Commission on Government Forecasting and Accountability

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For the Month Ended: October 2023

Inside this Issue

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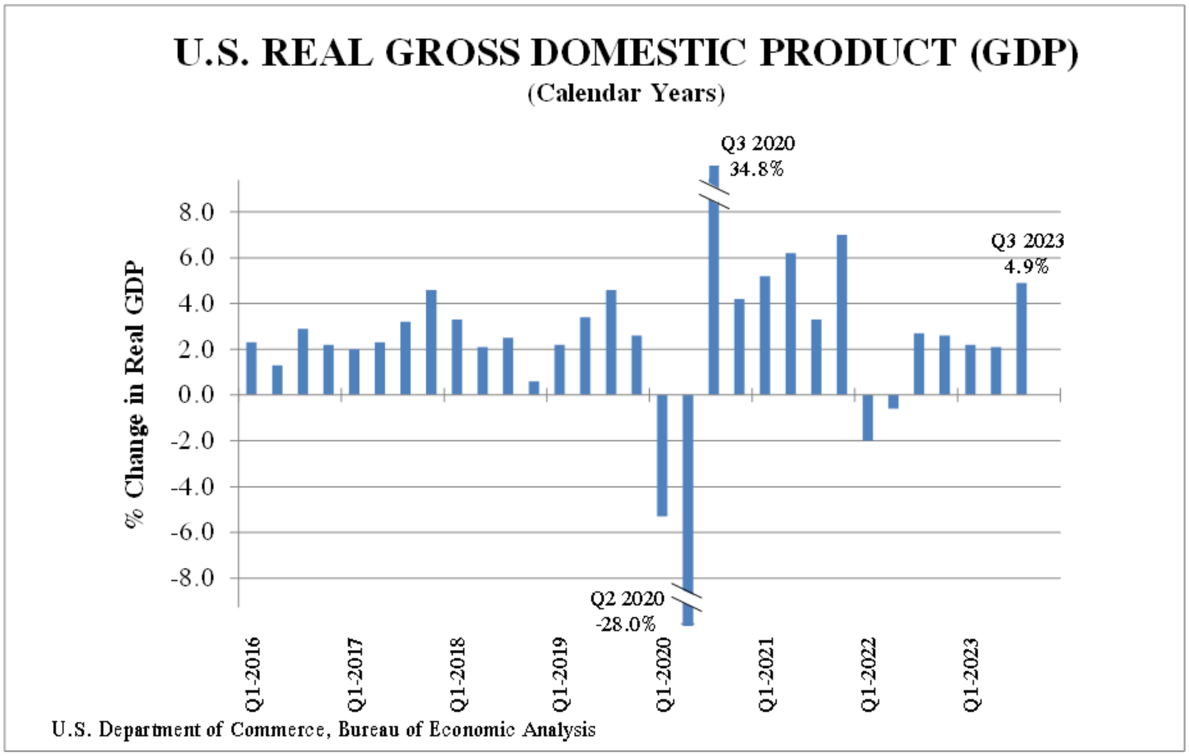
Economy: Stellar Third Quarter

Benjamin L. Varner, Chief Economist

Initial results from the third quarter show strong growth throughout the economy. The Bureau of Economic Analysis released an initial estimate for real Gross Domestic Product (GDP) of 4.9% growth last week. Real GDP is a comprehensive measure of U.S. economic activity that measures the value of the goods and services produced within the United States adjusted for inflation. This was the fastest the U.S. economy has grown since the fourth quarter of 2021 when it grew 7.0%. After that recent high, the nation's economy actually shrank during the first half of 2022. The country returned to solid growth of 2.7% in the third quarter of 2022 and had continued to grow at a slowing pace since then. During the first half of 2023, the economy expanded at just over a 2% rate, which is near the long-term trend, before accelerating in the third quarter. If you exclude the quarters coming out of the COVID-19 pandemic when the economy was reopening in 2020 and 2021, the third quarter of 2023 was the fifth highest growth quarter since 2001. The chart on the following page outlines these changes in economic growth.

Looking at the individual components of real GDP indicates almost universal growth. It shows consumer spending increased at a rate of 4.0%. Similar to overall real GDP, this was the largest increase going back to the fourth quarter of 2021. This robust consumer spending contributed over half of the total expansion seen this quarter. Overall consumer spending on goods picked back up to 4.8% after slowing to just 0.5% during the second quarter. Driven by recreational goods and vehicle sales, expenditures on durable goods increased a hearty 7.6%. Nondurable goods transactions rose 3.3% despite gasoline and



other energy goods actually being down compared to the previous quarter. Consumer spending on services was up an impressive 3.6% which is the highest quarterly rate over the last two years. Service sectors that contributed the most to this growth, in order of contribution, were: (1) Housing and utilities; (2) Health care; (3) Financial services and insurance; and (4) Food services and accommodations.

Business spending on nonresidential fixed investments was the one area of comparative weakness during the third quarter. Investment in structures was basically flat (1.6%) after two exceptional quarters (Q1 - 30.3%, Q2 - 16.1%) of growth powered by government incentives in the manufacturing sector. Equipment purchases decreased 3.8%, led by the continued slowdown in information processing equipment. Outlays for intellectual property products slackened to 2.6% with almost all the associated growth being related to software procurements.

This weakness in fixed business spending was more than offset by a small rebound in residential spending and renewed investment in private inventories. Residential fixed investment, which measures investment by businesses and households in residential structures and equipment (primarily new construction of single family and multifamily units) was up 3.9%. While this did not contribute that much to overall growth, it is a promising sign, as this was the first quarter of growth since the first quarter of 2021. Private business spending on inventories surged in the third quarter contributing 1.3% of the total 4.9% in growth. This growth was somewhat expected as reduced investment in inventory during the first quarter did not appear to be made up during the second quarter.

Net exports of goods and services was a slight drag on the economy but is likely not an indicator of an economy in trouble as both exports and imports increased. Exports increased 6.2% which is up from the -9.3% seen in the second quarter of 2023 but significantly lower than the increases seen during the middle part of 2022. This growth was fueled by 7.5% in goods exports, while service exports were up 3.7%. Total imports were up a smaller 5.7% when compared to exports. However, since imports are consistently larger than exports, the monetary decline in imports was greater than the increase seen in exports, leading to a slight decline in overall economic growth.

Government consumption expenditures and investments were up a brisk 4.6%. Expenditures at both the federal and state/local level equally contributed to this increase. Federal government outflows were up 6.2%. Defense spending, which expanded 8.0%, contributed about two-thirds of this growth, while the remainder can be attributed to nondefense expenditures which grew 3.9%. State and local government disbursements climbed 3.7%. The increase in expenditures at the federal level are primarily related to consumption expenditures, whereas the growth seen at the state and local government level was more a mix of both consumption and investment.

Overall, the economy appears to be humming along. Consumer spending remains resilient, while business spending has slowed some after a busy first half of the year. Residential investment has begun to expand once more, after nine quarters of contraction. Net exports are currently not having a large effect on the direction of the economy as the increases and declines in both exports and imports have been in sync over the past year. Increases in government expenditures are expected to continue to support the expansion of the economy in the coming quarters. Economic forecasters are expecting a slowing of the economy in the fourth quarter of 2023 and into 2024 related to various impediments to the economy (e.g., continued tight monetary policy by the Fed, high interest rates, potential government shut-down, resumption of the repayment of student loans, global political strife). However, economic slowdowns have been forecasted consistently over the past two years because of similar impediments, yet the economy continues to expand. The question continues to be how long can these potential economic hurdles be avoided before a major slowdown occurs.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS*	LATEST MONTH	PRIOR MONTH	A YEAR AGO
Unemployment Rate (Average) (Sep.)	4.4%	4.1%	4.6%
Inflation in Chicago (12-month percent change) (Sep.)	2.3%	2.3%	8.2%

	LATEST MONTH	CHANGE OVER PRIOR MONTH	CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (Sep.)	6,447.5	0.0%	-0.1%
Employment (thousands) (Sep.)	6,165.0	-0.2%	0.1%
Nonfarm Payroll Employment (Sep.)	6,159,000	13,400	79,400
New Car & Truck Registration (Sep.)	34,304	-7.2%	8.4%
Single Family Housing Permits (Sep.)	781	-5.9%	3.4%
Total Exports ($ mil) (Aug.)	6,303.2	-0.9%	-6.0%
Chicago Purchasing Managers Index (Oct.)	44.0	-0.2%	-2.7%

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

A Closer Look: Insurance Taxes and Fees

Anthony Bolton, Senior Revenue Analyst and Sarah Barlow, Senior Research Analyst

As part of this and future monthly briefings, the Commission will include a series of articles providing a closer look at some of Illinois' prominent tax revenue sources. Much of the information included in these synopses is detailed in the Commission's annual publication entitled, "Illinois Tax Handbook for Legislators", which can be found on our website using this link: https://www.ilga.gov/commission/lru/2023TaxHandbook.pdf. This series continues with a closer look at Illinois' Insurance Taxes and Fees.

Insurance Taxes and Fees in Illinois refers to the portion of taxes collected by the State of Illinois involving insurance companies. Depending on the type of insurance offered by a company and whether the company is incorporated in Illinois, their taxes and fees may differ. The following section provides further information on the components of Illinois Insurance Taxes and Fees.

Privilege Tax

This tax is levied on insurance companies and HMOs operating in Illinois. These companies are taxed at 0.4% of net taxable premiums for accident/health insurance and 0.5% for all other types of insurance. Originally, this tax was set at 2%, and was imposed on "foreign" companies (companies incorporated outside the state of Illinois) when it was enacted in 1853. In 1997, this tax was found unconstitutional by the Illinois Supreme Court. A replacement privilege tax (at the current rates and applicability) was enacted in 1998 and now applies to all companies doing business in Illinois, regardless of their state of incorporation.

Fire Marshal's Tax

This tax refers to the tax paid by all insurers who write fire or fire-related policies for Illinois. Currently, this tax is set at 1%. Originally, this tax was enacted in 1909 at 0.5%, before dropping to 0.25% in 1931, then increasing to 0.5% in 1941 and subsequently increasing to its current rate of 1% in 1979.

Surplus Line Producer's Tax

This tax refers to non-standard policies written by companies not licensed to do business in Illinois. An example of such a policy is one written for an amusement park or other entity. Currently, this tax rate is set at 3.5%. As an addendum to this tax, "industrial insureds" that purchase insurance from unauthorized insurers also pay this tax at a rate of 0.5% of gross premiums plus the fire marshal's tax (1%). Historically, the surplus line producer's tax was enacted at a rate of 2% in 1937 before rising to 3% in 1963. The current rate of 3.5% was set by law in 2003.

Workers' Compensation Commission Operations Fund Surcharge

This fee was enacted in 2003 on premiums for employers' liabilities under the Workers' Compensation Act/Workers' Occupational Diseases Act and is imposed on every company licensed/authorized by the Department of Insurance. Originally set at 1.5% of direct written premiums, this was reduced to 1.01% in 2004.

Distribution of Insurance Taxes and Fees Revenues

Insurance taxes and fees, once collected, are distributed to four primary funds. The vast majority of the taxes/fees revenues (such as the Privilege Tax) are distributed to the **General Revenue Fund**. Other fees, such as the plethora of minor fees collected under 215 ILCS 5/408 of the Illinois Insurance Code and up to 2% of the previously discussed charge on workers' compensation premiums, are distributed to the **Insurance Financial Regulation Fund**. The Fire Marshal's Tax is distributed to the **Fire Prevention Fund**. Finally, the fees collected from companies writing workers' compensation and employers' liability insurance policies are distributed to the **Insurance Producers' Administration Fund**.

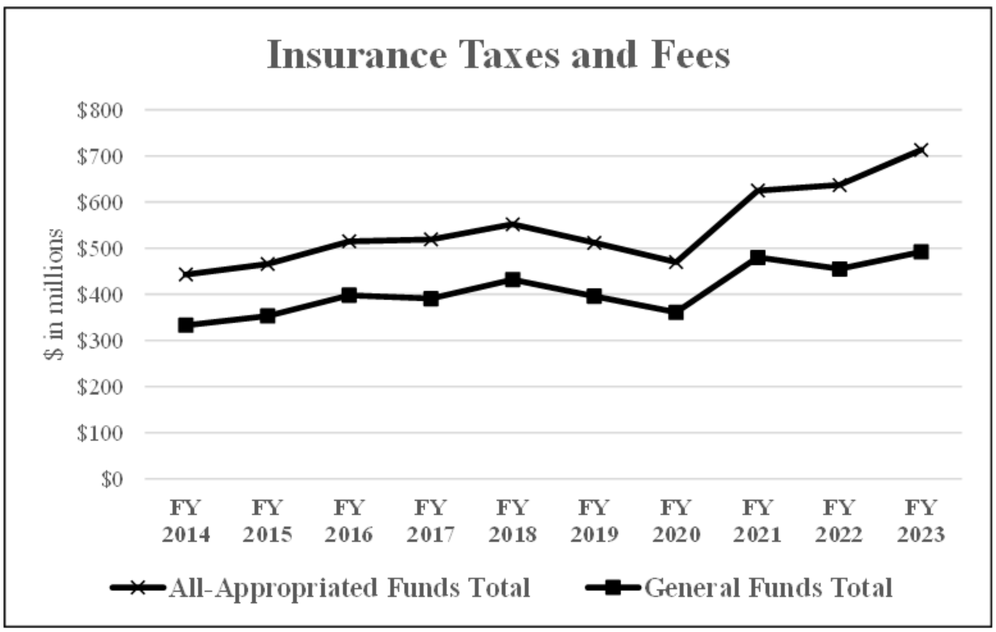
10-Year Revenue History

A historic breakdown of total revenues collected from the taxes and fees described above is illustrated below. Over the last decade, the revenues deposited into the General Revenue Fund (one of the State's General Funds) has ranged from a low of $333 million in FY 2014 to a high of $492 million in FY 2023. The All-Appropriated Funds total for this revenue source has similarly ranged from a low of $443 million in FY 2014 to a high of $713 in FY 2023. While the revenue from insurance taxes and fees has fluctuated over the past decade, it has been on a generally upward trend overall.

In terms of General Funds distributions, Insurance Taxes and Fees in total have averaged an increase of 4.6% over the last ten fiscal years. Over the last five fiscal years, this average has continued to rise, though at a slightly slower rate of 3.7%. In terms of overall revenues (All Appropriated Funds), receipts have grown at similar rates of 5.4% over the past decade and 6.3% over the past five years. The data behind these figures (General Funds and All Appropriated Funds) are illustrated in the following chart and graph.

State Revenue History of the **Insurance Taxes and Fees** *$ in millions*					
Fiscal Year	**General Funds Total**	**% Change**	**All-Appropriated Funds Total**	**% Change**
FY 2014	$333	-0.3%	$443	0.2%
FY 2015	$353	6.0%	$466	5.2%
FY 2016	$398	12.7%	$515	10.5%
FY 2017	$391	-1.8%	$519	0.8%
FY 2018	$432	10.5%	$552	6.4%
FY 2019	$396	-8.3%	$512	-7.2%
FY 2020	$361	-8.8%	$470	-8.2%
FY 2021	$480	33.0%	$625	33.0%
FY 2022	$455	-5.2%	$637	1.9%
FY 2023	$492	8.1%	$713	11.9%

Source: Illinois Comptroller's Traditional Budgetary Financial Report.



<u>Taxes Imposed by Federal and Other State Governments</u>

Various taxes are imposed on insurance companies and their premiums by other states as well as the federal government. For example, in the case of the Privilege Tax, other states have this tax at rates between less than 2% (16 states) to over 3% (4 states), with most exacting this tax at between 2-3% (27 states), while two states have a tax structure not based on percentages of premiums. Most states also have higher tax rates on out-of-state insurers than native insurance companies. The federal government taxes foreign insurance companies at up to 4% of premiums, depending on the type or insurance involved.

General Funds Receipts Rise in October with Large Boost from Federal Sources

Eric Noggle, Revenue Manager

It was an impressive month for revenues deposited into the State's General Funds as total receipts rose $572 million in October. The growth came from a variety of sources with the largest gains coming from Federal Sources. State coffers also benefitted from an extra receipting day in October, which specifically helped boost this month's Personal Income Tax totals.

For the month, the State's General Funds received $1.018 billion in receipts from Federal Sources, which was $531 million higher than last October. However, one of the primary reasons for this large increase is related to delayed reimbursements. In August 2023, it was announced that, after a comprehensive internal review of federal revenue reimbursements in the State's Medicaid related programs, the Illinois Department of Human Services and the Department of Healthcare and Family Services identified a computer programming error that led to incomplete federal Medicaid match claims for service dates between the end of 2020 and June 2022. The State was able to retroactively submit claims for this period of activity, resulting in a "one-time" federal match deposit of approximately $633 million in October. While this money would have been part of previous fiscal years' General Funds "base" total if not delayed, for the purpose of evaluating FY 2024's overall revenue performance, the Commission will separate these funds from "base" federal source dollars in its revenue tables. With this adjustment, "base" federal dollars actually fell $102 million in October.

The performance of Illinois' primary State sources were mixed. Personal Income Tax receipts had an impressive month in October, growing $233 million or +$194 million net of the non-General Funds distributions to the Refund Fund and Local Government Distributive Fund. As alluded to earlier, the "extra receipting day" provided over $200 million to this month's totals, heavily aiding in the source's 11% monthly increase. Corporate Income Tax revenues, on the other hand, fell $16 million [-$12 million net] in a relatively light month for these tax receipts. Sales Tax receipts continue to outpace last year's levels by adding $43 million in growth or +$34 million net of deposits to the Road Fund and certain other transportation funds.

It was another strong month for All Other State Sources, rising a combined $62 million. Again, the gains were led by Interest on State Funds & Investments which rose $48 million during the month. The Inheritance Tax also continued to improve its fiscal year performance, growing $6 million. Other modest increases came from Other Sources [+$8 million]; Public Utility Taxes [+$3 million]; and Insurance Taxes [+$1 million]. There were relatively minor declines in Corporate Franchise Taxes [-$3 million] and Liquor Taxes [-$1 million] for the month.

It was a mixed bag for the State's Transfers In. While Lottery transfers continued its strong FY 2024 with growth of $20 million in October, these gains were erased by declines in other areas. The primary reason for the $237 million decline in overall Transfers In is because last year's $197 million partial transfer from the Income Tax Refund Fund did not recur in October of this fiscal year. In addition, Other Transfers fell $37 million and Cannabis Transfers were flat for the month.

Furthermore, there were no Gaming Transfers from Illinois casinos in October, resulting in a decline of $23 million. This was largely due to the issuance of "hold-harmless" tax credits that were established under P.A. 101-0031 that provided tax credits to older casinos that are now collecting less after-tax adjusted gross receipts than they received in CY 2018. The Illinois Gaming Board reported that approximately $18 million in total tax credits were awarded to seven Illinois casinos due to this provision which was allegedly established to help offset the losses that would potentially occur due to competition from gaming expansion.

Year to Date

Through the first third of the fiscal year, total General Funds receipts are up $611 million. From a base revenue perspective, when accounting for both the removal of $764 million in one-time revenues from last year's ARPA reimbursements and this month's $633 million in one-time delayed federal matching funds, "base" revenues are up a net $742 million through October.

Personal Income Taxes are up $624 million so far this fiscal year, or +$516 million on a net basis. Corporate Income Taxes, however, are down slightly on both a gross basis [-$28 million] and a net basis [-$13 million]. Sales Taxes have risen $98 million through the first four months of FY 2024 [+$56 million net].

All Other State Sources are collectively $154 million higher through October. This is mainly due to the $153 million increase in Interest on State Funds and Investments. In addition, as mentioned previously, the Inheritance Tax is outpacing last year's levels with a year-to-date increase of $44 million. Insurance Taxes are also $13 million higher. The growth in these areas have offset losses from several other State sources, including Other Sources [-$24 million]; the Public Utility Tax [-$22 million]; the Cigarette Tax [-$9 million]; and the Liquor Tax [-$1 million].

The category of Transfers In will be a volatile category throughout the year due to the timing of transfers into the State's General Funds. After last month's Income Tax Refund Fund transfer, receipts for this category were up a combined $233 million through September. However, when accounting for October's activity and the lack of transfers this month from both the Income Tax Refund Fund and Gaming, the growth turns into a year-to-date combined deficit of $5 million. This is despite the $85 million rise in Lottery Transfers through October. This spread will worsen throughout the year, particularly in January, once the remaining $987 million from last year's Income Tax Refund Fund enters into the equation.

Despite the $531 million rise in Federal Sources this month, overall federal dollars are still $96 million lower than last year through October. This is because the FY 2023 four-month totals include $764 million in one-time ARPA reimbursements that did not repeat in FY 2024. From a Federal Sources base perspective, if these one-time ARPA revenues are removed from the equation, along with the $633 million in prior-year federal matching funds receipted in October, year-to-date base growth for Federal Sources is +$35 million (as shown in the following table).

Summary of Receipts

GENERAL FUNDS RECEIPTS: THROUGH OCTOBER

FY 2023 vs. FY 2024

($ millions)

Revenue Sources	FY 2023	FY 2024	$ CHANGE	% CHANGE
Net Personal Income Tax	$6,751	$7,267	$516	7.6%
Net Corporate Income Tax	$1,512	$1,499	($13)	-0.9%
Net Sales Tax	$3,627	$3,683	$56	1.5%
All Other State Sources	$970	$1,124	$154	15.9%
Transfers In	$1,161	$1,156	($5)	-0.4%
Federal Sources [base]	$1,366	$1,401	$35	2.6%
Base General Funds	$15,388	$16,130	$742	4.8%
Non-Base Gen Funds Revenues	$764	$633	($131)	-17.1%
Total General Funds	$16,152	$16,763	$611	3.8%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 1-Nov-23

OCTOBER ***FY 2023 vs. FY 2024*** ***($ millions)***				
Revenue Sources	**Oct. FY 2023**	**Oct. FY 2024**	**$ CHANGE**	**% CHANGE**
State Taxes				
Personal Income Tax	$2,027	$2,260	$233	11.5%
Corporate Income Tax (regular)	300	284	(16)	-5.3%
Sales Taxes	962	1,005	43	4.5%
Public Utility Taxes (regular)	51	54	3	5.9%
Cigarette Tax	20	20	0	0.0%
Liquor Gallonage Taxes	15	14	(1)	-6.7%
Inheritance Tax	43	49	6	14.0%
Insurance Taxes and Fees	1	2	1	100.0%
Corporate Franchise Tax & Fees	20	17	(3)	-15.0%
Interest on State Funds & Investments	15	63	48	320.0%
Cook County IGT	0	0	0	N/A
Other Sources	26	34	8	30.8%
Total State Taxes	$3,480	$3,802	$322	9.3%
Transfers In				
Lottery	$50	$70	$20	40.0%
Gaming	23	0	(23)	-100.0%
Cannabis	9	9	0	0.0%
Refund Fund	197	0	(197)	N/A
Other	84	47	(37)	-44.0%
Total Transfers In	$363	$126	($237)	-65.3%
Total State Sources	$3,843	$3,928	$85	2.2%
Federal Sources [base]	$487	$385	($102)	-20.9%
Total Federal & State Sources	$4,330	$4,313	($17)	-0.4%
Nongeneral Funds Distributions/Direct Receipts:				
Refund Fund				
Personal Income Tax	($188)	($207)	($19)	10.1%
Corporate Income Tax	(43)	($40)	3	-7.0%
Local Government Distributive Fund				
Personal Income Tax	(113)	(133)	(20)	17.7%
Corporate Income Tax	(18)	(17)	1	-5.6%
Sales Tax Distributions				
Deposits into Road Fund	(48)	(52)	(4)	8.3%
Distribution to the PTF and DPTF	(47)	(52)	(5)	10.6%
General Funds Subtotal [Base]	**$3,873**	**$3,812**	**($61)**	**-1.6%**
Prior Year Federal Matching Funds	$0	$633	$633	N/A
ARPA Reimb. for Essential Gov't Services	$0	$0	$0	N/A
Total General Funds	**$3,873**	**$4,445**	**$572**	**14.8%**

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 1-Nov-23

GENERAL FUNDS RECEIPTS: THROUGH OCTOBER

FY 2023 vs. FY 2024

($ millions)

Revenue Sources	FY 2023	FY 2024	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$7,928	$8,552	$624	7.9%
Corporate Income Tax (regular)	1,899	1,871	(28)	-1.5%
Sales Taxes	3,897	3,995	98	2.5%
Public Utility Taxes (regular)	230	208	(22)	-9.6%
Cigarette Tax	83	74	(9)	-10.8%
Liquor Gallonage Taxes	65	64	(1)	-1.5%
Inheritance Tax	161	205	44	27.3%
Insurance Taxes and Fees	133	146	13	9.8%
Corporate Franchise Tax & Fees	77	77	0	0.0%
Interest on State Funds & Investments	72	225	153	212.5%
Cook County IGT	0	0	0	N/A
Other Sources	149	125	(24)	-16.1%
Total State Taxes	$14,694	$15,542	$848	5.8%
Transfers In				
Lottery	$200	$285	$85	42.5%
Gaming	63	31	(32)	-50.8%
Cannabis	38	36	(2)	-5.3%
Refund Fund	493	555	62	12.6%
Other	367	249	(118)	-32.2%
Total Transfers In	$1,161	$1,156	($5)	-0.4%
Total State Sources	$15,855	$16,698	$843	5.3%
Federal Sources [base]	$1,366	$1,401	$35	2.6%
Total Federal & State Sources	$17,221	$18,099	$878	5.1%
Nongeneral Funds Distributions/Direct Receipts:				
Refund Fund				
Personal Income Tax	($734)	($783)	($49)	6.6%
Corporate Income Tax	(276)	(262)	14	-5.1%
Local Government Distributive Fund				
Personal Income Tax	(443)	(503)	(60)	13.5%
Corporate Income Tax	(111)	(110)	1	-0.9%
Sales Tax Distributions				
Deposits into Road Fund	(146)	(184)	(38)	26.0%
Distribution to the PTF and DPTF	(124)	(128)	(4)	3.2%
General Funds Subtotal [Base]	**$15,388**	**$16,130**	**$742**	**4.8%**
Prior Year Federal Matching Funds	$0	$633	$633	N/A
ARPA Reimb. for Essential Gov't Services	$764	$0	($764)	N/A
Total General Funds	**$16,152**	**$16,763**	**$611**	**3.8%**

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 1-Nov-23