

Cook County's Revenue System is Structurally Unable to Support the Public Services it Provides

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Executive Summary

Local governments, such as counties, cities, and townships, provide a number of basic public services that help create safe, clean, healthy, vibrant communities. Cook County, which has over five million residents and is the second largest county in the nation, is no exception.¹ It delivers such essential services as public safety, the operation of the largest court system in the United States, health care for poor and low-income individuals through three public hospitals and 14 community clinics, the operation of the largest jail facility in the nation, and economic and human development programs. The cost of the public services Cook County will provide in fiscal year 2007 is \$2.8 billion.² By comparison, the annual budget for Los Angeles County, which has nearly 10 million residents, is over \$21 billion annually.³

To deliver and sustain quality public services, local government must design and implement a revenue system – that is, a combination of taxes and fees – that adequately funds the services taxpayers desire and consume. Although taxes are often disdained, without them – and therefore, without the financial ability to support public services – our communities would be a far different place.

State and local governments across the country are facing significant fiscal challenges. According to a recent report by the U.S. Government Accountability Office (GAO), the cost of public services provided by local governments is growing at a rate greater than local revenues, resulting in expanding annual deficits.⁴ Annual health care costs, which are increasing faster than three times the general inflation rate,⁵ are the primary driver of this budgetary conundrum.⁶

Cook County is not immune to this trend, suffering through consistent deficits in recent years. In fiscal year 2006 alone, it is estimated that the County's expenditures exceeded revenues by more than \$479 million,⁷ more than double the size of the County's deficit of \$220.2 million in fiscal year 2002.⁸ To address its recurring budget problems, the County Board reduced appropriations for fiscal year 2007 by 11.4 percent, or \$41.1 million.⁹ Nonetheless, the County is expected to have a deficit of \$121 million for its operating budget at the end of the 2007 fiscal year.¹⁰ Moreover, the spending cuts made in 2007 will have negative consequences for County-provided services: fewer criminal prosecutors and public defenders, forcing the criminal justice system to operate at a slower pace and potentially inefficiently. The closing of several health clinics for the indigent will mean less access to health care for the less fortunate. Likewise, the reduction in health care professionals and medical equipment will mean longer waiting lists for medical procedures for low-income, chronically ill patients.

As pointed out by the GAO, on the cost side, local governments are being squeezed by soaring health care costs.¹¹ Cook County, as the largest provider of indigent health care in the state and the third largest provider of such care in the nation, has been significantly strained by rising health care costs. This is compounded by increasing demand for public health care services as the number of uninsured individuals continues to increase annually. According to the most recent report released by the U.S. Census Bureau, the number of uninsured Americans increased by more than two million between 2005 and 2006.¹² Fully 46 percent of all

Chicagoans are either uninsured or receive public health care coverage, up from 42 percent just four years ago.¹³ As employers continue to drop health insurance benefits for workers because of increasing costs – in Illinois, employer-sponsored health care coverage declined by nearly 15 percent between 1979 and 2003, falling from 75 percent of workers receiving employer-provided health insurance in 1979, to only 61 percent in 2003, the latest year for which data is available¹⁴ – public safety-net providers like Cook County are filling in the gap. For example, visits to the network of County hospitals and clinics increased by nearly 200,000 in fiscal year 2005 alone, as the number of prescriptions filled at the County increased by 73 percent between fiscal year 2003 and 2005.¹⁵

Cook County generates revenue to fund local public services from a combination of County-imposed taxes (primarily property, sales, cigarette, and gas taxes) and fees (e.g., federal Medicaid dollars that reimburse the County for medical services provided to Medicaid recipients, court appearance fees and fees for vital records). The majority of Cook County's tax and fee revenues do not grow with the economy, while the costs of the services the County provides do. For instance, the County's property tax levy – the amount of local property taxes it is permitted to collect each year under current law – has remained at the same level – \$720 million – for the past ten years.¹⁶ On an inflation adjusted basis, therefore, using the U.S. Bureau of Labor Statistics' Consumer Price Index, the County's local property tax revenue has lost 23 percent of its value over this ten-year period. The local property tax is the County's main tax revenue source for funding public services.¹⁷

The local sales tax is the second largest tax revenue source for Cook County, accounting for 13 percent of total County operating revenue for fiscal year 2007.¹⁸ However, the local sales tax only partially grows with the economy. The reason for this is that, under Illinois law, the sales tax base generally includes only the sale of goods, while excluding the sale of consumer services. This is problematic from a fiscal policy standpoint because the consumer services sector is the largest and fastest growing sector of the state's economy, while the consumer goods sector of the economy is actually declining.¹⁹ To illustrate, between 1965 and 2004, the sale of consumer services increased from 63 percent of the Illinois state economy to 77 percent.²⁰ Over the same period, the consumer goods sector of the state's economy declined from 32 percent to just 13 percent.²¹ The state's sales tax base is too narrow to track economic growth in the modern economy.

Meanwhile, as health care costs increase annually at rates far greater than regular inflation, federal Medicaid cuts in recent years have resulted in the County losing \$139 million in federal Medicaid funds between fiscal years 2005 and 2007.²² Accordingly, as County cost pressures increase, most of its revenue sources have either remained flat or actually declined in recent years. This ongoing fiscal mismatch between revenues that underperform inflation and service costs that grow at rates above inflation, has resulted in chronic annual budget deficits.

This report analyzes the County's fiscal system to determine whether it has the ability to fund and sustain the level of public services it currently provides. The analysis reveals Cook County has what is called a "structural deficit."²³ A structural deficit exists when a public entity's fiscal system is unable to generate sufficient revenue to support base-level public services from one year to the next, adjusting *solely* for annual inflationary costs. It is important to recognize that the model used in this report assumes service levels will remain constant – that is, when running simulations of the cost of public services into the future, no service expansions are projected from fiscal year 2007 levels. Therefore, the starting point for the analysis in this report is the service levels existing after the cuts made in fiscal year 2007.

Key Findings

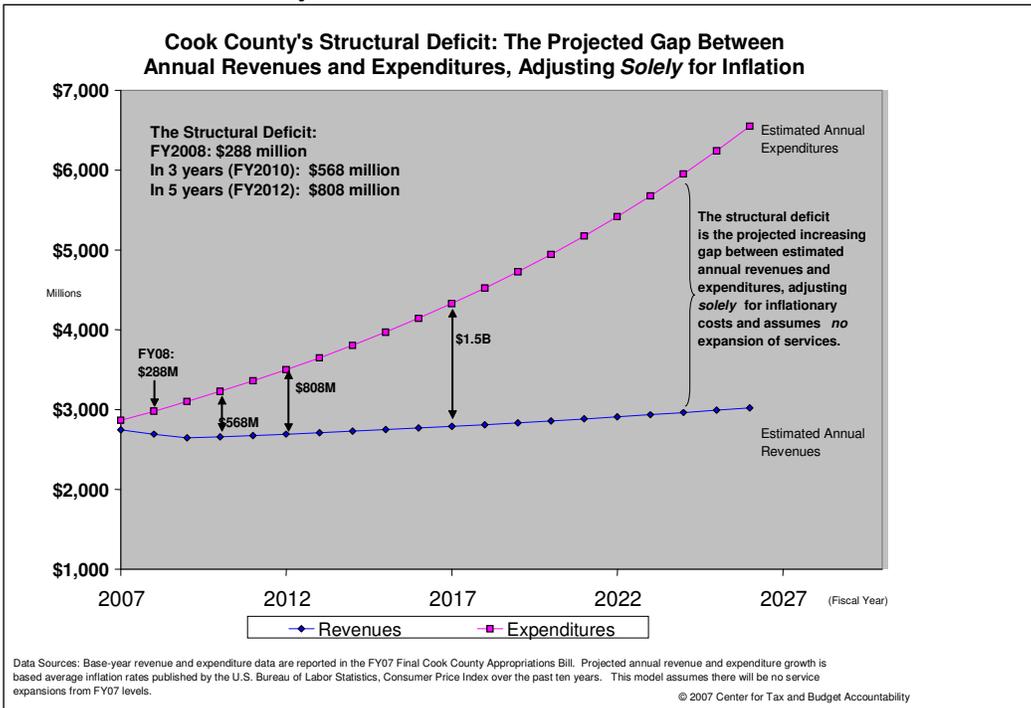
Following are the key findings of this report:

- **Cook County has a structural deficit.** The annual inflationary cost of Cook County continuing to provide current service levels from one fiscal year to the next significantly outpaces its projected annual revenue growth. Moreover, without a significant change in either revenues or expenditures, the County's structural deficit is projected to continue over time, worsening the County's total deficit.
- **The County's structural deficit has contributed substantially to its total deficit for fiscal year 2008, which is estimated to be \$288 million.** As a result of stagnant and declining annual revenues and annually increasing costs based on projections that take into account solely the inflationary cost of maintaining fiscal year 2007 public service levels, the County's structural deficit will cause its total deficit to increase to \$568 million in three years (fiscal year 2010), to \$808 million in five years (fiscal year 2012) and to \$1.5 billion in ten years (fiscal year 2017).
- **The cost of providing public services increases annually with inflation.** Based on historical inflationary trends over the past ten years using the U.S. Bureau of Labor Statistics' Consumer Price Index, the cost for County-provided services other than health care services (primarily public safety and public administration costs), is projected to grow at an average annual rate of 2.6 percent.²⁴ Using U.S. Congressional Budget Office projections, Medicaid costs are expected to grow at an average annual rate of 7.5 percent.²⁵ Cook County's revenue, however, is projected to grow at an average annual rate of only 0.5 percent. Accordingly, Cook County's current revenue system cannot support growing service costs.
- **The principal reason for the County's structural deficit is that the County's revenue system is fundamentally flawed: most of its revenue sources do not grow with the economy while costs do.** This makes it fiscally impossible under the County's current revenue system to fund the level of public services the County currently provides into future years. One primary reason for the disparity between County revenues and costs is that the amount of the County's property tax levy has been held at the same level – \$720 million – over the past ten years. After inflation, this flat revenue source has lost 23 percent of its value since 1997. That decline in value creates a significant fiscal strain for the County since property taxes fund 25 percent of the public services the County provides.
- **As a result of recent federal cuts to the Medicaid program, federal Medicaid dollars, which fund 16 percent of the County's total operating budget, and 51 percent of the County's health care system, declined by \$139 million between fiscal years 2005 and 2007.**²⁶ Under current federal law, it is likely the County will experience more Medicaid cuts in future years.²⁷
- **In fiscal year 2008, it is estimated the County will lose \$68.2 million upon the implementation of new federal Medicaid regulations.**²⁸ These cuts will impact the County every fiscal year thereafter: in 2009 the County's federal Medicaid funds will be cut by \$112.9 million, in 2010, the cuts are expected to amount to \$111.2 million. Over the five fiscal years between 2008 and 2012, the County stands to lose an estimated \$504.9 million in the aggregate.
- **The only revenue source used to fund basic public services in Cook County that grows annually is the sales tax, which funds 13 percent of County-provided services.**²⁹ However, under state law, the County is only permitted to impose a local sales tax on the sale of goods – it does not have the legal authority to tax the sale of consumer services. As a result of leaving a significant portion of the state's economy (consumer services) out of the sales tax base, the County's sales tax does not capture all economic growth.

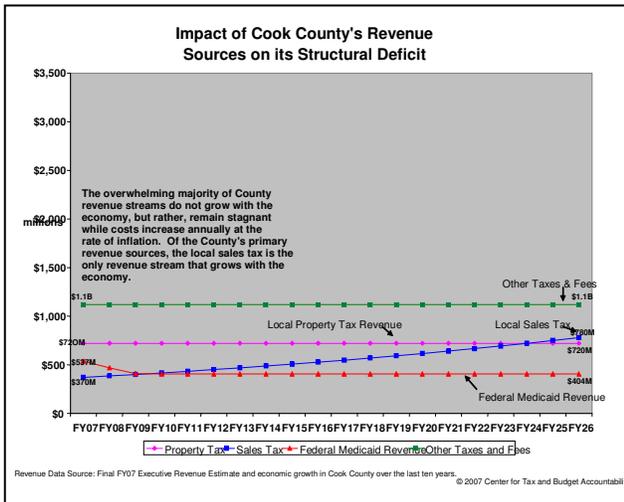
- **Nearly half – 47 percent – of patients in the Cook County health care system do not qualify or are not enrolled in Medicaid or Medicare, and do not have private health care coverage.** Medicaid is the public federal-state health insurance program for poor and low-income families, while Medicare is the federal public health insurance program for senior citizens. This means that the vast majority of care provided by the County is unreimbursed (*i.e.*, very little revenue is realized for this patient population). The fiscal strain this creates for the County is easy to demonstrate: in fiscal year 2006, only 2.6 percent of patient fee revenue came from patients with private insurance or self-pay patients (*i.e.*, patients who do not have private or public coverage). Data was not available on the amount of patient fee revenue received only from the uninsured, but clearly it is less than 2.6 percent of all patient fee revenue.
- **In addition to changes in federal law, there appear to be flaws in Cook County’s Medicaid and Medicare billing practices that inhibit the County’s ability to receive all federal and state funds to which it is entitled.** The County has a public duty to taxpayers to ensure that it bills and collects all Medicaid and Medicare revenue from the state and federal government to which it is entitled for health care services delivered to program enrollees. This is especially true during fiscally strapped times. Based on very conservative estimates, this could generate an additional \$40 million annually once a billing system is put in place at the Bureau of Health Services, the local agency responsible for running the Cook County health care system.³⁰
- **This report did *not* take into account the increasing demands placed on the public health care system as the number of uninsured low- and moderate-income families continues to rise.** Clearly, if the Cook County health care system is expected to cover families in this population, as it has throughout its history, the additional costs will need to be considered.
- **Unless Cook County undertakes fundamental fiscal reform so that its revenue sources grow with the economy and keep pace with the natural inflationary costs of providing public services from one year to the next, it cannot sustain current public service levels.**
- **In conjunction with fiscal reform, the County must implement a billing system at the Bureau of Health that captures all federal and state health care funds to which the County is entitled for public health services delivered.**

Principal Charts

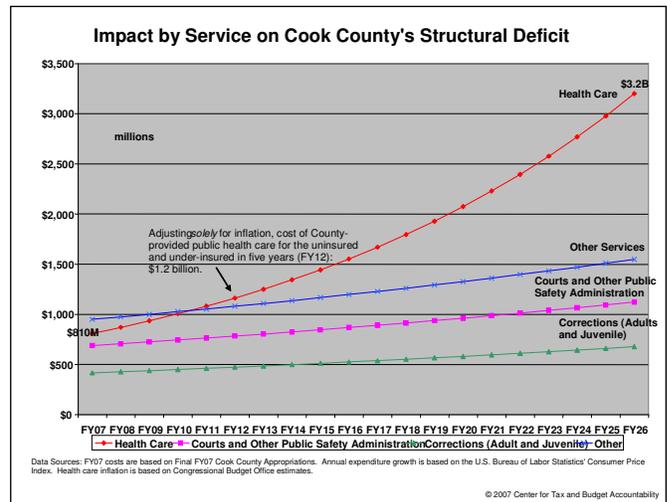
Cook County's Structural Deficit and its Growth Over Time



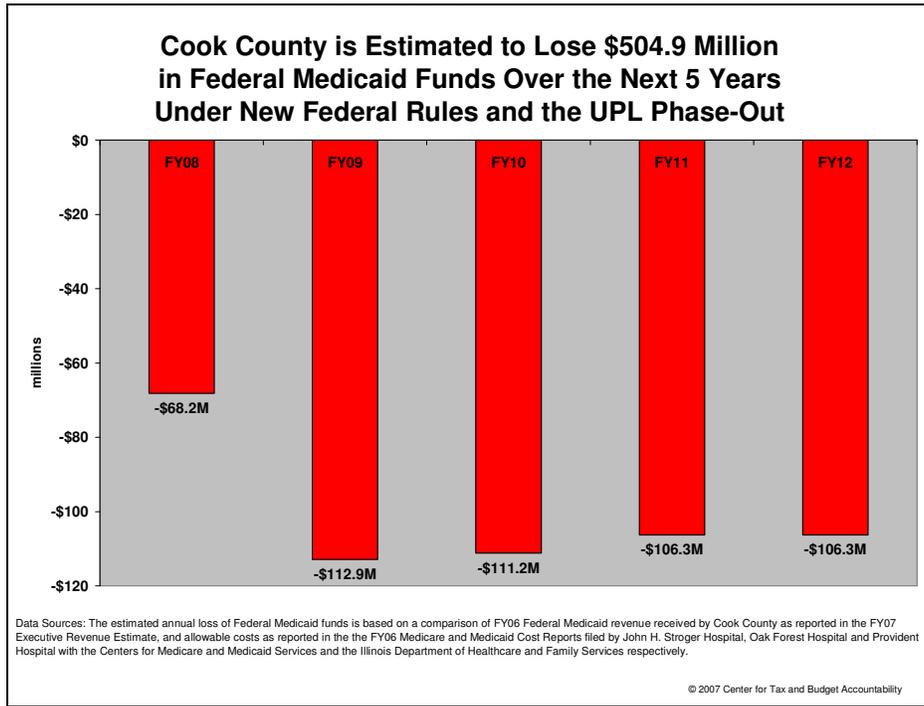
Estimated Annual Revenue Growth by Source



Estimated Annual Inflationary Cost Growth by Service



**The Amount of Federal Medicaid Funds Cook County
is Estimated to Lose Between Fiscal Years 2008 and 2012**



Endnotes

¹ According to U.S. Census Bureau data, Los Angeles County, California is the largest county in the nation, with 9.9 million residents; Cook County is second largest, with over 5 million residents; and Harris County, Texas is the third largest, with 3.6 million residents.

² This amount is the cost of financing the operation of public services for fiscal year 2007, based on the final 2007 Annual Appropriation Bill. It excludes fund balances from the prior year used to fund current year operations, and amounts spent on capital expenditures.

³ Los Angeles County 2007-08 Adopted Budget.

⁴ United States Government Accountability Office, "State and Local Governments: Persistent Fiscal Challenges Will Likely Emerge within the Next Decade," July 18, 2007.

⁵ The Kaiser Family Foundation.

⁶ United States Government Accountability Office, "State and Local Governments: Persistent Fiscal Challenges Will Likely Emerge within the Next Decade," July 18, 2007.

⁷ The FY06 budget deficit is an estimate based on an analysis of the Cook County, Illinois Comprehensive Annual Financial Reports for fiscal years 2002 through 2005 and the Final FY06 Executive Revenue Estimate. The estimated FY06 deficit is based on revenue projections reported in the final Fiscal Year 2007 Annual Appropriations Bill and an increase in expenditures of 2.9 percent for the fiscal year, the smallest increase in annual expenditures in the prior five years.

⁸ Cook County, Illinois Comprehensive Annual Financial Report for Fiscal Year Ended November 30, 2002.

⁹ Final Fiscal Year 2007 Annual Appropriations Bill, Cook County, Illinois.

¹⁰ *Id.*

¹¹ *Id.*, General Accountability Office.

¹² U. S. Census Bureau, "Income, Poverty, and Health Insurance Coverage in the United States: 2006," August 2007.

¹³ Gilead Outreach and Referral Center, "The Face of the Uninsured, A Detailed Description of Illinois' Uninsured," March 2007 (based on March 2006 U.S. Census data).

¹⁴ Northern Illinois University and the Center for Tax and Budget Accountability, "The State of Working Illinois," 2005.

¹⁵ Cook County Executive Budget Recommendation, Fiscal Year 2006, President's Budget Message.

¹⁶ Cook County, Illinois, FY2007 Executive Budget Briefing.

¹⁷ *Id.* See also, Final Fiscal Year 2007 Annual Appropriations Bill for Cook County (property taxes will fund 25 percent the County's operating budget for fiscal year 2007).

¹⁸ *Id.*

¹⁹ Based on U.S. Census Bureau, 2002 Economic Census data.

²⁰ Based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

²¹ *Id.*

²² 42 C.F.R. § 447.272(e)(2) (regulations limiting the use of the Medicaid upper payment limit). The estimated loss between fiscal years 2005 and 2007 as a result of the regulations is based on Medicaid revenue reported in the 2007 Executive Revenue Estimate of the 2007 Annual Appropriations Bill.

²³ The Center for Tax and Budget Accountability developed a model to determine a state or local government's structural deficit with the assistance of economics professor, Dr. Fred Giertz, Executive Director of the National Tax Association, University of Illinois Urbana. CTBA has identified the extent of the structural deficit problem in Illinois in its report "Private Sector Job Trends and the Illinois Structural Deficit," January 2007.

²⁴ U.S. Bureau of Labor Statistics' Consumer Price Index, CPI-U data from 1997 - 2006.

²⁵ Congressional Budget Office, "A Budget and Economic Outlook," 2007; CBO Testimony, Statement of Donald B. Marron, Acting Director of the CBO, "Medicaid Spending Growth and Options for Controlling Costs," July 2006.

²⁶ 42 C.F.R. § 447.272(e)(2) (regulations limiting the use of the Medicaid upper payment limit).

²⁷ 42 C.F.R. § 443, 447, and 457 (limiting Medicaid reimbursement to cost). As the federal regulations state in the Preamble, the new Medicaid cost limitations will not apply to payment under Section 701(d) of the Benefits Improvement Protection Act of 2000, which is commonly referred to as BIPA.

²⁸ *Id.* The estimated annual loss of federal Medicaid funds takes into account the phase-out of the Medicaid upper payment limits and the cost of the new regulations limiting Medicaid reimbursement to cost.

²⁹ Final Fiscal Year 2007 Annual Appropriation Bill.

³⁰ The estimate for additional annual patient fee revenue that could be collected if an efficient billing system were implemented in the County's health care system was based on a review of responses by billing contractors to Cook County's Requests for Proposals and related data. Estimates ranged from \$40 million to \$120 million, net to the County, in annual revenue. The most conservative estimate of \$40 million for purposes of this report. These amounts did not include one-time revenues, but rather, annual recurring amounts.