

Constitutional Highlights

From the Legislative Reference Bureau

Wisconsin Legislative Reference Bureau

October 2005, Volume V, No. 3

Wisconsin Constitution Article VIII, Section 3 CREDIT OF THE STATE

[With certain exceptions,] the credit of the state shall never be given, or loaned, in aid of any individual, association or corporation.

History and purpose of the section

Article VIII, section 3 was included in the original Wisconsin Constitution. The provision, along with the other provisions in article VIII of the Wisconsin Constitution, particularly the limits on contracting state debt in sections 4, 6, and 7 and the internal improvements clause in section 10, reflects the concern at the time our state constitution was drafted with the financial problems experienced by other states. The difficulties arose largely from debt that the states had incurred to provide financing for transportation projects. See, *Bushnell v. Beloit*, 10 Wis. 195 (1860), and Rick Champagne and Pam Kahler, *Internal Improvements*, Constitutional Highlights from the Legislative Reference Bureau, Vol. II, (2002).

The purpose of article VIII, section 3 is to prohibit the state from acting as a guarantor of debt incurred by someone other than the state. *State ex rel. Thomson v. Giessel*, 271 Wis. 15, 29 (1955). It was logical for the framers of the constitution, having placed limits on the ability of state government to be involved in the construction of works of internal improvement and to incur debt, to prohibit the state from guaranteeing payment of debt issued by another entity, a railroad company, for example.

Article VIII, section 3 was amended in 1975 to reflect the creation of article VIII, section 7 (2) (a) of the Wisconsin Constitution. That provision allows the state to incur debt to acquire, construct, or improve land, waters, property, highways, railways, buildings, equipment, or facilities for public purposes and to obtain funds for veterans' housing loans.

How courts interpret the section

The earliest cases interpreting article VIII, section 3 involved challenges to actions taken by local governments. The argument was that cities and towns were part of the state and that the state could not grant to a part of itself the power to do what the whole could not do. The Wisconsin Supreme Court rejected the notion that a city or a town is part of the state for the purpose of applying this provision, pointing out that other parts of article VIII obviously could not apply to local governments. *Clark v. City of Janesville*, 10 Wis. 136, 170 (1860). A city or town could give or loan its credit in aid of a corporation without the credit of the state being pledged in any way. *Bushnell v. Beloit*, 10 Wis. 195, 222 (1860). See also, *State ex rel. Hammermill Paper Co. v. La Plante*, 58 Wis. 2d 32 (1973) (holding, in a case involving the issuance of industrial revenue bonds, that the credit of a city is not the credit of the state).

Later cases required the court to consider whether the restriction on the lending of the state's credit applied to situations that more closely involved the state. Some of the cases concerned private nonprofit corporations created by state agencies to borrow money and use it to build buildings to be used by the state, such as state office buildings and university dormitories. Typically, the state leased the building back and the lease payments were set at a level sufficient to enable the nonprofit corporation to pay off the debt that it had incurred. The Wisconsin Supreme Court upheld these arrangements, holding that such a corporation is not an agency or instrumentality of the state and that the lease payments were payments for a service rendered, namely the use of the building, and did not represent an obligation on the state to pay the debts of another. *State ex rel. Wisconsin Dev. Authority v. Damman*, 228 Wis. 147 (1938), *State ex rel. Thomson v. Giessel*, 267 Wis. 331 (1954), and *State ex rel. Thomson v. Giessel*, 271 Wis. 15 (1955).

More recent cases involved authorities, such as the Wisconsin Housing and Economic Development Authority (WHEDA). An authority is a body "corporate and politic" that is intended not to be a state agency but is designed to carry on public purposes under state control. The Wisconsin Supreme Court recognized that the purpose of creating authorities was to allow the performance of activities that the state could not perform directly because of various constitutional limitations on the power of the state, including article VIII, section 3. However, the court rejected the argument that this purpose caused the laws creating authorities to be unconstitutional, saying "it is never an illegal evasion to accomplish a desired result, lawful in itself, by discovering a legal way to do it." *State ex rel. Warren v. Nusbaum*, 59 Wis. 2d 391, 425 (1973).

The central question in determining whether a law unconstitutionally gives or loans the credit of the state is whether the state has assumed a legally enforceable obligation to pay the debts of another. If the answer is "no," there is no violation of article VIII, section 3. *State ex rel. Wisconsin Dev. Authority v. Damman*, 228 Wis. 147, 197 (1938). Some parties have argued that a violation occurred because the involvement of the state was such that creditors of another entity would expect the state to pay in case of default or that the legislature would feel obligated to pay the debts of another entity. The court found that the expectations of creditors and the pressure that legislators might feel are not relevant to the constitutional issue. *State ex rel. Thomson v. Giessel*, 271 Wis. 15, 32 (1955). Some statutes specify that the state has a moral obligation to pay the debts of another entity in case that entity defaults. See, for example, section

234.93 (6) of the statutes, relating to WHEDA. But the statutes also provide that the state is not liable on the notes or bonds issued by those entities. There is no enforceable obligation, therefore the language acknowledging a moral obligation does not cause a constitutional violation. *Wisconsin Solid Waste Recycling Authority v. Earl*, 70 Wis. 2d 464, 482 (1975).

Strategies for reconciling legislation with the section

Legislation is often designed to provide financial assistance to individuals, associations, or corporations. There are many forms that governmental financial assistance might take. Conflict with article VIII, section 3 can be avoided by using a form of financial assistance other than a loan guarantee. Tax credits, grants, and even loans directly from the state are some examples of alternatives that do not give or loan the credit of the state.

If a loan guarantee program is desired, it is possible to have an entity other than the state provide the guarantee. For example, the Wisconsin Health and Educational Facilities Authority and WHEDA operate loan guarantee programs. See section 231.31 and subchapter II of chapter 234 of the statutes. When legislation creates a new entity to operate a loan guarantee program there is a risk that the entity will be so closely connected to the state that a court will find a violation of article VIII, section 3. Attempting to avoid that pitfall, legislation may result in so little state control that the entity cannot be forced to follow the legislature's will. This is a risk especially when trying to use a private, nonprofit corporation to run a program, such as a loan guarantee program. The Wisconsin Constitution authorizes corporations to be created only under general laws. This limits the ability of the legislature to impose specific requirements on one corporation. See article IV, section 31 (7) and article XI, section 1 of the Wisconsin Constitution and the Opinion of the Attorney General, 72 OAG 135 (1983) (discussing the limited control that the state could exercise over the Wisconsin Higher Education Corporation). Because an authority is neither a state agency nor a private corporation, the applicability of many state laws must be determined each time a new authority is created. For several reasons, then, when a new loan guarantee program is proposed, it may be advisable to assign administrative responsibility to one of the existing authorities.



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