

**REPORT**  
**STATE OF WISCONSIN**  
**JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS**  
**2023 ASSEMBLY BILL 387**

[Introduced by Representative Goeben and cosponsored by Senator Quinn]

This report concerns 2023 Assembly Bill 387, relating to creating a child care reimbursement account program, providing an income tax subtraction for certain contributions to a child care reimbursement account, and granting rule-making authority.

## **GENERAL NATURE OF PROPOSAL**

Assembly Bill 387 requires the Department of Financial Institutions (DFI) to establish a child care reimbursement account program under which a parent or other legal guardian may create a state tax-advantaged account to pay qualifying expenses of a qualifying child. Any person, with the account owner's permission, may contribute to an account established under the bill, and they may deduct the amount from income for state tax purposes. Assembly Bill 387 specifies that the maximum total contribution per account per calendar year is \$10,000. Any funds contributed to an account during a calendar year that are not expended for qualifying expenses incurred by December 31 of that year are forfeited to the program vendor.

A "qualifying child" is defined as a dependent who is less than 13 years of age. "Qualifying expenses" include expenses for the care of a qualifying child or household services incurred to enable the parent or legal guardian to be gainfully employed.

The bill requires DFI to contract with a vendor to administer the program. The program vendor may charge fees to account owners to cover the cost of administering the program. The contract must require the vendor to report certain information to the Department of Revenue (DOR), as specified in the bill.

## **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 Assembly Bill 387, 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 is 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. The opening balance of the general fund was estimated at \$6.88 billion, as of July 1, 2023, according to the Legislative Fiscal Bureau (LFB). Because this is more than double the \$2.53 billion SFRF monies received, it would be reasonable to assume the state could identify funding from other sources to offset revenue reduction under Assembly Bill 387 for the current fiscal biennium. The state also maintains a budget stabilization fund, consisting primarily of excess state revenues over budgeted amounts, with 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 Assembly Bill 387 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**

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

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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.

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, Louisiana, Mississippi, Montana, New Hampshire, Oklahoma, South Carolina, South Dakota, Tennessee, Texas, 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**

DFI estimates that its annual costs to administer the child care reimbursement account program would be \$114,000 (for staffing and expenses), plus indeterminate sums needed to retain a qualified third-party vendor and engage in marketing efforts to promote participation in the program. No estimate has been submitted from the Department of Revenue relating to the reduction in tax revenue under Assembly Bill 387.

## **PUBLIC POLICY INVOLVED**

The Joint Survey Committee on Tax Exemptions finds that the tax exemption created in the 2023 Assembly Bill 387 is **not good** public policy on a vote of Ayes, 6; Noes, 3.

**09/11/23**

**JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS**