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COMMENT: U.S. SOCIAL WELFARE POLICY

*Lance Liebman**

Professor Alstott's paper tells an important story about the current moment in American federalism as interpreted through the lens of the social welfare system.[1] From its beginning in 1935, Aid to Families with Dependent Children (AFDC) was the most important intellectual ingredient in the American commitment (or not) to poor families. AFDC was called an exercise in "cooperative federalism." States established and administered programs, receiving reimbursement for roughly fifty percent of their expenditures from the national government, which, however, imposed certain programmatic conditions.

Since the Republicans took control of Congress in the 1994 elections, Congress has emphasized two themes: cutting welfare eligibility (and especially reducing the time period over which benefits can be collected) and transferring authority from the national government to the states. But, as Professor Alstott nicely shows, the two goals sometimes conflict, as when there is support for a national rule that reduces benefits.

I would like to put "welfare," a $23 billion program, in the larger context of American social welfare, attempting to raise comparative international questions about federalism. Only historical contingencies explain the allocation of social responsibility between national and state governments in the U.S. Unemployment Insurance, a $22 billion program, is like AFDC: state programs with a degree of federal supervision. Workers' Compensation, which transfers $43 billion in a year, is entirely a state-level program. Indeed, states choose whether to operate government insurance funds or to require employers to purchase coverage from private companies. Income support for the long-term disabled is a federal program, part of the national Social Security system. Short-term disability is left to the states, and most of them have no benefit programs. Old-age benefits are national, and constitute the largest ($300 billion) part of Social Security. The national government finances health expenses for persons older than 65 (Medicare), divides with the states the finance of health expenses for the pre-65 poor (Medicaid), and leaves to employers (regulated to some degree by the states, to some degree nationally, and to some degree not at all) the finance of health benefits for those who are neither elderly nor poor.

But, as the above suggests, the allocation of social welfare authority between national and state government is only one part of the story of protection against and preparation for the vicissitudes of economic life. For the complete story, one

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[1] Anne L. Alstott, *Federalism and U.S. Social Welfare Policy: Fundamental Change and New Uncertainties*, 2 COLUM. J. EUR. L. 441 (1996). The author's note at the outset of Professor Alstott's contribution applies equally to the remarks made here.

must see the distribution of responsibility among the individual (or the family unit), the employer (or, as so often with two-worker families, two employers), and government (national, state, and local). And indeed, an additional institution that could be considered is the international labor market that plays, today, such a large role in determining the compensation (both wages and benefits) that an individual's skills can command. In this context, the investigation of federalism becomes a search both for national and state-level programmatic responsibility (social welfare programs) and for regulatory authority (what level of government is supervising what portions of the employer-employee "fringe benefit" relationship).

The aspect of this structure that is most interesting at this moment in the United States, and most subject to reconsideration, is worker (and worker's family) health benefits. The failure of the Bill Clinton/Hillary Clinton healthcare reform program in 1994 was a signal that most working Americans will receive health benefits from their employers for the foreseeable future. This is inherently a problematic relationship. It gives companies an incentive to discriminate in hiring against persons likely, because of genetic makeup, prior history, or age, to have more than average health expenses. National and state laws ban discrimination by age and by disability (now interpreted to ban discrimination because of testing positive for the HIV virus). Much of twentieth century history shows the attempt to create worker dignity and liberty in the shadow of employers: this is the struggle against the Industrial Revolution's version of feudalism. But an employer who pays for family health expenses has an interest (that we may wish to order him not to pursue) in whether the employee smokes or hang-glides, whether she follows treatment plans recommended by her physician, whether her partner is a legal spouse, and whether the children in her household are hers. It is no surprise that government is pressed to say that a health benefits plan must include coverage for mental illness, that an employee must (or must not) extend dependent coverage to a gay or lesbian partner, that a health plan must allow at least 48 hours in the hospital after childbirth, and so on. But to what level of government are these decisions assigned?

The American law on this subject will surprise European (not to mention Japanese) observers. First, a national law (the Employee Retirement Income Security Act of 1974[2]) makes "employee benefit plans" (not merely health plans) a matter of national government concern. Second, that same law tells the states to keep their hands off : "[the federal statute] shall supersede any and all State laws insofar as they may . . . relate to any employee benefit plan . . . ."[3] Third, however, the federal law allows states to continue to regulate "insurance," historically a matter of state responsibility. Fourth, "self-insurance" (a company which promises benefits, hires an insurance company to administer its plan, but retains the economic risks) is not "deemed" to be insurance for the purpose of permitting regulation by the state government. The result is that

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[2] Pub. L. No. 93-406, 88 Stat. 829 (1974) [ERISA] (codified and amended at various sections of Titles 26 and 29 of the United States Code).

[3] ERISA §514(a), 29 U.S.C. §1114(a) (1994).

companies have an incentive to self-insure, to avoid what are — at this moment — state regulations of health insurance that are more detailed and intrusive than the national rules. But the concerns of patients for proper treatment lead to political efforts to protect them from allegedly exaggerated attempts to reduce health costs, and it seems likely that the national government will expand its regulatory efforts. Furthermore, even though states cannot regulate self-insuring employers, they can regulate health care providers (physicians, hospitals, and especially health maintenance organizations), and expanded state regulatory efforts seem likely in this area as well. This is very far from a story of coherent government concern with an efficient health care system or effective assurance of necessary care to all citizens. It may be even further from a story of an effort to assign important public tasks to the level of government that is most capable of handling them. Rather, federalism confuses further an inherently complicated system by leaving individuals, employers, and providers unsure about the rules of the game, thus giving advantages to well-organized and -financed collective efforts to achieve private advantage by "playing the system." With health care expenses rising above fifteen percent of the total Gross National Product, it is no surprise that employers, labor unions, hospitals, physicians, drug companies, and many other special interests devote vast resources to protecting and advancing their positions at every level of government, nor that they are often extremely effective in achieving their goals.

Now let me tell another story, one that leads to different insights about federalism and social welfare as we approach a new century. In the United States, "Social Security" means a government program that taxes payrolls at 12.4 percent (up to the first $65,400 in annual income). The same program makes "old age" payments to persons 62 years of age or older. The age for full benefits, now 65, will gradually rise to 67 to hold down expenses as the population ages. Because Social Security benefits are redistributional, replacing a much larger percentage of income for low-wage workers than for those who earn more, workers who are middle income and above require supplemental pensions (or personal savings) if they are to maintain their standard of living in retirement. These private pensions are not mandatory; some employers provide them. These private pensions receive a large tax subsidy. When funds are set aside, the company deducts the money as a business expense. But the worker receives no taxable income until years (or decades) later when he retires. Postponing taxation on such large sums (hundreds of billions of dollars in the total economy) subsidizes well-off workers. To obtain the tax subsidy, a company must "fund" its plan and meet strict and technical requirements.

Large companies have so-called defined benefit plans that offer retirement benefits by formula: "if you retire at age 65, you will annually receive half the average of your final three years' income for the rest of your life." The company thus pools the risks of its work force, and the worker is assured an income that is appropriate to her wages. The company invests a large sum over time and must calculate annually the amount that must be added to the plan's assets to assure payment to future retirees. In addition, a government program "insures" approximately 80 percent of these benefits, so even if the pension

plan is mismanaged or the investment performance is poor, the worker will be protected.

Recently, companies have reduced their use of pension plans of this type. The plans are expensive, and so is the regulatory burden of complying with technical government rules. Instead, companies are offering very different retirement programs called defined contribution plans. Under these plans, the company offers the employee (for example) five percent of salary to invest, as well as the option to add five percent of the employee's own money. The employee is offered a range of investment options, such as common stock mutual funds, bond funds, and so on. The worker has an individual account, the company has met all its obligations when it invests her funds, and she may or may not have adequate income in retirement. The risks (and upside possibilities) are with the worker.

Now there is much discussion in the United States of changing from the current structure of Social Security (the basic public pension portion of retirement income) so that some of the funds would be invested in the stock market. This might be good for the national savings and investment rates. Supporters note the good return on stock market investments if they are held for a substantial period. But a system that pools and socializes risks and rewards would be replaced by one in which the individual's retirement income would depend upon the investment choices she makes.

There was a time in the United States when it seemed that issues of worker benefits and social welfare protections were being taken over by the national government. During the Nixon presidency in the early 1970s, the most recent period of national government expansion, federalization of Workers' Compensation was seriously considered, a national minimum income guarantee was briefly supported by the President, federal food stamp and disability programs were significantly expanded, and the national pension law was enacted. Such changes could have been explained, as were the Roosevelt and Truman nationalizations of labor-management regulation, as a response to the growth of a national labor market.

Instead, the United States entered a quarter century period, still underway, of strong political support for increased delegation of authority to the states. There are advantages to local discretion and administration, and some of those can be seen right now in at least modest successes with experimental programs offering job opportunities to single-parent welfare recipients. But a less elevated explanation for recent history is probably more convincing. With politics favoring reductions in guaranteed assistance (assured income for mothers and children; payment of health care expenses; pensions that preserve a worker's standard of living), elected national officials seek to delegate the difficult choices and the responsibility for unhappy outcomes. The federal government says to the states: "You choose whether to raise taxes or to leave mothers and children with no income." It says to employers: "You contract with a managed care company that will hold down health expenses by denying some benefits." And employers say to workers: "You choose how much to save for retirement and how to invest your retirement savings." All of this is downward delegation

with the goal of transferring responsibility for the mismatch (caused more than anything by the demographics of an aging population) between legitimate claims and available resources. And as always in a democracy, the efforts go too far and provoke reactions: state and federal legislation saying that some health expenses must be paid; court decisions saying employers cannot trick workers into giving up promised benefits; the search for imaginative ways to find the money and preserve old-age benefits.

This contemporary history suggests three insights. First, employers, so deeply involved in the American social welfare system, are major players in the political process. They regularly threaten state governments by saying they will move their operations to another state. They similarly threaten to move work to other countries. Very often, it appears that arguments over federal versus state authority show little more than that some participants in the political debate see short-term advantages from having a particular matter handled at one level of government or another.

Second, this peculiar American phenomenon now transfers itself to the international realm. Europe considers how to coordinate national health and pension systems because some workers will have a career in more than one country. NAFTA brings attention to coordination among Canada, the U.S., and Mexico. An internationalizing labor market will force attention to these questions in the coming decades. And as that happens, the international companies will have at least as much influence on outcomes as any particular institution of democratic government.

Third, national cultures are nevertheless not identical, and social welfare systems vary in the ways in which they assign responsibilities to individuals, to employers, and to different levels of government. The United States tradition is far more individualistic than the structures of western European societies or Japan. And at this moment, important social forces are moving the American system even further from shared and collectivized outcomes.