

An Observation of the State-Federal Relationship

BY WILLIAM T. POUND

Federalism always has been one of the most significant features of the American constitutional system. Its future will likely see both cooperation and conflict. That's nothing new. Federalism is, by its nature, a system of dynamic tension between levels of government and is constantly evolving into new relationships between states and the nation.

The American constitutional division of authority between nation and state has been emulated by many other countries since 1787, but in few as successfully as it has developed in the United States.

Before the Civil War, states generally dominated American federalism. But a stronger national government emerged after the war and grew with the advent of the income tax, World Wars I and II, and the Great Depression. A reinvigoration of state government began in the 1950s, however, with the formation of The Advisory Committee on Intergovernmental Relations to strengthen federal-state-local relationships. With the modernization of state legislatures in the 1960s and '70s, a new balance in our federal system emerged.

The 1960s saw the creation of Medicaid, a shared state-federal program, and in the '70s, general revenue sharing provided unrestricted federal financial assistance to states and localities. This experiment with "no-strings" and non-categorical sharing of federal revenues did not have a long life, however.

The last 30 years have been a period of more balanced federalism. State governments, for much of the period fiscally healthy, have become the country's creative laboratories and the initiators of most of the innovation in public policy. Creative environment and energy legislation, novel education reform and inventive health policy all flowed from the states.

The current economic recession, which began in December 2007, is one of the great-



est challenges to healthy federalism and to the ability of states to carry out their role as partners in the federal system. Fiscal shortfalls and constitutional requirements for balanced budgets restrain the capacity of the states to maintain their traditional priorities in K-12 and higher education, transportation and health care.

At the same time, the ability of the federal government to deficit spend, particularly as a counter to recession, allows it to expand its initiatives and, if it desires, direct states to act in particular ways at a time when it is very difficult for them to resist.

The Obama administration has expanded the use of the carrot in federal financial assistance to achieve its goals, particularly in education with the Race to the Top competition for funds. State and local governments still provide more than 90 percent of K-12 education funding, but the federal government has found an effective means of nationalizing goals through its much smaller share of the funding. Pushback has begun, however, with a number of states opting not to participate.

Whether this is a temporary change in the state-federal relationship or a more permanent one remains to be seen. There certainly

has been a growth in the percentage of federal funds in state budgets over the last 50 years, with Medicaid the big ticket item. Medicaid is now the primary vehicle for the expansion of health care to the uninsured. It currently accounts for 21 percent of state budgets and grows by the year. Under the vast new federal health reform, conflicts over the regulation of insurers, the operations of the exchange programs and risk pool funding are unavoidable.

The temporary stimulus of the American Recovery and Reinvestment Act funds soon will be over and their impact on cushioning state budgets from the downturn will be gone. What remains will be a large federal deficit. Future federal spending on domestic discretionary programs will be flat or declining. Reducing the deficit will require reduced spending or new revenues, or both. Either solution will affect state governments. The search for new revenues could have a major effect on traditional state revenue sources, particularly a national Value Added Tax on state sales taxes. It is easy to see considerable state-federal tension arising from this debate.

Many of the formal mechanisms of intergovernmental cooperation have been eliminated. The Advisory Committee on Intergovernmental Relations was abolished, a victim of rising partisanship in our politics. Intergovernmental concerns are not often prominent in congressional debate, though organizations like NCSL work to keep state concerns in the national dialogue.

Nearly all of our major domestic policy programs—Medicaid, family assistance, transportation and education—are managed by states or localities. This will only increase with health care expansion. In other policy areas the states have already prodded the federal government to act. The recent Arizona immigration law, state renewable energy standards, greenhouse gas standards, universal health coverage in several states, and education reform are examples.

The creative tension in federalism, however, can only be maintained by allowing a broad freedom of action in the states and avoiding over-reaching federal preemption and mandates.

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