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## State Sovereign Immunity and Privatization: Can Eleventh Amendment Immunity Extend to Private Entities?

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## Comments

### **State Sovereign Immunity and Privatization: Can Eleventh Amendment Immunity Extend to Private Entities?**

*Justin C. Carlin*\*

#### ABSTRACT

Since the privatization-boom of the 1980s and 1990s, state governments have transferred a large number of traditionally public functions to private firms by: (1) privatizing traditionally public entities, and (2) contracting out to traditionally private entities. For the first time in American law, entities in these types of privatization schemes are asserting state sovereign immunity as an affirmative defense in suits arising out of work performed on behalf of the government. As a consequence, there has been some confusion in the federal circuit courts concerning whether these entities are arms of the state for purposes of the Eleventh Amendment. Because state sovereign immunity can prevent injured parties from having their cases heard on the merits in federal court, courts should not extend state sovereign immunity to entities that the Eleventh Amendment does not cover. Moreover, because the arm-of-the-state test imposes costs on the judicial system, courts should not employ the test when there is an alternative, less-costly approach. This Comment makes four recommendations concerning state sovereign immunity and privatization that should assist federal courts and state legislatures in balancing the important judicial and governmental interests of fairness, efficiency, and proper deference to state sovereign immunity.

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## INTRODUCTION

Until Margaret Thatcher became Prime Minister of the United Kingdom, the conventional wisdom was that the government—and not the private sector—was best equipped to manage certain industries, such as the telecommunications industry and the utilities industry.<sup>1</sup> Today, however, the reality is that governments throughout the world, and especially in the U.S., have not only relinquished control over these industries, but also over a number of other public industries.<sup>2</sup> And, despite the fact that “privatization has not proven to be a cure-all panacea for ineffective government,”<sup>3</sup> there is virtually unanimous agreement that privatization has become a valuable tool of government.<sup>4</sup> Moreover, the impact of privatization has not

<sup>1</sup> See William L. Megginson & Jeffrey M. Netter, *From State to Market: A Survey of Empirical Studies on Privatization*, 39 J. ECON. LITERATURE 321, 324 (2001) (“Although the Thatcher government may not have been the first to launch a large privatization program, it was without question the most important historically . . . Thatcher adopted the label ‘privatization,’ which was originally coined by Peter Drucker and which replaced the term ‘denationalization.’”) (citations omitted); see also Sir Rhodes Boyson & Antonio Martino, *What We Can Learn from Margaret Thatcher*, Remarks at the Meeting of The Heritage Foundation’s Windsor Soc’y in Sea Island, GA (Oct. 3-6, 1999), in The Heritage Foundation Pol’y Archive, Nov. 24, 1999, available at <http://www.heritage.org/research/politicalphilosophy/hl650.cfm>. As Boyson and Martino note:

When Margaret Thatcher took office, there were 3 million private shareholders; when she left, there were almost 11 and a half million . . . When the gas industry was launched, the shares were oversubscribed by 500 percent . . . [Subsidized housing was] sold to tenants at knockdown prices, and between 1979 and 1989 owner occupation increased from 55 to 63 percent . . . [B]etween 1979 and 1987 the number of civil servants was reduced by 22.5 percent (732,000 to 567,000).

*Id.* Although privatization did not thrive until the Thatcher government, arguments in favor of privatization existed at English law and colonial law:

In every great monarchy in Europe the sale of the crown lands would produce a very large sum of money, which, if applied to the payment of public debts, would deliver from mortgage a much greater revenue than any which those lands ever afforded to the crown. . . . When the crown had become private property, they would, in the course of a few years, become well improved and well cultivated.

ADAM SMITH, *THE WEALTH OF NATIONS* 824 (Penguin Group 1982) (1776).

<sup>2</sup> Jody Freeman, *The Private Role in Public Governance*, 75 N.Y.U. L. REV. 543, 547 (2000) (“Virtually any example of service provision or regulation reveals a deep interdependence among public and private actors in accomplishing the business of government.”); Enrico C. Perotti, *Credible Privatization*, 85 AM. ECON. REV. 847 (1995) (“Privatization has recently become the policy of choice in both developed and developing countries, and an urgent necessity for the economies of Eastern Europe.”); William L. Megginson, *Think Again: Privatization*, 118 FOREIGN POL’Y 14 (2000) (“Over the past two decades, the privatization of state enterprises has gone from novelty act to global orthodoxy . . . The real question is how—not whether—to transfer state firms to private hands.”).

<sup>3</sup> See Keon S. Chi, Kelley A. Arnold, & Heather M. Perkins, *Privatization in State Government: Trends and Issues*, SPECTRUM: THE J. OF STATE GOV’T 19 (Sept. 2003).

<sup>4</sup> *Id.* at 20 (“[S]tate policymakers now tend to consider privatization as a cost saving device or as a way to manage their agencies and deliver public services without hiring new staff or experts in certain areas. It appears that privatization has now become a less ideological, less partisan, pragmatic approach for policymakers to consider.”). For theoretical and empirical accounts of why private entities some-

been limited to any one level of government. To the extent that privatization “encompasses the range of efforts by governments to move public functions into private hands and to use market-style competition,”<sup>5</sup> state governments have transferred a large number of traditionally public functions to private firms by: (1) privatizing traditionally public entities, and (2) by contracting out to traditionally private entities.<sup>6</sup> As of 2002, contracting out to traditionally private entities accounted for 86.9% of all state-level privatization schemes.<sup>7</sup>

Some of the legal implications of the privatization-boom have been noted.<sup>8</sup> Nevertheless, scholars and commentators have paid scant attention

times perform public functions better than government agencies, see E.S. SAVAS, *PRIVATIZATION AND PUBLIC-PRIVATE PARTNERSHIPS* (2000) (providing a detailed account of privatization in general and public-private partnerships in particular, and arguing that the shift from public to private government improves the productivity of government agencies); Anthony Boardman & Aidan R. Vining, *Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed, and State-Owned Enterprises*, 32 J.L. & ECON. 1 (1989) (reviewing empirical findings and concluding that, in a competitive environment, state-run enterprises and partially-privatized enterprises perform substantially worse than fully-privatized enterprises); Wei Li & Lixin Colin Xu, *The Impact of Privatization & Competition in the Telecommunications Sector Around the World*, 47 J.L. & ECON. 395, 395 (2004) (citing INTERNATIONAL TELECOMMUNICATIONS UNION (ITU), *TRENDS IN TELECOMMUNICATIONS REFORM: CONVERGENCE AND REGULATION* (1999); ITU, *TELECOMMUNICATIONS REFORM: EFFECTIVE REGULATION* (2002); ITU, *TELECOMMUNICATIONS REFORM: INTERCONNECTION REGULATION* (2001); PYRAMID RESEARCH, *WILL THE INTERNET CLOSE THE GAP?* (2000)) (evaluating data containing information on privatization from 177 countries and information on competition from up to 162 countries between 1990 and 2001 and concluding that full privatization improves the economic performance of a country’s telecommunications sector more than partial privatization). The Supreme Court has also recognized the virtues of privatization. See *Richardson v. McKnight*, 521 U.S. 399, 405-07 (1997).

<sup>5</sup> Martha Minow, *Public and Private Partnerships: Accounting for the New Religion*, 116 HARV. L. REV. 1271 (2003). Professors Megginson and Netter provide another useful definition: “Privatization can be defined as the government’s deliberate sale of state-owned assets or enterprises or to private economic assets.” Megginson & Netter, *supra* note 1, at 1.

<sup>6</sup> See Chi et al., *supra* note 3, at 15. Every U.S. state and commonwealth has privatized at least some services and programs. See KEON S. CHI, CINDY JASPER, MICHAEL J. SCOTT, COUNCIL OF STATE GOVERNMENTS, *PRIVATE PRACTICES: A REVIEW OF PRIVATIZATION IN STATE GOVERNMENT* 8, Fig. 6 (1998), available at <http://www.privatization.org/database/trendsandstatistics.html> (last visited Mar. 27, 2009). As of 1997, the U.S. Virgin Islands had the lowest number of privatized programs (five). *Id.* The State of Florida had the highest number (151). *Id.*

<sup>7</sup> See Chi et al., *supra* note 3, at 20.

<sup>8</sup> See, e.g., Symposium, *Redefining the Public Sector: Accountability and Democracy in the Era of Privatization*, 28 FORDHAM URB. L.J. 1307 (2001); Symposium, *New Forms of Governance: Ceding Public Power to Private Actors*, 49 UCLA L. REV. 1687 (2002); Symposium, *Public Values in an Era of Privatization*, 116 HARV. L. REV. 1211 (2003); Freeman, *supra* note 2; Jody Freeman, *The Contracting State*, 28 FLA. ST. U. L. REV. 155 (2001); Jody Freeman, *Collaborative Governance in the Administrative State*, 45 UCLA L. REV. 1 (2001); David J. Kennedy, *Due Process in a Privatized Welfare System*, 64 BROOK. L. REV. 231 (1998); Ira P. Robbins, *The Impact of the Delegation Doctrine on Prison Privatization*, 35 UCLA L. REV. 911 (1988); Dru Stevenson, *Privatization of the Welfare System: Delegation of the Commercial Contract*, 45 ARIZ. L. REV. 83 (2003); Daphne Barak-Erez, *A State Action Doctrine for an Age of Privatization*, 45 SYRACUSE L. REV. 1169 (1994); Sheila S. Kennedy, *When Is Private Public?*

to the question of whether quasi-government agencies, or so-called public/private “hybrid” entities, should be accorded state sovereign immunity. This result is surprising when one considers that extending state sovereign immunity to an entity can have severe repercussions on the would-be plaintiff—he is barred from bringing a suit against that entity. For this reason, “‘sovereignty’ has become an oppressive term in our courts. A state government that orders or allows its officials to violate citizens’ federal constitutional rights can invoke ‘sovereign’ immunity from all liability—even if such immunity means that the state’s wrongdoing will go partially or wholly unremedied.”<sup>9</sup>

In *Hess v. Port Authority Trans-Hudson Corp.*,<sup>10</sup> the Supreme Court labored to develop a standard by which courts could determine whether an entity or state agency is an arm of the state entitled to state sovereign immunity. *Hess* did not achieve its purpose because there has been some confusion in the federal circuit courts over whether state sovereign immunity extends to private entities that perform work for the government. Recently, the Ninth Circuit held that state sovereign immunity did not extend to a private entity,<sup>11</sup> bringing itself in line with the First, Fifth, Sixth, Seventh, and Tenth Circuits.<sup>12</sup> The Eleventh Circuit is the only circuit to have extended state sovereign immunity to a private entity;<sup>13</sup> all of the circuits have

*State Action in the Era of Privatization and Public-Private Partnerships*, 11 GEO. MASON U. CIV. RTS. L.J. 203 (2001); Michele Estrin Gilman, *Legal Accountability in an Era of Privatized Welfare*, 89 CAL. L. REV. 569 (2001); Ronald A. Cass, *Privatization: Politics, Law, and Theory*, 71 MARQ. L. REV. 449 (1998); Note, *The Privatization of California Correctional Facilities: A Population-Based Approach*, 18 STAN. L. & POL’Y REV. 438 (2007); Jon Michaels, *Deforming Welfare: How the Dominant Narratives of Devolution and Privatization Subverted Federal Welfare Reform*, 34 SETON HALL L. REV. 573 (2004); Alexander Volokh, *Privatization and the Law and Economics of Political Advocacy*, 60 STAN. L. REV. 1197 (2008); Abigail Hing Wen, *Suing the Government’s Servant: The Implications of Privatization for the Scope of Sovereign Immunities*, 103 COLUM. L. REV. 1538 (2003); Ellen Dannin, *Red Tape or Accountability: Privatization, Public-ization, and Public Values*, 15 CORNELL J.L. & PUB. POL’Y 111 (2005); Dru Stevenson, *Privatization of State Administrative Agencies*, 68 LA. L. REV. 1285 (2008); Paul R. Verkuil, *Public Law Limitations on Privatization of Government Functions*, 84 N.C. L. REV. 397 (2006); Gillian E. Metzger, *Privatization as Delegation*, 103 COLUM. L. REV. 1367 (2003).

<sup>9</sup> Akhil Reed Amar, *Of Sovereignty and Federalism*, 96 YALE L.J. 1425, 1426 (1987) (citing *Edelman v. Jordan*, 415 U.S. 651 (1974); *Hans v. Louisiana*, 134 U.S. 1 (1890); *Louisiana v. Jumel*, 107 U.S. 711 (1883)).

<sup>10</sup> *Hess v. Port Auth. Trans-Hudson Corp.*, 513 U.S. 30 (1994).

<sup>11</sup> See *Del Campo v. Kennedy*, 517 F.3d 1070 (2008).

<sup>12</sup> See *Fresenius Med. Care Cardiovascular Res., Inc. v. Puerto Rico*, 322 F.3d 56 (1st Cir. 2003); *United States ex rel Barron v. Deloitte & Touche, L.L.P.*, 381 F.3d 438, 439-42 (5th Cir. 2004); *Brotherton v. Cleveland*, 173 F.3d 552 (6th Cir. 1999); *Takle v. Univ. of Wisc. Hosp. & Clinics Auth.*, 402 F.3d 768 (7th Cir. 2005); *United States ex rel. Sikkenga v. Regence Bluecross Blueshield of Utah*, 472 F.3d 702 (10th Cir. 2006); see also *infra* Part II.C.

<sup>13</sup> See *Shands Teaching Hosp. & Clinics, Inc. v. Beech St. Corp.*, 208 F.3d 1308, 1311 (11th Cir. 2000) (setting forth a four-part test to determine whether a private entity contracted by the State is “contractually acting as [a] representative[] of the State”).

different arm-of-the-state tests;<sup>14</sup> and the Ninth Circuit is the only circuit to have declined to apply the arm-of-the-state test to a private entity.<sup>15</sup> This Comment attempts to reconcile this confusion by recommending an alternative approach to the arm-of-the-state inquiry when private entities performing work for the government invoke state sovereign immunity as an affirmative defense.

This Comment has four parts. Part I details the concept of state sovereign immunity, considering the origin of the doctrine at common law and the evolution of the doctrine in the American legal system. Part II describes the problems courts face in determining whether an entity is a sovereign. In so doing, it compares and contrasts landmark Supreme Court decisions involving municipal corporations and Compact Clause entities that invoked Eleventh Amendment immunity as defendants in federal court. It also summarizes five key decisions rendered in the federal circuit courts, each of which involved a private entity that asserted state sovereign immunity as an affirmative defense. Two of these decisions involve traditionally public entities that the state sought to privatize or “spin off” by statute. Three involve traditionally private entities that the state contracted to perform a public function.

Part III makes three observations concerning state sovereign immunity and the federal circuit courts’ arm-of-the-state jurisprudence. First, state sovereign immunity does not extend to private entities. Second, courts are applying arm-of-the-state analysis whenever an entity claims state sovereign immunity. Third, an erroneous finding of state sovereign immunity threatens a state’s sovereignty.

Part IV makes four recommendations. First, courts should expressly acknowledge that state sovereign immunity does not extend to private entities. Second, courts should adopt a per se rule against extending state sovereign immunity to traditionally private entities. Third, courts should apply the arm-of-the-state test to traditionally public entities that the state has allegedly privatized. Finally, when a state creates an entity to perform a government function, it should detail in the entity’s organic statute whether the entity is an arm of the state within the meaning of the Eleventh Amendment.

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<sup>14</sup> See *infra* Part II.C.

<sup>15</sup> See *Del Campo*, 517 F.3d at 1078; see also *infra* Part II.C.2.

## I. STATE SOVEREIGN IMMUNITY: ORIGIN AND DEVELOPMENT

### A. English Law and Colonial Law

The concept of sovereign immunity at English common law is summarized by remarks made in 1702 by Chief Justice John Holt: “If the plaintiff has a right, he must of necessity have means of vindication if he is injured in the exercise and enjoyment of it. Right and remedy, want of right and want of remedy, are reciprocal.”<sup>16</sup> By Henry III’s reign, it was well established that the King could not be sued without his consent; but sovereign immunity did not necessarily prevent an injured party from acquiring relief.<sup>17</sup> Because the King was regarded as the fountain of justice, he was obligated—by law and by conscience—to redress wrongs done to his subjects.<sup>18</sup> Indeed, an individual who had been injured by the King (and whose suit affected the Crown) could pursue his claims in regular courts.<sup>19</sup> Moreover, when it was necessary for an individual to bring a suit against the sovereign, the King would routinely consent to suit if the claim brought against him made out a *prima facie* legal claim.<sup>20</sup> In those instances, the King’s courts would provide the petitioner with redress in accordance with the substantive law.<sup>21</sup> Thus, “the expression ‘the King can do no wrong’ originally meant precisely the contrary to what it later came to mean. ‘It meant that the King must not, was not allowed, to do wrong. . . .’”<sup>22</sup>

Despite the variety of procedures available at common law to those injured by the King, the practice of obtaining redress for wrongs committed by the sovereign did not translate well in the American colonies, because there was not a King who could consent to suit.<sup>23</sup> Nevertheless, American lawyers at the time of the founding were familiar with the doctrine of sovereign immunity.<sup>24</sup> For this reason, there was dispute over whether Article

<sup>16</sup> CLYDE E. JACOBS, *THE ELEVENTH AMENDMENT AND SOVEREIGN IMMUNITY* 8 (1972) (quoting *Ashby v. White*, 87 Eng. Rep. 808 (Q.B. 1702)).

<sup>17</sup> See Louis L. Jaffe, *Suits Against Governments and Officers: Sovereign Immunity*, 77 HARV. L. REV. 1 (1963).

<sup>18</sup> See JACOBS, *supra* note 16, at 5.

<sup>19</sup> See Jaffe, *supra* note 17.

<sup>20</sup> See *id.*

<sup>21</sup> JACOBS, *supra* note 16, at 6.

<sup>22</sup> See Jaffe, *supra* note 17, at 4 (alteration omitted) (quoting Ehrlich, *No. XII: Proceedings Against the Crown* (1216-1377), at 74, in 6 OXFORD STUDIES IN SOCIAL AND LEGAL HISTORY (Vinogradoff ed., 1921)).

<sup>23</sup> See *id.* at 2.

<sup>24</sup> See JACOBS, *supra* note 16, at 7 (“The American edition of Sir William Blackstone’s *Commentaries on the Laws of England* was published in 1771 and 1772; this treatise . . . exercised great influence in the colonies . . . . From the maxim the king can do no wrong, he argued simply that ‘whatever

III, Section 2, Clause 1 of the Constitution—which extends the federal judicial power “to Controversies between a State and Citizens of another state . . . and between a State . . . and foreign States, Citizens or Subjects”<sup>25</sup>—authorized suits against non-consenting states in federal court.<sup>26</sup> At the time the Constitution was drafted, Alexander Hamilton took the position that the states retained their sovereignty:

It is inherent in the nature of sovereignty, not to be amenable to the suit of an individual without its consent. . . . ; and the exemption, as one of the attributes of sovereignty, is now enjoyed by the government of every state in the union. Unless, therefore, there is a surrender of this immunity in the plan of the convention, it will remain with the states . . . . The contracts between a nation and individuals, are only binding on the conscience of the sovereign, and have no pretension to a compulsive force.<sup>27</sup>

On the other hand, Edmund Randolph and James Wilson—members of the Committee of Detail from which Article III, Section 2 originated—interpreted Article III, Section 2 as making the states amenable to suit while establishing impartial tribunals.<sup>28</sup> No consensus was reached concerning its meaning.<sup>29</sup> Furthermore, it is unclear whether the states would have ratified the Constitution without sovereign immunity.<sup>30</sup>

Five years after the Constitution was adopted, the Supreme Court was forced to decide whether Article III authorized a citizen of one state to sue another state without its consent. In *Chisholm v. Georgia*,<sup>31</sup> a citizen of South Carolina brought a damages action against the State of Georgia for breach of contract. The Court rejected Georgia’s claim that a non-consenting state was immune from suit by a citizen of another state.<sup>32</sup> In a famous dissent, Justice James Iredell argued that the Supreme Court’s original jurisdiction should be interpreted with reference to common law prin-

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may be amiss in the conduct of public affairs is not chargeable personally on the king, nor is he, or his ministers, accountable for it to the people.”).

<sup>25</sup> U.S. CONST., art. III, §2, cl. 1.

<sup>26</sup> See Erwin Chemerinsky, *The Assumptions of Federalism*, 58 STAN. L. REV. 1763, 1784 (2006); see also JACOBS, *supra* note 16, at 28.

<sup>27</sup> THE FEDERALIST NO. 81, at 450 (Alexander Hamilton) (Robert A. Ferguson ed., 2006).

<sup>28</sup> See JACOBS, *supra* note 16, at 39.

<sup>29</sup> See *id.* at 39 (“[N]o uniform understanding was reached concerning the meaning of the clause extending the judicial power of the United States to ‘controversies between a state and citizens of another state.’”); see also Chemerinsky, *supra* note 26, at 1784 (“The dispute [at the ratifying conventions] was over whether the language of [Article III, Section 2, Clause 1] was meant to override the sovereign immunity that kept states from being sued in state courts.”).

<sup>30</sup> See *id.* at 40.

<sup>31</sup> *Chisholm v. Georgia*, 2 U.S. (2 Dall.) 419 (1793).

<sup>32</sup> See *id.* at 480.

ciples.<sup>33</sup> Assuming that “[a]ll the Courts of the United States must receive . . . all their authority . . . from the legislature only,”<sup>34</sup> Justice Iredell contended that Article III conferred jurisdiction to federal courts over certain claims but did not abrogate defenses.<sup>35</sup> Under this view, the State of Georgia would have been obligated to consent to suit by waiving its immunity because that was the customary practice at common law.

The *Chisholm* decision “fell upon the country with a profound shock.”<sup>36</sup> The State of Georgia, for instance, enacted a law forbidding anyone from enforcing the judgment; those who violated the law were to be subjected to the death penalty.<sup>37</sup> In any case, the most important reaction to *Chisholm* was unquestionably the proposal of a constitutional amendment to overrule the decision. Indeed, after much debate between Anti-Federalists and Federalists,<sup>38</sup> the states ratified the following version of the Eleventh Amendment: “The judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against any one of the United States by Citizens of another State or by Citizens or Subjects of any Foreign State.”<sup>39</sup>

## B. The Supreme Court and the Eleventh Amendment

By its terms, the text of the Eleventh Amendment appears to limit federal courts’ jurisdiction to suits against one state “by Citizens of another

<sup>33</sup> See *id.* at 432-35 (Iredell, J., dissenting).

<sup>34</sup> *Id.*

<sup>35</sup> See Note, *The Rehnquist Court’s Proper Restoration of State Sovereign Immunity*, 5 GEO. J.L. & PUB. POL’Y 205, 207 (2007) (citing 2 U.S. (2 Dall.) at 434-35).

<sup>36</sup> *Alden v. Maine*, 527 U.S. 706, 720 (1999) (quoting 1 C. WARREN, *THE SUPREME COURT IN UNITED STATES HISTORY* 96 (rev. ed. 1926)); accord *Hans v. Louisiana*, 134 U.S. 1, 11 (1890); *Principality of Monaco v. Mississippi*, 292 U.S. 313, 325 (1934); *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 69 (1996); DAVID P. CURRIE, *THE CONSTITUTION IN CONGRESS: THE FEDERALIST PERIOD, 1789-1801* 196 (1997) (“Newspapers representing a rainbow of opinion protested what they viewed as an unexpected blow to state sovereignty. Others spoke more concretely of prospective raids on state treasuries.”).

<sup>37</sup> See *Alden*, 527 U.S. 706 at 720.

<sup>38</sup> AKHIL REED AMAR, *AMERICA’S CONSTITUTION: A BIOGRAPHY* 334 (2005):

Some arch-states’ rightists objected in principle to the notion that a state could ever be dragged into federal court and forced to pay money, even in cases where the state *had* violated a federal law of the federal Constitution itself. But this extreme faction did not command enough support. . . . Instead, just as moderate Federalists had compromised with moderate Anti-Federalists to find common ground on the bill of rights, so once again common ground was found, repudiating *Chisholm*, but on a much narrower basis that even nationalists could live with. Had states’-rights extremists prevailed, the Eleventh Amendment would have read something like this: “No State shall ever be sued in any Article III court by any private party.”

<sup>39</sup> U.S. CONST. amend. XI.

State.”<sup>40</sup> Yet, in *Hans v. Louisiana*,<sup>41</sup> the Supreme Court interpreted the Eleventh Amendment to prohibit suits against a state by a private citizen.<sup>42</sup> In that case, Justice Joseph Bradley echoed Justice Iredell’s sentiment that Congress could not constitutionally enact a statute subjecting the states to suit in federal court. In support of his position, he cited the large deficiency of historical evidence in support of the idea:

Suppose that Congress, when proposing the Eleventh Amendment, had appended to it a proviso that nothing therein contained should prevent a State from being sued by its own citizens in cases arising under the Constitution or laws of the United States: can we imagine that it would have been adopted by the States? The supposition that it would is almost an absurdity on its face.<sup>43</sup>

*Hans* remains good law.<sup>44</sup>

Nearly twenty years after *Hans*, the Supreme Court created an exception to state sovereign immunity by holding that plaintiffs could bring suits against state officials for injunctive relief.<sup>45</sup> Even so, this so-called *Young* exception did not swallow the Eleventh Amendment. First, under *Hans*, plaintiffs are required to allege that the state official against whom they are bringing suit violated federal law.<sup>46</sup> Second, in *Edelman v. Jordan*,<sup>47</sup> the Supreme Court held that “the Eleventh Amendment permits official capacity actions against state officials for prospective relief . . . .”<sup>48</sup> In any case, *Young* and its progeny had a profound impact on nation-state relations, eliciting an “outcry . . . reminiscent of that following the decision in *Chisholm v. Georgia*.”<sup>49</sup> Even so, the Supreme Court has imposed additional limitations on the scope of the Eleventh Amendment. As of today, Congress can abrogate state sovereign immunity under Section 5 of the Four-

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<sup>40</sup> *See id.*

<sup>41</sup> *Hans v. Louisiana*, 134 U.S. 1 (1890).

<sup>42</sup> *See id.* at 15.

<sup>43</sup> *Id.*

<sup>44</sup> *See Fed. Mar. Comm’n v. S.C. State Ports Auth.*, 535 U.S. 743 (2002).

<sup>45</sup> *See Ex Parte Young*, 209 U.S. 123, 155 (1908).

<sup>46</sup> *See Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89 (1984).

<sup>47</sup> *Edelman v. Jordan*, 415 U.S. 651 (1974).

<sup>48</sup> HAROLD S. LEWIS, JR. & ELIZABETH J. NORMAN, *CIVIL RIGHTS LAW AND PRACTICE* § 5.35 (2d ed. 2001). *See also Edelman*, 415 U.S. at 665-69.

<sup>49</sup> JACOBS, *supra* note 16, at 146 (citation omitted). Nevertheless, Professor Jacobs notes that “[t]he reference was to events in North Carolina where resentment against the federal judiciary . . . appears to have been due not so much to *Ex Parte Young* as to the decision in *McNeill v. Southern Railroad*, 202 U.S. 543 (1906).” *Id.* at 195 n.5 (citation omitted). In that case, the Supreme Court “upheld a decree of the United States Circuit Court for the Eastern District of North Carolina prohibiting the enforcement of certain orders of the state corporation commission.” *Id.*

teenth Amendment.<sup>50</sup> In addition, the federal judiciary defines the scope of Congress's Fourteenth Amendment powers.<sup>51</sup>

## II. THE PROBLEM: WHEN IS AN ENTITY A SOVEREIGN?

Because states are typically immune from suit under the doctrine of state sovereign immunity, the Supreme Court has been forced to decide whether state agencies or instrumentalities of the state that administer the states' affairs are also immune from suit. The Court has repeatedly ruled that, unlike arms of the state, counties and political subdivisions are not entitled to Eleventh Amendment immunity.<sup>52</sup> Thus, the Supreme Court has endeavored to draw a line between arms of the state and political subdivisions when determining whether an entity is entitled to state sovereign immunity.

### A. What Are Arms of the State?

The Supreme Court's arm-of-the-state jurisprudence began in 1977 when it decided *Mount Healthy City School District Board of Education v. Doyle*.<sup>53</sup> In that case, an untenured Ohio school teacher sued the Mount Healthy City School Board on First and Fourteenth Amendment grounds after the school board refused to renew his contract.<sup>54</sup> In a unanimous opinion, the Supreme Court applied what appeared to be a balancing test to

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<sup>50</sup> See *Fitzpatrick v. Bitzer*, 427 U.S. 445, 456 (“[T]he Eleventh Amendment, and the principle of state sovereignty which it embodies, are necessarily limited by the enforcement provisions of Section 5 of the Fourteenth Amendment.”) (citation omitted).

<sup>51</sup> See *City of Boerne v. Flores*, 521 U.S. 507, 527-29 (1999). The *Boerne* Court held that “[t]here must be a congruence or proportionality between the injury to be prevented or remedied and the means adopted to that end.” *Id.* at 520. The Supreme Court has since applied *Boerne*'s “congruence and proportionality” test on a number of occasions. See *Kimel v. Florida Bd. of Regents*, 528 U.S. 62, 82-92 (2000) (applying the “congruence and proportionality” test to conclude that the Age Discrimination in Employment Act was not “appropriate legislation” under Section 5 of the Fourteenth Amendment); *Bd. of Trustees of the Univ. of Ala. v. Garrett*, 531 U.S. 356, 365-74 (2001) (applying the “congruence and proportionality” test to hold that suits in federal court by state employees to recover money damages for the State's failure to comply with Title I of the Americans with Disabilities Act was barred by the Eleventh Amendment); *Nevada Dep't of Human Res. v. Hibbs*, 538 U.S. 721, 726-35 (2003) (applying the “congruence and proportionality” test to conclude that state employees may recover money damages in federal court when state fails to comply with the Family and Medical Leave Act's family-care provision.); *Tennessee v. Lane*, 541 U.S. 509, 522-34 (2004) (applying the “congruence and proportionality” test to hold that Title II of the Americans with Disabilities Act constitutes a valid exercise of Congress' authority under Section 5 of the Fourteenth Amendment to enforce that Fourteenth Amendment's substantive guarantees).

<sup>52</sup> See, e.g., *Lincoln County v. Luning*, 133 U.S. 529, 530 (1890); see also *Moor v. County of Alameda*, 411 U.S. 693, 717-21 (1973).

<sup>53</sup> *Mt. Healthy City Sch. Dist. Bd. of Educ. v. Doyle*, 429 U.S. 274 (1977).

<sup>54</sup> *Id.* at 276.

hold that the school board was not entitled to Eleventh Amendment immunity. The Court reasoned that the school board was more like a county or city than an arm of the state.<sup>55</sup> Under Ohio law, political subdivisions were not part of the state.<sup>56</sup> Moreover, even though Ohio funded and directed the school board, the school board was permitted to issue bonds and levy taxes.<sup>57</sup> Thus, the *Mount Healthy* Court applied two factors: (1) how state law defined the entity; and (2) the degree to which the entity was financial independent.

In *Lake Country Estates, Inc. v. Tahoe Regional Planning Agency*,<sup>58</sup> the Supreme Court again applied a balancing test to determine whether a so-called Compact Clause entity was an arm of the state entitled to Eleventh Amendment immunity. Pursuant to Article I, Section 10, Clause 3 of the Constitution,<sup>59</sup> the State of California and the State of Nevada (and Congress) created the Tahoe Regional Planning Agency (TRPA) to regulate the development of the Lake Tahoe Basin region.<sup>60</sup> Thereafter, several individuals whose property was located in the region brought suit in federal district court, alleging that TRPA had engaged in conduct that destroyed the value of their property.<sup>61</sup>

The Supreme Court declined to extend Eleventh Amendment immunity to TRPA.<sup>62</sup> According to the Court, extending state sovereign immunity to an agency was inappropriate unless the states (and, in this instance, Congress) intended to do so.<sup>63</sup> Here, the Court considered the two *Mt. Healthy* factors but identified additional factors:

- (1) express provisions allocating responsibility for judgments;
- (2) the ratio of state to local members on the agency's governing board;
- (3) whether the entity's primary functions are traditionally state or local; and
- (4) the history of litigation between the state and entity.<sup>64</sup>

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<sup>55</sup> *Id.* at 280-81.

<sup>56</sup> *Id.* at 280 (citations omitted).

<sup>57</sup> *Id.* (citations omitted).

<sup>58</sup> *Lake Country Estates, Inc. v. Tahoe Reg'l Planning Agency*, 440 U.S. 391 (1978).

<sup>59</sup> U.S. CONST. art I, §10, cl. 3. The Compact Clause reads as follows:

No State shall, without Consent of Congress, lay any Duty of Tonnage, keep Troops, or Ships of War in time of Peace, enter into any Agreement or Compact with another State, or with a foreign Power, or engage in War, unless actually invaded, or in such imminent Danger as will not admit of delay.

<sup>60</sup> *Lake Country*, 440 U.S. at 394.

<sup>61</sup> *Id.*

<sup>62</sup> *Id.* at 400-01.

<sup>63</sup> *Id.*

<sup>64</sup> Note, *A Narrow Eleventh Amendment Immunity for Political Subdivisions: Reconciling the Arm of the State Doctrine with Federalism Principles*, 55 *FORDHAM L. REV.* 101, 106 (1986) (citing *Lake Country*, 440 U.S. at 400-02).

## B. *Hess* and Its Progeny: Modern Arm-of-the-State Analysis

Shortly after *Lake Country*, the Supreme Court was again confronted with a Compact Clause entity that invoked state sovereign immunity. In *Hess v. Port Authority Trans-Hudson Corp.*,<sup>65</sup> two railroad workers filed personal injury actions under the Federal Employers' Liability Act<sup>66</sup> against their employer, the Port Authority Trans-Hudson Corporation (PATH).<sup>67</sup> The State of New York and the State of New Jersey created PATH to govern commercial facilities in the port of New York.<sup>68</sup> PATH moved to dismiss the actions, claiming Eleventh Amendment immunity.<sup>69</sup>

### 1. The "Twin Purposes" of the Eleventh Amendment

The *Hess* Court observed that, unlike *Lake Country*, "the indicators of immunity . . . [did] not . . . all point in the same way."<sup>70</sup> Accordingly, the Court looked to "the Eleventh Amendment's twin reasons for being."<sup>71</sup> Because it had previously held that a state's dignity interest could not be implicated in the Compact Clause context, it looked solely to whether a judgment against PATH would affect the state's treasury.

The Court declined to extend Eleventh Amendment immunity to PATH solely because New York and New Jersey controlled it, reasoning that "ultimate control of every state entity resides with the State, for the State may destroy and reshape any unit it creates. Political subdivisions exist solely at the whim and behest of their State, yet cities and counties do not enjoy Eleventh Amendment immunity."<sup>72</sup> Moreover, the Court found that PATH was financially independent—even though it dedicated much of its surplus to projects that New York and New Jersey might otherwise finance.<sup>73</sup> According to the Court, "the proper focus is not on the use of [the entity's] profits or surplus, but rather on its losses and debts."<sup>74</sup> If the state is not obligated to pay the entity's debts, then "the Eleventh Amendment's *core concern* is not implicated."<sup>75</sup>

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<sup>65</sup> *Hess v. Port Auth. Trans-Hudson Corp.*, 513 U.S. 30 (1994).

<sup>66</sup> 45 U.S.C. § 51 (1988).

<sup>67</sup> *Hess*, 513 U.S. at 33.

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> *Id.* at 44.

<sup>71</sup> *Id.* at 47.

<sup>72</sup> *Id.* (citations omitted) (internal quotations omitted).

<sup>73</sup> *Id.* at 49.

<sup>74</sup> *Id.* at 51 (emphasis added).

<sup>75</sup> *Id.*

## 2. Control

Chief Justice Rehnquist and Justices O'Connor, Scalia, and Thomas dissented, arguing that the Eleventh Amendment bars federal jurisdiction of any suit against a state in "law or equity," thus belying the claim that the primary concern of the Eleventh Amendment is the state's treasury.<sup>76</sup> Instead, the proper inquiry "is whether the State possesses sufficient *control* over the entity performing governmental functions that the entity may properly be called an extension of the State itself."<sup>77</sup> The dissenting justices explained:

An arm of the State . . . is an entity that undertakes state functions and is politically accountable to the State, and by extension, to the electorate. The critical inquiry, then, should be whether and to what extent the elected state government exercises oversight over the entity. If the lines of oversight are clear and substantial—for example, if the State appoints and removes an entity's governing personnel and retains veto power over an entity's undertakings—then the entity should be deemed an arm of the State . . . .<sup>78</sup>

In any event, the dissent observed that the treasury factor was part of the equation.<sup>79</sup> On the facts in *Hess*, it would have found PATH immune from suit.<sup>80</sup>

## 3. A Gloss on *Hess*: Legal Liability for Judgments

The Supreme Court elaborated *Hess* in *Regents of the University of California v. Doe*<sup>81</sup> when a New York citizen brought a breach of contract action in federal court against the Regents of the University of California and several individual defendants. The plaintiff alleged that the University breached a contract by failing to employ him at a laboratory it operated for the federal government.<sup>82</sup> The Energy Department agreed to indemnify the University of California for any damages awards associated with the operation of the laboratory.<sup>83</sup> In a unanimous opinion, the Supreme Court held that the federal government's promise to indemnify the state against litiga-

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<sup>76</sup> *Id.* at 60.

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* at 61.

<sup>79</sup> *Id.* at 62.

<sup>80</sup> *Id.* at 63.

<sup>81</sup> *Regents of the Univ. of Cal. v. Doe*, 519 U.S. 425 (1997).

<sup>82</sup> *Id.* at 426-27.

<sup>83</sup> *Id.* at 428.

tion costs did not eliminate its Eleventh Amendment immunity because it was still *legally liable* for judgments.<sup>84</sup>

### C. A Circuit Split: Five Key Decisions

Given the difficulties in determining whether to extend state sovereign immunity to Compact Clause entities, it is perhaps understandable that there has been some confusion concerning whether private entities are arms of the state when such entities perform a public function. Because courts have not treated the issue uniformly, this Part selects and examines five cases from the federal circuit courts that involve private entities that invoked state sovereign immunity as an affirmative defense.<sup>85</sup> The entities in the First Circuit's and Seventh Circuit's decisions are examples of traditionally public entities that the state sought to privatize or "spin off" by statute. The entities in the Ninth, Tenth, and Eleventh circuits' decisions involve traditionally private entities that the state contracted to serve a public function. The decisions rendered in the Ninth and Eleventh circuits are examined first.

#### 1. The Eleventh Circuit's *Shands* Decision

The Eleventh Circuit's decision in *Shands Teaching Hospital and Clinics, Inc. v. Beech Street Corp.*<sup>86</sup> is the only case to have extended state sovereign immunity to a private entity. While managing a state employee health insurance plan, Florida's Department of Management Services (DMS) hired Unisys—a private corporation—to pay health care providers for services rendered to state employees and to provide state employees with a preferred provider organization (PPO) network.<sup>87</sup> Unisys then subcontracted Beech Street to institute the PPO network,<sup>88</sup> which included Shands Hospital.<sup>89</sup>

Shands Hospital sued Unisys and Beech Street when Unisys allegedly failed to pay for "covered medical services."<sup>90</sup> Unisys and Beech Street argued that the suit should be dismissed because they were arms of the

<sup>84</sup> *Id.* at 431.

<sup>85</sup> See also *United States ex rel. Barron v. Deloitte & Touche, L.L.P.*, 381 F.3d 438, 439-42 (5th Cir. 2004); *Brotherton v. Cleveland*, 173 F.3d 552 (6th Cir. 1999). For purposes of brevity, this Comment does not discuss the Fifth Circuit or the Sixth Circuit.

<sup>86</sup> *Shands Teaching Hosp. & Clinics, Inc. v. Beech St. Corp.*, 208 F.3d 1308 (11th Cir. 2000).

<sup>87</sup> *Id.* at 1309 (citing FLA. STAT. ANN. § 110.123(3)(d) (2000)).

<sup>88</sup> *Id.* at 1310.

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

state.<sup>91</sup> The Eleventh Circuit noted that it uses three factors to determine whether state sovereign immunity extends to entities other than the state:

(1) how state law defines the entity; (2) what degree of control the State maintains over the entity; and (3) from where the entity derives its funds and who is responsible for judgments against the entity.<sup>92</sup>

The court observed that “the pertinent inquiry is not into the nature of a corporation’s status in the abstract, but its function or role in a particular context.”<sup>93</sup>

Although there was “no case on point,” the Eleventh Circuit concluded that the suit should be dismissed because Unisys and Beech Street were simply acting at the behest of the State, with Florida funding and retaining nearly complete control over the program.<sup>94</sup> In addition, a favorable ruling on either of Shands’s claims would have implicated state funds. First, a declaratory judgment would have affected the state’s treasury because it might have affected the number of payouts that Florida was required to make.<sup>95</sup> Second, even if Unisys indemnified the state for the expenses, payment for Shands’s damages claim would have amounted to an obligation of the state.<sup>96</sup>

## 2. The Ninth Circuit’s *Del Campo* Decision

The most recent decision involving a private entity was *Del Campo v. Kennedy*.<sup>97</sup> After passing a statute criminalizing “the making, drawing, uttering, or delivery of any check, draft or money order . . . ‘with intent to defraud,’”<sup>98</sup> the State of California authorized district attorneys to create “bad check diversion programs” in which the district attorneys could drop charges against those who wrote bad checks.<sup>99</sup> Accordingly, the District Attorney in Santa Barbara hired American Corrective Counseling Services (ACCS) to run its diversion program.<sup>100</sup> The contract between the District Attorney and ACCS expressly stated that ACCS was an “independent contractor.”<sup>101</sup> Moreover, the contract required ACCS to indemnify the county,

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<sup>91</sup> *Id.*

<sup>92</sup> *Id.* at 1311 (citing *Stewart v. Baldwin County Bd. of Educ.*, 908 F.2d 1499, 1509 (11th Cir. 1990); *Tuveson v. Fla. Governor’s Council on Indian Affairs, Inc.*, 734 F.2d 730, 732 (11th Cir. 1984)).

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *Id.* at 1312.

<sup>96</sup> *Id.* at 1313.

<sup>97</sup> *Del Campo v. Kennedy*, 517 F.3d 1070 (2008).

<sup>98</sup> *Id.* at 1072 (citing CAL. PENAL CODE § 476(a) (2008)).

<sup>99</sup> *Id.* (citing CAL. PENAL CODE § 1001.60-67 (2008)).

<sup>100</sup> *Id.*

<sup>101</sup> *Id.* at 1072-73.

to carry its own insurance, and to manage nearly every aspect of the program.<sup>102</sup>

While ACCS was operating the diversion program, a dispute arose between ACCS and an individual whom ACCS accused of having passed a worthless check.<sup>103</sup> In particular, after disputing a collection fee levied by ACCS, Elena Del Campo brought suit against the District Attorney, ACCS, and several others for violation of her rights to equal protection and due process.<sup>104</sup> ACCS and the District Attorney claimed state sovereign immunity as arms of the state.<sup>105</sup> The Ninth Circuit assumed that the district attorney had acted as an arm of the state but held that ACCS was not entitled to state sovereign immunity.<sup>106</sup> The court reasoned that state sovereign immunity does not extend to private entities because the purpose of sovereign immunity is to protect the state's treasury and to accord the state a degree of dignity that is consistent with the status of sovereign.<sup>107</sup> The court did not think that these purposes would be furthered by extending state sovereign immunity to ACCS because, as a private corporation contracted by the state, it was more removed from state power than counties or Compact Clause agencies—which are routinely denied state sovereign immunity.<sup>108</sup>

The Ninth Circuit acknowledged that, in the past, it had looked to the five factors to determine whether an entity is an arm of the state:<sup>109</sup>

- (1) whether a money judgment would be satisfied out of state funds;
- (2) whether the entity performs central governmental functions;
- (3) whether the entity may sue or be sued;
- (4) whether the entity has the power to take property in its own name or only in the name of the state; and
- (5) the corporate status of the entity.<sup>110</sup>

The court concluded that only the second factor could ever be satisfied by a private entity.<sup>111</sup> Moreover, because it had previously declined to

<sup>102</sup> *Id.* at 1072.

<sup>103</sup> *Id.* at 1073.

<sup>104</sup> Del Campo also alleged violations of the Federal Fair Debt Collection Practices Act and California Constitution and California Unfair Business Practices Act. *See id.*

<sup>105</sup> *Id.*

<sup>106</sup> *Id.*

<sup>107</sup> *Id.* (citing *N. Ins. Co. v. Chatham County, Ga.*, 547 U.S. 189, 193 (2006) (quoting *Alden v. Maine*, 527 U.S. 706, 731 (1999) (alterations omitted)); *Fed. Mar. Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743 (2002); *Hess v. Port Auth. Trans-Hudson Corp.*, 513 U.S. 30 (1994)).

<sup>108</sup> *Del Campo*, 517 F.3d at 1075-76.

<sup>109</sup> *See id.* at 1076-81.

<sup>110</sup> *Id.* at 1077 (citing *U.S. ex rel. Ali v. Daniel, Mann, Johnson, & Mendenhall*, 355 F.3d 1140, 1147 (9th Cir. 2004) [hereinafter *DMJM*] (citing *Mitchell*, 861 F.2d at 201)).

<sup>111</sup> *Id.*

extend state sovereign immunity to a private entity when only the second factor had been satisfied, the court declined to apply the test on the ground that doing so would be a waste of judicial resources.<sup>112</sup> In dicta, the court criticized the Eleventh Circuit's *Shands* decision for having used a functional approach in an Eleventh Amendment case.<sup>113</sup>

### 3. The Tenth Circuit's *Sikkenga* Decision

The Tenth Circuit has also determined whether state sovereign immunity should extend to a private entity. In *United States ex rel. Sikkenga v. Regence Bluecross Blueshield of Utah*,<sup>114</sup> a former employee of Regence BlueCross BlueShield of Utah ("Regence") brought a false-claims<sup>115</sup> suit against Regence, three Regence managers, and Associated Regional and University Pathologists ("ARUP")—a laboratory owned by the University of Utah Medical Center. Among other things, Edyth Sikkenga claimed that ARUP submitted false claims to Regence and that Regence paid them.<sup>116</sup> Utah's Department of Health and Human Services had hired Regence to be its major Medicare Part B carrier,<sup>117</sup> which made Regence responsible for processing and paying Medicare Part B claims and for ensuring that claims were eligible for reimbursement under the Medicare program.<sup>118</sup> ARUP enjoyed almost complete autonomy in terms of its operations and funding.

ARUP argued that the suit was barred because it was entitled to state sovereign immunity. In light of the "coincidence of scope between the FCA and the Eleventh Amendment inquiries," the court applied its version of the arm-of-the-state analysis:

(1) the state's legal liability for a judgment; (2) the degree of autonomy for the state—both as a matter of law and the amount of guidance and control exercised by the state; and (3) the extent of financing the agency receives independent of the state treasury and its ability to provide for its own financing.<sup>119</sup>

The court found that Utah would not be liable for any judgment against ARUP.<sup>120</sup> First, Utah law established that any judgment against

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<sup>112</sup> *Id.* at 1078 (citing *DMJM*, *supra* note 110, at 1140).

<sup>113</sup> *Id.* (citing *Richardson v. McKnight*, 521 U.S. 399, 409 (1997)).

<sup>114</sup> *U.S. ex rel. Sikkenga v. Regence Bluecross Blueshield of Utah*, 472 F.3d 702 (10th Cir. 2006).

<sup>115</sup> *See* 31 U.S.C. § 3729(a) (2006).

<sup>116</sup> *U.S. ex rel. Sikkenga*, 472 F.3d at 707.

<sup>117</sup> *Id.* at 708.

<sup>118</sup> *Id.*

<sup>119</sup> *Id.* (citing *Sturdevant v. Paulsen*, 218 F.3d 1160, 1164 (10th Cir. 2000)).

<sup>120</sup> *Id.* at 718.

ARUP would be satisfied out of ARUP's treasury.<sup>121</sup> Second, although depletion of ARUP's general treasury would require the state to further fund the Utah Medical Center and the University,<sup>122</sup> it was bound by the Supreme Court's decision in *Regents of California v. Doe*<sup>123</sup> "to focus on legal liability for a judgment, rather than on the practical, or indirect, impact a judgment would have on the state's treasury."<sup>124</sup>

The court further found that ARUP's operations extended beyond educating the public.<sup>125</sup> First, ARUP was a nationwide commercial laboratory that earned the majority of its revenue from operations outside the University.<sup>126</sup> Second, ARUP possessed all of the hallmarks of a private entity—it could sue or be sued,<sup>127</sup> it could enter into contracts,<sup>128</sup> and it could maintain bank accounts.<sup>129</sup> Finally, the ties between the University and ARUP arose as an incidence of ownership.<sup>130</sup>

On the other hand, the court observed "a history of complex, intertwined relationships for funding capital improvement projects between the University and ARUP."<sup>131</sup> ARUP's financial statements were audited by independent accountants and subsequently included as separate items in the University of Utah's financial statements.<sup>132</sup> Moreover, ARUP was designed to be a "profit center" for the University Medical Center.<sup>133</sup>

In the end, the court held that ARUP was not entitled to state sovereign immunity because Utah intended for ARUP to be financially independent and to compete in the private sector.<sup>134</sup>

#### 4. The Seventh Circuit's *Takle* Decision

In *Takle v. University of Wisconsin Hospital and Clinics Authority*,<sup>135</sup> Joyce Takle brought a damages action against the University of Wisconsin Hospital and Clinic Authority (the "Authority") for violation of her rights

<sup>121</sup> *Id.* (citing UTAH CODE ANN. § 53 B-7-103(3)(d)).

<sup>122</sup> *Id.*

<sup>123</sup> *Id.* (citing *Regents of the Univ. of Cal. v. Doe*, 519 U.S. 425 (1997)).

<sup>124</sup> *Id.* (quoting *Sturdevant*, 218 F.3d at 1164 (quoting *Duke v. Grady Mun. Sch.*, 127 F.3d 972, 981 (10th Cir. 1997))).

<sup>125</sup> *Id.* at 719.

<sup>126</sup> *Id.*

<sup>127</sup> *Id.* (citing UTAH CODE ANN. §§ 16-10a-302(1), 53B-2-101).

<sup>128</sup> *Id.* (citing UTAH CODE ANN. § 53B-7-103(3)).

<sup>129</sup> *Id.* at 720 (citing UTAH CODE ANN. § 53B-7-103(3)).

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* at 721.

<sup>132</sup> *Id.*

<sup>133</sup> *Id.*

<sup>134</sup> *Id.* (citing *Hess*, 513 U.S. at 47).

<sup>135</sup> *Takle v. Univ. of Wis. Hosp. & Clinics Auth.*, 402 F.3d 768 (7th Cir. 2005).

under Title I of the American with Disabilities Act while employed at the University of Wisconsin Hospital and Clinics in Madison, Wisconsin (the “Hospital”). The Hospital was owned and operated by the Authority at the time of the alleged injury<sup>136</sup> but was previously part of the University of Wisconsin, an arm of the state.<sup>137</sup> The Wisconsin legislature had “spun off” the Hospital to the Authority by statute.<sup>138</sup> The Hospital was authorized to operate like a private hospital, except that some of the Hospital’s board members were appointed by the governor, while others were members by virtue of holding public office.<sup>139</sup> The majority of the Hospital’s employees continued to be deemed state employees,<sup>140</sup> and the state continued to own the Hospital’s buildings.<sup>141</sup> In addition, the Hospital was required to finance the university’s medical school and to provide state-mandated health services.<sup>142</sup>

Writing for the court, Judge Richard Posner framed the underlying legal question:

“The framers did not intend to abrogate [sovereign immunity]. . . . But what exactly is the ‘state’? The defendant in this case is . . . a hybrid entity; it has characteristics of both a state agency and a private foundation. Where on the public-private spectrum to locate it depends on the purpose of the doctrine of sovereign immunity, and that purpose is obscure because “sovereignty” is an obscure concept when applied to a state of the United States. Is Wisconsin’s “sovereignty” impaired if the [H]ospital is suable in a federal court? It would be if the [H]ospital were financed by the state so that any judgment against it would be paid out of state funds, unless the state had taken out some form of liability insurance—but that would not negate its liability; it would be the premise of its liability, for unless it were liable it wouldn’t need liability insurance.”<sup>143</sup>

The Seventh Circuit noted the twin purposes of sovereign immunity—protecting the state’s fiscal independence and protecting its dignity. The court dismissed the notion of dignity as being “difficult to translate into an operational legal standard”<sup>144</sup> but concluded that the state’s fiscal indepen-

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<sup>136</sup> *Id.*

<sup>137</sup> *Id.* at 770.

<sup>138</sup> *Id.*

<sup>139</sup> *Id.*

<sup>140</sup> *Id.* at 771.

<sup>141</sup> *Id.*

<sup>142</sup> *Id.*

<sup>143</sup> *Id.* at 769 (citing *Hess*, 513 U.S. at 48-51; *Kashani v. Purdue Univ.*, 813 F.2d 843, 845 (7th Cir. 1987); *Cash v. Granville Cty. Bd. of Educ.*, 242 F.2d 219, 223-24 (4th Cir. 2001); *Doe*, 519 U.S. at 430-31).

<sup>144</sup> *Id.*

dence was not implicated, notwithstanding the fact that a judgment against the Hospital might impair its ability to continue to provide benefits.<sup>145</sup> In addition, the court observed that there was nothing to indicate that the Hospital was a part of state government. First, a hospital is not inherently governmental.<sup>146</sup> Second, the hospital's organic statute authorized it to operate like a private hospital.<sup>147</sup> Finally, the public characteristics of the hospital were merely incidental to the transition from public to private.<sup>148</sup>

Taken together, the Seventh Circuit concluded that what it had was "a state's creation of a private entity, with the state using its leverage as the creator of the entity to insist that [the hospital] serve the state's interests as well as its own."<sup>149</sup> As a matter of public policy, the court concluded that privatized entities should not be permitted to enjoy the benefits of both being private and being immune from suit in federal court.<sup>150</sup>

### 5. The First Circuit's *Fresenius* Decision

Like *Takle*, *Fresenius Medical Care Cardiovascular Resources, Inc. v. Puerto Rico*<sup>151</sup> involved a suit against a public entity that the state had mostly privatized. *Fresenius Medical Care Cardiovascular Resources* ("FMC") brought a breach of contract action against Puerto Rico and the Caribbean Cardiovascular Center Corp. ("PRCCCC"), and PRCCCC moved to dismiss the claim, contending that it was an arm of the state<sup>152</sup> entitled to Eleventh Amendment immunity.<sup>153</sup> PRCCCC's enabling act<sup>154</sup> did not state that PRCCCC was an arm of the state but provided that PRCCCC was permitted to enter into contracts with the state and to borrow money from the Commonwealth.<sup>155</sup>

The First Circuit announced that it would follow the two-step analysis set forth in *Hess v. Port Authority Trans-Hudson Corp.*<sup>156</sup>—(1) whether the state clearly instructed the entity to share its sovereignty; and (2) whether the damages sought from the entity would be paid from the public trea-

<sup>145</sup> *Id.* at 769-70.

<sup>146</sup> *Id.* at 770.

<sup>147</sup> *Id.*

<sup>148</sup> *Id.* at 771.

<sup>149</sup> *Id.*

<sup>150</sup> *Id.*

<sup>151</sup> *Fresenius Med. Care Cardiovascular Res., Inc. v. Puerto Rico*, 322 F.3d 56 (1st Cir. 2003).

<sup>152</sup> The Commonwealth of Puerto Rico is treated as a state for Eleventh Amendment purposes. *Fresenius*, 322 F.3d at 61 (citing *P.R. Ports Auth. v. M/V Manhattan Prince*, 897 F.2d 1, 9 (1st Cir. 1990)).

<sup>153</sup> *Id.* at 59.

<sup>154</sup> P.R. LAWS ANN. 24, §§ 343-343k (2000).

<sup>155</sup> *Fresenius*, 322 F.3d at 69.

<sup>156</sup> *Hess*, 513 U.S. 30 (1994).

sury.<sup>157</sup> As indicia of Puerto Rico's intentions concerning whether PRCCCC was entitled to sovereign immunity, the court referred to how the Puerto Rico legislature structured PRCCCC.<sup>158</sup> In so doing, it looked at the following factors: PRCCCC's enabling act; state statutory law; state court decisions; PRCCCC functions; and control by the state.<sup>159</sup> Because some of the indicia did not indicate that PRCCCC was an arm of the state, the court proceeded to the second stage of the analysis by examining "what [was] said by state law on the topic and what in fact ha[d] happened."<sup>160</sup> Ultimately, the First Circuit ruled against PRCCCC, finding that PRCCCC's "argument [was] simply that a judgment would deplete its operating funds, that the Commonwealth might choose to rescue it, and that this would indirectly deplete the state treasury."<sup>161</sup>

### III. OBSERVATIONS

This Part makes three observations concerning state sovereign immunity and the federal circuit courts' arm-of-the-state jurisprudence. First, state sovereign immunity does not extend to private entities. Second, courts are applying arm-of-the-state analysis whenever a private entity claims state sovereign immunity. Third, an erroneous finding of state sovereign immunity threatens a state's sovereignty.

#### A. State Sovereign Immunity Does Not Extend to Private Entities

State sovereign immunity does not extend to private entities—even when these entities perform work on behalf of the state. First, extending state sovereign immunity to private entities does not serve either of the "twin purposes" of state sovereign immunity. Second, in any given privatization scheme, state governments do not exercise enough control over the entity as to clothe it with state sovereign immunity.

1. Extending state sovereign immunity to private entities does not serve the "twin purposes" of the Eleventh Amendment

A state's dignity and fiscal interests are not threatened when a court declines to extend state sovereign immunity to a private entity. First, a state is not made to answer for a private entity's wrongs when a private entity is

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<sup>157</sup> *Id.* at 68.

<sup>158</sup> *See id.* at 68-72.

<sup>159</sup> *Id.*

<sup>160</sup> *Id.* at 72 (footnote omitted).

<sup>161</sup> *Id.* at 75.

haled into court.<sup>162</sup> Because “[t]he preeminent purpose of state sovereign immunity is to accord States the dignity that is consistent with their status as sovereign entities,”<sup>163</sup> a state’s dignity is tarnished only when it is “required to answer the complaints of private parties in federal courts.”<sup>164</sup> Nevertheless, a state is not required to answer for private entities when such entities are sued in federal court. In the event of a lawsuit against the private entity, the named defendant in the case would be the private entity rather than the state. Moreover, the state would not be required to defend that entity.

Second, states are not financially responsible for private entities.<sup>165</sup> A private entity is “conceived as a fiscally independent entity” and is “financed predominately by private funds.”<sup>166</sup> To this end, private entities produce their own profits and do not depend on appropriations from the state government.<sup>167</sup> In cases of traditionally public entities that the state has privatized, the newly-created entity performs work on behalf of the government because the government permits the entity to operate as a private entity, not because the government funds the entity.<sup>168</sup> Even if a state agrees (for one reason or another) to appropriate money to a private entity, the private entity’s existence does not depend on that appropriation because it is permitted to acquire funds from additional sources.<sup>169</sup> Likewise, a state is not legally liable for a private entity’s debts.<sup>170</sup> If a court issues a judg-

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<sup>162</sup> See *Alden*, 527 U.S. at 748 (“The founding generation thought it ‘neither becoming nor convenient that the several States of the Union, invested with that large residuum of sovereignty which had not been delegated to the United States, should be summoned as defendants to answer the complaints of private persons.’”) (quoting *In re Ayers*, 123 U.S. 443, 505 (1887)).

<sup>163</sup> *Fed. Mar. Comm’n v. S.C. State Ports Auth.*, 535 U.S. 743, 760 (2002) (citing *Ayers*, 123 U.S. at 505).

<sup>164</sup> *Id.*

<sup>165</sup> See *Hess*, 513 U.S. 30, 45 (1994) (finding that a lack of financial responsibility of an entity by the state “point[s] away from Eleventh Amendment immunity. . .”).

<sup>166</sup> *Id.*

<sup>167</sup> To be sure, state governments will often support a “spin off” for a short period of time until the newly-created private entity is in position to fund itself without government assistance. The privatization scheme in *Hess* is an example of such a design. See *id.* at 45-46.

<sup>168</sup> See *Takle v. Univ. of Wisc. Hosp. & Clinics Auth.*, 402 F.3d 768, 771 (7th Cir. 2005) (finding that the State of Wisconsin “used its leverage as the creator as the creator of [the privatized entity at issue] to insist that it serve the state’s interests. . .”).

<sup>169</sup> See *Hess*, 513 U.S. at 45-46 (quoting *Comm’r v. Shamburg’s Estate*, 144 F.2d 998, 1002 (2d Cir. 1944) (“In the compact[,] the states agreed to make annual appropriations . . . for the expenses of the Authority until revenues from its operations were sufficient to meet its expenses. These annual appropriations were discontinued in 1934 because the revenues from the bridges, the Holland Tunnel and the Inland Terminal had become sufficient.”) (alterations omitted).

<sup>170</sup> See *id.* at 46 (“The States . . . bear no legal liability for Port Authority debts; they are not responsible for the payment of judgments against the Port Authority or PATH.”).

ment against a private entity, the private entity is exclusively responsible for the payment of that debt.<sup>171</sup>

2. State governments do not exercise enough control over private entities as to clothe them with state sovereign immunity

In any given privatization scheme, a state government will not exercise enough control over a private entity as to clothe that entity with state sovereign immunity. First, state governments do not exercise clear and immediate oversight over private entities. Apart from being obligated to perform a public function, a privatized entity need not seek the government's permission before acquiring property, governing itself, or participating in a business venture.<sup>172</sup> Moreover, it is immaterial that the state for which the private entity is performing work could potentially terminate its operations. As Justice O'Connor noted in *Hess*, "[v]irtually every enterprise, municipal or private, flourishes in some sense at the behest of the State. But . . . the Eleventh Amendment's protections [do not] hinge on this sort of abstraction."<sup>173</sup>

Second, although states often retain the right to appoint representatives to traditionally public entities that it has privatized, such appointment powers do not amount to control over the entity. When the government appoints individuals to positions in a private entity, these appointments do not have a direct impact on the entity's conduct.<sup>174</sup> To the contrary, the officials of a private entity (and not the state) are responsible for determining how the entity will behave. This is especially the case when the "power is diffused among different public officials who may hold quite different views of how the entity should conduct itself."<sup>175</sup> In the state sovereign immunity context, the Supreme Court has held that the power to appoint does not amount to control.<sup>176</sup>

Finally, any public characteristics of an entity that the state has privatized will be a product of the entity's transition from public to private.<sup>177</sup> In *Takle*, the Seventh Circuit observed that hospital's employees continued to be deemed state employees because the State of Wisconsin wished to avoid

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<sup>171</sup> *See id.*

<sup>172</sup> *See, e.g.*, 24 P.R. LAWS ANN. §§ 343b (2006).

<sup>173</sup> *Hess*, 513 U.S. at 62 (internal quotations omitted) (citations omitted).

<sup>174</sup> *See Takle v. Univ. of Wisc. Hosp. & Clinics Auth.*, 402 F.3d 768, 770-71 (7th Cir. 2005).

<sup>175</sup> *Takle*, 402 F.3d at 771.

<sup>176</sup> *See Auer v. Robbins*, 519 U.S. 452, 456 n.1 (1997) (finding that the governor's ability to appoint four of five Board members to an intra-state entity was insufficient state control as to make that entity an arm of the state entitled to state sovereign immunity).

<sup>177</sup> *Id.*

creating a new pension system.<sup>178</sup> In effect, the state had indulged a fiction for purposes of continuity. Such public characteristics do not indicate state control but rather represent an effort by the state to use its influence as the creator of the entity to require that the entity serve the state's interests.<sup>179</sup> As Judge Posner observed in *Takle*, because these types of connections between a state and an entity are found in many privatization schemes, they do not "require that privatization be treated as a farce in which the privatized entity enjoys the benefits both of not being the state . . . and of being the state."<sup>180</sup>

#### B. Courts Are Applying Arm-of-the-State Analysis Whenever an Entity Claims State Sovereign Immunity

Apart from the Ninth Circuit's recent decision in *Del Campo v. Kennedy*,<sup>181</sup> federal circuit courts have been employing the arm-of-the-state test whenever an entity has claimed state sovereign immunity.<sup>182</sup> In so doing, courts have applied the arm-of-the-state test to both traditionally public entities and traditionally private entities. For example, the First and Seventh circuits have applied arm-of-the-state analysis to traditionally public entities that the state allegedly privatized or "spun off" by statute.<sup>183</sup> The Ninth, Tenth and Eleventh circuits have applied arm-of-the-state analysis to traditionally private entities that the state contracted to perform a public function.<sup>184</sup> No circuit (including the Ninth Circuit) has distinguished between traditionally private entities and traditionally public entities for purposes of applying the arm-of-the-state test. Thus, federal circuit courts have either applied or declined to apply the arm-of-the-state test without regard to the particular privatization scheme in question.

#### C. An Erroneous Finding of State Sovereign Immunity Threatens a State's Sovereignty

An erroneous finding that an entity is an arm of the state can have devastating effects on a state's sovereignty. First, when a state transfers a traditionally public function to a private firm, an erroneous finding that the entity is an arm of the state can compromise the effectiveness of the privati-

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<sup>178</sup> *See id.*

<sup>179</sup> *Id.*

<sup>180</sup> *Id.*

<sup>181</sup> *Del Campo v. Kennedy*, 517 F.3d 1070 (9th Cir. 2008).

<sup>182</sup> *See supra* Part II.C.

<sup>183</sup> *See supra* Part II.C.4. and Part II.C.5.

<sup>184</sup> *See supra* Part II.C.1, Part II.C.2, and Part II.C.3.

zation scheme. Second, an erroneous finding that an entity is entitled to state sovereign immunity threatens the state's treasury.

1. An erroneous state sovereign immunity determination can have an adverse impact on a state's privatization scheme

In *Fresenius*, the First Circuit noted that “[n]ot all entities created by states are meant to share in a state's sovereignty. Some entities may be part of an effort at privatization, representing an assessment by the state that the private sector may perform a function better than the state.”<sup>185</sup> Accordingly, an erroneous arm-of-the-state finding not only violates the state's sovereign immunity by undermining its intentions but also by compromising the effectiveness of that state's privatization scheme.

First, because Congress cannot abrogate state sovereign immunity pursuant to its Article I powers, an erroneous arm-of-the-state finding might prevent the private entity's employees from enforcing the provisions of privately-enforceable Article I legislation.<sup>186</sup> An inability to enforce these provisions might limit the number of employees who would be willing to work for the entity, thus undermining the state's intentions and the effectiveness of its privatization scheme.<sup>187</sup>

Second, an erroneous arm-of-the-state finding might limit the private entity's ability to operate as a private entity. Absent an express waiver of sovereign immunity by the private entity, a private firm might refrain from contracting with the entity knowing that the arrangement would not be governed by private law.<sup>188</sup> As the First Circuit noted, “[t]he dollar cap on recovery found in many state sovereign immunity statutes would be a powerful disincentive to a private party to contract with an entity. . . .”<sup>189</sup>

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<sup>185</sup> *Fresenius Med. Care Cardiovascular Res., Inc. v. Puerto Rico*, 322 F.3d 56, 64 (1st Cir. 2003).

<sup>186</sup> *See id.*

<sup>187</sup> *See Fresenius*, 322 F.3d. at 64. As examples, the *Fresenius* court cited the Fair Labor Standards Act, 29 U.S.C. §§ 201-219 (2000); Title I of the American with Disabilities Act, 42 U.S.C. §§ 12111-12117 (2000); the Age Discrimination in Employment Act, 29 U.S.C. §§ 621-634 (2000); and the Family and Medical Leave Act, 29 U.S.C. §§ 2601-2654 (2000). *Id.* (citing *Alden v. Maine*, 527 U.S. 706, 712 (1999); *Bd. of Trs. of Univ. of Ala. v. Garrett*, 531 U.S. 356, 360 (2001); *Kimel v. Fla. Bd. of Regents*, 528 U.S. 62, 82-83 (2000); *Laro v. New Hampshire*, 259 F.3d 1, 4 (1st Cir. 2001)).

<sup>188</sup> *Id.*

<sup>189</sup> *Id.* (citation omitted).

2. An erroneous state sovereign immunity determination threatens the state's treasury

An erroneous arm-of-the-state finding violates a state's sovereign immunity by compromising the safety of its treasury. If an entity is deemed an arm of the state, the state is liable for any judgment rendered against that entity. Thus, where a state waives its sovereign immunity and consents to suit, an arm-of-the-state finding might subject the state to further liability than it intended.<sup>190</sup> Presumably, erroneous arm-of-the-state determinations by federal courts would have the undesirable consequence of discouraging states from consenting to suit (and thus from redressing wrongs done to its subjects) in an effort to avoid a greater level of liability than it is willing to endure.

#### IV. RECOMMENDATIONS

In light of the observations described in Part III, this Part makes four recommendations that should assist federal courts and state legislatures in balancing three critical (and often conflicting) interests—(1) giving proper deference to state sovereign immunity; (2) promoting fairness; and (3) increasing efficiency. First, courts should expressly acknowledge that state sovereign immunity does not extend to private entities. Second, courts should adopt a *per se* rule against extending state sovereign immunity to traditionally private entities. Third, courts should continue to apply the arm-of-the-state test to traditionally public entities. Finally, when a state legislature creates an entity to perform a government function, it should detail in the entity's organic statute whether that entity is an arm of the state within the meaning of the Eleventh Amendment.

Expressly acknowledging that a private entity cannot be an arm of the state will foster clarity among the courts. Moreover, adopting a *per se* rule against extending state sovereign immunity to traditionally private entities would have several beneficent effects. First, it would be more in keeping with the doctrine of state sovereign immunity—which, as noted in Part III.A, is not intended to extend to private entities. Second, it would enhance the legitimacy and efficacy of the American legal system by advancing principles of fairness and promoting good behavior. Third, it would allow for a more efficient federal judiciary.

In turn, state legislatures can bolster these positive effects by stating in an entity's organic statute whether that entity is an arm of the state. Indeed, an express statement in an entity's organic statute concerning its public or

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<sup>190</sup> See *id.* at 63.

private status for state sovereign immunity purposes would reduce the chances of a federal court erroneously finding (or not finding) that an entity is an arm of the state.

#### A. Courts Should Expressly Acknowledge That State Sovereign Immunity Does Not Extend to Private Entities

The Ninth Circuit is the only circuit to have made a blatant declaration that state sovereign immunity does not extend to private entities.<sup>191</sup> In so doing, it has said that applying arm-of-the-state to a private entity is “a category error. A category error . . . occurs when we place an entity in the wrong class or category of things, resulting in a fundamental error of analysis. Examples of category errors include inquiring into the gender of a rock or into which day of the week is reptilian.”<sup>192</sup> The other federal circuit courts should also expressly acknowledge that state sovereign immunity does not extend to private entities.

First, such an acknowledgement would foster clarity among the courts. Because of the complicated nature of the public-private distinction,<sup>193</sup> this acknowledgement would serve as a reminder to courts that the purpose of the arm-of-the-state test is to determine whether an entity is a governmental body, not to determine whether a private entity is an arm-of-the-state.<sup>194</sup>

Second, an express acknowledgement that private entities are not entitled to state sovereign immunity would advance principles of fairness and promote good behavior. It is axiomatic that injured parties be able to obtain relief when they are wronged.<sup>195</sup> Moreover, it is important that laws produce the proper incentives. An express acknowledgement by the courts that

<sup>191</sup> See *Del Campo*, 517 F.3d at 1078. The Seventh Circuit has implicitly suggested that state sovereign immunity does not extend to private entities. See *Takle*, 402 F.3d at 770 (7th Cir. 2005) (“It would be nice if the hospital’s organic statute stated outright that the hospital is a *private entity rather than an arm of the state*—that would resolve the issue. . .”) (emphasis added).

<sup>192</sup> *Id.* at 1078 n.11 (2008) (citing Gilbert Ryle, *Categories*, in COLLECTED PAPERS, VOL. II: COLLECTED ESSAYS, 1928-1968, 170-84 (1970)).

<sup>193</sup> For a fascinating account the elusive role of the public-private distinction in American law, see Paul M. Schoenhard, *A Three-Dimensional Approach to the Public-Private Distinction*, 2008 UTAH L. REV. 635 (2008). See also Morton J. Horowitz, *The History of the Public/Private Distinction*, 130 U. PA. L. REV. 1423 (1982); Paul Starr, *The Meaning of Privatization*, 6 YALE L. & POL’Y REV. 7 (1988) (“The terms public and private are fundamental to the language of our law . . . , but they are the source of continual frustration. Many things seem to be public and private at the same time in varying degrees and in different ways. As a result, we quarrel endlessly about whether some act or institution is really one or the other.”).

<sup>194</sup> *Del Campo*, 517 F.3d at 1077 (“The [arm-of-the-state] inquiry . . . is designed to discriminate between governmental bodies, not to determine whether private entities are arms of the state.”).

<sup>195</sup> See *supra* Part I.A.

state sovereign immunity does not extend to private entities would enhance both of these goals: injured parties would be afforded the opportunity to obtain redress for their injuries, and private entities would be disallowed from enjoying both the benefits of operating as a private entity and being immune from suit in federal court.<sup>196</sup> In turn, any given private entity would probably be more inclined to conform its conduct to the law, because the failure to do so might result in the entity being legally liable for damages.

Third, declining to extend state sovereign immunity to private entities would not reduce government efficiency by limiting the number of opportunities state governments would have to delegate public functions to private entities. Although private entities contracted by municipalities are not entitled to state sovereign immunity, there is no shortage of companies who are willing to perform work for these subdivisions.<sup>197</sup> Moreover, while courts have routinely denied private entities state sovereign immunity, there has been no appreciable decline in the number of opportunities available to state governments in the private sector.<sup>198</sup>

Finally, because government projects are massive and niche, they frequently confer benefits on the entity performing the project that would otherwise be unavailable to that entity.<sup>199</sup> Thus, it is reasonable to expect that many companies would continue to contract with the government even if doing so would expose them to a greater degree of liability.

## B. Courts Should Adopt a Per Se Rule against Extending State Sovereign Immunity to Traditionally private Entities

Courts should adopt a per se rule against extending state sovereign immunity to traditionally private entities. In implementing this rule, a court would refrain from applying arm-of-the-state analysis unless it concludes

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<sup>196</sup> See *Takle*, 402 F.3d at 771 (7th Cir. 2005) (“[Privatization schemes] should not be treated as a farce in which the privatized entity enjoys the benefits both of being the state and so being freed from the regulations that constrain state agencies, and of being the state and so being immune from suit in federal court.”).

<sup>197</sup> See Jeffrey D. Greene, *How Much Privatization: A Research Note Examining the Use of Privatization by Cities in 1982 and 1992*, 24 POL’Y STUD. J. 632, 632-40 (1996); see also REASON FOUNDATION, ANNUAL PRIVATIZATION REPORT 2008 23-27 (Leonard C. Gilroy ed, 2008), available at <http://www.reason.org/apr2008/>.

<sup>198</sup> See generally REASON FOUNDATION, *supra* note 197, at 9-23.

<sup>199</sup> At least one process-server company’s newsletter accounts the numerous benefits of securing government contracts that are unavailable in the private sector, such as “consistent, ongoing revenue”; strengthening a company’s client portfolio; increasing the value of a company; and preferential treatment to small-business and minority-owned businesses. See *Serve.Now.com*, The Benefits of Securing Government Contracts, <http://www.serve-now.com/news-events/view/benefits-securing-government-contracts/43> (last visited Mar. 27, 2009).

that the entity in question is a traditionally public entity. A court can determine whether an entity is traditionally public by asking if the entity was created by the state to perform a public function. If the entity was not so created, the court would conclude that that entity is traditionally private and decline to extend state sovereign immunity to that entity without employing the arm-of-the-state test.

### 1. Accuracy

First, a per se rule against extending state sovereign immunity to traditionally private entities would advance the important judicial goal of accuracy. Applying the arm-of-the-state test to traditionally private entities risks inaccurate results because it requires the court to engage in a cumbersome fact-sensitive inquiry when the result of that inquiry should be certain. Because traditionally private entities are perpetually private,<sup>200</sup> courts need not employ an arm-of-the-state test to determine that the entity is not an arm of the state. As the Ninth Circuit put it, applying arm-of-the-state analysis to these entities will always generate the same negative result.<sup>201</sup>

To be sure, the majority of the courts' decisions appear to have been correctly decided because few private entities have been permitted to shield themselves from suit by invoking state sovereign immunity. Nevertheless, applying arm-of-the-state analysis to traditionally private entities has occasionally led to the incorrect conclusion that a private entity is an arm of the state entitled to state sovereign immunity.<sup>202</sup> A per se rule against extending state sovereign immunity to traditionally private entities would produce more accurate results because courts would cease to entertain claims (and subject themselves to persuasion) when an entity that is undeserving of state sovereign immunity asserts that it is an arm of the state. In other words, a per se rule would eliminate the possibility of a court erroneously determining that a traditionally private entity is entitled to state sovereign immunity because it would not afford itself the opportunity to hold that it does. Obviously, a reduction in the number of faulty determinations would advance principles of fairness because courts would not needlessly deprive injured parties from having their cases heard on the merits.

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<sup>200</sup> The only exceptions to this proposition are conservatorships and receiverships. Because conservatorships and receiverships are uncommon, this Comment does not address how these arrangements should be addressed.

<sup>201</sup> *See id.*

<sup>202</sup> *See, e.g., Shands Teaching Hosp. & Clinics, Inc. v. Beech St. Corp.*, 208 F.3d 1308 (11th Cir. 2000).

## 2. Efficiency

Second, a *per se* rule against extending state sovereign immunity to traditionally private entities would advance the important judicial goal of efficiency. A *per se* rule would prevent the court from needlessly engaging in an onerous balancing test in order to discern whether an entity is an arm of the state entitled to state sovereign immunity. In addition, litigants would not have to engage in laborious discovery tactics in an attempt to influence the court's decision. This result would be substantial because, as of 2002, 86.9% of privatization schemes involved contracting out to traditionally private entities.<sup>203</sup>

### C. Courts Should Continue to Apply Arm-of-the-State Analysis to Traditionally Public Entities

Courts should continue to apply the arm-of-the-state test to traditionally public entities when those entities invoke state sovereign immunity. In so doing, a court would refrain from applying the arm-of-the-state test unless and until it concludes that the entity in question is a traditionally public entity. Like the determination of whether an entity is traditionally private,<sup>204</sup> a court can determine whether an entity is traditionally public by asking if the entity was created by the state to perform a public function. If the entity was so created, then the court would conclude that the entity is traditionally public and employ the arm-of-the-state test.

Unlike the result generated by the application of the arm-of-the-state test to traditionally private entities, the result generated by the application of the arm-of-the-state test to traditionally public entities will not always be negative. This different result is a product of the fact that it is not always clear whether a state government has "spun off" an entity to operate in the private sector. Because of the elusive nature of traditionally public entities, the arm-of-the-state test would assist courts in determining whether a traditionally public entity has been privatized. While the state need not do anything to make a traditionally private entity private,<sup>205</sup> the state must privatize a traditionally public entity in order to make that entity private.

#### 1. Accuracy

First, the arm-of-state analysis is well-suited to determine whether a traditionally public entity has been privatized because it asks the same

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<sup>203</sup> See Chi et al., *supra* note 3, at 13, Fig. 6.

<sup>204</sup> See *supra* Part IV.B.

<sup>205</sup> Del Campo v. Kennedy, 517 F.3d 1070, 1078 (2008) ("By their nature, [private] entities are not arms of the state.") (citation omitted).

questions that one would expect from any inquiry into the private or public status of an entity. Although the purpose of the arm-of-the-state test is to distinguish between governmental bodies, the different formulations of the arm-of-the-state test devised in the federal circuit courts can also be used to determine the public or private status of a traditionally public entity. The First Circuit's arm-of-the-state test is illustrative because it was applied in *Fresenius* to a traditionally public entity that Puerto Rico had allegedly privatized. There, the First Circuit asked the following: (1) whether the state clearly instructed the entity to share its sovereignty, and (2) whether the damages sought from the entity would be paid from the public treasury. As noted in Part II.C.5, structural indicators include the entity's enabling act, state statutory law, state court decisions, the entity's functions, and the amount of control the state exercises over the entity. After employing its version of the arm-of-the-state test, the court concluded that the entity in question was not an arm of the state. Based on the information it had gathered, it could have also determined whether the entity had been privatized.

## 2. Efficiency

Second, applying the arm-of-the-state test to determine if a traditionally public entity has been privatized would increase judicial efficiency. Because the arm-of-the-state test will be employed whenever a court finds that a traditionally public entity has been privatized, the immediate application of the arm-of-the-state test would simplify the process by allowing the court to simultaneously determine (1) whether the traditionally public entity has been privatized and (if not) (2) whether the entity is an arm-of-the-state. The benefits of this approach are apparent when one considers the consequences of adopting a different approach.

The alternative to applying arm-of-the-state analysis to determine whether a traditionally public entity has been privatized is to employ a different test. In effect, this would have the undesirable consequence of adding another layer onto the arm-of-the-state analysis in cases where the court finds that the entity in question has not been privatized. Indeed, in cases where the state has allegedly privatized an entity, a court would discern whether the entity in question has been privatized by the application of a fact-sensitive test that looks a lot like the arm-of-the-state test; it would then employ the arm-of-the-state test if it finds that the entity has not been privatized. This approach would be unnecessarily duplicative given the remarkably similar nature of the arm-of-the-state test and any other test designed to determine whether an entity has been privatized. As noted above, a court can apply the arm-of-the-state test to simultaneously determine both wheth-

er a traditionally public entity has been privatized and (if not) whether that entity is an arm-of-the-state.

D. State Legislatures Should Detail in an Entity's Organic Statute Whether an Entity Is an Arm of the State

Because an erroneous arm-of-the-state finding by a federal court can violate a state's sovereignty,<sup>206</sup> state legislatures should detail in an entity's organic statute whether the entity is an arm of the state for Eleventh Amendment purposes. Although federal courts have routinely referred to an entity's organic statute as an indication of the state's intent with respect to that entity's arm-of-the-state status, state legislatures have so far failed to make any kind of declaration in state-created entities' organic statutes concerning whether those entities are entitled to state sovereign immunity.<sup>207</sup> A short proviso at the end of the entity's organic statute would make clear to federal courts the state's intentions as to whether the entity is entitled to state sovereign immunity or is instead a product of privatization. A provision concerning an entity that the state wishes to privatize might read as follows: "Because the foregoing entity shall operate as a private entity in the private sector, it shall not be deemed an arm of the state for purposes of the Eleventh Amendment." On the other hand, a provision concerning an entity that the state wishes to remain public might read as follows: "Because the foregoing entity shall be subject to continuing state control, it shall be deemed an arm of the state for purposes of the Eleventh Amendment." Although these provisions would not be dispositive as to the public or private status of the entity,<sup>208</sup> they would at least make known the state's intentions concerning the entity, thereby reducing the likelihood of an erroneous arm-of-the-state finding by a federal court.

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<sup>206</sup> See *supra* Part III.C.

<sup>207</sup> See, e.g., *Fresenius Med. Care Cardiovascular Res., Inc. v. Puerto Rico*, 322 F.3d 56, 65 (1st Cir. 2003) ("The first step of the [arm-of-the-state] analysis concerns how the state has structured the entity . . . . After all, a state may easily make clear by statute its view that an entity is to share the state's immunity."); *Takle v. Univ. of Wisc. Hosp. & Clinics Auth.*, 402 F.3d 768, 770 (7th Cir. 2005) ("It would be nice if the hospital's organic statute stated outright that the hospital is a private entity rather than an arm of the state—that would resolve the issue—but it does not say that.").

<sup>208</sup> Of course, the question of whether an entity is entitled to state sovereign immunity is a question of federal law. See *Regents of the Univ. of Cal. v. Doe*, 519 U.S. 425, 429 n.5 (1997) ("Ultimately, of course, the question of whether a particular state agency is has the same kind of independent status as a county or is instead an arm of the state, and therefore "one of the United States" with the meaning of the Eleventh Amendment, is a question of federal law.").

## V. CONCLUSION

This Comment has highlighted an area of confusion in federal circuit courts that has received insufficient scholarly attention. Because privatization is a valuable tool of state government, the question of whether state sovereign immunity extends to private firms will continue to confront courts. This Comment has argued that courts should expressly acknowledge that state sovereign immunity does not extend to private entities. Such a declaration would foster clarity among the courts as to how to approach the arm-of-the-state inquiry and would promote principles of fairness by providing injured parties with an opportunity to have their cases heard on the merits in federal court. Moreover, courts should adopt a *per se* rule against extending state sovereign immunity to traditionally private entities while reserving the arm-of-the-state analysis for traditionally public entities that the court has allegedly privatized. This approach would not only be consistent with constitutional principles, but it would also promote accuracy and efficiency by reducing both the risk of judicial error and the number of occasions on which the court is required to employ the arm-of-the-state test. In addition, when a state creates an entity to perform a government function, it should detail in that entity's organic statute whether the entity is an arm of the state. A statute that accounts for the Eleventh Amendment would reduce the chances of a federal court erroneously finding (or not finding) that the entity is entitled to state sovereign immunity.