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# MTF Bulletin

March 26, 2026

## Fiscal Year 2027 Budget: A Closer Look

### *Surtax Spending in Governor Healey’s Operating Budget and Innovation & Capital Fund Supplemental Budget*

The Healey administration filed its Fiscal Year (FY) 2027 budget on January 28<sup>th</sup>. The Governor’s \$63.36 billion operating budget proposal increases spending over the FY 2026 General Appropriations Act (GAA) by \$2.3 billion (3.8 percent).

The revenue foundation for the Governor’s budget is the \$44.9 billion consensus revenue estimate, which includes \$2.7 billion in income surtax revenue.

Like in FY 2026, the administration also filed a Fair Share supplemental budget proposal to allocate \$1.15 billion in additional surplus surtax revenue that is currently held in the state’s Education and Transportation Innovation and Capital Fund. This will be the second year that this supplemental budget vehicle is being considered alongside the Governor’s operating budget proposal, and again, many of the investments proposed in the Innovation and Capital Fund supplemental budget are intended to complement funding levels in her FY 2027 spending plan.

Across the Governor’s FY 2027 budget and her supplemental budget proposal, there is a total of \$3.85 billion in surtax-supported spending.

### *Income Surtax Investments in the Governor’s FY 2027 Budget & 2026 Supplemental Surtax Bill*

	FY 2027 – Gov.	I&C Supp. Budget – Gov.	Total Funding	% of Total Surtax Spending
Education	\$1,725	\$358	\$2,083	54%
Transportation	\$975	\$785	\$1,760	46%
<b>Total Investments</b>	<b>\$2,700</b>	<b>\$1,153</b>	<b>\$3,853</b>	

*\$ in millions*

On March 18th, the House finalized their version of the Innovation and Capital Fund budget. In total, the House proposes spending \$1.29 billion<sup>1</sup> from the Innovation and Capital Fund, \$835 million for

<sup>1</sup> The House’s version of the Innovation and Capital Fund supplemental budget included \$1.29 billion in spending from the Innovation and Capital Fund and \$560 million in non-surtax supported spending.

transportation and \$455.6 million for education. When the House takes up their FY 2027 operating budget proposal next month, MTF will expand on this analysis to explain how the spending proposed in the House supplemental budget complements overall investment in education and transportation.

In this brief we will provide a review of surtax collections and spending since its implementation, a wholistic look at the investments proposed across the Governor's two bills, and note areas where the House's supplemental budget follows or differs from the Governor's proposal. We will also pose some key questions for the Legislature as they move the FY 2027 budget process forward.

### **Setting the Stage – Review of Surtax History & Process**

Following the passage of a ballot initiative in November 2022, the state instituted a new four percent income surtax on individuals whose income is over \$1 million<sup>2</sup>. As required by constitutional language, the new revenue must support increased state investment in our education and transportation systems.

In the FY 2024 state budget, policymakers established a system for collecting and distributing surtax resources. During the consensus revenue process the administration and the legislature agree to cap the amount of surtax revenue that can be spent in each year's operating budget. This cap is intentionally set lower than expected collections, which allows for a level of protection against uncertainty and for the growth of surtax trust funds.

Surtax revenue that is collected above the operating budget cap is divided between the Innovation and Capital Fund (85 percent) and a surtax reserve fund (15 percent). The resources set aside in the Innovation and Capital Fund can then be used to support additional supplemental, one-time investments.

Though the surtax has quickly become a key piece of the Massachusetts budget picture, it is important to remember that it is still a relatively new source of revenue. FY 2027 will be the fourth year that the surtax has been used to support spending in the state's operating budget and only the second year that surplus surtax collections have also been spent through a surtax supplemental budget. Policymakers also currently have only two full years of surtax collections, FY 2024 and FY 2025, to build expectations around.

The next section will detail how surtax collections have been distributed in the past few budget cycles and what that means as we look at the budget proposals for FY 2027 and beyond. For additional information on the process established to implement the surtax, please see MTF's report on [FY 2026 Budget Surtax Spending](#).

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<sup>2</sup> The surtax threshold increases annually for inflation, for tax year 2025 the threshold is \$1,083,150.

## Looking Back and Forward – Surtax Collections & Spending

### Overview of Surtax Revenue Projections & Collections

When the income surtax was first implemented, there was uncertainty surrounding the level of revenue that would be generated and how stable surtax revenue would be over time.

The majority of surtax revenues are collected through non-withheld income taxes, which are closely tied to stock market performance. Therefore, like capital gains revenue, the revenue from the income surtax is likely to experience some level of volatility and we could see significant declines in revenue during an economic downturn.

Surtax collections have exceeded expectations thus far, just passing \$3 billion in FY 2025; but there is still limited data to assess collection trends over the coming years. This continued uncertainty presents a clear challenge for policymakers as income surtax spending trends have only grown since the implementation of the surtax.

*Income Surtax Collections, FY 2023 – FY 2025<sup>3</sup>*

	FY 2023	FY 2024	FY 2025
Surtax Revenue – Withheld Income	\$52	\$362	\$461
Surtax Revenue – Non-Withheld Income	\$294	\$2,054	\$2,588
<b>Total Surtax Revenue</b>	<b>\$346</b>	<b>\$2,416</b>	<b>\$3,049</b>

*\$ in millions*

### Overview of Surtax Spending

The table below provides a summary of total surtax spending to date, through both the General Appropriations Act (GAA), and the Innovation & Capital supplemental budget.

*Income Surtax Spending, FY 2024 – FY 2027*

	FY 2024	FY 2025	FY 2026	FY 2027 - Gov
General Appropriations Act (GAA)	\$1,000	\$1,300	\$2,400	\$2,700
Innovation & Capital Supplemental Budget	-	-	\$1,320	\$1,153
<b>Total Investment</b>	<b>\$1,000</b>	<b>\$1,300</b>	<b>\$3,720</b>	<b>\$3,853</b>

*\$ in millions*

<sup>3</sup> Based on FY 2025 surtax certification, surtax collections are divided 85 percent in non-withheld income and 15 percent in withheld income for FY 2023 and FY 2024 collections.

In FY 2024 and FY 2025, budget writers set conservative operating budget spending caps of \$1 billion and \$1.3 billion, respectively. Using this new revenue source, policymakers supported large new education programs – like free community college, universal school meals, and child care operational grants – and increased state investment in public transportation infrastructure and workforce development.

In FY 2026 and FY 2027, policymakers agreed to increase the surtax spending cap in the operating budget by more than \$1 billion, setting the cap at a level equal to total surtax revenue projections in both years. At the same time, two large Innovation and Capital Fund supplemental budgets were put forward using surplus reserves that were built up in prior years when the operating budget spending cap remained low.

As written about in MTF’s report on the [FY 2027 Consensus Revenue Agreement](#), this creates two significant challenges for using surtax equitably and sustainably:

1. Incorporating a majority of surtax collections into the operating budget and shifting the costs of major programs onto the surtax, threatens the long-term structural stability of the overall state budget.
2. Allocating a growing share of the surtax in the operating budget also leaves fewer resources for the Innovation and Capital Fund to be able to invest in critical capital and infrastructure projects, especially in the transportation sector – threatening the goal of dividing surtax revenues equally between education and transportation.

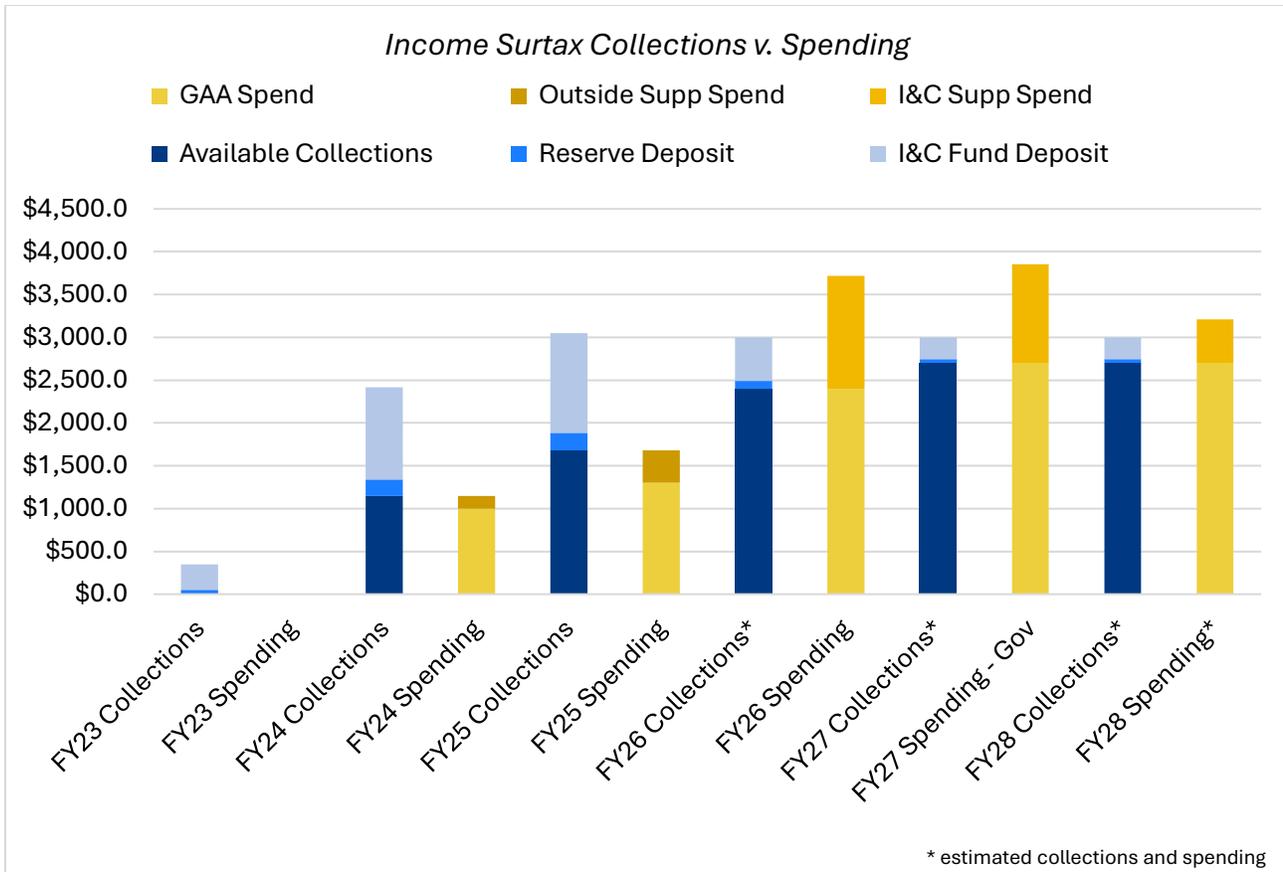
### *Implications of Surtax Collections & Spending Trends*

For the first few years of surtax collections, budget writers were conservative in their use of the surtax in the state budget. However, in FY 2026 and FY 2027, budget writers agreed to spend nearly the entirety of expected surtax revenue in the operating budget. This trend puts us on the path to a surtax spending cliff that policymakers will have to contend with in the near future.

MTF has tracked surtax collections and spending decisions since FY 2023 and broken them down in the chart below.

Surtax collections for FY 2026 and FY 2027 represent an estimate based on a scenario where the state collects roughly the same in surtax as in FY 2025 (approximately \$3 billion).

For this exercise, MTF also estimated FY 2028 surtax collections to be level at \$3 billion and assumed the surtax spending cap for the operating budget would be level with the FY 2027 cap of \$2.7 billion. Following the approach taken in prior years, the funding available for policymakers to use in the FY 2028 Innovation and Capital supplemental budget would equal the FY 2026 deposit into the Innovation and Capital Fund. These assumptions allow us to demonstrate the reality facing policymakers in future fiscal years as surtax revenues and spending begin to moderate.



Reading this chart there are three main takeaways:

- The conservative surtax spending caps in FY 2024 and FY 2025 left sufficient funding for two large supplemental spending bills in FY 2026 and FY 2027.** – The operating budget spending caps in FY 2024 and FY 2025 allowed significant deposits into the Innovation and Capital Fund, over \$1 billion in both years. Budget writers chose to spend nearly the entirety of these reserves to support supplemental surtax spending in FY 2026 and FY 2027.
- When we combine surtax spending in the operating and supplemental budgets, in FY 2026 and FY 2027 the state will spend almost \$4 billion in surtax revenue each year, creating a major imbalance between surtax revenue and spending.** – The state budget is left at the edge of a surtax spending cliff as we are now spending almost \$1 billion more than we expect to collect in surtax revenue annually. We will not be able to sustain this level of surtax spending growth going forward, as can be seen in the chart for FY 2028 where total surtax spending would be only slightly higher than \$3 billion in MTF’s scenario.
- A greater shift of surtax revenue onto the operating budget in FY 2026 and FY 2027 means a more constrained picture for supplemental spending in FY 2028 and beyond.** – The decision by budget writers to allocate \$2.4 billion and \$2.7 billion of surtax revenue in

the operating budget in FY 2026 and FY 2027 means that there will be much smaller ongoing deposits into both the surtax Reserve Fund and the Innovation and Capital Fund. Therefore, we are unlikely to see a large supplemental budget in FY 2028, which has implications for all surtax spending, but especially for continued investment in capital projects and innovative initiatives.

Budget writers will ultimately have to make some hard decisions starting in the next budget cycle as they contend with the need to bring overall surtax spending back down and with the reality that surtax has been used to support many large ongoing programs and initiatives in the past few years.

### **Surtax Spending in the Governor’s FY 2027 Budget**

Governor Healey’s FY 2027 operating budget relies on \$2.7 billion in revenue generated by the surtax; consistent with the income surtax spending cap agreed to by the administration, House, and Senate during the consensus revenue process. This represents a \$300 million increase over the \$2.4 billion in surtax-supported spending included in the FY 2026 GAA.

*Surtax Spending in the Governor’s FY 2027 Operating Budget*

	<b>FY 2026 GAA</b>	<b>FY 2027 – Gov.</b>
<b>Education</b>	<b>\$1,688</b>	<b>\$1,725</b>
<i>Early Education</i>	\$661	\$636
<i>K-12 Education</i>	\$760	\$853
<i>Higher Education</i>	\$267	\$236
<b>Transportation</b>	<b>\$712</b>	<b>\$975</b>
<i>CTF Transfer</i>	\$550	\$975
<i>RTAs</i>	\$162	-
<b>Total Investments</b>	<b>\$2,400</b>	<b>\$2,700</b>

*\$ in millions*

The Governor proposes spending \$1.7 billion in the education sector (64 percent) and \$975 million in the transportation sector (36 percent) in her operating budget. As written in previous MTF publications, this imbalance in the operating budget is to be expected as investments in the Innovation and Capital supplemental budgets tend to lean heavier towards transportation rather than education, which can be seen in the next section on the supplemental budget.

When spending is combined across the two bills, the division between education (54 percent) and transportation (46 percent) surtax investment is closer to an even divide. Including the Governor’s proposals for FY 2027, since FY 2024 57 percent of total surtax spending has gone to education and 43 percent has gone to education.

*Education v. Transportation Operating Budget Surtax Spending*

Fiscal Year	Education	Transportation
FY 2024 GAA	52%	48%
FY 2025 GAA	59%	41%
FY 2026 GAA	70%	30%
FY 2027 – Gov.	64%	36%

Across the Governor’s proposals for surtax spending in the operating budget, three key themes emerge: (1) maintaining existing programs and core commitments in the education sector, (2) leveraging the surtax to maximize the state’s borrowing capacity for transportation and infrastructure, and (3) alleviating budget pressure felt from maintaining programs with growing costs across both sectors.

*Maintaining Core Education Programs with Limits on New Spending*

A majority of the Governor’s surtax spending in the education sector goes to funding five large programs: the Student Opportunity Act (SOA), the Commonwealth Cares for Children (C3) grant program, Child Care Financial Assistance (CCFA), universal school meals, and free community college.

These investments maintain key priorities of the administration but do not leave much room for any significant new areas of investment. The Governor proposes increased funding for the Commonwealth Preschool Partnership Initiative (CPPI) to expand pre-K access to more Gateway Cities not yet participating in the program, but this is the main area of growth seen in the Governor’s operating budget surtax spending for education.

*Top 5 Education Programs in Surtax Spending in Governor Healey’s Operating Budget Proposal*

Program	FY 2027 – Gov.
Student Opportunity Act	\$550
C3 Child Care Grants	\$360
Child Care Financial Assistance	\$244
Universal School Meals	\$198
Free Community College	\$137
<b>% of Education Surtax Spending</b>	<b>86%</b>

*\$ in millions*

The Governor also allocates surtax revenue to support her Reimagining High School initiative, K-12 early literacy, school transportation reimbursements, mental health supports, higher education financial aid and the State University SUCCESS program.

Overall, when it comes to education, surtax funding in the operating budget largely goes to maintaining key state commitments, like funding the final year of SOA implementation and funding sustained levels of access to other programs in the education system. Following the first few years

where surtax spending in the budget was new and we saw several programs being created using the new source of funding, the Governor’s proposal reflects the reality that surtax revenue is leveling out and that spending is increasingly spoken for in the operating budget.

*Continued Use of the Commonwealth Transportation Fund to Maximize Investment*

The Governor proposes a transfer of \$975 million in surtax revenue to the Commonwealth Transportation Fund (CTF) in her FY 2027 operating budget. This builds off a proposal that was first adopted in the FY 2025 GAA and represents a \$425 million increase to the transfer that was adopted in the FY 2026 budget. In FY 2027, the Governor outlines that the \$975 million will be distributed to the MBTA, the Massachusetts Department of Transportation (MassDot), and Regional Transit Authorities (RTAs).

*Governor’s Proposed Distribution of the Surtax CTF Transfer*

Surtax Distribution	FY 2027 – Gov.
MBTA	\$470
MassDot	\$220
RTAs	\$185
Other	\$100
<b>Total Transfer to the CTF</b>	<b>\$975</b>

*\$ in millions*

Of note is that the Governor proposes spending the total \$975 million transfer and does not propose reserving a portion of the transfer for CTF debt service payments, as was done in previous years.

As MTF has written previously, this dedication of surtax revenue into the CTF to support transportation spending is a thoughtful strategy to establish a reliable ongoing stream of revenue to expand the state’s borrowing capacity for transportation and capital spending that does not place limits on what is spent in the operating budget. The strategy is also consistent with the recommendations put forward by the state’s Transportation Funding Task Force (TFTF) which proposed that a significant portion of surtax revenue should be dedicated to the CTF to expand the state’s capital spending capacity.

*Using the Surtax to Alleviate Budget Pressure*

Across both the education and transportation sectors of the Governor’s operating budget, the surtax is being used to support a larger share of longstanding, high-cost programs.

- Child Care Financial Assistance (CCFA)** – The Governor funds CCFA at a total of \$1.2 billion in FY 2027 and allocates \$244 million in surtax revenue in her operating budget and another \$150 million of surplus surtax in her supplemental budget to support the program in FY 2027. Taken together, about 33 percent of CCFA’s budget is supported with surtax funds in the Governor’s proposal. Unlike in prior years where surtax funding for CCFA was directed towards specific expansion initiatives or rate increases, in FY 2027, the Governor is using

surtax to support program maintenance that was historically supported by General Fund resources.

- **Human Services Transportation** – The Governor funds human services transportation at \$450 million in FY 2027, \$100 million of which is being supported by surtax funds through the CTF. Previously, funding to support human services transportation was divided between multiple agencies, mainly MassHealth. Once again, we see the Governor proposing the use of surtax revenue to fund services that have been historically supported through General Fund resources.
- **Chapter 70 State Aid** – The Governor funds the state’s Chapter 70 program at a total of \$7.6 billion in FY 2027. Of that, \$550 million comes from the surtax. Chapter 70 Aid and the completed implementation of the SOA is one of the state’s largest commitments, making up about 11 percent of the Governor’s total spending figure in her FY 2027 budget. In the Governor’s proposal almost 13 percent of the cost of Chapter 70 is supported through surtax or one-time trust funds, illustrating the challenge budget writers face in continuing to support such a crucial program.

These examples illustrate a continuing tendency we have seen in recent years to shift maintenance funding for core programs onto the surtax as costs increase, thereby alleviating similar pressures in other areas of the budget. We will return to this trend in the concluding sections of this report where we can see an increased reliance on the surtax to support increases in education and transportation spending.

### Supplemental Surtax Spending from the Innovation & Capital Fund

Governor Healey’s 2026 Innovation and Capital Fund supplemental budget, filed on the same day as her FY 2027 operating budget proposal, spends \$1.2 billion in surplus surtax revenue that was collected in FY 2025.<sup>4</sup> This is about \$166 million less than what was appropriated through last year’s Innovation & Capital Fund supplemental budget.

*Surtax Spending in the Governor’s Innovation & Capital Fund Supplemental Budget*

	2025 I&C Supp. Budget	2026 I&C Supp. Budget - Gov	2026 I&C Supp. Budget - House
<b>Education</b>	<b>\$561</b>	<b>\$363</b>	<b>\$456</b>
<i>Early Education</i>	\$46	\$150	\$189
<i>K-12 Education</i>	\$378	\$190	\$199 <sup>5</sup>

<sup>4</sup> Separate from her operating budget and Innovation & Capital supplemental budget, the Governor also proposes using \$200 million in surplus surtax to support research at public higher education institutions in response to federal funding declines in that area as part of her DRIVE initiative.

<sup>5</sup> House Innovation and Capital Fund supplemental budget spending for K-12 includes \$8 million in spending adopted during House debate for non-local earmark line-items.

<i>Higher Education</i>	\$137	\$23 <sup>6</sup>	\$38
<i>House Debate Spending</i>	-	-	\$29
<b>Transportation</b>	<b>\$758</b>	<b>\$790</b>	<b>\$834</b>
<i>MBTA</i>	\$548	\$645	\$740
<i>MassDOT</i>	\$16	\$80	\$30
<i>RTAs</i>	\$50	\$60	\$25
<i>Other/Local Transportation</i>	\$144	-	\$30
<i>House Debate Spending</i>	-	-	\$9
<b>Total Investments</b>	<b>\$1,319</b>	<b>\$1,153</b>	<b>\$1,290</b>

*\$ in millions*

In the Governor’s supplemental budget, education receives 32 percent (\$363 million) of available resources and transportation receives 68 percent (\$785 million). However, because surtax spending in the operating budget is skewed more towards education, taken together, the Governor’s two proposals divide total surtax investments more evenly, 54 percent to education and 46 percent to transportation. The Governor’s proposal is a more even distribution than we saw at the conclusion of the FY 2026 budget cycle where education received 60 percent and transportation received 40 percent of surtax resources across the two proposals.

In their supplemental budget, the House spends 35 percent (\$455.6 million) of surplus surtax revenues on education and 65 percent (\$835 million) on transportation. A majority of the investments proposed by the House largely mirror those included either in the Governor’s proposal or in last year’s final Innovation and Capital supplemental budget, with some additional spending for income-eligible CCFA, higher education scholarships, and the MBTA.

#### *Supporting the MBTA*

By far the largest appropriation found in the Governor’s Innovation & Capital supplemental budget is a \$523 million transfer of surplus surtax resources to the MBTA’s deficiency fund. The Governor also directs another \$122 million to the Workforce and Safety Reserve to address staffing shortages and support safety initiatives. MTF categories these investments as one-time in our analysis of the supplemental budget, but the funding transferred to the MBTA’s accounts will ultimately be spent on operating costs in FY 2027. The total funding dedicated to the MBTA in FY 2027, if maintained in FY 2028, would allow the authority to close the full projected budget gap in FY 2027 and provide more budget stability in FY 2028. The House exceeds the Governor’s proposed investment by providing a total of \$740 million for the MBTA in their supplemental budget, broken down below.

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<sup>6</sup> Includes \$5 million transfer to the Spinout Success Fund.

*MBTA Investments in the Innovation & Capital Fund Supplemental Budget*

	<b>2025 I&amp;C Supp. Budget</b>	<b>2026 I&amp;C Supp. Budget - Gov</b>	<b>2026 I&amp;C Supp. Budget - House</b>
MBTA Reserve/Operating Subsidy	\$300	\$523	\$525
MBTA Physical Infrastructure	\$40	-	\$60
Low-Income Fair Relief	\$20	-	\$20
MBTA Workforce & Safety Reserve	\$175	\$122	\$125
Water Transportation Infrastructure	\$13	-	\$10
<b>Total Investments</b>	<b>\$548</b>	<b>\$645</b>	<b>\$740</b>

*\$ in millions*

These proposals demonstrate the continued strategy to utilize the surtax and the Innovation and Capital Fund to support the stabilization of the MBTA. Across the Governor’s operating and supplemental budgets, about 29 percent of surtax revenue is directed towards the agency.

MTF supports the use of the surtax to provide multi-year funding for the MBTA to improve funding predictability, however it should be noted that the continued use of the Innovation and Capital Fund to make large transfers to the authority raises sustainability concerns as the fund’s balance will likely be diminished in the coming years. Identifying other strategies to support operating funding for the MBTA will be key as surtax collections level out and surplus reserves that have been especially used to support transportation are drawn down.

*Operating v. One-Time Spending*

When the Innovation and Capital Fund was created, it was intended to support one-time and capital-related expenditures. In the Governor’s proposal this year, a majority of funds appropriated in the supplemental budget are dedicated towards one-time uses.

*Operating v. One-Time Spending in the Innovation & Capital Supplemental Budget*

	<b>One-Time Spending</b>	<b>Operating Spending</b>
2025 I&C Supplemental Budget	79%	21%
2026 I&C Supplemental Budget – Gov.	74%	26%
2026 I&C Supplemental Budget - House	71%	29%

MTF categorizes 74 percent of the Governor’s spending in the Innovation & Capital supplemental budget as one-time and 26 percent as operating spending. The operating spending in the Governor’s proposal is found in three areas:

- **Adult Basic Education (ABE) & English for Speakers of Other Languages (ESOL)** – The Governor dedicates \$5 million to reduce the waitlist for ESOL services and expand training capacity. ABE also receives \$58 million in the Governor’s operating budget.
- **Special Education (SPED) Circuit Breaker** – The Governor includes a \$150 million reserve in her supplemental budget for the SPED Circuit Breaker program. This funding, combined with \$653 million in the operating budget, is intended to fully meet the program’s obligations for both instructional and transportation reimbursement.
- **Early Education & Care (EEC) High-Quality & Affordability Fund** – The Governor proposes transferring \$150 million of surplus surtax to the EEC High-Quality & Affordability trust fund which is ultimately used in the Governor’s FY 2027 budget to support CCFA program costs.

Though the Governor does a better job this year focusing the resources from the Innovation and Capital Fund on one-time uses, the use of surplus funds to support the SPED Circuit Breaker program and CCFA maintenance costs in particular raises some concerns. In addition to the operating spending proposed by the Governor’s supplemental budget, the House also includes further funding (\$39 million) to support CCFA.

Furthermore, though not categorized as ongoing, there are other areas where one-time transfers of surplus dollars are being used in the Governor’s FY 2027 budget to support operating expenses, including the subsidy to the MBTA, as discussed above.

### Putting it All Together

#### *Thinking Wholistically About FY 2027*

Altogether, the FY 2027 budget cycle will direct almost \$3.9 billion in surtax spending across the education and transportation sectors. The majority of the funding proposed in the Governor’s operating budget and surtax supplemental budget are dedicated towards fulfilling core priorities of the Healey administration – funding the final year of the Student Opportunity Act, providing multi-year support to the MBTA, and continuing support for key programs like the C3 grant program, free community college, and other programs across both sectors.

#### *Income Surtax Investments in the Governor’s FY 2027 Budget & 2026 Supplemental Surtax Bill*

	<b>FY 2027 – Gov.</b>	<b>I&amp;C Supp. Budget – Gov.</b>	<b>Total Funding</b>	<b>% of Total Surtax Spending</b>
Education	\$1,725	\$358	\$2,083	54%
Transportation	\$975	\$785	\$1,760	46%
<b>Total Investments</b>	<b>\$2,700</b>	<b>\$1,153</b>	<b>\$3,853</b>	

*\$ in millions*

As in FY 2026, we see proposals in the Governor's Innovation and Capital Fund supplemental budget that are intended to supplement operating costs for large high-cost programs and initiatives, and we see a slightly uneven distribution of resources between the education and transportation sectors even when looking across both budget vehicles.

As policymakers in the House and Senate turn their attention to responding to the Governor's proposals and crafting their own budgets, they will have to contend with a challenging fiscal picture, national economic uncertainty, and spending pressures at the state level. The layer of the surtax onto the larger budget picture offers some opportunities, as well as challenges, for the House and Senate as they work to craft a balanced budget for FY 2027.

### **Key Questions for the House & Senate**

- ***Will the House and Senate use the surtax in new areas, like the Governor did with the proposal to use surtax revenue to support human services transportation?***

*The Governor's use of surtax revenues to fund human services transportation in her operating budget represents a new use of the surtax in the transportation space.*

*The Fair Share Amendment constitutionally directs surtax resources to be spent on public education and public transportation programs and initiatives, as well as public infrastructure projects. When the surtax was first implemented there were many discussions about what programs fell into the categories of education and transportation spending. For example, using the surtax to support the state's early education and child care system was initially a debated issue, though there has now been consensus that EEC is an acceptable area where the surtax has been able to make a real impact. The Governor's budget now includes a proposal that expands surtax spending for transportation to a new area, human services transportation.*

*As the House and Senate craft their own budget proposals for FY 2027, MTF would urge policymakers to prioritize using surtax revenues to support core public transportation and infrastructure programs. While other state programs may face cost pressures related to transportation, maintaining the surtax's original intent will strengthen its long-term impact on the education and transportation sectors.*

- ***How has the surtax contributed to increased spending in the education and transportation sectors in the state's operating budget, and what does that mean for how we think about the use of surtax revenues going forward?***

*As discussed throughout the brief, the surtax has been critical to the growth in spending for both the education and transportation sectors. Surtax revenue has been used to support the*

creation of new programs and has been increasingly used to invest in existing programs that were previously supported by the General Fund and other resources.

*Increased Education & Transportation Operating Budget Spending Since FY 2023*

	FY 2023 GAA	FY 2027 – Gov.	\$ Change: FY 2023 – FY 2027
Education	\$9,893	\$13,117	+ \$3,224
Transportation	\$753 <sup>7</sup>	\$1,344	+ \$591

*\$ in millions*

The chart above looks at the increase in investment seen in the state’s operating budget for education and transportation. Comparing the Governor’s FY 2027 budget to the FY 2023 GAA, education spending has grown by more than \$3 billion and transportation spending has increased by \$591 million. Since FY 2023, the state has collectively spent almost \$4.7 billion and \$2.7 billion of the surtax on education and transportation, respectively, in the operating budget. This tells us that not only has surtax revenue been used to support all new operating budget spending that we have seen in both sectors, it has also been used to invest in programs that were previously supported by other revenue sources, mainly the General Fund. In addition to spending included in the operating budget, the Innovation and Capital supplemental budget has been used to invest additional resources<sup>8</sup> in both sectors. As discussed earlier, spending included in the Innovation and Capital supplemental budget has been used to further support operating as well as one-time investment in education and transportation.

Since its implementation, the state has been able to rely on the surtax to support the significant expansion of education and transportation spending. The use of the surtax has also allowed budget writers to create room for General Fund resources to be used in other areas and sectors. As we look to the continued use of the surtax in the operating budget, policymakers should remain aware that that core education and transportation programs are now increasingly reliant on surtax resources and how this might impact the larger budget picture if surtax resources decline during a future economic downturn.

- **How should policymakers approach supplemental surtax spending in FY 2027 to limit potential budget exposure in future years?**

<sup>7</sup> Excludes \$266 million from a one-time transportation reserve funded in FY 2023.

<sup>8</sup> The 2025 Innovation and Capital supplemental budget appropriated \$561 million for education and \$758 million for transportation. The Governor’s 2026 supplemental budget invests \$358 million and \$975 million for education and transportation respectively, and the House includes greater funding levels in their version of the supplemental budget (\$456 million for education and \$834 million for transportation).

*Returning to the information laid out at the beginning of this report, policymakers should also understand the implications of ongoing surtax revenue and spending trends. FY 2026 and FY 2027 are marked by significant overall surtax spending bolstered by the Innovation and Capital Fund supplemental budgets. As surtax collections level out and surtax is increasingly spent in the operating budget, leading to smaller deposits into the fund going forward, budget writers will need to plan for reduced levels of overall surtax spending starting in FY 2028.*

*In order to reduce the impact of a surtax cliff effect as supplemental surtax spending is reduced going forward, MTF recommends that spending in the Innovation and Capital supplemental budget be focused largely on one-time uses rather than on large operating investments which will need to be supported with other resources next year.*