Alert

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COZEN O'CONNOR

Cozen Currents: The Regulatory State(s)

“With the Trump administration’s aggressive plans for a rollback of federal regulation, blue states are already looking to fill the void, demonstrating that nature abhors a vacuum in the political realm as well.” — Howard Schweitzer, CEO, Cozen O’Connor Public Strategies

The Cozen Lens

- The Trump administration marks a departure from the high-water mark of federal regulation under former President Biden, leaving a regulatory vacuum for the states.
- The Trump administration is scrutinizing government contractors amid efforts to reduce government spending. However, not all contracts are equally at risk, and some other reforms being pursued could create new opportunities for contractors.
- The GOP is looking to reform Medicaid without cutting beneficiary benefits to significantly help pay for its massive tax cuts package. The political and practical challenge is that many of the reforms under discussion would ultimately affect benefits and available services, and because of this will be politically difficult.

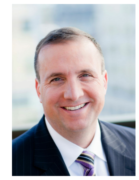
States Set to Fill the Regulatory Void

Regulation Under Trump 2.0. The inauguration of President Trump means that the federal government is taking its foot off the gas pedal in regulation and enforcement across industries.

- Trump marks a departure from his predecessor in two key ways. First, he has begun to unravel former President Biden’s legacy in areas from environmental rules to AI guardrails, though the actual deregulatory process takes time. While Trump can undo Biden’s executive orders with the stroke of a pen, officials must follow the same procedures applied in propagating rules to roll them back in a legally defensible way.
- Equally as significant is that a lack of new regulation is expected under Trump 2.0. The Biden administration represented a high-water mark for federal regulation. Businesses can be confident that major new rules won’t emerge for the next four years.
- In the absence of new regulations on the federal level, blue states have the opportunity to take the baton from the former Biden administration. Their rules can have a broader impact beyond state borders due to the size of the state’s market, the concentration of a particular industry in the state, such as Wall Street in New York or Silicon Valley in California, or copycat efforts from like-minded states.

States Take the Lead. In the absence of federal regulation on certain issues, state leaders can go further than their counterparts in Washington, DC.

- Congressional Republicans seek to overturn the Biden Consumer Financial Protection Bureau’s rule to cap overdraft fees at $5 for banks and credit unions with over $10 billion in assets. While this rule may be blocked (and the Congressional Review Act prevents it from returning in a substantially similar form), the New York Department of Financial Services is poised to replace it. Governor Kathy Hochul (D-NY) announced a proposal to ban fees for overdrafts under $20 and fees that are greater than the amount of the overdraft, among other



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Related Practice Areas

- Government Relations - Cozen O'Connor Public Strategies provisions. Though not as far-reaching as the federal rule, the Empire State proposal could ultimately be more impactful.

- Trump eliminated Biden's executive order on AI, but California policymakers have pitched instituting new guardrails for the emerging technology. The California Privacy Protection Agency has proposed rules for automated decision-making technology and lawmakers have introduced legislation to regulate AI. They include a bill from state Senator Scott Wiener (D) focused on protections for AI industry whistleblowers and the establishment of a public cloud computing cluster and a bill from Assemblymember Rebecca Bauer-Kahan (D) to combat algorithmic discrimination. If successful, California's efforts could set a de facto national AI standard.

A Big Role for State AGs. Attorneys general (AGs) are positioned to fill the regulatory and enforcement vacuum left by the Trump administration.

- Democratic AGs are on the front lines of resisting Trump administration actions in the courts. The nation's 23 Democratic AGs meet regularly to coordinate their legal response to the White House's actions. With Republicans in full control of the federal government, the judicial system presents a feasible route for the president's opponents to push back against his agenda.
- Acknowledging the centrality of Attorney General Rob Bonta (D-CA) to the state's plans to shield left-leaning policies from Trump, the California legislature devoted $25 million to fund legal battles with Trump in a special session called by Governor Gavin Newsom (D-CA) after the election.
- Fights over major environmental regulations are likely to be a hot topic for Democratic AGs under Trump 2.0. For example, Environmental Protection Agency Administrator Lee Zeldin has called on Congress to overturn California's emissions waivers (which 16 other states and DC have also adopted) under the Congressional Review Act, a tool that hasn't been used for this purpose. Bonta told Politico that "we're prepared to defend ourselves if it's wrongfully weaponized." The future of the waivers may ultimately depend on the outcome of litigation.

Government Contractors Defend the Spend

Contractors Under a Microscope. As the Trump administration looks at ways to reduce government spending, it has turned its sights toward government contractors.

- The most targeted effort aimed at government contractors has been made by General Services Administration acting Director Stephen Ehikian, who, in a memo, ordered federal agencies to review contracts with 10 of the government's largest contractors. The list includes household names like Deloitte, Booz Allen Hamilton, and IBM.
- The targeting of these firms has prompted a sudden lobbying effort by executives meeting with Trump administration officials to "defend the spend" as they find themselves in the administration's crosshairs. Ehikian set a March 7 deadline for agencies to decide whether to end or keep contracts and ordered those kept to be verified as "mission critical and provides substantive technical support."

Differentiated Risk Levels. While government contractors as a whole are under scrutiny, some of their contracts are likely safer than others.

- Like the Trump administration's efforts to reduce spending so far, the risk exposure of contractors is likely not even across the government. Instead, the danger of any given contract is more likely tied to the agency it comes from rather than who the contractor is.
- In particular, the more closely a contract is linked to national security, the more likely it is to be shielded. The Department of Defense, Department of Homeland Security, and intelligence community are unlikely to be the focus of spending cuts during President Trump's second term, and those protections likely extend to the contracts tied to those agencies.
- On the other hand, contracts with agencies that DOGE has targeted for cuts are at a much higher risk level. This has particularly resulted in lost contracts for businesses connected to the US Agency for International Development or diversity, equity, and inclusion initiatives. In addition, other agencies that are not linked with Trump's priorities, such as the Environmental Protection Agency and Consumer Financial Protection Bureau, are also likely to see their

associated contractor spending significantly reduced.

Silver Linings? While the pressure on government contractors is serious, some other ways the Trump administration may look to reform the government could create opportunities.

- One consequence of Trump's push to reduce the number of federal employees is that it could increase the government's reliance on contractors. While the goal of a smaller government will mean that not every position will need to be replaced, contractors could be required to fill some gaps to allow the government to continue fulfilling necessary tasks.
- As much as Trump is discussing cutting federal spending, a more accurate picture may show that funding is more likely to shift to become more concentrated in areas he sees as political priorities, such as defense and homeland security. As a result, despite the pressure on contractors elsewhere, not only will contracts in these areas likely be safer, but there are more likely to be new opportunities connected to these issues than elsewhere across the federal government.

Medicaid Cuts Are in the Eye of the Beholder

A Rock and a Hard Place. Reducing the deficit, protecting the social safety net, and giant tax cuts — different factions of the GOP have different answers for how to achieve these three objectives.

- The number one GOP priority is tax cuts, but what that means is an entirely different question. President Trump reportedly has a $10 trillion wish list for the GOP's tax cut efforts, meaning the administration can hardly be satisfied with the House budget resolution's $4.5 trillion *maximum* deficit increase over the next ten years. Meanwhile, deficit hawks and the House Freedom Caucus (HFC) want government spending and the deficit to *fall*. Lastly, there is a loose group of moderates and swing district Republicans who are making a stand against substantially cutting the social programs necessary to pass massive tax reform without completely exploding the deficit.
- Despite concerns from some moderate Republicans, House Republicans, including those concerned moderates, voted to pass the House Budget, even though it effectively requires substantial Medicaid cuts – when given assurances from Republican leadership that ultimately things would look very different on the Medicaid front once the Senate weighed in. The House budget resolution requires the Energy and Commerce Committee to find $880 billion in savings over the next ten years. This committee's jurisdiction when it comes to mandatory funding is almost entirely Medicare and Medicaid spending., Given the President's repeated assurances that he would not cut Medicare, along with its status as a third rail of politics, that only leaves cuts to Medicaid to fill the gap. The key to a path forward, on this as on all matters, requires finding at least the lowest common denominator all parts of the GOP can support.
- Implementing especially harsh reforms like Medicaid block grants, per-capita cap, or making changes to federal matching rates for the program would save the hundreds of billions of dollars that the HFC and the House budget resolution demand but would result in tens of millions of Americans losing access to health care. Populists like Senator John Hawley (R-MO) and members in swing districts especially reliant on the program like Rep. David Valadao (R-CA) have made it clear that such an option is politically untenable. Passing reconciliation with reductions in future outlays to Medicaid would require moderate Republicans shifting their perspective to: what if they could find Medicaid cuts that they can message aren't actually "cuts"? Enter, the ground floor of the GOP's Medicaid reform: work requirements, eligibility checks, and reduced provider taxes.

The Magic Three. The GOP is workshopping major Medicaid reforms as defensibly being under the category of "waste, fraud, and abuse." As the debate has evolved in this direction over the past week or two, states, health care providers, and beneficiary advocates, have begun to argue that this characterization is incorrect; that the administrative burdens of work requirements are ultimately what causes people to lose coverage, not the fact that they're not working; and that reduced provider taxes are either a cost shift to states or another way that beneficiaries will lose access to care in a number of different forms as fewer dollars are available for the program.

- Work requirements are a hill the Republicans are willing to die on for ideological reasons.

Luckily for them, much of the country agrees with their stance, including 66 percent of Independents according to a 2023 poll. The second is another easy sell to voters — just expanding the range of checks states run to make sure people are eligible for the benefits they receive. The third is wonky but argues that states are maximizing the federal contribution toward Medicaid costs by taxing health providers and insurers in their state. When states use this revenue to increase Medicaid reimbursement rates, those supporting restricting these policies argue that states then receive more matching funds from the federal government than they otherwise would. This is being sold as "fixing a loophole" and bringing back established cost-sharing levels into effect. Certain states that are following these developments are concerned that ultimately this will not bring costs down, but transfer them back to the states. Providers are concerned that if states have fewer dollars, ultimately their reimbursement will be cut, which for many of them, could create significant financial challenges.

- While most politically viable combinations of these three would not save enough to meet the $880 billion requirement, some in Republican leadership are recasting them to be easy wins for the party as a whole. The HFC gets some progress towards the larger cuts they're seeking; meanwhile, the savings both offset tax cuts and go towards the budget resolution requirements for spending cuts.
- Whether this argument will continue to be persuasive (or even go *further* to other changes) is uncertain. Large majorities of both parties oppose cutting funding for Medicaid, many supporters of President Trump are Medicaid beneficiaries, and advocacy on these particular policies is ramping up now that the policies in play are clearer. Democrats have retooled their messaging apparatus towards attacking the GOP for setting up cuts to Medicaid, hoping for a repeat of their incredible performance in 2018, largely on the back of critiquing the ultimately unsuccessful attempt to repeal Obamacare. Vulnerable lawmakers have had to put themselves on the record against cuts and the GOP as a whole has canceled town halls in response to the backlash.