

To: Dr. Andalib Khelghati, Superintendent of Schools, Members of the Board of Education

From: Raphael Obafemi, Chief Financial Officer/CSBO

Date: January 5, 2026

Re: Illinois FY2026–FY2031 Fiscal Outlook and Potential Implications for K–12 Education

Each fall, the Governor’s Office of Management and Budget (GOMB) releases the Illinois Economic and Fiscal Policy Report, the State’s primary long-term fiscal planning document. The 2025 report, released on October 9, 2025, signals a notable shift from recent fiscal stability toward increasing structural deficits, driven largely by federal policy changes, slowing economic growth, and rising statutorily mandated costs. These developments have important implications for future education funding and budget planning.

### **Overall Fiscal Outlook**

GOMB now projects a General Funds deficit of \$267 million in the current FY2026, despite the enactment of a balanced budget earlier this year. Looking ahead, the deficit is projected to widen substantially—reaching \$2.2 billion in FY2027 and growing to \$5.3 billion by FY2031 if no policy changes are made. Over the five-year period, General Funds revenues are expected to grow at an average annual rate of 2.1%, while expenditures are projected to grow at 3.7%, creating a widening structural imbalance.

### **Key Federal Drivers of the Deficit**

A significant share of the State’s fiscal pressure stems from federal actions, particularly H.R. 1\*, the federal Budget Reconciliation Bill enacted in July 2025. Major impacts include:

- **Federal tax code changes**, especially expanded business expensing provisions, which reduce Illinois’ taxable income base and are expected to lower State income tax revenues by more than \$830 million in FY2026 alone.
- **SNAP cost shifts**, beginning in FY2027, will increase Illinois’ share of administrative costs to 75% and expose the State to penalties tied to payment error rates, with potential annual costs estimated at \$705 million.
- **Medicaid provider tax limitations**, phasing in during FY2028, which are projected to reduce combined state and federal Medicaid revenues by approximately \$4.5 billion by FY2031.

### **FY2026 Conditions**

General Funds revenues for FY2026 are now estimated at \$54.8 billion—nearly \$450 million less than anticipated when the budget was adopted—largely due to weaker individual and corporate income tax receipts. Expenditures, estimated at \$55.1 billion, remain elevated due to pensions, debt service, Medicaid, and K–12 education funding obligations. Together, these factors result in the current projected deficit. In response, GOMB has directed agencies to maintain four percent spending reserves and has recommended targeted “decoupling” from certain federal tax provisions to recover lost revenue.

### **Implications for Education**

Education remains one of the State’s largest and fastest-growing General Funds commitments. Fixed

costs—including pensions, Medicaid, debt service, and education—are projected to account for approximately 64% of General Funds expenditures by FY2027. While GOMB does not recommend immediate reductions to education funding, the growing structural deficit and limited budget flexibility increase the risk of slower growth in future education appropriations or heightened scrutiny of education spending as fiscal pressures intensify.

### **Reserves and Long-Term Considerations**

Illinois' Budget Stabilization Fund stands at approximately \$2.4 billion, with an additional \$161 million deposit planned in FY2026. While this represents meaningful progress, the reserve balance covers fewer than 15 days of operating expenditures and is insufficient to address multi-year structural deficits. GOMB emphasizes that reserves should be preserved for economic downturns, not used to fund ongoing operations.

### **Conclusion**

Illinois is transitioning from a period of recovery and relative fiscal stability to one of heightened fiscal uncertainty. Federal tax and program changes, combined with slowing revenue growth and rising mandated costs, are expected to strain the State's finances through FY2031. For the education system, this environment underscores the importance of cautious long-term planning, close monitoring of State budget developments, and continued advocacy for stable and predictable education funding as the State confronts growing structural challenges.

\*One Beautiful Bill Act

## **POTENTIAL IMPACTS OF ILLINOIS' PROJECTED FISCAL DEFICITS ON K-12 EDUCATION FUNDING AND DISTRICT BUDGET**

Building on the overview of the Governor's Office of Management and Budget (GOMB) FY2026–FY2031 fiscal outlook, this section of the memorandum provides a deeper analysis of how the State's emerging structural deficits may affect specific K–12 education programs and future funding scenarios.

### **1. Evidence-Based Funding (EBF) Formula**

The Evidence-Based Funding formula remains the primary mechanism for distributing General State Aid (GSA) to school districts. While the State has consistently increased EBF appropriations in recent years, the widening structural deficit creates several risks:

- **Slower growth or flat funding:** As General Funds pressures intensify, annual EBF increases may be reduced below historical levels or temporarily paused.
- **Distributional impacts:** Under flat or reduced growth scenarios, districts furthest from adequacy would continue to receive a greater share of new dollars, potentially leaving near-adequacy districts with little or no increase.
- **Long-term adequacy delays:** A prolonged period of constrained EBF growth would extend the timeline for many districts to reach adequacy targets.

## 2. Special Education and High-Cost Services

Special education expenditures are largely driven by federal mandates and student needs, limiting districts' flexibility:

- **State reimbursement pressures:** If State revenues weaken, reimbursement rates for special education transportation and high-cost placements may stagnate or decline in real terms.
- **Local cost shifts:** Districts may be required to absorb a greater share of special education costs, increasing pressure on local operating budgets.
- **Service delivery challenges:** Rising personnel and service costs, combined with limited State growth, may strain districts' ability to maintain current service levels.

## 3. Early Childhood and Pre-K Programs

Early childhood programs are more vulnerable than formula-driven K–12 aid because they rely on discretionary appropriations\*\*:

- **Expansion delays:** Planned expansions of preschool for all or early childhood grants could be slowed or deferred.
- **Grant volatility:** Competitive grant programs may experience funding freezes or reallocations during budget stress.
- **Equity considerations:** Reductions or stagnation in early childhood funding may disproportionately affect high-need communities where access gaps remain largest.

## 4. Categorical Grants and Targeted Programs

Programs such as bilingual education, transportation, career and technical education (CTE), and student support services may face heightened scrutiny:

- **Prioritization risk:** In an environment where fixed costs dominate the budget, categorical grants may be viewed as more adjustable than core formula aid.
- **Compliance vs. capacity:** While some categorical programs are federally or legally required, State funding levels may not keep pace with compliance costs.
- **Program consolidation:** The State may consider consolidating or restructuring categorical programs to control costs.

## 5. Pension and Benefit Cost Pressures

Teacher pension contributions and retiree benefits are major drivers of State expenditure growth:

- **Crowding-out effect:** Rising pension costs increase competition for limited General Funds, indirectly constraining education program growth.
- **Limited near-term relief:** Pension obligations are constitutionally protected, leaving little flexibility to redirect funds toward classrooms or new initiatives.

## 6. Future Funding Scenarios

Based on GOMB projections, several plausible education funding scenarios emerge:

- **Baseline/Status Quo Scenario:** Modest EBF increases continue but below inflation, resulting in declining purchasing power for districts.

- **Constrained Growth Scenario:** EBF and categorical funding are prorated for one or more years, shifting cost pressures to local districts.
- **Targeted Protection Scenario:** The State prioritizes EBF and special education while limiting or reducing growth in discretionary and pilot programs.
- **Structural Adjustment Scenario:** Revenue actions (e.g., tax code decoupling) partially offset federal impacts, allowing modest but uneven growth in education funding.

## 7. Planning Considerations for Districts and the Board

Given the State's projected fiscal path, districts and Boards of Education may wish to:

- Incorporate multi-year budget forecasting that assumes slower State funding growth.
- Closely monitor State discussions around tax policy decoupling and Medicaid/SNAP cost shifts, which will influence education funding capacity.
- Maintain or rebuild local fund balances where possible to buffer against volatility.
- Prioritize investments with long-term cost containment benefits, such as staff retention, efficiency initiatives, and shared services.

## Conclusion

While K–12 education remains a core State priority, Illinois' projected structural deficits significantly increase fiscal risk over the next five years. The most likely impact is not immediate reductions, but rather slower growth, constrained flexibility, and heightened competition for General Funds. Proactive planning and realistic assumptions about State funding trajectories will be essential to maintaining program stability and educational outcomes in this evolving fiscal environment.

**\*\*In Illinois, a discretionary appropriation is a portion of the state budget that is not required by statute, formula, or constitutional mandate and therefore can be adjusted, reduced, delayed, or eliminated by the General Assembly during the annual budget process.**