


CSG GROWTH & PROSPERITY >>> VIRTUAL SUMMIT OF THE STATES 2.0

**The Future of Federalism:
State/Federal Relations
in an Era of Austerity**

**Thursday, April 14
3:00 p.m. EDT**

CSG GROWTH & PROSPERITY >>> VIRTUAL SUMMIT OF THE STATES 2.0



**Jim Blumstein,
Professor of Law at Vanderbilt University**

ON COOPERATIVE FEDERALISM

**THE FUTURE OF FEDERALISM:
STATE/FEDERAL RELATIONS
IN AN ERA OF AUSTERITY**

**Council of State Governments' Growth and
Prosperity Virtual Summit
April 14, 2011**

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BRIEF OVERVIEW OF PRESENTATION

- **Cooperative Federalism: How It Works, Its Rationale, and Some Risks**
- **Some Constitutional Basics**
- **Application to State Challenges to the Affordable Care Act – The Expanded Medicaid Mandate**

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**COOPERATIVE
FEDERALISM:
HOW IT WORKS,
ITS RATIONALE,
AND SOME RISKS**

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**FEDERAL-STATE PARTNERSHIP WITH FEDERAL
FUNDING MATCHING STATE EXPENDITURES**

- States Voluntarily Apply for Funding
- Federal Government Approves State's Application and Automatically Matches State Spending Under a Formula
 - The Automatic Matching Feature Describes Medicaid
 - Programs Such as the Children's Health Insurance Program (CHIP) Are Different, With a Fixed Federal Allocation to a State Based on a Formula
- Ongoing Nature of Relationship
- Federal Government Establishes Parameters or Rules for Spending
 - Targeted Covered Services
 - Eligibility of Potential Beneficiaries
- Federal Regulations Typically Allow States Some Flexibility in Determining (i) Range of Covered Services Actually Provided and (ii) Eligible Beneficiaries Actually Enrolled Within Federally Established Parameters

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BENEFITS FOR THE STATES

- Enhanced Choices/Options
- Access to Additional Resources and Programmatic Benefits – But Limited By State Fiscal Constraints Imposed by State “Co-payment” Requirements
- Bitter With the Sweet – States Must Accept Federal Terms and Conditions Attached to Receipt of Federal Funds

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BENEFITS FOR THE FEDERAL GOVERNMENT

- Achieves Federal Priorities and Establishes Federal Program Leadership
- Builds on State Administrative and Political Infrastructure
- Encourages State Buy-in Through Programmatic Investments With Favorable Federal Financial Incentives
- Leverages Federal Resources by Requiring Substantial State Expenditures

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RISKS TO STATES

- Political Moral Hazard
- Incentives for Program Expansion by States
 - The Problem of Leaving Federal Money On the Table
 - The Problem of Receiving Bill Gates’ House With Attendant Spending Obligations
- Risk of Mandated Program Expansion Imposed by the Federal Government After Initial State Decision to Participate
 - Effect on State Costs of Participation
 - Displacement of Political Accountability With Federal Government Driving State Expenditures After Initial State Decision to Participate
- The “Lock-in” Effect
 - State-level Political Dependency
 - Political Narcotic Effect
 - Difficult to Reduce or Eliminate Cooperative Federalism Programs Because of Fiscal Pain of Withdrawal
 - The Bait and Switch Problem: Impetus for Federally Mandated Program Expansions (The Story of Medicaid)

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RISKS TO FEDERAL GOVERNMENT

- Under Automatic Matching (Medicaid), State Program Expansion Drives the Federal Budget
- Incentive to Ratchet Up Program Costs, as Federal Costs Are Driven in Large Part by State Political Choices
- Incentive for States’ Game Playing by Raising Funds in Ways that Eliminate the Restraint on State Spending by the State Expenditure Requirements (Medicaid Provider Taxes)
- Program Advocates May See These “Risks” to the Federal Government as Advantages -- Ways Around Budgetary Resistance to Increases in Program Expenditures

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SOME CONSTITUTIONAL BASICS

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STATES MUST BE ALLOWED TO DECIDE KNOWINGLY AND VOLUNTARILY WHETHER OR NOT TO PARTICIPATE IN A COOPERATIVE FEDERALISM PROGRAM

- The Anti-Commandeering Principle Protects States from Involuntarily Participating in a Cooperative Federalism Program
- The Federal Government Can Financially Induce but not Mandate State Participation
- Such Inducement Cannot Cross the Line Into Coercion

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THE RELATIONSHIP BETWEEN THE FEDERAL GOVERNMENT AND THE STATES IN COOPERATIVE FEDERALISM PROGRAMS IS GOVERNED, IN GENERAL, BY PRINCIPLES OF CONTRACT LAW

- Programs Such As Medicaid Are Ongoing in Nature
- These Ongoing Programs Are Relational Contracts
- Under Conventional Contract Doctrine, There Is a Significant Difference Between What a Party Can Do at the Formation of the Contract (Contract Formation Stage) and When An Ongoing Contract is Modified (Contract Modification Stage)
 - The Risk of Excessive Leverage at Contract Modification Stage
 - The Duty of Fairness at Contract Modification Stage

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THE CLEAR STATEMENT RULE

- Terms and Conditions of Cooperative Federalism Programs Such as Medicaid Must Be Spelled Out “unambiguously” so that States Can Knowingly Make a Choice Regarding Participation “Cognizant of the Consequences of Their Participation”
- Knowing Acceptance by States of Conditions Attaching to Federal Spending Programs Is a Cornerstone of the Constitutional Legitimacy of Federal Spending Programs
- Knowing Acceptance Cannot Exist Unless States Are Aware, in Advance, of the Conditions Being Imposed on Them When They Choose to Participate in a Cooperative Federalism Program

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THE CLEAR STATEMENT RULE

- States Can Only “Knowingly Accept” Conditions of Which They Are Aware and Which They Can “Ascertain” At the Time They Decide to Participate
- Implied Conditions Can Satisfy the Clear Statement Rule If They Are Foreseeable and Comport With Community Standards of Fairness
 - The Proper Perspective For Making This Assessment Is That of the State Official Who Must Decide Whether the State Should Participate in the Cooperative Federalism Program
 - That State Official Must “Clearly Understand” the Obligations Being Undertaken By the State When It Chooses to Participate

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THE TIMING OF THE CLEAR STATEMENT OBLIGATION

- Contract Formation Stage vs. Contract Modification Stage
- Should Apply at Contract Formation Stage to Allow States to Determine Whether Knowingly to Accept Obligations from Participation in a Cooperative Federalism Program
- Application at Contract Modification Stage Allows Federal Government to Perform a Bait and Switch – Setting a Low Standard of Obligations at Contract Formation and Then, Through Contract Modification, Raising the Bar Once States Are Locked In to a Program
- Clear Statement Rule Has Constitutional Foundation – Respecting State Autonomy and Right to Decline to Participate in a Cooperative Federalism Program

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APPLICATION TO STATE CHALLENGES TO THE AFFORDABLE CARE ACT – THE EXPANDED MEDICAID MANDATE

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THE EXPANDED MEDICAID MANDATE OF THE AFFORDABLE CARE ACT (ACA)

- Traditional Medicaid Linked to Public Assistance – *i.e.*, Poverty Medicine
- Federal Premium Subsidy on State-based Exchanges for Persons With Incomes from 100% - 400% of Poverty
- No Federal Premium Subsidy on State-based Exchanges for Persons With Incomes under 100% of Poverty
- New Medicaid Requires States to Include Persons With Incomes Under 133% of Poverty or Be Excluded Entirely from Medicaid

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THE ACA IMPOSES CONDITIONS ON MEDICAID IN THE NATURE OF CONTRACT MODIFICATION

- Medicaid Is an Ongoing Program – A Relational Contract
- The Contract Formation Stage Occurred When a State Chose to Participate in Medicaid

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THE ACA IMPOSES CONDITIONS ON MEDICAID IN THE NATURE OF CONTRACT MODIFICATION

- For a State to Be “cognizant of the consequences of [its] participation” in Medicaid, It must Be Aware of and Be Able to Ascertain the Nature, Scope, and Magnitude of Its Financial Obligation
 - Congress’ Power to Impose Conditions on Cooperative Federalism Programs “does not include surprising participating States with postacceptance or ‘retroactive’ conditions”
 - States Cannot Knowingly Accept Terms and Conditions on Federal Spending Programs If They Are Unaware of or Cannot Reasonably Foresee the Conditions Imposed
 - Fine-tuning the Specific Application of a Program, Within the Program’s Original Parameters, Is Clearly a Foreseeable Implied Term of a Contract in a Cooperative Federalism Program
 - A Substantial Modification of an Ongoing Program, Where That Program Comprises a Substantial Component of a State’s Budget (As With the ACA), Imposes Unforeseeable Financial Obligations Beyond What Could Have Been Expected When States Initially Chose to Participate in Medicaid

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IS THE CLEAR STATEMENT OBLIGATION SATISFIED BY THE ACA?

- Clear Statement Is Not Satisfied If It Applies at the Contract Formation Stage Regarding the Additional Conditions Imposed on State Medicaid Programs by the ACA
- Clear Statement Is Satisfied If It Applies at the Contract Modification Stage Regarding the Additional Conditions Imposed on State Medicaid Programs by the ACA
 - States Are Aware of Their Obligations Effective January 1, 2014
 - Is This Enough?

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IS THE CLEAR STATEMENT OBLIGATION SATISFIED BY THE ACA?

- My View of the Proper Resolution of This Timing Issue
 - Additional Protections Are Accorded at Contract Modification Because of Concerns With Excessive Leveraging
 - Consider This Example:
 - A Fishing Vessel Goes Out to Sea
 - Once the Ship Is in Fishing Waters, the Crew Demands a Substantial Wage Increase
 - This Additional Term Is Imposed at Contract Modification and Is Not Upheld Because of Excessive Leveraging
 - Had the Crew Sought the Same Raise Before Setting Sail (*i.e.*, at Contract Formation), a Different Result Would Obtain

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IS THE CLEAR STATEMENT OBLIGATION SATISFIED BY THE ACA?

- To Protect the Integrity of State Decisionmaking and Its Political Process, a State Must Be Able to Understand Clearly the Financial Implications of Its Decision to Participate in Medicaid
 - And that Understanding Must Arise at the Contract Formation Stage
 - Allowing Clear Statement to Be Satisfied at the Contract Modification Stage Allows for Excessive Leveraging – Bait and Switch
 - It Allows an End-run Around the Protections Contemplated by the Clear Statement Rule

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IS THE CLEAR STATEMENT OBLIGATION SATISFIED BY THE ACA?

- But the Objective of the Clear Statement Rule Is to Give State Officials a Clear Understanding of Their Fiscal Risks and Obligations When They Sign Up for an Ongoing Federal Spending Program
- If, as the Supreme Court Has Stated, Federal Power to Impose Conditions “does not include surprising participating States with postacceptance or ‘retroactive’ conditions,” Then the Clear Statement Rule Must Be Applied at the Time That States Choose to Participate in Medicaid
 - That Standard Should Apply When (a) the Contract Modification is Substantial and Unforeseeable and (b) When the Contract Modification Has a Significant Financial Impact on a Program That Comprises a Substantial Component of a State’s Budget (such as Medicaid)

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WHAT IS THE APPROPRIATE REMEDY?

- The Federal Government Cannot Be Required to Maintain a Spending Program It No Longer Wishes to Sustain
- But, In the Absence of Clear Statement, It Cannot Impose Through Contract Modification Conditions That Are Substantially More Onerous and That Affect a Substantial Component of a State's Budget
- To Achieve Its Goals under ACA, the Federal Government Must Recreate a Contract Formation Situation, Where It Can Provide a State With a Clear Statement of Its Obligations under New Medicaid
 - To Recreate Contract Formation, the Federal Government Must Discontinue Traditional Medicaid
 - The States Need Not Opt Out of Traditional Medicaid, Since Traditional Medicaid Would No Longer Exist
 - This Would Get the Political Accountability Right
 - States Face No Choice Since Their Continued Participation in Traditional Medicaid Is Precluded by Federal Action

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WHAT IS THE APPROPRIATE REMEDY?

- The Federal Government Can Achieve Its ACA Goals by Establishing New Medicaid
 - This is Contract Formation
 - States Would Be Invited to Opt In to New Medicaid (Not Opt Out of Traditional Medicaid)
 - Clear Statement Would Then Apply at the Appropriate Contract Formation Stage
 - States Would Then Be Able Knowingly to Accept the Terms and Conditions of New Medicaid – Covering Persons With Incomes Under 133% of Poverty
 - State Officials Would Clearly Understand the Nature, Scope, and Magnitude of Their Obligations Under New Medicaid
 - The State's Political Process Would Then Be Invoked to Determine Whether to Sign Up for New Medicaid – Not to Opt Out of Traditional Medicaid

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Questions?

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