

# Band-Aid Budget Redux

## Briefly

*The Legislature has passed a supplemental operating budget that would increase 2025–27 appropriations from funds subject to the outlook (NGFO) by \$2.348 billion (3.0%) compared to the enacted 2025–27 biennial budget. Revised 2025–27 appropriations would be \$80.206 billion, which is 11.4% higher than actual 2023–25 spending.*

*Since the biennial budget was adopted last year, the NGFO revenue forecast increased by \$166.0 million through 2027–29. On top of that, the Legislature adopted an income tax and tapped the rainy day fund.*

*Although revenues have been increasing, the supplemental budget passed by the Legislature would widen the gap between spending and revenues: appropriations for 2025–27 would exceed revenues by \$4.9 billion.*

*Assuming the income tax remains law, it would not solve the budget problem. Even with income tax revenues, spending growth would need to be held well below average in order to close the gap.*

*The 2026 supplemental balances in the current biennium due to one-time revenues and dubious accounting assumptions. Another budget deficit is likely in the next biennium.*

The biennial budget enacted last year was unsustainable, even though the Legislature adopted historically large tax increases. It papered over known budget problems, even as it increased spending by \$5.9 billion (WRC 2025). A similar story played out this year.

Gov. Ferguson has not yet signed the budget or all the tax bills.

## Overview

Table A1 in the appendix (on page 7) shows the estimated NGFO (see the box below) balance sheet and outlook for the 2026 supplemental operating budget, as passed by the Legislature.

**Resources.** The February 2026 revenue forecast estimates that NGFO revenues will increase by 12.1% in 2025–27 and 6.8% in 2027–29. Revenues in the February forecast are \$166.0 million higher than assumed in the enacted 2025–27 budget (over the 2023–25, 2025–27, and 2027–29 period).

Additionally, the Legislature increased taxes. Overall, tax changes are estimated to increase NGFO revenues by a net of \$36.0 million in 2025–27 and \$2.201 billion in 2027–29. The major tax changes include:

- ESSB 6346, which establishes an income tax. (The bill has been signed by the governor.) The bill also

## NGFO

Under the four-year balanced budget requirement, a positive ending balance is required in both the current and following biennium for “funds subject to the outlook.” This is a synthetic “account” that rolls up the general fund–state (the state’s primary budget account) with the education legacy trust account, the opportunity pathways account, the workforce education investment account, and the fair start for kids account. It is also called the near general fund–outlook, or NGFO.

increases the business and occupation (B&O) tax credit for small businesses; rolls back most of last year's ESSB 5814 (which applied the sales tax to many services); and exempts diapers, over-the-counter drugs, and certain hygiene products from the sales tax. The budget assumes it will reduce revenues by \$55.4 million in 2025–27 and increase revenues by \$2.292 billion in 2027–29. However, the revenue estimate is based on an earlier version of the bill. A fiscal note that reflects the version that was passed by the Legislature estimates that it will reduce revenues by \$46.4 million in 2025–27 and increase revenues by \$2.309 billion in 2027–29.

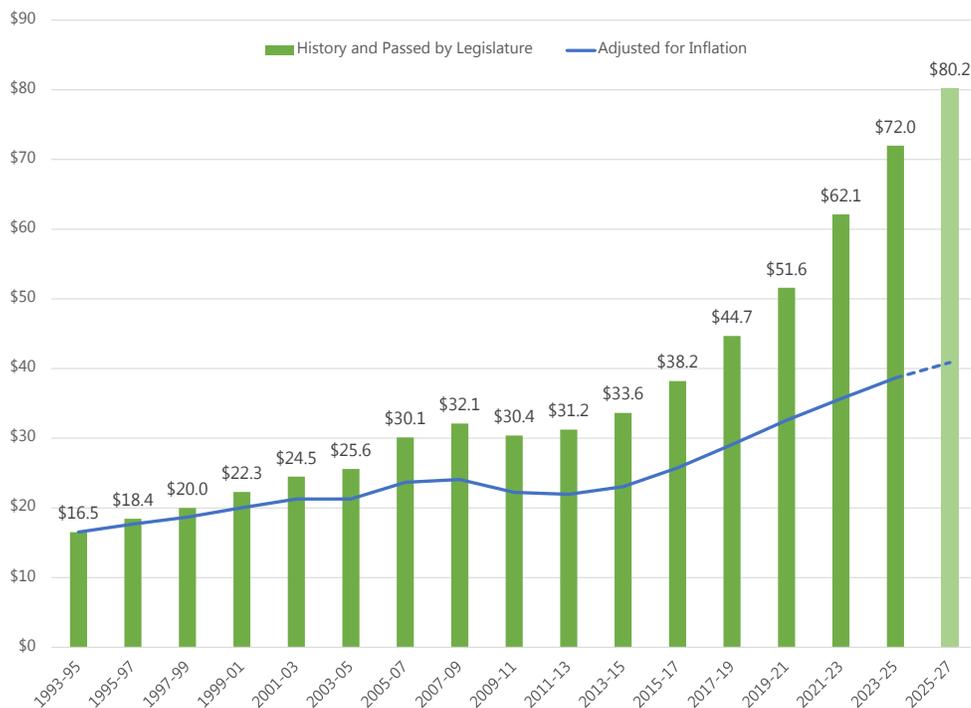
- ESSB 6231, which would apply sales and use taxes to data center refurbishments. This would increase revenues by \$63.0 million in 2025–27 and \$140.5 million in 2027–29.
- ESB 6228, which would increase the B&O tax rate for warehousing and reselling prescription drugs. This would increase revenues by \$24.0 million in 2025–27 and \$141.7 million in 2027–29. The revenue estimate is based on an earlier version of the bill; there is not yet a fiscal note for the version that was passed by the Legislature.
- EHB 2487, which would clarify that the B&O tax exemption for entities that pay the insurance premiums tax only applies to companies that directly pay the tax. Additionally, the workforce education investment surcharge cap would be lowered to \$25 million for qualifying insurers. The budget assumes this would increase revenues by \$55.6 million in 2025–27 and \$17.2 million in 2027–29. The revenue estimate is based on an earlier version of the bill; there is not yet a fiscal note for the version that was passed by the Legislature.
- ESB 6347, which rolls back the estate tax rate increases that were adopted last year. (The bill has been signed by the governor.) The budget assumes it will reduce revenues by \$44.8 million in 2025–27 and \$389.9 million in 2027–29. However, that fiscal estimate does not reflect late amendments to the bill. As enacted, the bill sets the exclusion amount at \$3.0 million for estates of people dying on or after July 1, 2026, and it again uses a defunct inflation adjustment method. (Effectively, the \$3.0 million exclusion will not be adjusted for inflation.) A fiscal note that reflects the version that was passed by the Legislature estimates that it will reduce revenues by \$41.1 million in 2025–27 and \$340.7 million in 2027–29.

The budget would also transfer \$1.662 billion from other accounts to the NGFO. This includes:

- \$880.0 million from the budget stabilization account (BSA, or the rainy day fund),
- \$394.6 million in estimated capital gains revenues that would otherwise go to the common school construction account,
- \$375.0 million from the public works assistance account,
- \$10.0 million from the state treasurer's service account, and
- \$10.0 million from the Washington state library-archives building account.

**Spending.** The 2026 supplemental would increase 2025–27 NGFO appropriations by \$2.348 billion (3.0%) compared to the enacted 2025–27 biennial budget. Revised 2025–27 appropriations would be \$80.206 billion, which is 11.4% higher than actual 2023–25 spending. The change in appropriations is comprised of a maintenance level increase of \$1.727 billion and \$621.3 million in new policy. The new

Chart 1: NGFO Spending (Dollars in Billions)



policy is the net of new increases totaling \$1.592 billion and reductions totaling \$970.4 million. (More details on new spending are included in the appendix, beginning on page 8.)

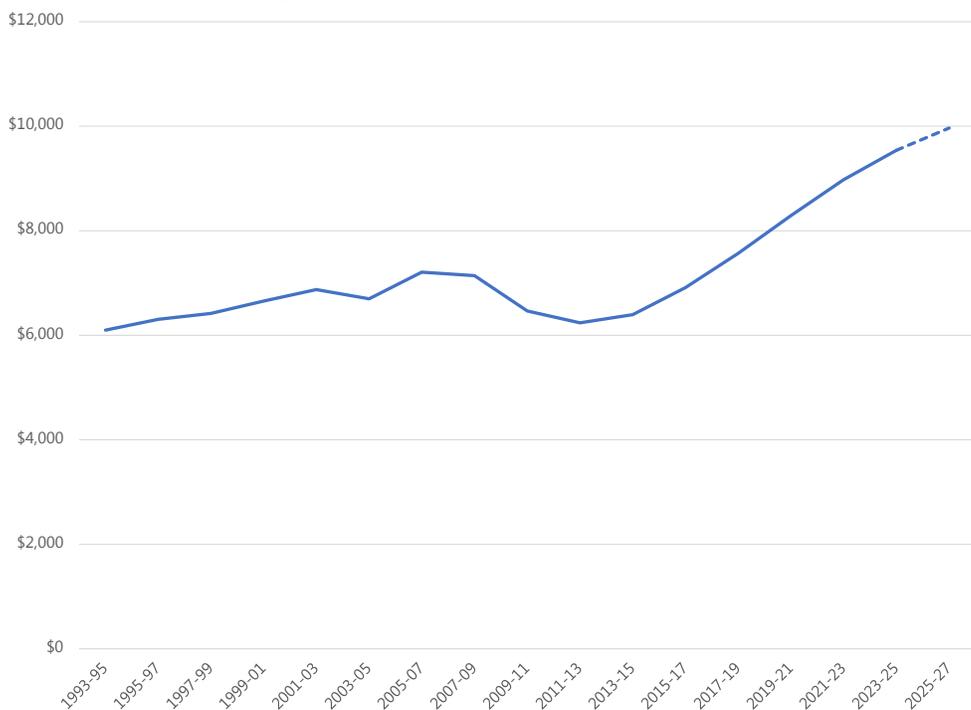
**Reserves.** As noted above, the budget would transfer \$880.0 million from the BSA to the NGFO. Additionally, the budget would appropriate \$141.3 million from the BSA for fire suppression costs. The BSA balance is estimated to be \$1.032 billion at the end of 2025–

27. The unrestricted NGFO ending balance is estimated to be \$231 million at the end of 2025–27. (However, as discussed below, this relies on unusual accounting assumptions.) Together, total reserves at the end of 2025–27 are estimated to be \$1.262 billion (3.2% of revenues and other resources).

**Outlook.** The budget balances over four years without assuming 4.5% annual revenue growth in the

second biennium. The Legislature estimates that the unrestricted NGFO ending balance would be \$563 million in 2027–29. (The balance in FY 2028 would be *negative* \$878 million.) The outlook assumes that the state will use \$880.0 million from the expected surplus in the Law Enforcement Officers’ and Firefighters’ retirement system Plan 1 (LEOFF 1) to backfill the BSA in 2027–29. This would make the BSA balance \$2.772 billion. Total reserves would be \$3.335

Chart 2: NGFO Spending Per Capita (Adjusted for Inflation)



billion in 2027–29 (7.8% of revenues and other resources).

### The Gap Between Spending and Revenues Widens

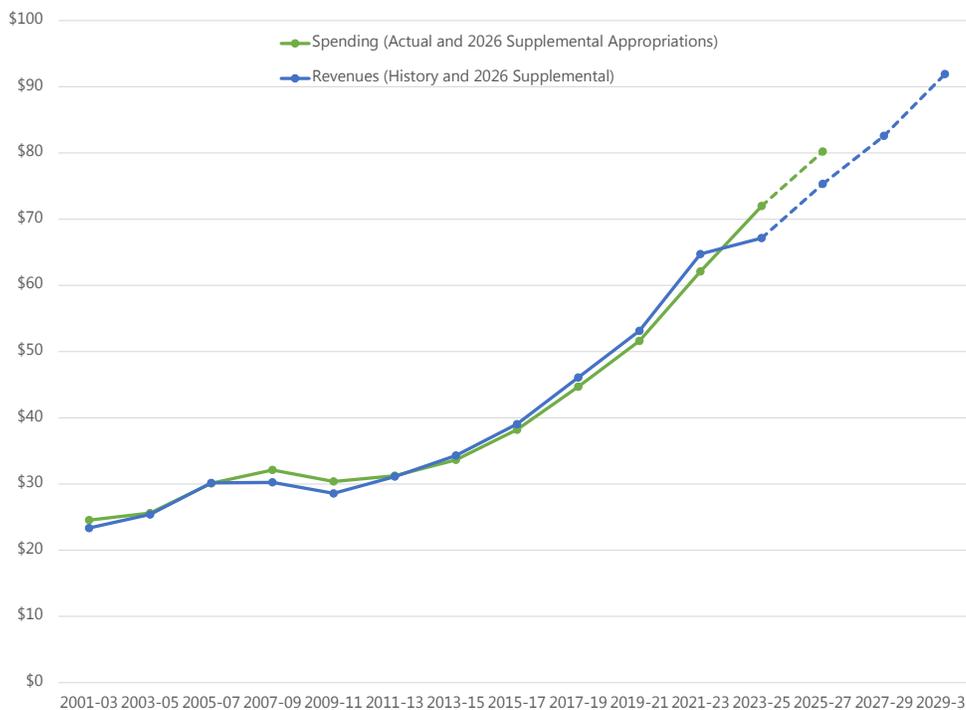
Washington has been experiencing budget shortfalls because, in 2023–25, the Legislature adopted budgets that increased appropriations by 15.8% at a time when revenues were expected to grow by just 3.5% (WRC 2024). Actual spending in 2023–25 exceeded revenues by \$4.842 billion. The supplemental budget passed by the Legislature would widen that gap: appropriations for 2025–27 would exceed revenues by \$4.894 billion. (This estimate is based on the revenues assumed in the budget. The gap is \$4.881 billion after updating revenues to reflect fiscal notes that have been revised so far. As more final fiscal notes for tax bills are published, the figure could change.)

Revenues are not declining; instead, the Legislature has chosen to appropriate more than it collects in revenues. Nor are changes in federal government policy related to Medicaid and Supplemental Nutrition Assistance Program (SNAP) driving the increase in state spending. The supplemental would appropriate \$39.4 million from the NGFO at the maintenance level and another \$50.0 million for new policy spending related to the federal H.R. 1.

On the contrary, the largest policy increase in the supplemental budget is related to the state’s increasing tort liabilities. The 2026 supplemental includes \$956.1 million to backfill the state liability account. (That accounts for 60.1% of the new policy increases in the budget.) This problem surfaced last year, but the Legislature chose not to address it in the biennial budget.

The spending increases are partially offset by program reductions and shifts of programs to other funds. These include savings of \$239.9 million from shifting funding for higher education programs from the NGFO to the higher education institutions’ building accounts and \$143.3 million from changes to child care income eligibility and rate policies.

Chart 3: NGFO Spending and Revenues (Dollars in Billions)



The child care program changes (passed by the Legislature in SHB 2689) would save an estimated \$638.1 million in 2027–29, as they would permanently change policies that were planned for 2027–29 under the Fair Start for Kids Act. Other than that, the supplemental does not reflect much effort to find long-term budget savings.

## Budget Relies on One-Time Resources and Unusual Accounting Assumptions

Despite increasing revenues, the budget relies heavily on one-time resources. Not only does it tap the rainy day fund, but it retains all capital gains revenues in 2025–27 in the education legacy trust account (a fund subject to the outlook). Capital gains tax revenues are generally volatile, yet they do not feed into the BSA. To help manage their volatility, statute specifies that any collections over \$500 million a year (adjusted annually for inflation) be deposited in the common school construction account. (For FY 2026, the threshold is about \$540 million.) The 2026 supplemental would instead use all capital gains revenues in 2025–27 for general, ongoing spending.

Additionally, the budget relies on two accounting assumptions that obscure the true budget picture.

First, it continues the recent practice of assuming unusually large reversions, which are appropriations that are not ultimately spent. After years of assuming reversions equaling 0.5% of general fund–state appropriations, the Legislature in 2023 began assuming a higher percentage. (Higher reversions mean larger ending balances.) The 2026 supplemental assumes reversions of 1% in 2026 and 0.9% thereafter. Along with additional reversions related to K–3 class sizes, this means that the ending balance is \$766.5 million higher in 2025–27 and \$768.1 million higher in 2027–29 than it would be if based only on the appropriations level.

Second, the 2026 supplemental assumes prior period adjustments of \$250 million each biennium. Prior period adjustments are included in the outlook’s resources section to correct errors in prior fiscal years. These adjustments are normally assumed to be \$41 million a biennium.

The unusually high assumptions for reversions and prior period adjustments are deviations from previous accounting norms that serve to increase the size of the ending fund balance. Without them, we estimate that the unrestricted NGFO ending balance of the 2026 supplemental would be *negative* \$786 million in 2025–27 and *negative* \$1.472 billion over four years.

Even given the unusual accounting assumptions, the unrestricted ending balance in 2025–27 is very low, at 0.6% of revenues and other resources. That is as low as the ending balance for the biennium in the budget adopted last year, which was the lowest since 2013. Further, the outlook estimates that the unrestricted ending balance will be *negative* \$878 million in FY 2028. Total reserves in each biennium would be less than 10% of revenues and other resources, which is the level recommended by the state treasurer (OST 2026).

## The Income Tax Will Not Save the Day

In addition to the accounting assumptions described above, the budget balances over four years because it assumes revenues from the income tax in FY 2029. The tax will certainly be challenged in court and on the ballot, so there is some risk that revenues might never materialize.

Assuming the income tax remains law, it would not solve the budget problem. The outlook assumes appropriations growth of just 2.8% from 2025–27 to 2027–29 and leaves an ending balance of just \$563 million. By statute, the outlook cannot include an estimate of the cost of future collective bargaining agreements (CBAs) with employees and non-employees. The 2025–27 CBAs (plus the cost of extending them to non-represented employees) increased appropriations by about \$1.9 billion. This suggests that

the CBAs for 2027–29 would increase spending above the 2.8% assumed growth.

Indeed, average biennial spending growth going back to 2003–05 is about 10.6%. If state spending is allowed to grow just at that average in 2027–29 and 2029–31, the gap between spending and revenues will continue to grow, despite income tax revenues. Assuming biennial spending growth of 10.6%, and assuming revenues estimated in currently available fiscal notes for bills that passed this year, the gap will grow to \$6.071 billion in 2027–29 and \$6.182 billion in 2029–31 (the first biennium in which there are two years of income tax collections). The Legislature will still need to act to reduce the spending level to match revenues.

The budget bill does include a few provisions that suggest the Legislature is willing to consider such steps. It would require budgets for the next few biennia to assume the actual revenue forecast in the second biennium, rather than the 4.5% annual revenue growth that is allowed by the four-year balanced budget statute. Additionally, it would establish a Joint Legislative-Executive Committee on Budget Transparency and Fiscal Sustainability.

## Comment

Instead of making any effort to close the gap between spending and revenues, the Legislature chose to widen it. The 2026 supplemental balances in the current biennium due to one-time revenues and dubious accounting assumptions. The four-year balance is even less sustainable because of its reliance on an income tax that could be overturned and a low ending fund balance that is unlikely to cover the cost of collective bargaining agreements or any additional maintenance level spending cost increases. Expect more budget problems next year.

## References

Office of the State Treasurer (OST). 2026. "[Debt and Credit Analysis](#)."

Washington Research Council (WRC). 2024. "[Anatomy of the Projected State Budget Shortfall](#)." PB 24–08. Oct. 23.

———. 2025. "[The Band-Aid Budget: \\$9 Billion in New Taxes and \\$7 Billion in Savings, But No Lasting Solutions](#)." PB 25–03. July 17.

## Appendix

Table A1: Estimated NGFO Outlook (Dollars in Millions)

	<b>Passed Legislature</b>	
	<i>2025-27</i>	<i>2027-29</i>
Beginning Balance	2,536	231
Revenue		
Feb. 2026 Revenue Forecast	75,276	80,381
<b>Revenue Legislation</b>	<b>36</b>	<b>2,200</b>
<i>Total Revenue</i>	<i>75,312</i>	<i>82,581</i>
Other Resource Changes		
Transfer to Budget Stabilization Account	(706)	(785)
Budget Driven Revenue	(10)	(11)
<b>Prior Period Adjustments</b>	<b>250</b>	<b>250</b>
Enacted Transfers	625	7
<b>Transfer from BSA</b>	<b>880</b>	<b>0</b>
<b>Other Proposed Transfers</b>	<b>388</b>	<b>0</b>
<b>Capital Gains Revenues Retained</b>	<b>395</b>	<b>0</b>
<i>Total Other Resource Changes</i>	<i>1,822</i>	<i>(539)</i>
<i>Total Resources</i>	<i>79,670</i>	<i>82,273</i>
Spending		
2025 Enacted Budget	77,858	80,331
Maintenance Level Change	1,727	1,968
<b>Net Policy Level Change</b>	<b>621</b>	<b>179</b>
<b>Reversions</b>	<b>(766)</b>	<b>(768)</b>
<i>Total Spending</i>	<i>79,440</i>	<i>81,710</i>
Unrestricted Ending Fund Balance	231	563
Budget Stabilization Account Beg. Balance	1,269	1,032
Transfers from GFS and Interest Earnings	784	860
<b>Transfer to GFS</b>	<b>(880)</b>	<b>0</b>
<b>Appropriations from BSA</b>	<b>(141)</b>	<b>0</b>
<b>Transfer from LEOFF 1</b>	<b>0</b>	<b>880</b>
Projected BSA Ending Balance	1,032	2,772
<i>Total Reserves</i>	<i>1,262</i>	<i>3,335</i>
Sources: OPR, SCS		
<b>Adjusted to Remove Accounting Assumptions</b>		
Unrestricted NGFO Ending Balance	(786)	(1,472)
Total Reserves	246	1,300
Source: WRC estimates		

Table A2: Appropriations (Dollars in Thousands)

	<b>Original 2025-27</b>		<b>2026 Supplemental</b>		<b>Revised 2025-27</b>	
	<u>NGFO</u>	<u>All Funds</u>	<u>NGFO</u>	<u>All Funds</u>	<u>NGFO</u>	<u>All Funds</u>
Legislative	297,933	326,315	3,238	3,412	301,171	329,727
Judicial	610,606	751,505	12,188	17,278	622,794	768,783
Governmental Operations	2,075,054	8,601,896	101,965	1,481,094	2,177,019	10,082,990
DSHS	12,125,652	25,021,499	292,319	719,476	12,417,971	25,740,975
HCA	8,924,197	38,033,098	511,311	1,946,656	9,435,508	39,979,754
DCYF	4,614,422	5,903,859	1,241,462	1,617,682	5,855,884	7,521,541
Dept. of Corrections	3,286,734	3,340,568	98,143	91,270	3,384,877	3,431,838
Other Human Services	539,606	4,465,879	(15,851)	111,555	523,755	4,577,434
Natural Resources	1,050,868	3,756,697	(1,268)	227,833	1,049,600	3,984,530
Transportation	169,831	333,589	875	20,648	170,706	354,237
Public Schools	33,666,884	36,406,761	208,090	207,648	33,874,974	36,614,409
Higher Education	6,164,204	18,923,070	(65,481)	175,420	6,098,723	19,098,490
Other Education	102,840	182,085	2,126	1,846	104,966	183,931
Special Appropriations	4,228,841	4,364,275	(41,222)	256,841	4,187,619	4,621,116
<b>Total</b>	<b>77,857,672</b>	<b>150,411,096</b>	<b>2,347,895</b>	<b>6,878,659</b>	<b>80,205,567</b>	<b>157,289,755</b>

Table A3: Total NGFO Policy Changes in the 2026 Supplemental, Plus Major Items (Dollars in Thousands)

	<b><u>2025-27</u></b>
<b>Legislative</b>	<b>(74)</b>
<b>Judicial</b>	<b>10,673</b>
<b>Governmental Operations</b>	<b>15,580</b>
Services for victims of crimes	19,355
Permanent supportive housing	15,000
Income tax implementation	10,238
Shift emergency housing and shelter grants to housing trust account	(24,000)
<b>Department of Social and Health Services (DSHS)</b>	<b>(107,973)</b>
Support services for refugees	25,000
H.R. 1: state services for lawfully present noncitizens who will lose Medicaid access	17,824
State hospital overtime costs	14,879
H.R. 1: work requirements and staffing	12,410
H.R. 1: other IT costs	7,392
Phase down nursing home rate add-ons	(9,864)
Olympic Heritage Behavioral Health underspend	(14,879)
Maple Lane campus remodelling delays	(20,168)
Delay assisted living facility rate rebase by one year	(21,016)
Shift funding for WorkFirst services to other accounts	(38,000)
Disproportionate share hospital program reduction delay (related to federal changes)	(70,038)

Table A3 continued: Total NGFO Policy Changes in the 2026 Supplemental, Plus Major Items  
 (Dollars in Thousands)

	<b>2025-27</b>
<b>Health Care Authority (HCA)</b>	<b>32,619</b>
Restoring savings not realized from Medicaid program integrity activities	71,000
Cannabis revenue distributions	64,381
H.R. 1: work requirements and staffing	8,414
H.R. 1: state services for lawfully present noncitizens who will lose Medicaid access	1,999
Community behavioral health support services case mix	(10,364)
Delays to implementation of statewide electronic health record solution	(10,594)
Substance use disorder treatment services shifted to opioid account	(18,700)
Long-term civil commitment beds	(20,386)
Apple Health expansion population moved from managed care to fee-for-service	(28,525)
<b>Dept. of Children, Youth, and Families (DCYF)</b>	<b>(121,270)</b>
Eliminate enhanced regional rates for Working Connections Child Care (WCCC)	(15,463)
Eliminate prospective and enrollment-based pay for child care	(36,261)
Modify WCCC attendance-based provider reimbursement	(91,560)
<b>Dept. of Corrections</b>	<b>34,413</b>
Reopen medium security beds at Monroe Correctional Complex	16,644
Relief coverage for custody staff and additional staff for hospital watches	8,282
<b>Other Human Services</b>	<b>(3,946)</b>
Reproductive health services	8,600
<b>Natural Resources</b>	<b>(14,433)</b>
Invasive beetle eradication	6,175
Administrative reductions	(2,572)
Wildfire activities shifted to dedicated account	(6,000)
<b>Transportation</b>	<b>(3,589)</b>
<b>Public Schools</b>	<b>(80,463)</b>
Reduce Running Start funding cap	(7,004)
Assuming longer school bus operating lives to reduce depreciation payments	(21,105)
Maintain local effort enhancement at \$150 per pupil instead of increasing it	(25,093)
Reduce funding for the transition to kindergarten program	(27,269)
<b>Higher Education</b>	<b>(229,332)</b>
UW Center for Behavioral Health and Learning	15,000
Administrative reductions	(5,421)
Shift funding to institutions' building accounts	(239,871)
<b>Other Education</b>	<b>(173)</b>
<b>Other Appropriations</b>	<b>1,089,284</b>
Liability account	956,061
Other central services	89,018
Employee compensation	18,483
State health care affordability account	25,000
<b>Total</b>	<b>621,316</b>