

**REPORT**  
**STATE OF WISCONSIN**  
**JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS**  
**2023 ASSEMBLY BILL 793**

[Introduced by Representative Binsfeld and co-sponsored by Senator Cabral-Guevara]

This report relates to 2023 Assembly Bill 793, relating to modifying the tax treatment of college savings accounts and the employee college savings account contribution credit.

## **GENERAL NATURE OF PROPOSAL**

The bill modifies the individual income tax treatment for contributions to and withdrawals from college savings accounts and the employee college savings account contribution credit.

### **Contributions to and Withdrawals From College Savings Accounts**

Under the state's college savings programs, anyone may contribute to an account, commonly called a "529 account," for the benefit of a prospective student. Individuals may claim a deduction from state income tax for contributions to accounts established under Wisconsin's programs. The bill increases the maximum amount of contributions to a 529 account that may be deducted for state individual income tax purposes to \$5,000, indexed for inflation, or \$2,500, indexed for inflation, for a married individual filing a separate return, and repeals the contribution limitation for divorced individuals.

In addition, the bill revises certain references to federal law to more accurately reflect the state's prior conformation to the federal definition of qualified higher education expenses. The bill also amends the administration of college savings accounts to require the use of a first-in, first-out accounting method for account withdrawals and restrictions on carry-overs of contributions.

### **Employee College Savings Account Contribution Credit**

Under current law, with respect to the employee college savings account contribution tax credit, a qualified employer is eligible to claim an income tax credit for an amount equal to 25 percent of their contribution to an employee's college savings account. The credit is subject to a maximum that is 25 percent of the maximum amount an individual may claim as a deduction for a contribution to a college savings account.

The bill revises the maximum to be 50 percent of the amount the employer contributes, not to exceed \$800, adjusted for inflation. The bill also specifically permits sole proprietors to claim the employee college savings account contribution tax credit, and the bill specifies that credits may be claimed only for employees whose compensation is reported, or required to be reported, on a W-2 form.

## **LEGALITY INVOLVED**

The bill raises potential issues relating to the receipt of federal funds through the state fiscal recovery fund (SFRF) created under the American Rescue Plan Act (ARPA). In total, Wisconsin received \$2.53 billion in SFRF funds. ARPA prohibits states from using SFRF funds "to either

directly or indirectly offset reduction in [their] net tax revenue” that results from a change in law that “reduces any tax.” [42 U.S.C. s. 802 (c) (2) (A).] This is sometimes referred to as the “tax offset” provision under ARPA.

### **Treasury Determination**

The question posed by the tax offset provision, in relation to the bill, is whether the U.S. Department of the Treasury (the Treasury) would determine there were insufficient funds from other sources to offset the reduction in revenue under the bill. It appears unlikely that the Treasury would make this determination in the current fiscal biennium, as explained below.

In its guidance, the Treasury has stated that a violation of the tax offset provision occurs when there is a reduction in net tax revenue caused by changes in the law and the state cannot identify sufficient funds from sources other than federal relief funds to offset the reduction in net tax revenue. [31 C.F.R. 35.8.] Statements issued by the Treasury in connection with its publication of the final rule refer to “three sources of funds that may offset a reduction in net revenue” without resulting in a violation, which are: “organic revenue growth, increases in revenue due to policy changes (e.g., an increase in tax rate), and certain cuts in spending.” [See 31 C.F.R. Part 35, Final Rule, Supplementary Information, pg. 316.<sup>1</sup>]

The state Department of Administration (DOA) is responsible for reporting reductions in net revenue under ARPA. The department calculates that, as of August 28, 2023, the remaining margin for tax reductions before triggering potential recoupment was around \$113 million for fiscal year 2023-24 and \$319 million for fiscal year 2024-25. However, DOA assumes the general fund surplus cannot be included as available for covered tax reductions. This appears to contradict the Treasury’s suggestion in the supplemental information accompanying the final rule, which is that organic revenue growth may offset revenue reduction, as described above.

If the general fund surplus were taken into account, the remaining margin for tax reductions would be significantly greater. As of January 24, 2024, the Legislative Fiscal Bureau projects that the closing, net general fund balance at the end of this biennium (June 30, 2025) is estimated to be \$3.15 billion. Because this is more than the \$2.53 billion in total SFRF monies received, it is reasonable to assume the state could identify funding from other sources to offset any revenue reduction under the bill for the current fiscal biennium. The state also maintains a budget stabilization fund, consisting primarily of excess state revenues over budgeted amounts, which had a cash balance of \$1.79 billion, as of the end of May, 2023.

For these reasons, notwithstanding DOA’s estimate, it appears unlikely that the Treasury would determine there were insufficient funds from other sources to offset the revenue reduction under the bill for the current fiscal biennium. With respect to future fiscal years, beyond the current fiscal biennium, it is unclear whether the tax offset provision under ARPA will continue to apply. The period covered by the tax offset provision ends on the last day of the fiscal year in which all SFRF funds have been expended by a state or returned to the Treasury. [31 C.F.R. 35.3.] If the tax offset provision under ARPA applies in future fiscal years, beyond the current fiscal biennium, the Treasury’s likelihood of making an adverse determination may differ, depending on the amount and source of monies in the general fund at that time.

### **Federal Court Injunctions**

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<sup>1</sup> Visit <https://home.treasury.gov/system/files/136/SLFRF-Final-Rule.pdf> to review the Treasury’s supplemental information for 31 C.F.R. Part 35, Final Rule.

In addition to the fact that an adverse determination from the Treasury appears unlikely, the outcomes in several recent court actions have cast doubt over the federal government's ability to enforce the tax offset provision under ARPA. Various states have filed lawsuits, individually or in combination with other states, against Treasury Secretary Janet Yellen and the Treasury, in relation to the enforcement of the provision.

Most significantly, the tax offset provision was held unenforceable by the U.S. Court of Appeals for the Eleventh Circuit, in *West Virginia v. U.S. Dep't of the Treasury*, 59 F.4th 1124 (11th Cir. 2023). The Eleventh Circuit upheld a lower court's order enjoining enforcement against 13 state plaintiffs. In its decision, the court affirmed that Congress is given spending authority in the Constitution and has the power to condition giving money to states on certain action, but that any conditions must be (among other factors) unambiguous. [Id. at 1140–41.] However, in this case, the court said the provision fails to provide a standard against which a state can assess whether it will reduce or has reduced net tax revenue, and it fails to define what a "direct or indirect offset" means. The court also said the novelty and scope of ARPA compounds those issues because the restriction is targeted at a state's entire budget. [Id. at 1144–47.]

Ultimately, the Eleventh Circuit found in favor of the plaintiffs and upheld an injunction preventing the tax offset provision from being enforced against the 13 states. As a result, the provision is not enforceable against Alabama, Arkansas, Alaska, Florida, Iowa, Kansas, Montana, New Hampshire, Oklahoma, South Carolina, South Dakota, Utah, and West Virginia.

Additionally, the U.S. Court of Appeals for the Sixth Circuit upheld an injunction blocking enforcement of the tax offset provision against Tennessee, one of the two state plaintiffs in *Kentucky v. Yellen*, 54 F.4th 325 (6th Cir. 2022). In its ruling on the merits, the Sixth Circuit found that the language of the offset provision was "impermissibly vague." [Id. at 330.] According to recent news reports, the Treasury has chosen not to appeal this decision.

Finally, in a lawsuit brought by Texas, Mississippi, and Louisiana, a federal district court in Texas upheld an injunction against enforcement of the tax offset provision against those states, in *Texas v. Yellen*, 597 F.Supp.3d 1005 (N.D. Tex. 2022). The court said it granted an injunction because the provision was coercive and commandeering. [Id. at 1012-15.] The U.S. Court of Appeals for the Fifth Circuit granted an appeal, and heard oral arguments on April 3, 2023, but the court has not yet released a decision.

Similarly to these states, if the Treasury sought recoupment of any SFRF funds expended by Wisconsin, as a result of the enactment of the bill, the state could contest the validity of the Treasury's action in court. This could include arguments against enforcement that have been successful in other jurisdictions.

## **FISCAL EFFECT**

The Department of Revenue (DOR) estimates that increasing the maximum deduction amount for a contribution to a college savings account will reduce state revenue by approximately \$1.7 million annually beginning in fiscal year 2025. DOR also estimates that the modifications to the employee college savings account contribution credit will result in some additional minimal state revenue loss. DOR notes that, to the extent allowing sole proprietors claims creates a new pool of credits, the fiscal impact will be larger.

## **PUBLIC POLICY INVOLVED**

The Joint Survey Committee on Tax Exemptions finds that the tax exemption related provisions in the bill are good public policy on a vote of Ayes, 9; Noes, 0.

**03/07/24**

**JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS**