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MTF Bulletin

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Innovation & Capital Fund Supplemental Budget

Conference Committee Preview

On January 22nd, alongside their budget proposal for Fiscal Year (FY) 2026, the Healey-Driscoll administration filed the first ever Innovation and Capital Fund supplemental budget. The supplemental spending bill appropriated \$1.32 billion in surplus surtax revenues collected in FY 2023 and FY 2024, and like all revenue generated by the four percent surtax on income over \$1 million, these resources are constitutionally obligated to support education and transportation-related initiatives.

The House and Senate have now each acted on their own versions of the supplemental budget, and all differences between the two bills must be reconciled through a conference committee. Conference negotiations for the supplemental budget will be taking place alongside deliberations on the FY 2026 budget, creating new challenges and opportunities for policymakers.

In this bulletin, MTF reviews the major differences between the House and Senate bills, and compares proposed spending to available resources. It also highlights MTF's recommendations for policymakers to ensure that these unique revenues are used strategically and sustainably:

- **Achieve an even divide of surtax revenues between education and transportation** by using Innovation and Capital Fund supplemental spending to complement investments in the FY 2026 operating budget.
- **Provide multi-year support for the MBTA operating budget** and fulfill the major components of the Healey administration's transportation finance strategy.
- **Maximize the impact of supplemental surtax revenues** by supporting innovative strategies that save the state long-term costs or promote cost efficiencies.

Education and Transportation Innovation & Capital Fund

The resources available to policymakers to support the supplemental spending bill are held in the Education and Transportation Innovation and Capital Fund (the "IC Fund"). As MTF has previously [described](#), the IC Fund was created as part of the FY 2024 state budget to collect 85 percent of surtax revenues collected above the "surtax spending cap" set for the annual operating budget.

Between FY 2023 and FY 2024, the state collected a total of \$2.6 billion in surtax revenues and the surtax spending cap in the FY 2024 General Appropriations Act (GAA) was set at \$1 billion. As the table below demonstrates, by the beginning of FY 2025 the balance of the IC Fund had reached \$1.32 billion.

According to statute, revenues deposited into the IC Fund must be used to support one-time and capital related investments for education and transportation. This distinction, between surtax spending in the annual operating budget versus supplemental spending bills is important for several reasons.

First, surplus surtax revenue collections are not guaranteed in future fiscal years. Using essentially one-time revenues to support ongoing costs creates long term challenges for the structural balance of the state budget as a whole, and near-term challenges for the programs that will face funding cliffs when those resources are no longer available.

Second, the education and transportation sectors have unique needs, and to ultimately achieve an even distribution of overall surtax investments between them, maintaining a unique avenue for one-time and capital-related spending is critical. As surtax-supported spending for education increasingly requires a larger share of the surtax spending cap in the operating budget, the Innovation and Capital Fund provides a clear opportunity to make key investments in transportation.

House and Senate Spending Proposals

Like the Healey administration, both the House and Senate presented their Innovation and Capital Fund supplemental budget proposals in partnership with their spending plans for FY 2026. The House finalized its bill the week before the House Ways and Means budget was released, adopting \$1.26 billion in spending supported by the surtax; while the Senate similarly passed a \$1.27 billion bill two days after releasing the Senate Ways and Means budget for FY 2026.

Estimated Balance of the Innovation & Capital Fund

	Governor	House	Senate
Starting Balance	\$1,320.0	\$1,320.0	\$1,320.0
Proposed Supplemental Spending	\$1,320.0	\$1,257.2	\$1,268.9
Remaining Balance	\$0.0	\$62.8	\$51.1

\$ in millions

At a high-level, both bills include roughly the same level of spending, leaving between \$50 to \$63 million remaining in the IC Fund. However, at the line-item level significant spending differences emerge.

One of the first tasks of a budget conference committee is to assess all shared and unique spending across the two bills. This will lead to a “maximum spending” estimate, which can then be compared to available

Above Cap Income Surtax Collections & Distribution

	FY 2023	FY 2024
Total Collections	\$242	\$2,460
Surtax Spending Cap	\$0	\$1,000
Above Cap Surtax Collections	\$242	\$1,460
Distribution of Above Cap Surtax		
EEC Operational Grant Fund	\$0	\$150
85% to the Innovation & Capital Fund	\$206	\$1,114
15% to Surtax Reserve Fund	\$36	\$197
Innovation & Capital Fund Balance	\$1,319	
Surtax Reserve Fund Balance	\$233	

\$ in millions

resources. Between the House and Senate bills, nearly \$1.9 billion in spending has been proposed; a total more than \$500 million greater than the \$1.32 billion available in the IC Fund.

Summary of House & Senate Spending Differences¹

	House	SWM
Total Spending	\$1,257.2	\$1,268.9
Spending in Common	\$645.1	
Unique Spending	\$612.1	\$623.8
Maximum Spending	\$1,881.0	

\$ in millions

Shared Spending Priorities

Of the \$1.9 billion maximum spending estimate, approximately \$645 million supports shared spending priorities; including \$287 million for education-related investments and \$358 million for transportation initiatives. Items that are adopted by both the House and Senate are generally assured to be included in the final bill, at least at the shared spending level.

In the education sector, both the House and Senate include funding for Career Technical Education Capital Grants, Waitlist Remediation for Adult Basic Education and English Language Services, and Early Literacy Tutoring. The largest shared investment between the two branches for education is \$190 million for the Special Education Circuit Breaker

Shared Surtax Spending – Education

Education Program	House	Senate	Shared Spending
CTE Capital Grants	\$50	\$100	\$50
ABE & ESOL Waitlist Remediation	\$9	\$10	\$9
High Dosage Early Literacy Tutoring	\$25	\$25	\$25
SPED Circuit Breaker Reserve	\$190	\$190	\$190
Local Education Projects	\$14	\$21	\$14

\$ in millions

program, which will complement the operating budget funding level for the program in FY 2026. The total projected cost to fully fund the Special Education Circuit Breaker program in FY 2026 is \$682 million.

For transportation, the House and Senate bills reflect \$358 million in shared spending. This includes the same level of investment in RTA Workforce Supports and Low-Income Fare Relief at the MBTA, as well as a minimum level of MBTA reserve spending equal to \$300 million. As further discussed below, the different

¹ MTF's estimate of shared and unique spending includes spending supported by the income surtax. It does not include the \$58 million appropriation for the Special Education Circuit Breaker Program funded by the Student Opportunity Act Investment Fund; nor the \$5 million appropriation for the Boston Holocaust Museum, which the Senate proposes funding with Transitional Escrow Fund resources.

approaches taken to stabilize the MBTA's operating budget will be one of the major challenges faced by conference negotiators during the reconciliation process.

Both chambers adopted hundreds of local earmarks related to education and transportation during the debate process. The majority of these earmarks are unique to each branch; however, for this analysis, earmark spending by category is considered wholistically.

In total, the House bill reflects \$43 million in earmark spending, while the Senate bill includes \$34 million for local projects, programs, and communities.

Shared Surtax Spending – Transportation

Transportation Program	House	Senate	Shared Spending
Low-Income Fare Relief	\$20	\$20	\$20
MBTA Workforce / Safety Reserve	\$400	\$100	\$100
MBTA Reserve Replenishment	\$300	\$200	\$200
RTA Workforce Supports	\$25	\$25	\$25
Local Transportation Projects	\$29	\$13	\$13

\$ in millions

Unique Spending Priorities

Collectively, the House and Senate bills include more than \$1.2 billion in unique spending initiatives, representing at least 65 percent of all proposed spending. Of that total, \$412 million is related to education investments and \$824 million is tied to transportation.

The primary drivers of spending differences in the education sector are related to K-12 education and higher education. In their respective proposals, the House and Senate included funding for large and unique grant programs. For example, the House bill includes a total of \$20 million for public higher education endowment match incentives; while the Senate bill includes \$190 million for higher education capital improvement projects.

In the transportation sector, the largest amount of unique spending is related to the MBTA. The House's supplemental spending bill includes \$473 million in MBTA investments not found in the Senate bill, including additional resources for physical infrastructure improvements, revenue mitigation, and two MBTA reserves. In contrast, the Senate includes \$70 million for the MBTA related to ferry transportation and commuter rail infrastructure improvements.

Other notable spending items not shared between the two bills include a \$50 million grant program adopted by the Senate to provide cost relief to districts whose school construction projects have been impacted by

Unique Spending by Category

Education	House Unique	Senate Unique
Early Education	\$55.5	\$0.0
K-12 Education	\$35.0	\$101.5
Higher Education	\$22.5	\$190.0
Other Education	\$0.0	\$7.3
Total Unique Spending	\$411.8	
Transportation	House Unique	Senate Unique
MBTA	\$473.0	\$70.0
RTAs	\$0.0	\$50.0
DOT	\$10.0	\$205.0
Other Transportation	\$16.1	\$0.0
Total Unique Spending	\$824.1	

\$ in millions

high inflation, a \$55.5 million House investment in early education, and a Senate program that dedicates \$165 million to municipal roadway construction projects.

Ultimately, assessing unique spending across two bills is important because if a program is not adopted by both branches, its funding level is not guaranteed in the final bill. Additionally, when policymakers are constrained by a set amount of available resources – as they are in the IC supplemental budget – unique spending items are most likely to face funding cuts during the conference process.

Proposed Spending v. Available Resources

As demonstrated above, between the House and Senate bills nearly \$1.9 billion in total spending has been proposed. When this maximum spending level is compared to available resources, policymakers are faced with a spending and resource gap of at least \$500 million.

Maximum Supplemental Budget Spending v. Available Resources

	House	Senate
Total Spending	\$1,257.2	\$1,268.9
Spending in Common	\$645.1	
Unique Spending	\$612.1	\$623.8
Maximum Spending	\$1,881.0	
Available Revenues	\$1,320.0	
Difference	-\$561.0	

\$ in millions

As budget writers begin to reconcile the spending differences between their two proposals they will be faced with challenging decisions regarding how the surtax revenues in the IC Fund can be used to fulfill the priorities of each branch, support critical state programs, and make meaningful progress on numerous education and transportation initiatives.

MTF Recommendations

The Innovation and Capital Fund supplemental budget offers policymakers a unique opportunity to make meaningful investments in the state's capital needs, explore innovative solutions to policy problems, and establish a precedent for how to use surplus surtax revenues to sustainably complement other state investments.

In MTF's [testimony](#) before the Joint Committee on Ways and Means regarding how to use the resources in the IC Fund, three high-level principles and three specific spending recommendations were identified for policymakers.

Principles for the Use of Resources in the Innovation and Capital Fund:

1. Achieve an even distribution of surtax revenues between education and transportation using operating budget and supplemental surtax resources.
2. Use supplemental surtax revenues for one-time or temporary costs to safeguard the structural balance of the state budget and maintain a distinct avenue for capital infrastructure investments.
3. Maximize the impact of supplemental surtax revenues by supporting innovative strategies that save the state long-term costs or promote cost efficiencies.

Spending Recommendations for the Innovation and Capital Fund Supplemental Budget:

1. Provide multi-year operating budget support for the MBTA, closing projected budget gaps and allowing the authority to continue making improvements to ridership, service, and safety.
2. Advance the recommendations of the Transportation Finance Task Force to eliminate transportation structural deficits, expand capital spending capacity, and achieve a 50/50 divide of surtax resources.
3. Address the increasing costs of out-of-district special education transportation, which are increasing at a rate unsustainable for the state or local budgets.

With the House and Senate bills now finalized, several of these recommendations have been refined and expanded upon to address the specific spending decisions before the conference committee.

- **Provide multi-year operating budget support for the MBTA, closing projected budget gaps and allowing the authority to continue making improvements to ridership, service, and safety.**

One of the largest differences between the House and Senate bills is the approach taken to stabilizing the MBTA's operating budget over the next several years. The House largely follows the strategy put forward by Governor Healey, dedicating a total of \$1.48 billion to the authority through their FY 2026 operating budget proposal and the Innovation and Capital Fund supplemental budget. The Senate, in contrast, directs \$890 million to the MBTA.

MBTA Funding Proposals, House v. Senate Budgets

	House	Senate
FY 2026 Operating Budget	\$687	\$500
Supplemental Surtax Spending	\$793	\$390
<i>MBTA Physical Infrastructure</i>	\$60	\$0
<i>Low-Income Fare Relief</i>	\$20	\$20
<i>MBTA Workforce / Safety Reserve</i>	\$400	\$100
<i>MBTA Reserve Replenishment</i>	\$300	\$200
<i>Revenue & Traffic Mitigation</i>	\$13	\$0
<i>Water Transportation Infrastructure</i>	\$0	\$20
<i>Commuter Rail Infrastructure</i>	\$0	\$50
Total Funding for the MBTA	\$1,480	\$890

\$ in millions

The transportation finance plan adopted by the House is expected to close 90 percent of the MBTA's projected operating budget deficits over the next three fiscal years, with the authority expected to close the remaining ten percent. The Senate anticipates its proposed spending level would only close the MBTA's projecting operating budget gap in FY 2026.

MTF strongly urges conference negotiators to provide multiple years of operating budget support to the MBTA. By alleviating the authority's budget pressures in the short-term, policymakers can ensure that long-term and sustainable improvements to MBTA service and safety remain on track – a major accomplishment.

- **Achieve an even distribution of surtax revenues across the education and transportation sectors using operating and supplemental surtax resources.**

Like the Healey administration, the House was successful in evenly dividing surtax revenues between education and transportation through their FY 2026 operating budget and supplemental budget proposals. In contrast, surtax spending in the Senate's bills was more heavily weighted towards education. MTF encourages conference committee members to adopt a spending plan approach that moves closer towards a 50/50 divide of surtax revenues.

Proposed Surtax Spending in FY 2026: House v. Senate

	House	% of Spending	Senate	% of Spending
Education	\$1,590	50%	\$1,740	55%
Transportation	\$1,622	50%	\$1,435	45%
Total Surtax Spending	\$3,212		\$3,175	

\$ in millions

Ultimately, reaching an even division of surtax revenues between the two sectors will require a larger share of spending in the supplemental budget to be dedicated towards transportation, including the MBTA.

- **Maximize the impact of supplemental surtax revenues by supporting innovative strategies that save the state long-term costs or promote cost efficiencies.**

The state's operating and capital budgets face myriad resource and cost pressures, many of which specifically impact the education and transportation sectors. Surplus surtax revenues present policymakers with new opportunities to address these pressures and identify novel strategies to achieve long-term state finance goals. Two proposals included by the House and Senate, respectively, speak to these opportunities and deserve consideration for the final bill.

- **Out-of-District Special Education Transportation** – The House bill includes \$250,000 for the Office of the Inspector General to conduct a general review of student transportation services and provide recommendations to reduce costs and maximize the purchasing power of districts.

Proactively seeking recommendations to reduce costs in future fiscal years is a responsible and forward-looking initiative. In future spending bills, this proposal could be bolstered by one-time implementation and capital grants to districts to pilot or expand new solutions for providing student transportation more cost effectively, or by partnering with education policy researchers to assess viable options for improvements.

- **Higher Education Capital Investments** – The Senate proposes using \$190 million to address a portion of the deferred maintenance backlog at public institutions of higher education. Dedicating a substantial portion of surplus surtax revenues towards public higher education capital is a worthwhile investment. When campus infrastructure and buildings deteriorate, it threatens their ability to serve the needs of students and the state’s future workforce. In future fiscal years, MTF strongly urges policymakers to securitize a dedicated stream of surtax revenues for higher education. Through a permanent allocation of resources, the administration anticipated the ability to support the issuance of up to \$2.5 billion in Special Obligation (SO) bonds over the next ten years. Ultimately, that will allow lawmakers to build on this initial investment and make large-scale progress on deferred maintenance needs across Community College, State University, and University of Massachusetts campuses.