

2026–27 State Budget: Tackling the Structural Deficit

SUMMARY

- Pennsylvania’s structural deficit has reached \$4.8 billion due to excessive spending. Under Gov. Josh Shapiro and his predecessor, Tom Wolf, state spending has consistently grown at a faster pace than the state economy.
- That current structural deficit represents a looming tax hike of nearly \$1,500 per family of four.
- Lawmakers can balance the budget without tax hikes by tackling the structural deficit with slower spending growth, tapping the shadow budget, a focus on growing the economy, and human service reforms that protect resources for eligible Pennsylvanians.

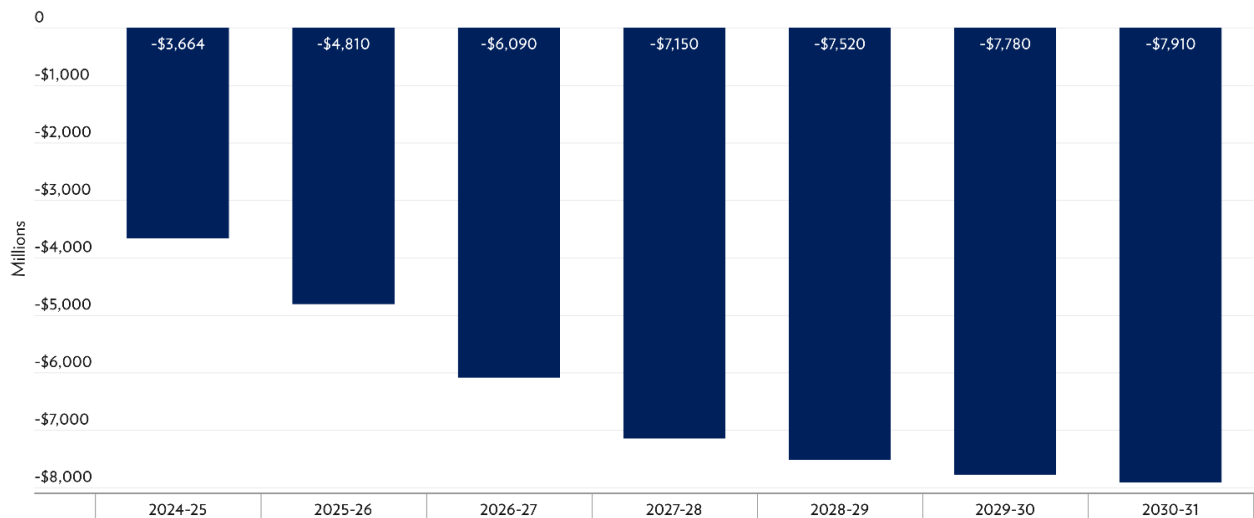
SIZE OF THE DEFICIT

Pennsylvania’s 2025–26 General Fund budget spends \$50.09 billion, compared to net revenues (after refunds) of \$45.3 billion. This \$4.8 billion deficit was covered by using most of the remaining fund balance, along with billions in one-time sources, including reserves from the “shadow budget.”

The Independent Fiscal Office (IFO) projects the **structural deficit will increase** from \$4.8 billion to about \$6 billion by the end of fiscal year (FY) 2026–27 and **almost \$8 billion by 2031**. General Fund spending has grown **50 percent since** FY 2018–19, outpacing revenue growth by \$5 billion. State spending growth also outpaced population growth (1 percent) and inflation (30 percent) over the same period. To eliminate the structural deficit, Pennsylvanians would face a tax hike of up to \$1,500 per family of four.

Long Terms Deficits (IFO Projections)

By increasing spending and using one-time sources, Gov. Shapiro expanded the structural deficit



Source: Independent Fiscal Office, “Pennsylvania Fiscal Outlook: FY 2025–26 to 2030–31”, <https://www.ifo.state.pa.us/releases/881/Pennsylvania-Fiscal-Outlook-FY-2025-26-to-FY-2030-31/>

SLOW SPENDING TO ELIMINATE THE DEFICIT

For the upcoming 2026–27 budget, the Taxpayer Protection Act (TPA) Index sets the spending increase limit at \$1.53 billion, or a 3.07 percent increase. If state spending growth had stayed within the TPA limit since 2019, state spending would be at \$42 billion.

Given the excessive increase in recent years that greatly exceeded the TPA index and created a \$4.8 billion structural deficit, even a modest increase in spending is fiscally irresponsible and would necessitate a broad-based tax hike on working families. Flat funding would approximately cut the structural deficit in half.

DRIVERS OF THE DEFICIT

Education and human services continue to drive the deficit. State spending for district public schools increased **\$5.1 billion over the last five years**, while the 2025–26 budget slashed funding for public cyber charter schools by an estimated \$178 million. Meanwhile, the public school student population continues to decline, dropping by **more than 12,000** since 2020.

The biggest cost-driver continues to be Medicaid, the largest program within the Department of Human Services. Medicaid spending consistently grows **faster than revenue**. Medical Assistance spending grew 4 percent between FY 2024–25 and FY 2025–26 compared to total General Fund revenue growth of 3.6 percent. Long-Term Living appropriations grew 10 percent. Since 2018, Medicaid spending increased 71 percent, more than \$5 billion.

The implementation of work requirements for healthy adults eligible for Medicaid and Supplemental Nutrition Assistance Program (SNAP) is projected to generate savings as Pennsylvanians move back into the workforce. The IFO projects \$135 million in annual state Medicaid savings. Likewise, SNAP work requirements are **reducing the healthy adult population dependent on food assistance**. Declining enrollment is a sign of a healthy economy.

Under federal legislation, Pennsylvania will pay a portion of SNAP benefit costs if the payment error rate remains above 6 percent. In 2024, Pennsylvania's payment error rate was 10.8 percent. The IFO projects a benefit **cost of \$173 million** in FY 2027–28 due to a payment error rate between 6 and 8 percent. The federal government will begin penalizing states for high Medicaid payment error rates in 2030. Looking at 2024 spending levels, the 11.4 percent error rate will cost state taxpayers an **additional \$2.2 billion**.

REDUCING THE STRUCTURAL DEFICIT

Lawmakers have tools to eliminate the structural deficit without raising taxes or borrowing.

- First, spending increases must be in line with the broader economy.
- Second, lawmakers can continue to tap shadow budget reserves. Last year, they transferred \$675 million without impacting programs. In 2025, the Commonwealth Foundation estimated lawmakers could tap **\$2.89 billion** in excess shadow budget fund reserves without impacting yearly distributions.
- Lawmakers can build on program integrity reforms to regulator check death and income records last year by ending all self-attestation and conducting audits to identify the source of payment errors.
- Finally, lawmakers should reduce corporate welfare spending. Last year, Shapiro proposed an **additional \$100 million** in handouts on top of \$1.6 billion in existing programs.