on as part of a rush-job for this Board. That is an unfair bait-and-switch for TAB members not equipped by experience or expertise or political heft to cope with. For these reasons, I cannot endorse the Medicaid portion of the TAB report, even though I agree that a number of the suggested efficiencies are worthy of further study by persons with significant Illinois health care policy expertise.

Another reason I disagree with the tone and some of the content of the Medicaid portion of the report is that I think it oversells the potential savings and tries to slant the policy debate in ways that disserve the Governor and limit his freedom of motion. It puts out highly speculative savings as solid projections, and it cloaks the policy changes needed to accomplish those savings as “savings” and “improvements” although we know that those characterizations are either clearly not true (because they are changes in policy rather than efficiencies) or, at best, not sufficiently supported as yet. This sets up the Governor for unfair criticism if he decides not to pursue any of the ideas: he will be criticized for failing to pursue “efficiencies identified by his own blue ribbon committee.” That does not help him at all and I will not be a part of it, no matter how well intended.

I disagree with several areas in the Medicaid portion of the report and I believe they may lead to unintended negative consequences for the vulnerable populations that depend on Medicaid as well as the entire provider system—hospitals, physicians, nursing homes, pharmacists, clinics—all of which are affected by changes to the way Medicaid operates. All opportunities for reductions in Illinois’ Medicaid program must be viewed within the larger context of the role that Medicaid plays in Illinois’ economy. According to an analysis from the Center for Tax and Budget Accountability (CTBA), reductions in Medicaid will likely contribute to increasing the numbers of uninsured, stripping their access to health care, causing Illinois hospitals and other providers to be forced to bear the cost of providing additional charity and uncompensated care to these families.<sup>30</sup> CTBA’s analysis shows that if the state were to cut its Medicaid program, it would reduce the flow of dollars to hospitals, clinics, nursing homes and pharmacies, which in turn would most likely reduce employment, income, state tax revenue and economic output.

In general, I agree with the point by point analysis – tentatively supporting some ideas and strongly opposing others -- contained in the May 8, 2009, Memo to the TAB that was authored and supported by leading advocacy and health policy organizations in this state: Health and Disability Advocates, Campaign for Better Health Care, AIDS Foundation of Chicago, Illinois Primary Health Care Association, Sargent Shriver National Center on Poverty Law, and Illinois Academy of Family Physicians. Many of those positions were further elaborated and supported in whole or in part in testimony to the subcommittee on that date by John Bouman, President of the Shriver Center (a signer of the memo), and by Howard Peters of the Illinois Hospital Association (not a signer of the memo). I was informed of that testimony. Much of what follows here is from those sources, among others I will cite. My specific comments follow:

The introductory paragraph vastly oversimplifies Illinois medical assistance programs that would be affected by the TAB’s recommendations. It describes in general terms the Medicaid federal funding scheme (FMAP). But it fails to mention the State Children’s Health Insurance Program, which funds many of the children covered in the report’s bulk description of “Medicaid.” Those children’s coverage is supported by 65% federal matching funds, and the children that Illinois covers who will be eligible for those matching funds was significantly expanded this past January in the federal reauthorization of the

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<sup>30</sup> Illinois’ Medicaid Program: Financing Challenges in the Face of Federal Medicaid Cuts and a Flawed State Fiscal System,” Center for Tax and Budget Accountability, Heather O’Donnell and Ralph Martire, September 2006.

program. Estimates are that Illinois will realize around \$150 million additional federal funds annually for children's coverage. That money is not accounted for or spoken of in the TAB report.

**In the section, “Medicaid Enrollment,” the report states, “From 2003 to 2008 the Medicaid population grew at an average rate of 7.8% per year, while the population of Illinois grew at only 0.5% during the same time period (see Appendix 1).”** This is not a useful comparison. It would have been adequate to note the expansion in enrollment, which is certainly true. This expansion was a conscious state policy choice that had bi-partisan support and was conducted throughout and in spite of a period of financial stress in the state. It has been an agreed-upon state priority and a worthy one. The comparison to the state's population increase is irrelevant, but very revealing about the bias embedded in the report to which I object. This is a device designed to take on the state's previous policy choices, not to dispassionately examine ways to pursue those choices more efficiently.

Similarly, the report notes that 19% of Illinois people are enrolled in “Medicaid” (which, for the report's purposes, includes all forms of health coverage supported by the state including several that are not technically funded under the Medicaid statute, like children's health insurance), and it notes that this is above the national average. It is unclear why this fact is noted at all. If we assume that Illinois is covering people because it wants to, and that the TAB's job is to identify ways this might be done more efficiently, then what's the point of a loaded comment about the national average? I think the report continues to be infused with rhetoric and views urging new policy directions. That is not the TAB's job. (It is also not clear that the comparison is accurate, since other states may not include non-Medicaid populations in their totals of covered people in the same way that our report defines “Medicaid.”)

In addition to democratically adopted policy choices to expand coverage, Medicaid enrollment growth fluctuates based largely on the economic circumstances of the state – we are in a recession, so more people need the program. Over the past years, more families have become eligible for Medicaid coverage due not only to job loss but also to the concurrent decrease of employer-sponsored health insurance.<sup>31</sup> Illinois decided to step in to help rectify this failure of the private insurance system for low-income workers and their children. The policy choices Illinois has made have been reasonable ones. They are not to be upset just because we are in a recession; indeed, the tough economic circumstances have driven those choices, and I think this has been a wise and appropriate government response to a serious problem widespread in our state. It is highly presumptuous for this Board to question those considered and funded policy choices after two months of surface study, and without be asked to do so.

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<sup>31</sup> See Families USA, Premiums Versus paychecks: A growing Burden for Illinois Workers, October 2008, available at: <http://www.familiesusa.org/assets/pdfs/premiums-vs-paychecks-2008/illinois.pdf> (stating, “Some employers have concluded that they can no longer afford to offer health insurance to their workers and have dropped coverage, driving an increase in the number of uninsured workers. The proportion of Americans covered by employment-based insurance dropped by more than 5 percentage points between 2000 and 2007.... During the same period, the number of uninsured Americans rose from 38.4 million to 45.7 million—an increase of nearly 20 percent. In Illinois, the number of uninsured people under age 65 is now 1,713,000 (approximately 15.2 percent of the non-elderly population).”)

Additionally, it is noteworthy to consider that national health reform will undoubtedly influence the operation of the Medicaid system and the American Recovery and Reinvestment Act of 2009 (ARRA) funds for at least the next 18 months are conditioned upon maintaining or improving enrollment in Medicaid.

**Throughout the “Medicaid Spending” section, the report uses the terms “spending” and “liabilities” interchangeably.** This can lead to confusion and inaccuracy. As the Department of Healthcare and Family Services (DFS) has explained, “liabilities” are the annual amounts obligated within a given year to pay for the health care services rendered to Medicaid beneficiaries during that year. Moreover, according to CTBA, “The most appropriate measure of Medicaid expansion over time is program liability. ...Tracking the total liability amount for a fiscal year eliminates the possibility of counting the unpaid, deferred obligations left over from the prior year.” Looking at liabilities allows an analysis of true usage and cost patterns by factoring out the amount in each year’s budget that actually pays for services rendered in a prior year.

**In the same “Medicaid Spending” section, the report states that “Medicaid is now the largest single state expense in Illinois, accounting for over 40% of general fund appropriations.”** This statement of the expenditure level does not account for the large role of federal funds. It is astonishing that this report does not isolate the state funds spending in Medicaid as its sole focus. The TAB was created to deal with state spending. This report deliberately hides the state spending aspect of Medicaid. The dimensions of this error and its potential to mislead the discussion are substantial. In fiscal year 2006, for example, the state money devoted to Medicaid was 19.4% of state general revenue spending and 18.6% of state funds spent in the entire budget (compared to the 40% that the report uses by including the huge federal portion of the program in its sole statement of Medicaid’s part of the budget).<sup>32</sup> We certainly need to look at Medicaid (and anything else) for potential efficiencies, but we should take care to avoid a false sense of the dimension of the problem. We also need to understand and acknowledge that with our current federal matching rate, we would need to cut \$2.40 of overall Medicaid spending to get \$1.00 of state funds savings.

A unique aspect of the funding situation that the report ignores has to do with hospitals. This was explained in a filing by the Illinois Hospital Association that the report fails to note. Because of unique funding mechanisms, only about 25% or \$1.1 billion of hospital payments is from state funding. And the Hospital Assessment Program also generates NON-State funds of approximately \$735 million for other Medicaid needs, such as long-term care and developmental disability services, in the current fiscal year. All of this is simply subsumed in the report’s assessment of Medicaid spending trends. Failing to focus the report on the spending of state funds therefore fails to accurately address the problem the Governor charged the TAB to address, and it also risks suggesting initiatives that could needlessly endanger these other sources of funds.

**In this same section, the report states that, “Capitated managed care spending accounts for only 2.5% of all Medicaid liabilities.”** This statement is incomplete in that it ignores the significant failures,

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<sup>32</sup> “Medicaid and State Budgets: Looking at the Facts,” Georgetown University Health Policy Institute, Center for Children and Families (May 2008)(state by state chart).



abuses and outright fraud that have attended the history of capitated managed care in Medicaid in Illinois. Illinois is no ignorant stranger to capitated managed care; it has been tried more than once. What looks promising on paper has not performed on the ground, and it is not fair to criticize choices that have been based on real experience. The 2.5% figure is a testament to the open mind of Illinois administrators, who could not have been blamed if they had cut capitated managed care off altogether. The current HMO providers in Illinois appear to be doing their best to improve. It is certainly reasonable for the report to suggest the possible greater use of capitated managed care, but the report's stated commitment to a program that has had a lengthy history of significant practical problems is not justified.

**In this same “Medicaid Spending” section, the report states, “if that growth rate can be reduced to 3% per year, Medicaid liabilities in 2019 would be substantially less....”** This is by far the most troubling statement in the report, because it sets up a standardless savings target and it is not based on any reasonable or responsible factors. First, it is entirely circular, as if to say, “if we spend \$1 billion less on Medicaid we will be able to save \$1 billion.” Fair enough, but that was not TAB's charge, and nobody needs a TAB to tell them something like that. The 3% is stated as Illinois' target growth rate without any substantiation, and, apparently, independent of all the other factors. It is unclear why this “3%” should be the starting point rather than using a thoughtful and careful analysis to arrive at an ending point. It seems to have been picked out of thin air. The reader is not given any citations to research or analysis as to whether 3% is a fair and/or accurate rate given economic and other factors, or comparisons to the private market, the general cost of living, other states, or the federal government. The TAB should produce as many efficiency ideas as it can – the resulting savings are what they are, and the more the merrier. But to start with a false goal and attempt to shoehorn the process into that goal is not proper and was not the charge. Yet if the TAB puts it out there, the Governor will have to answer to it. This is not fair to him.

In the section “Impact of Savings Opportunities,” the report adopts a 7% projected baseline Medicaid growth rate, describes it as “unsustainably high,” and then states that “savings opportunities must cut costs in the short term (while maintaining or improving service effectiveness and quality) *and* substantially slow this growth rate going forward.” (emphasis in the original) However, the reader is not provided necessary information. First, ARRA requires prompt payment in order for Illinois [or any state] to receive the enhanced match rate.<sup>33</sup> That one-time spending on back bills skews these annual growth rates. Also, for all of these figures, it is unclear whether the FMAP funds and the even higher SCHIP federal funds and the hospital assessment and other non-state funds are accounted for in the calculations – that is, we are not seeing projections for the spending of state dollars or trend lines for those dollars. Our job is to look at state funds. The report's fixation on creating a sense of crisis about the overall state and federal Medicaid spending thus clouds the issue rather than clarifies it. Next, it does not make sense to predict endless 7 % annual growth in the Medicaid program when the growth in liability from 2008 to 2009 was just 4.2 percent. Additionally, data from the Illinois Department of Healthcare and Family Services' (HFS) Division of Medical Programs indicate that, “Over the last four years, HFS has been able to achieve an average liability growth of 4.4 percent, lower than the average growth rate for Medicaid programs nationwide of 5.5 percent for the same period. This has been accomplished through the

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<sup>33</sup> The American Recovery and Reinvestment Act of 2009, P.L. No. 111-5

ongoing implementation of efficiency measures.”<sup>34</sup> Moreover, the era of aggressive expansion in Medicaid eligibility and related enrollment is past – we have just come out of it. The report notes this as historical fact, but then fails to account for it in its Medicaid spending projections. Enrollment in the coming years (barring major federally-funded reforms) will now follow ordinary economic and public health patterns, not eligibility changes. It is not correct to project growth based on the enrollment track record of the expansion period. The HFS projections appear closer to the mark.

Lastly, the use of the words “unsustainably high” to describe the Medicaid spending growth rate, stated as a given fact, is a political conclusion and description that TAB was not asked to make. It is also factually unwarranted without more careful analysis and deliberation. The report, if it decided to intrude on political choices in a more even-handed way, could say that this rate of growth, *if it proves true*, “may challenge the state’s decision to assign high priority to these expenditures in the state budget” rather than using the conclusory “unsustainably high,” as if there was no choice about it. I agree that we must find efficiencies in Medicaid, but, as a policy matter, if Illinois wants to sustain these programs and finds a way to do it, then the spending is not “unsustainably high.” I am perplexed at the report’s insistence on characterizations like this, because they are not necessary to the TAB’s work. We all appear to agree that Illinois should alter its Medicaid program in responsible and carefully studied ways that promote efficiency and do not reduce access and eligibility or decrease the quality of care. The additional rhetorical positioning is unnecessary, and it makes me fear that the report may be aimed at goals beyond the TAB’s actual charge.

In general on the issue of Medicaid cost inflation, there is a lack of acknowledgement that Medicaid is part of a larger health care system in this country, so that Medicaid cost inflation is largely just an expression of inflation in the larger system. I am told that Medicaid inflation is consistently several points lower than inflation in the larger health care system of which it is a part (that is, Medicaid liability growth is several points lower every year than the CPI for health care services). Since it seems likely that the entire health care system in this country is headed for reforms aimed at cutting costs (among other things – see President Obama’s comprehensive reform plans, recent public releases from the U.S. Senate Finance Committee, and recent release from the U.S. House Education and Commerce Committee), the Board should at least note the fact that one of the main ways to support reduction in Medicaid costs is to fully support the success of the national reform effort. And, regardless of the Board’s policy preferences in the national debate, it should at least note this source of potentially reduced pressure on state funded Medicaid spending in the near future.

**The Report posits two sets of “Savings Projections,” One by HFS and one by TAB itself.** Both projections use the 7% annual growth rate as representative of the current system and fail to focus on just the state spending in the program. Both use the 3% growth rate as the ultimate target that they reach over five years. As stated above, I reject both of these figures and find these projections to be artificial and potentially damaging. TAB was asked to come up with as many ideas as possible, and we should do so.

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<sup>34</sup> Presentation given by Theresa Eagleson, Administrator, Divisions of Medical Programs, HFS, to the TAB Medicaid Subcommittee, April 10, 2009, at p. 28.

For each of these, the savings are what they are. TAB was not asked to set up an artificial straightjacket against which to judge the state's performance. This approach posits savings that not only are unreal and unrelated to state funds expenditures, but also are an unfair target for Governor Quinn to have to meet and could drive policy choices in ways unrelated to the state's policy preferences and actual health outcomes. Each of the TAB's suggested opportunities should have its own projected potential savings, prefaced with qualifying statements like "If Illinois decides to do this, and if Illinois is able to successfully implement the changes without damaging care, and if the experience here mirrors the experience in XYZ state, then the initiative could produce savings in the range of ABC amount." This would set up a fair value statement for the Governor to consider and a fair potential savings outcome for him to be measured against, and it would not artificially confine the state's policy choices.

Another problem with this section is that the TAB's proposed aggressive savings estimates are not adequately substantiated. The Department of Healthcare and Family Services (DHFS) estimated that the cost/saving recommendations for "care management" between year 1 and year 5 to be \$40 million-\$310 million. The TAB report states that "*more aggressive savings rates are attainable quickly*" and sets the care management goals between year 1 and year 5 at \$95 million-\$855 million, respectively. The TAB staff's assumptions of getting to the higher savings amounts more quickly have not been explained. This is not only unfair to the Governor as a benchmark, but it is also a recipe for forcing the HMO's to deny needed care in order to produce the target number.

**In the Medicaid report section "Promote Cost-Effective Care Management Strategies that Focus on the Health of the Person, Promote Prevention and Wellness, and Provide a 'Medical Home,'" it states, without documentation, that "there is a high rate of emergency room usage in Illinois for all Medicaid beneficiaries."** The report does not adequately note the reality in many Illinois neighborhoods that care is unavailable outside the ER due to a lack of primary care providers, lack of access when sickness strikes outside traditional office hours, and other factors.

The report also does not go deeply enough into the evidence of how Illinois compares to other states. It cites a Kaiser Foundation study, in 2006 and 2007, that inpatient hospital procedures comprised over 45% of Medicaid acute care spending in Illinois compared to the national average of 25%. The chart does not accurately reflect the amount spent on hospital services for states that rely heavily on MCOs for Medicaid and should not be the basis of comparing Illinois to other states and the national average. Additionally, the supposition that Illinois Medicaid relies too heavily on "costly" inpatient procedures is questionable since, according to the nonpartisan Kaiser Commission on Medicaid and the Uninsured, Illinois ranks 42<sup>nd</sup> among states in per beneficiary expenditures (Illinois is at \$4,129 per beneficiary; the national average is \$4,575). In fact, the three states mentioned in the report as having significant success in implementing a broad-based capitated managed care program all have higher per beneficiary expenditures than Illinois (North Carolina \$4,943, Pennsylvania \$4,832 and Wisconsin \$4,440) according to the nonpartisan Kaiser Commission on Medicaid and the Uninsured. This data supports HFS' contention that its management of the fee for service program results in lower costs to the state than if the program relied more heavily on a capitated managed care model. The TAB report should at least mention these factors when suggesting unproven fixes for a program that may not be broken.

**In this same section there is a bulleted statement: “Enhance the Primary Care Case Management (PCCM) system so beneficiaries are given a true medical home, with adequate provider incentives to drive quality of care, prevention and wellness, as well as appropriate patient disciplines to ensure proper health outcomes....” that contains the idea that “incorporating provider risk-sharing such as reductions in PMPM payments, would encourage physicians to provide top care, including adequate hours and access for Medicaid patients.” This same bullet includes the statement that, “HFS also needs to ensure that primary care physicians are making only proper referrals, and it needs to limit doctor shopping within the PCCM system....”** Many of these are good ideas, but I disagree with the tone of this statement as it puts the onus on the Medicaid patient without acknowledging the failings of the larger healthcare system, such as the lack of primary care providers and other health care providers who accept Medicaid. Moreover, the PCCM system limits the beneficiaries’ choices by requiring diagnosis and referral from the primary care doctor. The reality is that there is a shortage of options for Medicaid patients to access primary care; placing additional constraints on them without increasing community supports and primary care provider access will result in patients going without any medical care, leading to cost increases through costly ER visits and acute care hospital stays down the road. Medicaid patients need incentives for accessing preventive care, not penalties.

There is a crisis in the supply of health care providers in the Medicaid system. Until there are adequate rates and payment cycles, any system that imposes penalties on providers will have a net effect of decreasing care by chasing providers out of the system. Our pay for performance initiatives should be incentives, not penalties. Lastly, ARRA specifically conditions its funds on the state ensuring no impediments to enrolling in Medicaid and accessing care.<sup>35</sup>

**In the same section “Promote Cost-Effective Care Management Strategies that Focus on the Health of the Person, Promote Prevention and Wellness, and Provide a ‘Medical Home,’” the next bulleted statement is, “Expand the capitated managed care program, in which managed care organizations assume the full risk for medical care, provide beneficiaries with a quality network of medical providers, and monitor health outcomes to ensure quality of care, prevention and wellness.”** I disagree, at least as to children and working adults. Capitated managed care is based on taking current spending and arriving at a per member per month flat rate. Thus, to accomplish any savings, the

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<sup>35</sup> “Review of the Calculations of Temporary Increases in Federal Medical Assistance Percentages Under the American Recovery and Reinvestment Act,” Department of Health and Human Services (HHS), Office of the Inspector General, available at: <http://oig.hhs.gov/oas/reports/region9/90900075.pdf>, stating, “Section 5000 of the ARRA provides these [FMAP] increases to help avert cuts in health care provider payment rates, benefits, or services and to prevent changes in income eligibility requirements that would reduce the number of individuals eligible for Medicaid.... Pursuant to section 5001(f) of the ARRA, a State is not eligible for an FMAP increase if the State restricted Medicaid eligibility standards, methodologies, or procedures under its State plan after July 1, 2008. In addition, pursuant to sections 5001(f) and (g) of the ARRA, a State is not eligible for an FMAP increase if the State (1) fails to comply with prompt payment requirements, (2) deposits the increased funds in any reserve or rainy day account, or (3) requires increased local government contributions toward the non-Federal share of Medicaid expenditures in a State where local governments are required to contribute.”

Managed Care company has to provide less care overall than it provides now. The problem with the current system for children and working adults is that there is not enough well-child, well-person, preventive and primary care. Illinois needs to invest in *that* care in order to get the longer term savings that come from healthier people, avoided ER visits and avoided hospitalizations. For the managed care organization to make money for itself and save money for the state, it has to provide *less* care in the short term, not more, and thus Illinois will be less likely to get the health outcomes or long-term savings it could get through prevention and primary care. Expansion of managed care to this population should be very carefully studied and cautious.

Capitated managed care for people with disabilities and for seniors is often associated with problems in accessing needed and prescribed specialty care or hospital care. It is not at all clear that the current fee for service arrangement, with the disease management component that already serves a majority of beneficiaries and is producing significant savings, is not the better course. You get the savings and the access to care. Changes to this system must be carefully studied before upsetting this ongoing project in mid-course.

In general, I am cautious about dramatic expansion or mandatory implementation of capitated managed care because of the poor track record of MCOs in Illinois. As detailed in testimony this year to the Senate Deficit Reduction Committee by Health and Disability Advocates, discovery in the case of *Memisovski v. Maram* revealed that well child care at Medicaid HMOs in Cook County was well below that provided in fee for service, and it revealed that the HMOs could not account for the amount of care being provided.<sup>36</sup> One prominent Medicaid HMO (Amerigroup) was found guilty of bilking the state out of hundreds of millions of dollars by not providing care to pregnant women and other enrollees. While this situation may have improved somewhat in the recent past, the Medicaid report should have included this history to caution the reader.

**Under this same bulleted statement the report states that, “this year, only about 2.5% of all Illinois Medicaid liabilities will be for full-risk capitated managed care providers.”** Care should be taken not to mislead the reader into assuming that capitated managed care provides cost-savings unachievable by other methods and that the 2.5% of Illinois Medicaid providers who are full-risk capitated managed care providers achieve greater cost savings for the State than the current PCCM Illinois Health Connect system, while providing equal or better care. The report lacks HFS data showing whether full-risk capitated managed care providers provide quality care at greater savings. Also, as previously noted, some full-risk capitated managed care providers in Illinois have excluded large populations of Medicaid enrollees needing care, such as pregnant women (see the Amerigroup fraud litigation), and thus data in Illinois will not be persuasive until fully cleansed of the effects of this unlawful practice. Until there is clear evidence that necessary care is being provided to children on Medicaid in managed care organizations, I cannot support any significant expansions in this delivery method without much more proof that practices have changed, that the provision of care can be accounted for with monthly evidence of meeting care benchmarks, and that MCOs would risk financial penalties for not providing data.

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<sup>36</sup> *Memisovski v. Maram*, No. 92 C 1982, 2004 WL 18783312 (N.D. Ill. Aug. 23, 2004). The Opinion, other decisions by the court, and many case materials are available in the Sargent Shriver National Center on Poverty Law’s website; see [www.povertylaw.org/poverty-law-library/case/53800/53827](http://www.povertylaw.org/poverty-law-library/case/53800/53827).

**The paragraph under this same bulleted statement reports, without providing substantiation, that other states have had “significant success” in implementing capitated managed care.** I disagree with this unsubstantiated implication that capitated managed care in other states has lower acute care costs than fee for service care with primary care case management in Illinois.

**Another bulleted statement says Illinois should “explore the cost-effectiveness of competitively bidding certain non-emergent, elective hospital procedures ... in areas outside of the capitated managed care program, provided that there is access and quality care is not compromised.”** Given Illinois’ history with selective contracting for hospital services, any such exploration should be undertaken with great caution. In 1984, Illinois implemented the Illinois Competitive Access and Reimbursement Equity (ICARE) program for hospitals, a competitively bid program for hospital procedures. While the program was in place, several hospitals closed, including many in high Medicaid areas, diminishing access to care for beneficiaries. The ICARE program was discontinued in 1991 after litigation was filed against the state and federal government challenging the operation of the program. It seems unlikely, given current rates and payment cycles, that a competitive bidding program for hospital services would result in “lower cost and higher quality.” If a competitive contracting concept is to be explored, it must be done thoroughly and with great caution because of the potential harm to the health care safety net that such a program can inflict.

**Another bulleted statement provides, “Reduce reliance on high-cost emergency rooms for primary care through effective, best-practice diversion strategies,” and further states, “Illinois could also adopt additional strategies to decrease emergency room use, including: Requiring a co-payment for patients that inappropriately use emergent care...”** I oppose Medicaid co-payments. According to Families USA, a sizeable body of research indicates that increases in cost-sharing, such as co-payments, reduce access to necessary care.<sup>37</sup>

Also, the author’s use of the term “inappropriately” is problematic. *Who* will decide whether a use is inappropriate given the lack of primary care providers and the lack of primary care providers who are open during non-business hours? There are reasonable ways to reduce inappropriate ER visits that do not reduce the numbers of doctors in the system or punish rational behavior by people who have no other place to find needed, even if not technically emergent, care.

**Another bulleted statement reports, “implement mandatory care management for all eligible seniors, adults with disabilities and those with mental illness.”** I would urge caution here. People in these categories tend to be intensely suspicious of mandatory programs in which the care manager is not seen as an ally. It is not at all clear that a mandatory program would outperform a voluntary disease

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<sup>37</sup> Families USA citing Martin Chalkley and Ray Robinson, *Theory and Evidence on Cost Sharing in Health Care: An Economic Perspective* (London: Office of Health Economics, 1997); and Joseph P. Newhouse, *Free for All?: Lessons from the RAND Health Insurance Experiment* (Boston: Harvard University Press, 1996 reprint).

management program, like the existing one Illinois already provides. That program can be expanded and marketed better, to reach more people, and it can be implemented in “automatic” ways that establish the relationship without coercion.

**Another bulleted statement provides, “Implement pay-for-performance strategies that will align incentives with quality outcomes.”** I oppose punitive types of pay-for-performance, rather than performance based on incentives. Low-income persons could be harmed if their providers are penalized financially more than others due to their patients being less healthy in general and less able to participate in follow-up care. Pay-for-performance must not induce providers to “cherry-pick” the healthiest patients or deny care for people with complex health issues. Above all, the payment scheme must not further depress the numbers of providers participating in Medicaid.

Focusing on pay-for-performance in isolation will not achieve the anticipated health outcomes and fiscal savings. Instead, I support including pay-for-performance as part of a three-component payment system that also includes an encounter fee and monthly care management fee. Encounter fees pay for the face-to-face time spent with the patient. Care management fees reflect the value of physician and non-physician staff work that falls outside of the face-to-face patient encounters as well as pay for services associated with coordination of care, both within a given practice and between consultant, ancillary providers and community resources.

**The next part of the Medicaid section states, “Reverse the Bias Toward Institutional Care in the Long-term Care System,” and lists several ideas for achieving this goal.** I strongly urge caution in implementing these ideas prematurely. Illinois currently lacks adequate community resources (e.g., quality, affordable housing, adequate number of quality home health aides) to absorb a large exodus of elderly and disabled into the communities. Illinois needs to be responsible to these vulnerable populations and invest in short-term expenditures in order to capture these longer-term cost savings.

**The Medicaid section, “Other Ideas,” includes, “global budgeting” as well as a “section 1115 waiver.”** I oppose global waivers or any version of a block grant or capping of federal funds. The main “flexibility” that states can get within a global waiver is to reduce the benefits package otherwise required by Medicaid law and it can create waiting lists for services. I oppose any policy or waiver that would directly or indirectly (by starving the program of funds) force state officials to cut spending on the program by providing less care or by providing care to fewer people or by paying providers less for the care they provide in a way that damages access or quality. Such a program would be problematic for Illinois in times of economic insecurity, such as the present.

If Illinois were under such a program today, the state would find itself with actual expenditures outstripping the agreed upon trend rate, and the state would be responsible for paying the increased expenses—with 100% state funds or cutting the program. The federal matching grant financing system is the single most important counter-cyclical federal support for state budgets in general, and for the health care needs of lower income children, working parents, people with disabilities and the elderly. Global budgeting would deliberately cap federal funds, depriving the state of this counter-cyclical support and thereby cutting needed revenue, not spending. This is no time for recommending curtailment of the state’s revenue streams.

## Additional Resources for Medicaid Reform

### Organization

### Website

#### *State/Local*

AAR P Illinois	<a href="http://www.aarp.org/states/il/advocacy/">www.aarp.org/states/il/advocacy/</a>
AIDS Foundation of Illinois	<a href="http://www.aidschicago.org/advocacy/index.php">www.aidschicago.org/advocacy/index.php</a>
Campaign for Better Health Care	<a href="http://www.cbhconline.org">www.cbhconline.org</a>
Center For Budget & Tax Accountability	<a href="http://www.ctbaonline.org/">www.ctbaonline.org/</a>
Citizen Action Illinois	<a href="http://www.citizenaction-il.org">www.citizenaction-il.org</a>
Health & Disability Advocates	<a href="http://www.hdadvocates.org/">www.hdadvocates.org/</a>
Illinois Academy of Family Physicians	<a href="http://www.iafp.com/">www.iafp.com/</a>
Illinois Hospital Association	<a href="http://www.ihatoday.org/">www.ihatoday.org/</a>
Illinois Maternal & Child Health Coalition	<a href="http://www.ilmaternal.org/">www.ilmaternal.org/</a>
Illinois PIRG	<a href="http://www.illinoispirg.org/issues/health-care--rx-drugs">www.illinoispirg.org/issues/health-care--rx-drugs</a>
Sargent Shriver Nat'l Ctr on Poverty Law	<a href="http://www.povertylaw.org/advocacy/health">www.povertylaw.org/advocacy/health</a>
Voices for Illinois Children	<a href="http://voices4kids.org/">http://voices4kids.org/</a>

#### *Federal*

Center on Budget & Policy Priorities	<a href="http://www.cbpp.org/">http://www.cbpp.org/</a>
Community Catalyst	<a href="http://communitycatalyst.org/">http://communitycatalyst.org/</a>
Families USA	<a href="http://familiesusa.org/">http://familiesusa.org/</a>
First Focus	<a href="http://www.firstfocus.net/">http://www.firstfocus.net/</a>
Georgetown Center for Children & Families	<a href="http://ccf.georgetown.edu/">http://ccf.georgetown.edu/</a>
Kaiser Family Foundation	<a href="http://kff.org/">http://kff.org/</a>
Robert Wood Johnson Foundation	<a href="http://rwjf.org/">http://rwjf.org/</a>

Signed by the following TAB members:

Dory Rand



## **MINORITY REPORT**

**Author: Stephen B. Schnorf**

**Co-Signors: H. Woods Bowman, Dory Rand, Richard H. Sewell**

Governor Quinn,

Your Taxpayer Action Board has worked hard for the past 60 days. I believe it has been a very necessary exercise, but unfortunately you will hear from well-respected interest groups that they were denied an opportunity for input. Although you are getting some good recommendations from it, I'm afraid we do you no favors.

As a result of our report, you will now be expected by many to implement all of our ideas and save several billion dollars over the next few years, including more than 1.2 billion dollars in FY10 alone and you will be damned by your opponents for failing to do so

Unfortunately, many of the suggestions we make will be difficult almost to the point of impossible to implement. Others, when implemented, will undoubtedly take longer and save less than we have suggested. My best personal estimate is that you will be able to save very little, if any, money in FY10. If I were working on the budget, I would be thrilled if there were \$200 million in actual, achievable FY10 savings. I think it is also important to remember that our suggestions aren't the ordained word, handed down from on high. I believe if you had appointed 30 different people, with 15 different consultants, you would likely be getting a very different set of proposals. Take everything we say to you with some grain of salt.

Many of the savings we project as attainable are in the area of employee salaries (we recommend freezing and cutting them) and benefits (we recommend reducing them, and having employees pay more for them). Those sorts of changes will have to be bargained with your unions. Based on my personal experiences, your largest union will not agree to re-open their one year old, four year contract. Again, based on my experience, you will be able to negotiate savings in these areas, as the State has in the past, but they will be within the context of the existing contract, they will not come easily or quickly, and they will not be a one way street.

Because I know you are limited as to how many thickets you can wade into at any given time, my minority report is an attempt to both suggest some possible time-saving prioritizations and to identify some proposals that just plain may not be worth your time. Still others, presented as simple rational good public policy recommendations, are in fact issues about which well-informed and respected parties will disagree. I also believe we should point out to you the wide range of oxen we suggest you gore. Others in the TAB group disagreed with me on that matter, feeling it was unnecessarily alarmist, so I am including in this minority report a brief list of people and groups that will feel they are inexplicably targeted and/or victimized by our report.

They will include: families and friends of people with serious mental health pharmaceutical needs, families and friends of people currently residing in state-operated facilities for the mentally ill and developmentally disabled, local governments, local school districts, their teachers and the unions that represent them, retired teachers, state university faculty and employees, and retirees, family and friends of nursing home residents who need 24 skilled care, pharmacists, pharmaceutical companies, state employees and retirees and their unions, hospitals, nursing home operators and employees, and many others. At the same time there are groups that will and do believe they are well served by these proposals.

## **Solutions in Search of a Problem**

In three instances at least, I believe you are being directed toward fixing things that probably aren't really very broken, and that might not be a best use of your time and energy. You will also encounter very organized, active opposition from well-run and funded constituencies.

- In the arena of prescription drugs, you are being encouraged to both narrow down the network of available providers and to reduce the dispensing fee currently paid to pharmacists. You are advised that the dispensing fees may well be higher than they need to be and that by limiting the participating providers you can move volume and thereby negotiate lower costs.

In fact, analysis of the data indicates that the Illinois Medicaid prescription program is one of the very best managed, most efficient such programs in the country. I would advise you to be alert to potential unintended consequences of taking something that works as well or better than any anywhere else and trying to make it cheaper. Right now the effort to steer recipients to generic, not name-brand drugs, is working very well. You currently incent pharmacists for helping with that, through a two-tiered dispensing fee.

The real costs in the pharmacy program are in the cost of the drugs, not the cost of dispensing them. Dispensing fees currently represent less than 5% of the total spending on pharmaceuticals. Even a slight negative movement in the generic/brand-name split would cost you far more than could ever be saved by adjusting dispensing fees, and that is the unintended consequence I worry about.

On both proposals, I suggest working closely with pharmacists and the associations that represent them and relying on the advice of your staff in the Medicaid program, who have a reputation of managing the pharmacy program very well.

- Regarding long-term care, you are advised to “re-balance” it. That is a euphemism for cutting funding to nursing homes. Normally I would expect to see as a part of that strategy a recommendation to spend part of the money saved by the cuts on community care type programs but we say “enhance”. The underlying rationale for the recommendation is that because of our rapidly aging population, nursing home spending is spiraling out of control, and those hordes of additional people going into nursing homes will ruin us financially and could be served both better and more cheaply through community programs.

That all makes pretty good sense except for one of the underlying assumptions. Our population is aging. More and more people need the resources of nursing homes and community care programs. But, because of a good gatekeeper program put in place several years ago, and alternatives expanded every year since, they aren't being served in nursing homes. Our Medicaid paid nursing home days of service has decreased in the past 10 years while the number of seniors served in alternative to nursing home community care type programs have increased exponentially.

The current gatekeeper system is working quite well. In the past decade your nursing home costs have only increased about 1.5 percent per year. That is a very good cost increase rate compared to almost any other entitlement program in Illinois State Government, and very different than the community care program, which has grown at about 15% a year.

- You are told in no uncertain terms that our Medicaid program overspends on hospital inpatient, outpatient, lab tests, and emergency room use. In looking at total Medicaid spending that is a conclusion that one might reasonably reach. However, if layers are peeled back and a look taken at State dollars spent on hospitals, you see a different picture. Unlike the normal approximately 50/50 split between State and Federal on expenses (currently temporarily more like 60/40), State dollars spent on hospitals tend to be a closer to a 75/25 split. That is primarily because of the hospital assessment program results in hospital dollars (nominally) sent to the State being returned to the hospitals along with additional federal dollars in rates and other ways.

I caution that care should be taken to not let damage to the assessment program be an unintended consequence of unnecessarily tampering with hospital Medicaid payments. That is especially important because the assessment program generates federal dollars that are used to pay for hundreds of millions of non-hospital Medicaid services. To quote the Illinois Hospital Association regarding Section 1115 Waivers, "such an approach would have enormous, negative consequences that would actually jeopardize, if not eliminate, key funding sources for the State. A block grant approach for Medicaid would lock the State in at its currently poorly funded level while shifting ALL of the risk to the State"

## Why?

One of the recommendations in our report involves GASB (Governmental Accounting Standards Board) 45, a somewhat arcane accounting rule that is followed by Illinois already. No one around the country except consultants (i.e., no state government that I could find) appears to rate GASB as currently an issue of significant importance regarding employee and retiree health benefits. We do no harm by pointing it out, but since it involves no savings over the next 1, 2, or 5 years I don't understand why we included it. In fact, instead of short term savings, we recommend that you spend \$12 billion.

## Pensions Misconceptions

We tell you that expansion of the pension systems' alternative formula to highway maintenance workers is a "distortion" of a formula intended for police officers and firefighters. We neglect to tell you that significantly more highway maintainers are killed or seriously injured in the line of duty each year than officers of the Illinois State Police are. That information casts the "distortion" in a very different light.

Of course the State's future costs for its pension systems can be reduced by reducing benefits, raising the retirement age, and increasing employee contributions. I seriously doubt that you needed this Board to tell you that. I believe those approaches represent policy question to be sorted out among you, the State's unions, and the General Assembly.

Your monumental problem here is not the ordinary cost of the current pension program, it is the staggering amount and carrying costs of the unfunded liability. It is my personal opinion that Pension Obligation Bonds, used properly and for the right purpose represent perhaps the only potential cost-saving measure in that regard.

We advise you that consolidation of pension administration is "likely to meet resistance from the current plan administrators". I believe that will be the least of your problems. The affected beneficiaries, both current annuitants and current employee, feel a sense of security from their representation on the current governing boards. That is where the fight will be, and those individuals reside in droves in every legislative district in the state.

## Privatization/Outsourcing

Throughout we suggest to you that there are savings to be achieved through privatization and/or outsourcing certain work currently performed by state employees, and there may be. We are apparently reluctant to remind you and others that most of the savings from such measures will be achieved by replacing unionized state employees receiving good benefits and wages with employees of private employers receiving lower benefits and perhaps wages.

We also fail to alert you to a most on-point example of the State trying to do just that. The State opened a veterans' home in Anna, Illinois, in 1994 using a private contractor, selected through a competitive procurement. The costs of operating that home were lower than the costs at state operated veterans' homes. AFSCME rather easily organized the workers at the home, since their wages were much lower than state employees wages and eventually went on strike over their inability to reach a satisfactory contract agreement with the private operator. The private contractor incurred enormous expenses bringing in temp nurses and other employees from as far as St Louis, as did the State in providing 24/7 on-site monitors to assure the quality of care. Local nursing homes and hospitals (non-union) were very unhappy that the situation was driving up local wage scales for them. The State had to re-negotiate its contract with the private contractor, eliminating most of the savings, and finally, where I believe future similar efforts will be headed,

"Those who do not learn from history are **doomed** to repeat it" --George Santayana. ...

## Governor signs bill to de-privatize Anna Veterans' Home

August 26, 2003

Gov. Rod Blagojevich has brought Anna Veterans' Home in from the cold, when he journeyed to Anna on Aug. 25 and signed HB 2983. The home, opened in 1994 as the only state facility run by a private company, will now be operated directly by the state Department of Veterans' Affairs.

"It's a great victory for the residents, the workers, the community and the union," Council 31 staff representative Debby Lippincott said. "When we organized the home in 1994, we said the goal was to deprivatize it. Southern Illinois citizens and communities are too often treated like they are second class, and having the only veterans' home not operated by the state was a glaring example."

Members of Local 3280 are celebrating their new status as state employees, which will bring them under the state master contract, greatly expanding their pensions, medical coverage and other benefits.

"The residents believe they'll get better care," said Shelley Ellis, who works at the home and helped organize the union there. "It feels like, downstate, we don't matter sometimes, so it will be good for our entire area."

Blagojevich traveled to Anna for the signing ceremony, casting a welcome spotlight on that community and the home itself.

"Once the workers organized and got a fair contract, the privateers could no longer wring their profits out of the wage levels of the workers," Council 31 Deputy Director Roberta Lynch said.

## Glossary

For some reason we report to you in bureaucrat-speak. I quite openly confess that I don't know exactly what some of our recommendations mean. However, I do understand what many of them mean; to assist you I will provide translations.

1. **Re-design, modify, restructure, efficiency, re-balance, consolidate, manage, re-allocate, "bring into the 21<sup>st</sup> century", minimize, improve, introduce, co-locate, streamline, shift, "determine the appropriate balance", cost-effective, explore, maximize efficiencies=cut**
2. **Enhance, maximize=spend or increase**

I don't understand why some insist on denying that eggs must be broken to make omelets. I suspect it is because many people believe there is such waste in government it should be easy to realize painless savings. The financial circumstances the state is in are dire. We annually spend more than we take in. More and more of our citizens seem to want more services from government. We arguably under fund our schools, definitely under fund our pensions, cost-shift

onto vendors, local governments, school districts, property owners, etc expenses we wish to incur but can't pay, and at the same time tell people "don't worry, government finance is complicated". That is a fairy land in which we no longer dare reside.

You can, and I believe you will, get some savings from the suggestions in this report. It probably won't equal billions and it certainly won't all happen over 12-18 months. Good luck.

Stephen B. Schnorf

## **SPECIAL CONCURRENCE WITH MINORITY COMMENT/TAXPAYER ACTION BOARD REPORT**

**Author: Mark W. Schwiebert**

MARK W. SCHWIEBERT  
3913 – 14<sup>TH</sup> STREET  
ROCK ISLAND, ILLINOIS 61201

June 2, 2009

The Honorable Patrick Quinn  
Governor  
State of Illinois

Dear Governor Quinn:

I take this opportunity to express substantial concurrence with the Report of the Taxpayer Action Board, but with a caveat as to certain suggested opportunities outlined in the Report. The Report raises many excellent suggestions of ways to significantly reduce the cost of state government in a far ranging and comprehensive way. While some of the suggested opportunities would require the pain of cutbacks, others – such as more efficient use of technology to share information, coordinate purchasing, or streamline services – do not require sacrifice so much as adoption of best practices already followed elsewhere.

Of concern in the Report, however, are suggestions regarding possible shifting of current State responsibilities to other levels of government - local or federal. Suggested shifting of Medicaid assisted clients to programs with higher federal participation, and possible redirection of funds from local governments into State coffers, would likely have the unintended consequence of merely relocating deficit problems instead of fixing them. As a former vice president of the Illinois Municipal League and Mayor of Rock Island for 20 years before recently retiring, I can attest firsthand to the adverse consequences of unfunded mandates directed to local government from the State and Federal level. Taking away historic local revenue distributions at a time when cities are hurting more than ever due to recession-driven service demands and revenue losses, would solve nothing. It would instead pass off deficit problems at the State level to local taxpayers. Similarly, shifting costs to the federal level, already faced with soaring deficits, may have less immediate but no less long term adverse consequences.

Opportunities we propose should seek to address the State's financial challenges without burden-shifting to other levels of government in our federal system.

On a more positive note, as suggested in the Report, the opportunities for saving and even making money for the State from sustainable processes and products is considerable. By incorporating green design principals in State buildings and vehicle fleets, we may save millions of dollars statewide. A local example may be found in Rock Island where, through purchase and upgrade of a hundred year old power plant on the Rock River, Rock Island now very conservatively projects saving about \$2 million in energy costs and earning another \$2 million in energy credit sales over the next twenty years. Similarly, with cutting edge research facilities at the University of Illinois and other public and private universities across Illinois, as well as the U.S.D.A. Research Center in Peoria are already developing in Illinois new sustainable products and processes from hydrogen cells to biofuels. The Department of Commerce and Economic Opportunity, working with these institutions, could become an honest broker to position Illinois as a sustainability leader in the U.S. and globally. Since over half of the Fiscal Year '09 deficit is attributable to losses in revenue due to the recession, reversing these losses by packaging our enormous educational and research base for economic development also directly addresses deficit issues.

In closing, it was a pleasure and privilege to serve on the Taxpayer Action Board. Capably chaired by Tom Johnson, staffed by talented professionals, and comprised of experienced and gifted members from across the State, TAB produced a good preliminary blueprint for tackling our State's serious financial woes. With thoughtful follow up by your office and the legislature; we cannot only turn this train around, but begin moving in a positive and prosperous direction for present and future generations of Illinoisans.

I would welcome the opportunity to assist further as may be useful.

Respectfully,

Mark W. Schwiebert