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April 3, 2025

The Honorable Aaron Michlewitz
Chairman, House Committee on Ways and Means
State House, Room

The Honorable Michael Rodrigues
Chairman, Senate Committee on Ways and Means
State House, Room 212

Massachusetts Taxpayers Foundation Testimony on House Bill 55

An Act making appropriations for the fiscal year 2025 to provide for supplementing certain existing appropriations and for certain other activities and projects

Chairman Michlewitz, Chairman Rodrigues, members of the House and Senate Committees on Ways and Means,

Thank you for the opportunity to testify today on House Bill 55, *An Act making appropriations for the fiscal year 2025 to provide for supplementing certain existing appropriations and for certain other activities and projects*, also known as the surplus surtax supplemental budget.

Before addressing the Massachusetts Taxpayers Foundation's specific recommendations regarding this supplemental spending bill, I want to first thank you for the work done in collaboration with the Healey administration to develop and implement a structure to collect, track, and spend surtax revenue collections that is clear and transparent. It is due to that structure that over the last two years a sustainable level of surtax-supported spending has been incorporated into the operating budget, and it is why policymakers now have an opportunity to deploy a further \$1.32 billion in surtax resources currently held in the Education and Transportation Innovation and Capital Fund. As we will share in our testimony, this bill is a unique opportunity to make meaningful investments in our capital needs, explore innovative solutions to policy problems, and establish a precedent for how this fund can be used sustainably to complement other state investments.

Governor Healey filed her administration's surplus surtax spending proposal on January 22nd, alongside her Fiscal Year (FY) 2026 budget recommendation. As the Legislature now undertakes their own budget development process and considers action on the surplus surtax supplemental budget, MTF recommends adhering to **three principles for the appropriation of resources from the Innovation and Capital Fund:**

1. **Achieve an even division of surtax revenues between education and transportation using operating budget and supplemental surtax resources.** MTF has consistently advocated for equally dividing surtax revenues between education and transportation. However, the unique needs of each sector present challenges in achieving that even division solely through the annual operating budget. To date, surtax revenues for education have been used to support and sustain large new programs, including Universal School Meals, Childcare Stabilization Grants, and Free Community College. These programs represent ongoing costs for the state and require a large share of the surtax spending cap in the annual budget. Conversely, many of the most pressing needs in the transportation sector are related to capital and infrastructure improvements; costs uniquely suited for the surplus surtax revenues held in the Innovation and Capital Fund. Ultimately, the even distribution of surtax revenues between education and transportation should be accomplished through a holistic assessment of spending in the operating budget and through supplemental spending bills. This will ensure that each sector is receiving its fair share of resources, as well as the resources most appropriate to meet their distinct needs.

2. **Use supplemental surtax spending for one-time or temporary costs.** FY 2026 represents the first opportunity lawmakers have to appropriate \$1.32 billion in supplemental surtax resources. While this funding may be used to complement priorities and programs funded through the operating budget, the Innovation and Capital Fund was specifically created to support one-time and capital-related costs. This distinction between the types of surtax-supported spending in the operating budget and through supplemental spending bills is important for two primary reasons:
 1. The level of above-cap surtax collections deposited into the Innovation and Capital Fund cannot be reliably predicted. Given the increase in the operating threshold for surtax spending and the underlying volatility of these revenues, using them to support ongoing operating expenses will create long-term structural budget challenges and near-term funding cliffs for programs supported by this revenue.
 2. As detailed above, 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 investments in transportation.

3. **Use supplemental surtax revenues to support innovative strategies that save the state long-term costs or promote cost efficiencies.** This year, policymakers have access to \$1.32 billion in surplus surtax revenues to support additional investments in education and transportation. This likely represents the high-water mark for the Education and Transportation Innovation and Capital Fund, as the surtax spending cap in the operating

budget has increased and total surtax revenue collections are projected to level out at approximately \$2.4 billion. For example, in FY 2026, if total surtax revenue collections are \$2.4 billion and the surtax spending cap is set at \$1.95 billion, the above-cap surtax amount will fall to only \$450 million.

The fact that the amount of surplus surtax revenues available in future years will decrease underscores the importance of limiting spending to one-time or capital-related costs, and it highlights the unique opportunity policymakers have to identify innovative strategies that support long-term cost savings and efficiencies. As further detailed below, several education and transportation-related programs are increasing cost pressures on the state and local budgets. Dedicating a modest portion of surplus surtax revenues towards identifying and studying strategies to manage cost growth for key programs achieves the short-term goal of using these resources in support of innovation, and the long-term goal of aligning state spending and revenue growth trends.

These three principles describe MTF's high-level priorities for the expenditure of resources from the Innovation and Capital Fund. There are also several specific spending proposals that we support:

- **Advancing the recommendations of the Transportation Finance Task Force.** On January 14th, Governor Healey unveiled her administration's plan to invest \$8 billion into the state's transportation system over the following ten years. The plan, guided by the recommendations of the Transportation Finance Task Force, focused on eliminating transportation structural deficits, most notably at the MBTA, while also expanding capital spending by \$6.2 billion over the next decade. The core elements of the plan are reflected in the administration's FY 2026 budget and the surplus supplemental spending bill. MTF strongly supports these elements of the Governor's spending bill proposals to reach a 50/50 surtax split and provide sustainable increases in transportation investments.
- **Closing the MBTA's operating budget deficit for FY 2026 – FY 2028.** The Healey administration projects that the combination of \$687 million in annual operating support for the MBTA and the \$300 million investment to restore MBTA reserves included in the supplemental budget will meet 90 percent of the MBTA's budget gaps over the next three fiscal years. The MBTA will be responsible for solving the remaining 10 percent of the budget gap in each of the next three years. MTF's past research has highlighted the need to provide budget certainty for transit agencies in the near-term and this proposal provides a clear path towards achieving that goal. Additionally, given the uncertainties that exist at the federal level related to transportation funding, agreement on a state strategy to stabilize the MBTA budget is even more critical.
- **Addressing the increasing costs of out-of-district special education transportation.** In FY 2026, spending growth in the state budget is predominantly driven by cost increases for non-discretionary programs, including state aid for public schools through the Special Education Circuit Breaker Program. In particular, the costs of out-of-district special education transportation are increasing at a rate that is unsustainable for the state budget

and local municipalities. Due to these cost pressures, the state should seek to identify and support strategies that improve efficiencies and rein in spending growth; and as discussed above, surplus surtax revenues provide a unique opportunity to support that type of innovation. At the district level, one-time planning and implementation grants could support multi-district collaborations to transport students to out-of-district programs; while at the state level, grant funding for independent research and analysis could provide policymakers with several options to control costs in future fiscal years.

Lastly, any considerations of state spending – through the operating budget or supplemental spending bills – must acknowledge that Massachusetts may soon face significant shifts in the state and federal partnership. These shifts could have profound impacts on the public, non-profit, and private sectors, as well as the broader state economy.

While there are currently many more questions than answers regarding the impacts of federal action on Massachusetts, MTF urges policymakers to be proactive in preparing for a state funding or policy response. In particular, MTF strongly recommends developing a structure that allows for the sharing of information and response coordination between the administration, House, and Senate. A collaborative State Federal Response Team can engage in scenario planning, assess new developments, and monitor the direct and indirect impacts of federal action.

Thank you for the opportunity to submit this testimony today. MTF looks forward to continuing to work with the House, Senate, and Healey administration on the FY 2026 budget, the surplus surtax supplemental budget, and the state's response to federal action.

Sincerely,

A handwritten signature in black ink, appearing to read "D. Howgate". The signature is stylized and cursive.

Doug Howgate, President