June 2012
*Center for Tenth Amendment Studies*

# A Silver Lining: The Supreme Court's Ruling on ObamaCare's Medicaid Expansion

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## Key Points

- The Supreme Court handed down a historic decision in ObamaCare. The law's main provisions were unfortunately upheld.
- The Court struck down the Medicaid expansion provisions of ObamaCare. In doing so, a majority of the Justices embraced important federalist principles, sometimes departing from long-standing precedent.
- In its ruling on Medicaid, the Court agreed with the Texas Public Policy Foundation's view that conditions attached to a federal program must not go beyond the manner in which federal funds are spent. States will now be shielded from some of the worst excesses of federal overreach.

## Introduction

The Supreme Court's decision in ObamaCare was historic on many levels. The main provisions of ObamaCare were upheld, on the basis of a questionable distinction between a "tax" and a "tax penalty." But a majority of the Justices agreed on a remarkable number of quintessentially Tenth Amendment propositions, sometimes in dramatic departures from longstanding precedent.

Writing for the majority, Chief Justice John Roberts managed to chase the individual mandate (the mandate that most working Americans purchase health insurance or pay a tax penalty each year) out from under the reinforced bunker of the federal government's interstate commerce power and onto the thin ice of a tax that is not a tax penalty.* That could have major consequences, both for the long-term future of the Court's Commerce Clause jurisprudence, and for the parliamentary devices that could be used to defeat the law right now: Revenue measures (and bills that repeal them) are generally favored and face fewer obstacles to enactment.

But what could turn out to be a historic shift was the Court's ruling on the federalism challenge to ObamaCare's Medicaid provisions. The Medicaid program was designed to serve certain categories of poor people: pregnant women, the disabled, needy families, children, etc. (Medi*care*, by contrast, serves the elderly, regardless of income). ObamaCare transforms that safety-net into a vast antipoverty wealth-redistribution scheme, and threatens states with the loss of all Medicaid funds if they don't comply.

That penalty was too much for the Roberts Court, which struck it down as unconstitutional in a milestone ruling.

Medicaid is a "cooperative condition grant program" under which the federal government offers state governments monetary incentives to adopt federal preferences on how to structure the program and ignore local preferences. Such programs represent a grave threat to the independent functioning of state governments, because the financial penalty for states that decline to comply with federal preferences are normally overwhelming, even when it involves a small fraction of the state budget. And ObamaCare reached much too far into the states' budgets.

Under ObamaCare, the penalty for not complying with the law's Medicaid-expansion provisions included not just the forfeiture of huge federal subsidies for the expansion (subsidies the state's residents are paying for in federal taxes) but also of all other federal Medicaid funds. On average, states devote nearly 22 percent of their budgets to Medicaid, and "anywhere from 50 percent to 83 percent" of that is paid for by the federal government."[1] For the Court, that penalty was too stiff, and left states with little choice in fact but to comply. The Court reasoned that because the new conditions under ObamaCare constituted not a "modification" of

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* Under long-standing precedent, a tax penalty is unconstitutional if it is designed to enforce a mandate that is unconstitutional.

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the program, but a fundamental transformation, they could not be conditioned on a penalty so onerous as the loss of Medicaid funds unrelated to the expansion.

## The Court's Analysis

This ruling may at first glance appear technical and esoteric. But in fact, it represents a significant curtailment of the federal government's power to compel state compliance with "generous" social programs. The Court ruled that it would be unconstitutional for the federal government to penalize states that refuse to comply with the Medicaid expansion by cutting off *all* Medicaid funding.

And yet if states refuse to participate in the expansion, the federal government may still cut off the subsidies provided by ObamaCare for the expansion itself. That raises many of the same questions the Court thought it was resolving in this ruling. Still, the decision marks the first time in modern constitutional history that the framework of dual sovereignty—the independent existence of the states within their proper sphere of authority—has been used to limit the plenary federal power to tax and spend "for the general welfare."

That holding constitutes a resounding vindication of the position taken and advocated for by the Texas Public Policy Foundation and like-minded colleagues from the outset of this litigation. The Foundation submitted a brief for the 11th Circuit Court of Appeals, from which the case was before the Supreme Court, arguing that the penalties involved in the Medicaid expansion left states no choice "in fact" but to comply, and rendered any theoretical free choice illusory. The Foundation then published a lengthy law review article in the *Texas Review of Law and Politics* (fall 2011) further elaborating a theoretical critique of the Court's permissive doctrine of federal conditional grants, arguing that such programs erode both the accountability and responsiveness of federal and state government, in violation of the Court's emerging doctrine of federalism. Finally the Foundation submitted a brief for the Supreme Court in the present case, arguing that if ObamaCare's "heavy-handed expansion of Medicaid does not surpass [constitutional limits], no Act of Congress ever will" and that the Court should modify the unworkable coercion doctrine articulated in the seminal case of *South Dakota vs. Dole* (1987).

Against all expectations, the Court embraced every one of these positions, reversing not just both of lower courts, but also every other federal court that has upheld a coercive federal grant program in living memory. And, the consequences could be far-reaching, for now every federal conditional grant program may be constitutionally vulnerable on the basis of this ruling.

Justices Breyer and Kagan joined the Court's opinion on Medicaid. The opinion was largely embraced by the dissent, which would have gone even further. That leads to the first remarkable observation about the Court's opinion: Seven of the nine justices rejected the complete deference that federal courts had long shown the government in its exercise of the taxing-and-spending power.

As the Court noted, federal conditional grants are "much in the nature of a contract."[2] To be valid, contracts must be voluntarily entered into: It is a basic principle of contract law that coerced agreements are unenforceable. "The legitimacy of Congress's exercise of the spending power thus rests on whether the State voluntarily and knowingly accepts the terms of this contract."[3]

In both of its amicus briefs on this issue (for the 11th Circuit, and for the Supreme Court on Medicaid) the Foundation argued that ObamaCare impermissibly changes the terms of a contract in midstream.[4] In its brief before the 11th Circuit, the Foundation argued:

> The problems presented by any conditional federal grant program are particularly acute where the federal government makes more onerous the conditions attaching to an existing program in which the States are already heavily invested. Even assuming that the Medicaid program itself is not categorically coercive (an assumption that seems

> far less valid given the failure of any meaningful limit on the conditional spending power in the years since *Dole*), surely changing the original conditions on which States relied to their detriment in establishing federally-compliant Medicaid programs presents a different calculus: The case for arms-length contract principles upon which the State voluntariness requirement rests is far weaker when the conditions are made more onerous in mid-stream.[5]

This argument faced a major hurdle, however: The Social Security Act, which created Medicaid, has a specific provision that reserves "[t]he right to alter, amend, or repeal any provision" of that law.[6] In other words, when states first entered into the Medicaid program starting in the early 1970s, they were warned that the continued flow of federal matching funds might end if they did not accept future modifications of the original program. For many commentators and legal scholars, this appeared to foreclose any realistic possibility that the Court would strike down the Medicaid expansion requirement on the basis of a theory that did not also strike down Medicaid itself—and that was not going to happen.

The Court found a way to square this circle, however, by introducing a distinction heretofore unknown in Spending clause jurisprudence: that between a transformation of the original program and a mere modification of it. The Court noted that Medicaid was designed to cover medical services for four particular categories of the needy: the disabled, the blind, the elderly, and needy families with dependent children. It then noted that ObamaCare's Medicaid expansion constitutes a "shift in kind, not merely degree" from this paradigm:

> Previous amendments to the Medicaid eligibility merely altered and expanded the boundaries of these categories. Under the Affordable Care Act, Medicaid is transformed into a program to meet the health care needs of the entire nonelderly population with income below 133 percent of the poverty level. It is no longer a program to care to the neediest among us, but rather an element of a comprehensive national plan to provide universal health insurance coverage.[7]

From the start of this litigation, the Foundation has argued that leaving the states with no choice in fact but to comply with the conditions attached to federal funds constitutes commandeering of state agencies in the service of federal policies. We noted that, according to the seminal cases of *New York v. United States*,[8] and *Printz v. United States*,[9] commandeering violates the imperative of protecting the federal structure of our Constitution, by reducing the accountability of government. Again the Court agreed: "Respecting this limitation is critical to ensuring that Spending Clause legislation does not undermine the status of the States as independent sovereigns in our federal system[….] When the State has no choice, the Federal Government can achieve its objectives without accountability, just as in *New York* and *Printz*."[10]

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The Court affirmed that Congress may attach appropriate conditions to the receipt of federal funds by the states. But "[c]onditions that do not here govern the use of the funds […] cannot be justified on that basis. When, for example, such conditions take the form of threats to terminate other significant independent grants, the conditions are properly viewed as a means of pressuring the States to accept policy changes."[11] This is the heart of the Court's ruling on Medicaid, and it represents a significant curtailment of the indeterminate and permissive doctrine articulated in the classic conditional spending case, *South Dakota v. Dole*.[12] It is also precisely the modification of the *Dole* doctrine that the Foundation argued for in its amicus brief for the Court, relying on the dissent of Sandra Day O'Connor in that case: The conditions must relate to the federal interest in a particular program, and should not touch on collateral programs or policies.

In *Dole* the Court ruled that Congress could penalize states that refused to raise their drinking age to 21 by taking away up to 5 percent of federal highway funds. Relying on *Steward Machine Co. v. Davis*,[13] the Court noted that Congress could "encourage" states to adopt certain policies by attaching conditions to federal funds—so long as it did not cross

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the line into compulsion. The Court recognized that "in some circumstances the financial inducement offered by Congress might be so coercive as to pass the point at which 'pressure turns into compulsion.'"[14]

Alas, *Dole* provided woefully little guidance on how courts should determine where that point is. That has led virtually all federal courts since then, including the district and appeals courts below, to allow any and all conditions attached to federal grant programs. But faced with ObamaCare's Medicaid expansion provision, the Supreme Court simply refused to go further:

> The Court in Steward Machine did not attempt to "fix the outermost line" where persuasion gives way to coercion. 301 U. S., at 591. The Court found it "[e]nough for present purposes that wherever the line may be, this statute is within it." Ibid. We have no need to fix a line either. It is enough for today that wherever that line may be, this statute is surely beyond it. Congress may not simply "conscript state [agencies] into the national bureaucratic army," [citation omitted], and that is what it is attempting to do with the Medicaid expansion.[15]

One of the two pegs on which the Roberts Court hung its ruling on Medicaid expansion was the comparatively modest scale of the penalty in *Dole*. "[T]he federal funds at stake [in *Dole*] constituted less than half of one percent of South Dakota's budget at the time."[16] By contrast, under the provisions of the Medicaid expansion, states stand to lose "not merely a relatively small percentage of its existing Medicaid funding, but all of it," on average more than 20 percent of each state's total budget. This, wrote Roberts, is "much more than relatively mild encouragement—it is a gun to the head."[17]

It is difficult to say what the consequences of the Court's ruling on the Medicaid expansion might be, given its embrace of the indeterminate reasoning in *Dole*. The distinction between "encouragement" and "compulsion" that is at the heart of *Dole's* coercion doctrine is based on a logical fallacy. No matter how onerous the penalty, coercion always theoretically implies free will on the part of the coerced party. The cost-benefit analysis may be weighted infinitely towards accepting the condition rather than foregoing the "offered" benefit, but there is still a choice. Conversely, even if the penalty is a single dollar, there is still coercion. This is especially true when the dollar in question belongs to the coerced party to begin with.

South Dakota's drinking age had no impact on the manner in which federal highway funds were to be spent. The issue of a given state's drinking age was entirely collateral to a program whose sole purpose was to enlist the states in maintaining the federal highway system. For this reason, it is difficult to escape the conclusion that *Dole* was wrongly decided: the Court should have struck down the penalty in the federal highway bill.

From a Tenth Amendment point of view, the potential strength of the Court's ruling lies in its embrace of an argument the Foundation made in its initial brief before the 11th Circuit: The penalty attached to a conditional federal program must preserve the states' freedom of choice "not merely in theory but *in fact.*" The Court thus elevated the actual burden on states above the theoretical freedom of choice that was the basis of the Court's permissive coercion doctrine. Courts will continue to have little guidance in determining how much pressure is too much—as noted above, the distinction is logically impossible to draw in any determinate or systematic way—but it seems fairly clear that courts will now find it much easier to conclude that penalties are unduly coercive if they are much more than nominal. That casts a dark shadow over the constitutionality of the whole range of existing federal grant programs. Many will now be vulnerable to constitutional challenge.

The other peg in the Court's ruling—the distinction between modification and transformation in programs whose condi-

tions are changed in mid-stream—also has significant promise, because it is based on the notion that the federal conditions must relate to the manner in which the federal funds are to be spent, and not collateral state programs or policies.

The Court did not explicitly overrule *Dole*, but this passage in its opinion is likely to replace the *Dole* formulation as the standard articulation of the coercion doctrine:

> Congress has no authority to order the States to regulate according to its instructions: Congress may offer the States grants and require the States to comply with accompanying conditions, but the States must have a genuine choice whether to accept the offer. The States are given no such choice in this case: They must either accept a basic change in the nature of Medicaid, or risk losing all Medicaid funding.[18]

## Conclusion

Despite the Court's holding that the individual mandate may be sustained as a "tax" and despite the limitations of its holding on Medicaid expansion, the Court's decision on Medicaid constitutes a significant victory for the Constitution and its Tenth Amendment. This silver lining in the Court's opinion was predicated on the Court's acceptance of a series of propositions that the Foundation and like-minded colleagues across the country have worked hard to bring into the mainstream, in particular the proposition that the Constitution requires accountable and representative government at all levels of the federal scheme.

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## Endnotes

[1] *National Federal of Independent Business v. Sebelius*, 567 U.S. ___ (2012), p. 59 (Scalia, J., dissenting). (Hereinafter, "NFIB v. Sebelius"; page numbers refer to the Court's opinion unless otherwise noted).
[2] *NFIB v. Sebelius*, p. 46.
[3] *NFIB v. Sebelius*, p. 47.
[4] *See*, TPPF S.Ct. Brief on Medicaid, p. 23.
[5] TPPF 11th Cir. Brief, p. 8.
[6] 42 U.S.C. § 1304.
[7] *NFIB v. Sebelius*, p. 53.
[8] 504 U.S. 144 (1992).
[9] 521 U.S. 898 (1997).
[10] *NFIB v. Sebelius*, pp. 47-48
[11] *NFIB v. Sebelius*, p. 50.
[12] 483 U.S. 203 (1987).
[13] 301 U.S. 548 (1937).
[14] 483 U.S. at 211, quoting Steward Machine Co. 301 U.S. at 590.
[15] *NFIB v. Sebelius*, p. 55.
[16] *NFIB v. Sebelius*, p. 51.
[17] Ibid.
[18] *NFIB v. Sebelius,* p. 58-59.

## About the Author

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