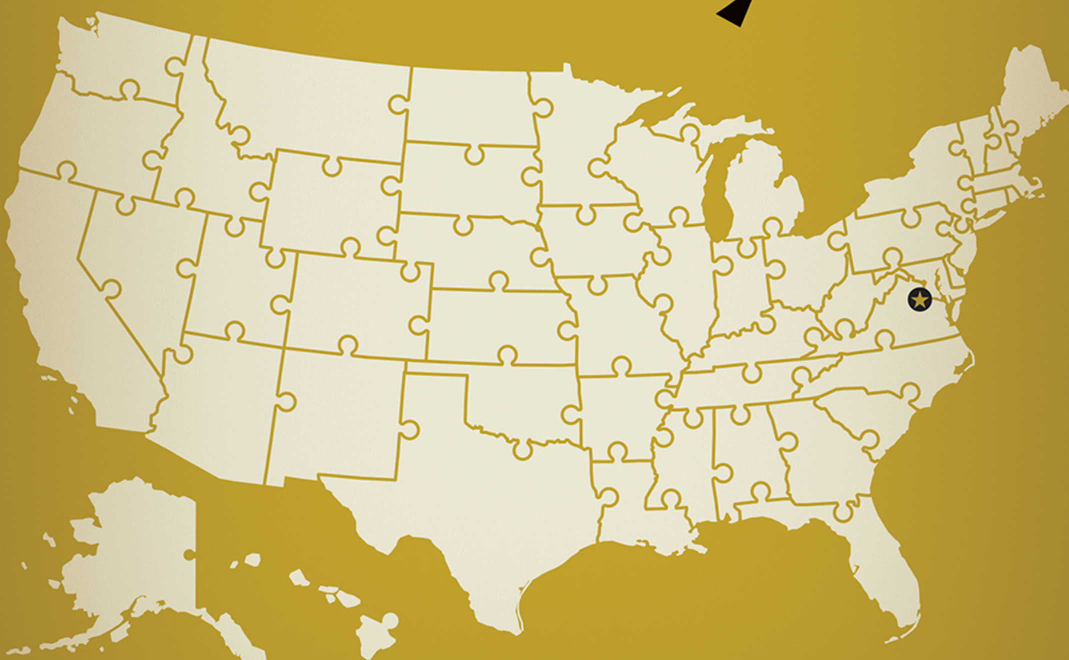
Perspectives on Political and Economic Governance

American Federalism Today



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DISCUSSANT REMARKS AND DISCUSSION

The Current State of Federalism

Discussants: Daniel L. Rubinfeld and Thad Kousser

Douglas Rivers: Why don't Delaware and Hawaii and Rhode Island get disproportionate shares? Or is this just due to agriculture?

Jonathan Rodden: They do.

Rivers: It didn't look like it on the graph.

Rodden: Let's see how . . . Which graph? Oh, the public-sector graph?

Rivers: Yes.

Rodden: That's an interesting question. I think this is why, I think when it comes to the public sector, I agree that it has a lot to do with . . . This is not a graph of transfers. If we look at a graph of the transfers, you'll see that Rhode Island does pretty well, and New Hampshire and Maine, but for some reason it doesn't have the same stimulative impact on the public sector. And so that leads to the . . . I think Michael's idea that it has a lot to do with sparsity, but if you just take, you run some regressions and you control for population density, federal transfer still is a pretty good predictor of public sector.

Paul E. Peterson: Do you control for percentage of the land in a state that is owned by the federal government? In Wyoming, Utah, Nevada, and other western states, the federal government owns a lot of the land.

Michael J. Boskin: Land, a huge amount.

Rodden: How that affects the state and local public sector, it's not clear to me. I mean, Wyoming runs its own hospital system and there's some other things that are interesting things that are going on in these states.

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Daniel L. Rubinfeld: Three great papers. With respect to Jonathan's paper, I wonder whether some of the phenomenon he's talking about has to do with capital improvements that made the need for employment to be reduced for certain public functions. And also I wonder whether the distinction between who is running the programs and who is funding them is crucial. A good example would be education in California. K–12 education is primarily managed locally, as we know, but over the years, education has been taken over by the state. That disconnect creates an analytical problem from my point of view, and it does suggest that it's a little hard to look at the data. Flipping over to David Brady's paper, what strikes me is that perceptions about the effectiveness of the public sector do matter, at least in the short run. So to the extent to which people are successful in characterizing programs one way or the other, that seems to have a big effect in the short run on how these programs are evaluated. But over time, I think the realities of the effectiveness of the program does make a difference, which is good news from my point of view. Moving on, I have a few things to say about John Cogan's excellent paper. I learned a lot from reading it, but what strikes me—and this is consistent with what I think he said in the paper—is if you put aside the entitlement programs, for lots of reasons revenue raising can be very effective at the federal level. So it's natural to think about growing the center, thereby substantially raising revenues, which in turn would make all these grant programs make sense. One of the examples that I think is worth discussing is a program that has been quite successful, Obamacare. What is interesting about the program is that it's an expansion of Medicaid.

Under Obamacare, Medicaid, as we know, has been given as an option for growth at the state level. Some states liked it, some didn't. But what is interesting is that a number of the states that accepted the expansion of Obamacare had opposed it initially but now are quite happy about it, because it's been very popular.

Now, to focus a little more on the revenue-raising side of the story: I always ponder the flypaper effect, which Jonathan has talked about in his paper. I think one thing we can all agree on is money does tend to stick where it hits. And there is a lot of evidence supporting the view that the flypaper effect applies to all levels of government. But the curiosity in my mind is the local level, particularly with respect to schools, where there are some efficiencies, despite the fact that the grants tend to stick, thereby effectuating budget cuts.

THAD KOUSSER: I'll try to be as concise as an academic possibly can. And I think I'm going to follow up; I'm reestimating my comments for your paper, and so I'll follow up with written comments. Jonathan Rodden poses this wonderful puzzle that I don't think anyone has brought to the fore before, right? Why has federal aid to the states ratcheted up at the same time over the last two decades that spending and local school employment has ratcheted down? And so of course that begs the explanation, and I think the implicit explanation in this paper is it's a pure federalism power play, right? Local governments are creatures of the states. States can do it to the locals when times are tough. You cut local governments and keep the state employment. That might be going on but let me throw out a few other possible things to explain this.

One is the peculiar structure of federal grants, especially in Medicaid, which is the bulk of the money. This is the eight-thousand-pound gorilla in these intergovernmental transfers, and it's designed in a highly targeted way, where states get matching dollars. California, for every dollar it spends, it gets $1.60 from the federal government in 2010, which is this key moment here. Texas though, because it's poorer, gets $2.44; Mississippi gets $5.61. This could explain why some of the small states, smaller states that are poor, but not Hawaii, and others are taking this big deficit. So what does that mean? That means when times are good, you can spend. When times are good, Mississippi can spend $100 million of state money and get $661 million worth of healthcare for its citizens. When times are bad, in order to trim $100 million from its deficit, it has to cut $661 million worth of services. So that distorts state incentives and that takes money. Well then, why don't we cut schools? Because dollar for dollar, a school cut is a lot less painful than healthcare cuts. So that both ratchets healthcare spending up and ratchets education spending down. Also healthcare, welfare, public safety, those are all . . . they have countercyclical demand. When times are bad, there's more demand for them. Schools don't have that dynamic, and so that may make schools easier to cut. And then finally, it could be purely a partisan story. In 2009, when local governments were large, Republicans controlled 43 percent of state lower houses and had nine trifectas of governors and both houses in the legislature. Today, Republicans have 55 percent of statehouse seats and twenty-two trifectas.

Michael T. Hartney: I have a question for Jonathan [Rodden] about your paper. More broadly, do you see the role of public-sector unions factoring in at all to what may be going on? And a smaller question was on the graph that everyone was talking about, with the number of workers per capita. I think it'd be interesting to break that one out by local school employees in particular, because when somebody reformulated what you're doing, and saying, Oh, there's been a decrease in school employees, something went off in my mind. And I was saying, well, that denominator there should be students, not necessarily people in the state, because we've had a decrease in enrollment oftentimes and an increase in hires.

Rodden: Yeah. I guess kind of like Michael McConnell in his presentation earlier, I'm not taking a normative position on what the right number of public employees should be and whether moving it up or down is a good or a bad thing. I'm just trying to understand it. But I think it's right that it should be broken down by employment category, and take a look at how much of it is in education, which I think that's where a lot of the action is.

And then the question about public employee unions. There are a lot of questions that I have about . . . I mean, first, I guess, I would've expected not to see these cuts, given the power of labor unions, but I wonder if that isn't part of the story, in that the states—it's not necessarily the goal of the labor union to maximize the number of employees, it's to take care of the more senior employees among those who are already employed. And so it could be that there's a tension there, that in places where public-sector unions are strong and have traditionally been strong, that the amount of money that's spent on benefits squeezes out the possibility of new hires and makes it harder to retain people. I'd let others who know more about this weigh in on that.

Eric A. Hanushek: But Michael's point is that employment in education hasn't gone down. I mean that, in fact, the population that's being served has gone down much more rapidly than the employment. And so that normalizing education by the population in a state gives a misleading picture that things are shrinking.

Rodden: Yeah. I am not looking at education employment alone. I am looking at total public-sector employment, so it would be odd to examine public-sector employment per student, and in any case, I am primarily focused on the timing of expansions and contractions relative to recessions.

Again, it could be that the movement is in the proper direction. But it does certainly happen very . . . If it's a good thing, recessions are quite an opportunity to make it happen. If it's a bad thing, then you see it differently.

Boskin: In some areas—I don't know about the data on employment—but in some areas there's a lot of documentation of federal spending being partially offset by state and local spending, for example on infrastructure. The CBO estimates about a third of a dollar for every dollar. And in recent years, we've created this expectation that there's going to be explosions of spending in the next crisis, and it creates an incentive for states and localities to wait and get on the gravy train when it happens, which also can't be the most efficient way, especially to plan stuff like infrastructure.

Rodden: That's really interesting. That'd be interesting to try to show, see empirically how that plays out.

Boskin: So I think that's something that's probably worth looking into. But the CBO has done a variety of studies on this, on infrastructure in particular.

Thomas MaCurdy: Hey, Jonathan [Rodden], one point I wanted to make is if you consider federal spending, you have to look at federal contractors. That's where the federal government has really moved a lot of its employment. Civil service laws constrain employment and discourage performance. Government can fire contractors if they do not perform. Consider defense—there's been a huge shift from civil service to federal contractors. If you look in the health area, federal contractors work everywhere. So, I believe it's really a misrepresentation to look only at federal employment. There has been a huge increase in federal government employment paid through private contractors. And the same is not true in states. States' public unions are much more prominent, and a lot of state employment is public employment.

Rodden: Yeah, this paper, I'm really mainly looking at state and local and not federal. But I think the same . . . I guess what some people are telling me is that it's very different across states but that there is a movement toward—

MaCurdy: Well, there are also differences across states in the amount of employment supported by contractors versus public unions.

Rodden: Yeah. There are aspects of something that you would've hired some people for twenty years ago. You now make a contract with the—

MaCurdy: They've gone to private in some cases and gone to public in others. You must carefully measure and document these trends if you want to understand what's going on.

Boskin: I think that's an important point. It's useful to take a look at a definition that it's employees that are doing stuff because of the state spending. That might include NGOs in some instance, for example. Of course, contractors too.

MaCurdy: Well, there's a lot, but it's hard to acquire the data on this.

Rodden: I would like to gather some ideas about how to examine some case studies. I'm very curious about that. I'd like to get some data on the transition from public employees to contractors.

MaCurdy: That'd be a good area for case studies, because there's a lot of useful information relevant to this topic.

Peterson: The other measurement issue is when you look at percentages of state spending that is going to local governments, there's two sides of the coin. One is: How much is going to the local governments and how much money is being spent by the state themselves? And so if you have a huge increase, say in Medicaid, you're going to have a huge increase in state expenditure. But that could be driving the percentages. You're interpreting that the percentages are all being driven by the size of the grants going to the state and local government. But you're actually looking at the share of state expenditure that's going to state and local governments.

Rodden: I'm mostly looking at real per capita data. I didn't do too much with shares in the paper. This is related to what Thad was arguing earlier. I think it's right, that a lot of the incentives being created by Medicaid direct the resources away from support for state and local governments.