

Budgeting for Results Commission Meeting

September 7, 2011

12 PM – 2 PM

James R. Thompson Center, 100 West Randolph, 9th Floor, Room 9-040

Illinois State Capitol Building, Room 205

Attendees:

Commissioners Participating (Chicago):

State Senator Dan Kotowski (Chair)

Alex Rorke, Governor's Economic Recovery Commission (Co-Chair)

Cristal Thomas, Deputy Governor

John Kamis, Senior Advisor to the Governor

State Senator Pamela Althof

Carole Brown, Managing Director at Barclays Capital

Alderman Will Burns

State Representative Will Davis

State Representative Kent Gaffney

Larry Joseph, Director, Budget and Tax Policy at Voices for Illinois Children

Jim Lewis, Senior Program Officer at Chicago Community Trust

Lyle Logan, Vice President at Northern Trust Bank

State Senator Tony Munoz

Roger Myerson, Glen A. Lloyd Professor of Economics at the University of Chicago

Maria de Jesus Prado, President at Prado and Renteria

Jose Sanchez, CEO and President of Norwegian American Hospital

Steve Schnorf, Budget Consultant

Commissioners Participating (Springfield):

Kevin Semlow, Director of Legislative Affairs at Illinois Farm Bureau

Commissioner Participating (Telephone):

Donna Sims Wilson, Executive Vice President, Castleoak Securities

Commissioners Not Participating:

Shelia Simon, Lieutenant Governor

John Bouman, President of the Sargent Shriver National Center on Poverty Law

Meeting:

I. Approval of the minutes for the August 19th Meeting

Chairman Kotowski called the meeting to order. He briefly explained the meeting's agenda to the Commission. The first two items on the agenda (or, a presentation by COGFA and a discussion on the scope of the November report) were included in the meeting's agenda in response to recommendations made by Commission members

at the August 19th meeting. Commission moved to adopt minutes from August 19th meeting; minutes were adopted by consensus.

II. Follow up from the August 19th Meeting – Presentation from COGFA

Jim Muschinske, the Revenue Manager at the Commission on Government Forecasting and Accountability (COGFA) gave a presentation explaining the FY 2012 Economic Forecast and Revenue Estimate and the FY 2011 Revenue Review. The presentation consisted of 3 parts: (1) background on COGFA; (2) the current state of the Illinois and national economies; and (3) COGFA's revenue forecasts for FY 2011 and FY 2012. Some of the information in this presentation came from COGFA's August 2011 report and can be located at the following link: <http://www.ilga.gov/commission/cgfa2006/Upload/0811revenue.pdf>.

Jim Muschinske began the presentation by briefly describing COGFA's duties. COGFA functions as a bi-partisan, joint legislative commission. It supports the General Assembly by providing legislators with information relevant to the Illinois economy, taxes, other sources of revenue, and debt obligations. It prepares annual revenue estimates with periodic updates, analyzes the fiscal impact of revenue bills, produces State Debt Impact Notes, conducts a periodic assessment of capital facility plans, annually evaluates the state group health insurance program, annually approves contract renewals promulgated by the Department of Central Management Services, implements the State Facility Closure Act, and provides annual estimates of public pension funding requirements, along with preparing pension impact notes.

One of the most important duties of COGFA, however, consists of analyzing current state revenues to produce a revenue forecast. COGFA experts examine a variety of information about the national and state economies, including: Changes in Real Gross Domestic Product (GDP), Consumer Spending, Construction, Exports, Employment, Unemployment, and several indexes, including the Purchasing Managers Index, Non-Manufacturing Index, Consumer Price Index, and Misery Index.

Changes in Real GDP, Consumer Spending, and Construction data inform COGFA about the general state of the national and Illinois economies. Changes in Real GDP showed that gross GDP grew modestly in FY 2010. Although economic activity has modestly grown in FY 2011, it weakened during the last two fiscal quarters. Consumer spending, which accounts for two-thirds or more of total spending, has only shown modest improvement since the 2008 recession. COGFA believes that many consumers are reluctant to engage in the economy for two reasons: the sharp decline in home prices that resulted after the late-2007 recession, and the "soft patch" that the economy has remained in for the first two years of the recovery. Depressed home prices also contributed to the high levels of unemployment in the construction industry.

Additionally, the Consumer Price Index and the Misery Index provide insight into the current and future state of the Illinois and national economies. The Consumer Price Index for FY 2011 is higher than FY 2010, but the soft patch in the economy, high levels of unemployment, housing depression, and uncertainties about the national and international situations are likely to keep recovery progress minimal. The Misery Index (or the combination of the unemployment rate plus inflation) remains higher than when the United States entered the last recession (at 12.6).

Information about the economic state of Illinois and national businesses derives from the Purchasing Managers Index and the Non-Manufacturing Index. The Purchasing Managers Index indicates that business strength has improved since the recession, although it weakened during the summer of FY 2011, contributing to the current "soft patch" of the economy. The Non-Manufacturing Index shows that consumer business and service sectors of the economy expanded for 19 months throughout February 2011, but that expansion seems to have slowed. Illinois exports continue to improve after the global recession, with Illinois ranking 5th in the nation. Illinois employment shows some gains, but Illinois never recovered jobs lost after the 2001 recession, making the

subsequent recession even more difficult. Illinois' unemployment rate aligns with the federal government (over 9%), and unemployment will continue to pose a problem for the state.

The presentation then briefly addressed how the agency develops its revenue forecasts for FY 2011 through FY 2012. COGFA presented three models to choose from when establishing a revenue forecast: (1) the baseline, or the most likely solution with a 55% chance of occurrence; (2) the optimistic scenario, with a 20% chance of occurrence; and (3) the pessimistic alternative, with a 25% chance of occurrence. The baseline shows a modest pace of recovery, the optimistic scenario shows a v-shaped recovery, and the pessimistic alternative shows a w-shaped recovery. COGFA uses a hybrid of the baseline and pessimistic alternative to make its revenue forecasts.

As an example, COGFA provided an overview of its FY 2011 revenue forecasts. In FY 2011, Illinois grew \$3.398 billion over the previous fiscal year. Tax changes and the tax amnesty program largely contributed to the increase. (\$2.326 billion in growth resulted from higher taxes, and \$315 million in growth resulted from the tax amnesty program.) However, over \$500 million in Federal funding disappeared as a result of less Medicaid matching money. Revenues for FY 2011 grew \$1.903 billion over the initial revenue projections used to create the FY 2011 budget during the previous year. The majority of this growth resulted from the tax changes enacted in the middle of the year. Overall, FY 2011 revenues performed as expected by COGFA.

COGFA's FY 2012 revenue estimate is \$813 million higher than the estimate produced by GOMB. Most of the differences between the two estimates appear in personal income tax and sales tax. COGFA believes that the delayed implementation of the January 2011 tax increase resulted in only a 10% growth in January revenue. COGFA anticipates that when residents file their final personal income taxes, they will account for the withholding that was not adjusted, and revenue will rise again. COGFA also believes that its sales tax estimate (2%) is more accurate than the estimate produced by GOMB (4.7%). COGFA expects personal income tax to grow by over \$4 billion, corporate tax to grow over \$500 million, and base sales taxes to grow only \$7 million in FY 2012. In FY 2012, transfers are anticipated to fall by \$344 million and federal funding sources are expected to fall by over \$1 billion.

Jim Muschinske concluded the presentation by explaining that over \$6 billion of FY 2011 revenues had to be used to pay off old bills. He said that the recent tax increase will not solve the state's fiscal problems. Illinois should expect financial difficulties for the foreseeable future.

Discussion:

Commission members first wanted to know what COGFA expects to happen in the transition years when the income tax disappears. Jim Muschinske explained that over the next two years the income tax will decline, and by FY 2025, it will essentially vanish.

Members then inquired whether the FY 2011 (FY 2012?) revenue estimates take the \$6 billion dollar pension payments into account. Jim Muschinske stated that the estimates did not. In FY 2011, the lapse spending was six months, and it will be the same in FY 2012 until December. **COGFA anticipates improvement of approximately \$1 billion as the number for the balance after lapse in FY 2012.**

Discussion then shifted to the factors that go into compiling COGFA's revenue estimate. Jim Muschinske explained that the first consideration in compiling a revenue estimate revolves around the subjective matter of measuring the anticipated growth rate. COGFA utilizes a variety of resources to produce the concrete data (such as Moodys.com) from which subjective conclusions are drawn. The COGFA Revenue Unit has over 80 years of experience in forecasting revenues. In determining its revenue estimates, COGFA essentially examines at hard data and then makes a subjective decision about where state growth should end up.

Commission members then asked for a concrete number of average annual revenue growth. Jim Muschinske replied that the number would be under 3%. COGFA intends to closely monitor FY 2013. COGFA also wants to closely monitor the economy over the next several months in order to determine whether its current “soft-patch” will linger on for another quarter or whether the nation will end up in another recession. COGFA explained that the next fiscal quarter will impact the future of FY 2013. **COGFA models indicate a potential downshift in the number of individuals actually employed after February or March which could jeopardize decent growth in FY 2013. COGFA does not specifically forecast employment numbers, but incorporates anticipated trends into the overall revenue model. Employment numbers constitute only one element for COGFA’s annual revenue estimate. Caution was also raised from the standpoint of receipt timing. Specifically, while FY 2012 should benefit from annualization of the recent tax increases as well as from implementation timing, FY 2013 will not. As a result, on a year over year percent basis, FY 2013 will be significantly less than each of the two preceding years.**

Lastly, Commission members wanted to know how the current situation facing municipalities and large companies will factor into the state tax. Jim Muschinske hypothesized that consumers will continue to refrain from fully-engaging in the economy. He explained that the economy moves in a circular, not linear, pattern. When a “hiccup” occurs, it reverberates throughout the entire circle. Once things begin to go poorly for the economy, the circle cannot easily be altered. Currently, the national economy experienced a “hiccup” on its road to expansion. Recoveries occur in “fits and starts” and the national economy is currently experiencing those “fits and starts.”

III. Scope of the Report – Chairman Kotowski and John Kamis

Chairman Kotowski and John Kamis explained that the outcomes and subgoals of the report should be finished by early November. After the outcomes and subgoals are completed, the Commission will explore allocations. The OMB staff person responsible for outcomes (Ellen McCurdy) would like feedback from the Commissioners on the proposed outcomes and subgoals. The plan for the next few weeks calls for the Commissioners to divide into groups, compile their recommendations on outcomes and subgoals, and discuss them as a Commission.

Discussion:

Commission members wanted to know how they would communicate about recommended outcomes and subgoals. John Kamis explained that statute binds the Commission to a tight time frame. The Commission, with the consent of its members, can continue to work for another year after submitting its first report. If the Commission consents, then the November report would serve as a preliminary report to the GA, and the Commission would work over the next year to produce a more complete report. BFR takes several years for proper implementation.

Prior to the next meeting, Commission members will send their recommendations on outcomes and subgoals to Commission staff, in addition to ranking their preferences for either the Allocations or the Mandates work-group through e-mail. Feedback on outcomes and subgoals will help determine how the Commission would like to submit its recommendations and should respond to data examining how other states compile their outcomes and subgoals. After submitting feedback to Commission staff, Commission members will receive a presentation about the Committee’s recommendations at the next meeting. The presentation will highlight the areas of general agreement and provide all Commission members with the opportunity to have their opinions heard. The Commission will hold parallel discussions on outcomes and subgoals after submitting its initial feedback.

Other Commission members wanted to learn how the GA will utilize the November report. They were concerned that recommendations made in the initial report might create a framework for future reports that will prove difficult to change. They believed that the Commission's November report might lay the foundation for all future reports, and Commission members did not want to constrain themselves with the framework of the first report. John Kamis explained that the Commission includes members from each of the four caucuses so that the GA will have an understanding of how the Commission constructed its November report and could weigh the report's influence accordingly. The Commission's recommendations can either be accepted or rejected by the GA. The GA is not statutorily required to abide by the Commission's report.

The discussion then moved to the November report's requirement that the Commission review, and make recommendations on, state mandates. The Commission agreed that reviewing 1700 mandates compiled by state agencies proved difficult, and that examining 150 mandates seemed more manageable. The debate centered on whether the Commission should examine controversial or mundane mandates, larger or smaller mandates, or statutory transfer mandates. John Kamis explained that the Commission would receive a chart with the 150 mandates identified by Commission staff, in addition to the 100 largest mandates (in terms of dollar amounts). Commission members agreed that they should examine statutory transfer mandates as part of their November report. Indeed, Commissioners noted that \$2.1 billion of the state budget consists of automatic transfers out and never goes through the appropriations process.

John Kamis identified Allocations as the largest challenge for the Commission. He presented documents compiled by Emily Monk (GOMB) that showed the historical percentages of allocations over the last 6 years and the aggregate spending levels. Other documents show FY 2012 spending break outs by Funds. Another set of documents showed state agencies' last 6 years of budgeted appropriations, with the changes in annual appropriations tracked. John Kamis identified historical percentages as the most important factor for the Commission to consider when preparing to address the allocations component of its report.

Some Commission members expressed concern over these documents. They noticed that pension contributions were not treated separately (and consistently) in the documents. They believed that pension contributions should be set aside each year in order for the documents to reveal the true trends in state spending. Other Commission members wanted the documents to show what the agencies allocated towards outcomes. Some Commissioners questioned the subjectivity (and agenda) of the OMB report.

Discussion then turned to using real budget numbers when making allocations to outcomes. Commission members decided that BFR requires looking at real revenue numbers, not abstract numbers. BFR allocates real revenue to real programs within the state's budget that produce real results that improve residents' lives. The trade-off in using real revenue numbers for the BFR process is that it forces Commission members to meet their recommended outcomes and subgoals with only the available financial resources at their disposal.

Commission staff will provide a draft outline of a report for the Commission to use in compiling its November report.

IV. Strategic Management Reporting Tool – Curt Clemons-Mosby, OMB

Curt Clemons-Mosby (OMB) gave a two part presentation on: Logic Models and SMART. A Logic Model is "an information system that enables an analyst or other non-expert to understand a program's components and establish a measurable result." Logic models assist the analyst in visualizing the flow of the program. Logic models clarify: (1) the components of a program; (2) its customers; (3) the services provided by the program; (4) the immediate products or outputs that the program produces; and (5) the outcomes that the program should generate.

There are five key definitions for Logic Models and Performance Metrics: (1) inputs; (2) activity measures; (3) outputs; (4) outcomes; and (5) programs. Inputs are “the time, money, personnel, and resources that are necessary in order to allow a program to function to its full potential.” Activity measures are “information or data used to quantify the delivery of state services.” Examples of inputs are the number of individuals served or the number of cases closed. Outputs are “the results of program activity.” Outcomes are “reliable and valid translation of activity/output measures that allows observers to see if a program has met its goal.” Lastly, programs are “separately identifiable and managerially discrete functions within an organization designed to meet a statutory requirement or a defined citizen need.” Programs can also be defined as “sets of activities undertaken to realize one common purpose with an identifiable end result or outcome.”

Logic Models can also help to develop performance metrics. Recent state law requires agencies to report metric data to GOMB on a quarterly basis. Agencies will enter data into a web-based mechanism administered by GOMB. GOMB will evaluate the collected data against the outcomes and subgoals by using the SMART system. In this manner, raw data reported by the agencies will be transformed by GOMB into specific information about program performance.

SMART stands for “Strategic Management Accountability Reporting Tool.” It is based on the federal PART system (Program Assessment Rating Tool). Dr. Patrick Mullen at the University of Illinois-Springfield previously developed the PART system and worked with the state to develop the SMART system. SMART consists of 10-part questionnaire completed by GOMB analysts. Each of the ten questions carries a certain amount of weight. GOMB analysts will collect data from agencies throughout the year to answer “yes” or “no” questions related to state programs. GOMB analysts must provide written evidence to support their answers to the questionnaire in order to ensure objectivity. After the scores for the questionnaire have been added, the program receives a rating ranging from “not effective” to “effective.” SMART evaluations, in addition to other policy determinations, will designate the allocation of resources for the following fiscal year.

V. Performance Based Contracting and BFR Implementation – Dr. Laya Suleiman Gonzalez, DHS

Dr. Suleiman Gonzalez gave a presentation about the process of implementing BFR from an agency perspective. The presentation included 5 components: (1) a basic overview of the Department of Human Services (DHS); (2) the Department’s preliminary step in implementing BFR (developing major outcomes); (3) the Department’s first step in implementing BFR (conducting an assessment); (4) the Department’s second step in implementing BFR (compiling measurements); (5) the Department’s third step in implementing BFR (performance-based contracting); and (6) the Department’s fourth step in implementing BFR (outcome based management). DHS provides basic support services (such as food stamps, housing, and cash assistance), as well as development and early intervention, disability and rehabilitation supports, and treatment for infants, children, youth, and adults. DHS has 6 divisions: (1) the Division of Human Capital Development; (2) the Division of Community Health and Prevention; (3) the Division of Developmental Disabilities; (4) the Division of Rehabilitation Services; (5) the Division of Alcohol and Substance Abuse; and (6) the Division of Mental Health.

The preliminary step for DHS in implementing BFR was to develop major outcomes. DHS developed 4 major outcomes: (1) Safety Net and Basic Supports; (2) Prevention and Early Intervention; (3) Community Integration and Maximum Independence; and (4) Resiliency and Recovery. The major outcomes were then divided into more specific results, or subgoals.

Safety Net and Basic Supports subgoals include providing basic cash, medical, housing, food assistance, and work supports to Illinois’ most vulnerable families. Prevention and Early Intervention subgoals include services provided for children and youth. Community Integration and Maximum Independence subgoals assist Illinois residents with physical, cognitive, and developmental disabilities. Resiliency and Recovery subgoals help Illinois residents who struggle with substance abuse and mental illness.

DHS provided Commission members with a sample list of performance metrics that they developed for each of the 6 divisions. These measurements typically included the number of individuals being served by each division. For instance, the number of households served by Medicaid, General Assistance, Aid to the Aged Blind or Disabled, Temporary Assistance to Needy Families, or Non-Assistance Food Stamps were 1.224 million in FY 2008, 1.306 million in FY 2009, 1.448 million in FY 2010, and an estimated 1.597 million in FY 2011. The Department further used performance metrics to identify a growing demand for services at a time when the agency was experiencing a decrease in internal staffing levels to provide those services. For instance, in July 2008, there was a dramatic increase in the need for Food Stamps but there was also a decrease in agency staffing levels. Because only internal staff can process Food Stamps, the Department's capacity to process Food Stamps was diminished at a time of increasing need for these services.

The first step for DHS in implementing BFR was to conduct an Assessment. The Assessment identified General Revenue Funds (GRF) and connected funds to program line items. They first tried to clean up how the line items connected to programs. For instance, one line item may fund multiple programs or a single program may receive funding from multiple lines in the state budget. After connecting funding to programs, DHS compiled current measurements in a program logic format. DHS used the following questions to compile information: (1) OUTPUTS: Who? Where? What? How well?; (2) OUTCOMES: So what? What was the benefit to the individual or family?; and (3) IMPACT: So what? What was the benefit to the society, region, or the state? Performance measures for Outputs included: population and geographical information (such as population research, client characteristics, and location); services (such as types of services, units of service, and unit cost); and quality (such as error rates, client satisfaction, and certification). Output measurements answered two questions: (1) What DHS does; and (2) How DHS does it.

The second step for DHS in implementing BFR consisted of compiling measurements. The Department had to figure out how and what to measure, in addition to how to collect data. DHS collected measurements on data and outputs. Collection methodology included excel reports, paper reports, and web-based reports. Outputs provided the Department with population, size, client characteristics, race, ethnicity, date of birth, and an identification number. This information was combined into one simple number to track results.

DHS also had to consider what type of services and cost measurements it wanted, as well as ways to incentivize quality measurements. DHS decided that if it wanted self-sufficiency, it needed to make an investment in activities to measure outcomes. It utilized the Human Services Commission, a group of experts who thought through the outcomes and subgoals in order to determine how the Department could measure differences in an individual's life.

DHS performed several cost-benefit analyses on its measurements. For instance, every SNAP dollar stimulates the economy by \$1.84. SNAP benefits resulted in \$4.6 billion in economic activity for Illinois. In addition, every dollar spent on child care saved \$13 for the state. DHS worked to figure out opportunity costs. The Department asked the question: 'If DHS did not provide its current services, what problem(s) would result?'

The third step in DHS' process was to conduct performance-based contracting. DHS prioritized its Tier I (high spending items) and moved them to performance-based contracting. It separated its Tier II (less-expensive items) for performance-based contracting at a later time. All of DHS' recent contracts require performance-based contracting. DHS included explicit performance measurements in each contract. The Department lifted some items out of program contracts to determine outcomes. This way, DHS can identify what the contract requires and the specific requirements that providers will be reporting on quickly and in one location.

DHS created a separate section in its FY 2012 contracts that require annual reports from providers. There are seven performance standards for providers in DHS' programs manual. Examples of performance standards for

providers include a facility remaining open 100% of its business days. If a facility is only open 85% of the time, then it is not performing.

DHS additionally established consequences for providers who fail to meet performance standards. For instance, their contracts will not be renewed for the next fiscal year if they are not performing. Instead, their money will be allocated to a higher performing program. An example of this type of situation happened recently with the program Teen Reach. Teen Reach programs and contractors that had been around a long time were better equipped to report data than other programs that recently began providing Teen Reach services to DHS. As a result, the older programs and contractors were allowed to continue providing services and were awarded additional funding for results.

DHS reviewed and refined previous performance measurements and monitored its providers. It used a combination of national and federal indicators, evidence/research based indicators, philanthropic partners, provider partners, and other state performance dashboards to arrive at improved performance and outcome measurement.

The fourth and final step in DHS' implementation of BFR is outcome based management. Outcome based management includes defining DHS' program logic models, improving DHS' performance and outcome indicators, and refining DHS' tracking and reporting system. DHS has not accomplished this final step, but it plans to achieve it in the near future. DHS will need to reform its IT infrastructure, contracts, and capacity building prior to developing a priority outcome that guides its appropriation. DHS wants to link its investments and outcomes in order to have appropriations investments, programs/initiatives, performance indicators, and priority outcomes feeding into each other.

Discussion:

Some members inquired whether DHS' work (particularly administering Food Stamps) could be completed online. Dr. Suleiman Gonzalez stated that some of the work could be conducted online, but stated the Department cannot solely depend on the internet. Some of the new federal health care reforms under the Affordable Care Act will create an online system to help DHS with its daily duties. One project, The Framework, will build agency efficiency by incorporating 6 agencies under one data enterprise system. The system will make processes more efficient across the board.

Other members noted that DHS implemented two years of standards before conducting performance-based contracting. Some of the Department's standards came from the federal government. Dr. Suleiman Gonzalez confirmed that some vendors engaged in a type of performance-based contracting before the Department began requiring it in its contracts. The entire Division of Alcohol and Substance Abuse uses performance-based contracting. DHS believes that all performance-based contracting should follow the Division's model. Standards in the Division come from federal indicators, other state indicators, and providers. The Department was not clear on whether vendors who lost contracts had previously missed payments from the state.

VI. Next Steps, Public Hearings – John Kamis and Chairman Kotowski

Commission members will receive a list of outcomes and subgoals, along with a link of what other states are doing. They are expected to provide feedback to Commission staff on proposed outcomes and subgoals. Commission members will also receive a list of state mandates (including mandated transfers). They will rank what parts of the November report they would like to work on. Commission members will also receive a template of the November report for use as a guideline. Public hearings will be scheduled for the month of October, with one hearing held in Chicago and another hearing held in Springfield.