

1 introduced at this point.

2 Senator Moynihan. As I understand it, Mr. Chairman, our
3 purpose is to agree to principles here and what is agreed to
4 will be then drafted, but there are various documents.

5 Senator Curtis. Can staff tell us what the issue is?

6 Mr. Shapiro. In 1976, Congress dealt with the problems
7 of New York City and enacted two pieces of legislation which
8 were intended to assist New York with respect to their finan-
9 cial problems. One of the concerns that New York had was
10 that it was not able to sell any of its bonds. They were
11 not able to find purchasers of those bonds.

12 The laws that were passed, the first one, Public Law
13 94-236, permitted New York City and employee pension funds to
14 purchase up to \$2.5 billion of either New York City or MAC
15 bonds. MAC is the Municipal Acceptance Corporation, which is
16 a state agency which assisted New York in purchasing its
17 paper and routed the funds to New York City.

18 The concern at that time was that it allowed the New
19 York City pension plans to purchase these bonds. The Internal
20 Revenue contains certain provisions that provide for limita-
21 tions on pension funds, the city plans, which dealt with the
22 fact that the plans must be for the exclusive benefits of its
23 employees and the second provision provided that the pension
24 funds could not have self-dealing.

25 There was a concern that the fact that the pension plans



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1 would purchase New York City bonds, would be considered as
2 self-dealing, the pension fund, self-dealing with New York
3 City and violate the exclusive benefit rule, the rule that
4 said that the pension funds must exclusively benefit the
5 employees.

6 To the extent the pension funds purchased New York bonds
7 that it may have violated self-dealing and violated the use
8 of the pension funds for the employees. Congress passed a law
9 which allowed the pension funds to purchase these bonds without
10 violating either the self-dealing prohibitions or the exclu-
11 sive benefit rules. This meant that the pension funds could
12 purchase these bonds without losing their tax exemption.

13 The law that Congress passed was in accord with an
14 agreement that was worked out by New York City in November,
15 1975, along with the pension funds and 11 commercial banks
16 in New York. This agreement extended into 1978 and is
17 expiring and there has been discussion between New York City
18 and the Treasury Department and so representatives on the
19 House side, and the Banking Committee there, as well as the
20 Ways and Means Committee as well as the Banking Committee
21 on the Senate side and members of the Finance Committee.

22 Senator Moynihan has a series of proposals that would
23 provide that the pension funds could extend the authority
24 that they could hold the bonds up through 1982 without violating
25 the self-dealing prohibition or the exclusive benefit rules

1 but there is also a series of provisions that would require,
2 for fiscal stability in New York City, such as requiring a
3 limitation as to the amount of city bonds that the pension
4 funds could hold as far as its assets, limitations on state
5 funds, provisions looking towards New York City balancing
6 its budget or becoming fiscally solvent.

7 These are general guidelines which are trying to preserve
8 the fiscal situation in New York City while the pension funds
9 purchase the bonds to make sure that the employees are really
10 protected.

11 This is the general summary of the concepts that Senator
12 Moynihan has constructed.

13 Senator Curtis. It seems to me that this is an internal
14 problem for New York, and I have no objection. I just want to
15 ask one question.

16 Is what has been done in the past and what is proposed
17 today drawn narrowly enough so that it applies to the New York
18 City situation and nothing more?

19 Mr. Shapiro. That is correct, Senator Curtis. It is
20 drawn to apply only to New York City.

21 Senator Curtis. We could argue for a long time about the
22 desirability of certain things in reference to pensions. Since
23 it involves them only, I think it is an internal problem.

24 Senator Bentsen. Mr. Chairman, if I might comment on
25 this, I chaired the Subcommittee hearings on it. I feel very

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1 Senator Byrd. I might want to present amendments to the
2 amendments at the appropriate time. We do not have a bill
3 before us, as I understand it. The Committee does not have a
4 bill before it.

5 Senator Bentsen. Of course, it has been often done in
6 this Committee that we discuss the concepts and then let the
7 staff draft the final legislation that we are trying to
8 achieve the objective. I think we ought to hear what Senator
9 Byrd has in mind as a possible change in the amendment.

10 Senator Byrd. Of course, it is difficult to suggest an
11 amendment until we get the bill, but I would not be satisfied
12 with a balanced budget by 1982. New York City was given three
13 years to balance its budget in 1975. It has not balanced its
14 budget.

15 This would give New York City four more years in which to
16 balance its budget. I would like to have the opportunity to
17 consider that part of the bill, at least, prior to the time that
18 the Committee acts on it.

19 Senator Bentsen. The reason I chose 1982, as you know,
20 there was considerable controversy in the hearings in the
21 Senate Banking Committee, and they finally accepted 1982.
22 That was the figure in the House bill, which I recall, and it
23 was also the Administration's position.

24 In turn, we tightened up on the criterion for achieving
25 that balanced budget because, as I recall, they had a New

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1 York approach to what a balanced budget was and we did not
2 accept that, and we talked about generally accepted accounting
3 procedures being utilized in deciding whether or not a balanced
4 budget had been achieved.

5 Senator Moynihan. Perhaps I could speak, Mr. Chairman,
6 to this point?

7 I wonder if Senator Byrd's concern might more usefully
8 be directed to the legislation which has been adopted by the
9 Banking Committee at this point where -- that is where the
10 issue of the balanced budget resides. This is a mirror
11 image.

12 Senator Byrd. That is what I thought. That was the
13 assumption I was proceeding on. This sheet brings the balanced
14 budget into the proposed legislation before this Committee, as
15 I understand it.

16 Senaor Moynihan.. That is correct.

17 May I say that the City of New York's budget is always
18 balanced, because the city's charter requires it to be. The
19 behavior of the past has been to borrow large amounts of money
20 for capital projects and use them for current expenditure, and
21 the city's four-year plan will take you down to the point
22 where, by fiscal 1982, there will be none of that and,
23 according to generally-accepted accounting principals, it
24 will be a balanced budget.

25 I would have to say there is no prospect of anything

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1 sooner than that. And I would suggest that three years ago
2 the city had a deficit -- four years ago -- of \$5 billion.

3 Senator Bentsen. Let me add further that what we are
4 talking about essentially is the extension of P.L. 94-236
5 which he had here, plus the amendments that I referred to.
6 I think that one of the very key provisions in this, Senator
7 Byrd, is the fact that the Secretary must say that they are
8 making substantial progress each year towards that balanced
9 budget. That has to be achieved by 1982.

10 That is the wording of my amendment. Unless they are
11 making that substantial progress, they are not in compliance.

12 I would much rather have an earlier date, too.

13 Senator Byrd. Of course, when we speak about a balanced
14 budget, just as we did three years ago, we mean on a generally
15 acceptable accounting method, not on a fictitious method.

16 Senator Bentsen. I changed the wording to bring that
17 about. I did not accept the New York standard, whatever it
18 was. It was not generally accepted accounting procedures
19 for the balanced budget. I share the very concern that you
20 are talking about.

21 Senator Byrd. The general legislation that we are
22 speaking generally about, the legislation that we are discus-
23 sing today, the extension of -- what is it, P.L. 94-236 --
24 as I understand that proposal, assuming that Congress approves
25 the proposal as it is now, the bonds which were guaranteed by

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1 the Federal government could be sold only to pension funds.

2 Mr. Shapiro. Senator Byrd, that is a provision that the
3 Senate Banking Committee agreed to. The House-passed bill
4 allowed the bonds to be sold to anyone. To the extent that
5 they were guaranteed for that period, they would be taxable.
6 Once the guarantee period is over, then they would revert to
7 their tax-exempt status.

8 The Senate Banking Committee, when they reviewed the
9 House-passed bill, revised it to the extent to make it that
10 they may only be purchased by the pension funds and then they
11 would be tax-exempt, because the pension funds are automatically
12 tax-exempt.

13 Senator Byrd. I assume, then, that the Senate Banking
14 Committee proposal provides that the pension funds cannot
15 dispose of the bonds to private individuals, or banks, or what
16 have you.

17 Mr. Shapiro. Senator, if they do so, it loses the
18 guarantee. The guarantee is only available during the time
19 period to the pension funds.

20 Senator Bentsen. Again, Senator Byrd, if I may inter-
21 rupt, the Secretary is supposed to disprove the purchase of
22 any more of the city indebtedness by those funds unless he
23 makes a determination each year that substantial progress is
24 being made towards a balanced budget.

25 I must say, in all candor, I do not think the Secretary



1 particularly looks forward to that responsibility. I think
 2 he would rather see it go to someone else, but I think that
 3 is where it ought to be.

4 Senator Byrd. I think that is an excellent provision.
 5 My only hesitancy is in regard to the date involved.

6 Like Senator Curtis, I think the overall aspects of the
 7 bill, speaking of the bill broadly and leaving out the
 8 last part about a balanced budget, speaking broadly, it seems
 9 to me to be an internal problem with New York City, whether
 10 the pension fund should buy them or not buy them. I have no
 11 objection to that phase of it. As a matter of fact, if they
 12 are going to be guaranteed, I think it is better to have it
 13 the way the Senate Banking Committee has a proposal, to be
 14 guaranteed only if purchased by the pension funds.

15 Then the pension funds would be restricted in the funds
 16 that they could put into the bonds.

17 Senator Talmadge. Are you ready for the vote?

18 Senator Moynihan. Mr. Chairman, I have one matter. I
 19 would like to say that I believe that Senator Bentsen's
 20 amendments have strengthened this bill and made it a better
 21 one, and I want to express my appreciation to him.

22 At the same time, Secretary Carswell is here, Mr. Chair-
 23 man and we are just a little concerned to be quite clear that
 24 the Committee understands the provision with respect to the
 25 Treasury's certifying that progress has been made towards the

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1 1982 goal. The Secretary does not want to have to approve each
 2 sale as such in these terms, but rather make this determination
 3 at a periodic interval and let the Emergency Financial
 4 Control Board be the actual auditor, because these are compli-
 5 cated matters well beyond my comprehension, it is said to be
 6 beyond the comprehension of bond lawyers also. In any event,
 7 bond lawyers will have to speak.

8 I wonder if the Chair would ask Secretary Carswell to
 9 come to the witness table and to explain his understanding
 10 and make certain that it meets Senator Bentsen's understand-
 11 ing.

12 Senator Talmadge. Secretary Carswell, would you come
 13 up, please?

14 Senator Moynihan. Perhaps Senator Bentsen would say to
 15 the group what he just said to me, and Secretary Carswell can
 16 respond.

17 Senator Bentsen. In my personal viewpoint, I am not
 18 asking for the Secretary to make a determination on each
 19 security purchased throughout the year, but I think that he
 20 should arrive at an objective, independent decision and it
 21 should be his responsibility at least once a year that sub-
 22 stantial progress is being made.

23 I do not want that passed off to some board, with all
 24 due respect to the state of New York. I want to be sure that
 25 the Secretary has that responsibility at least once a year.

1 Senator Talmadge. Is that your understanding, Mr.
2 Secretary?

3 Mr. Carswell. Yes, sir. I understand what the Senator
4 said.

5 Senator Bentsen. I am sure that the Secretary would just
6 as soon not have that responsibility.

7 Mr. Carswell. I guess that is correct. What we would
8 like, however, is the understanding that, in interpreting
9 what substantial progress means, that we would have reference
10 to the four-year budget plan and the Emergency Financial
11 Control Board's conclusions as to whether that budget plan
12 was, in fact, being met. That is the statutory responsibility
13 that they have in New York.

14 Senator Bentsen. I think that that, by itself, does not
15 eliminate the responsibility of the Secretary in arriving at
16 that decision independently.

17 Mr. Carswell. I understand that, sir. It is just that
18 the words "substantial progress" can mean a lot of different
19 things to a lot of different people.

20 Senator Bentsen. That is why I want that hung on the
21 Secretary.

22 Mr. Carswell. Our problem is that we have to get people
23 to agree now to put up money four years in the future and
24 that includes not just the pension funds, but also the banks
25 and other financial institutions. And we are simply not going

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1 to have commitments that everybody can rely on if the
2 standards are so vague that they cannot reasonably anticipate
3 that the Secretary will be able to make the findings.

4 Senator Bentsen. Let's have the Secretary draw up stan-
5 dards. They are going to be audited by an independent outside
6 auditor, public accountant, as I understand it, and he will
7 have the benefit of that also. I would not have any objec-
8 tion to the Secretary -- what do you think, Harry? -- drawing
9 up the standards.

10 Senator Byrd. I normally would not be, but I am a little
11 concerned about the comments of the Under Secretary because
12 I am not sure where we would go.

13 Mr. Shapiro. As I understand it, the deficits are to
14 be determined by the generally accepted accounting principles.
15 They would be the --standards.

16 Secretary Bentsen. That is right, but the Secretary is
17 talking about what is substantial progress? I can understand
18 that there is a variable there.

19 Mr. Carswell. There is a four-year budget plan and that
20 would lay out, year by year, what the progress is supposed
21 to be.

22 Senator Bentsen. I do not want one of these budget
23 plans that says all the progress is accomplished in the fourth
24 year, either.

25 Mr. Carswell. No. The plan that has been presented by the

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1 city, and I assume they will adhere to, and will be adopted
2 by the Emergency Financial Control Board, is a plan that
3 will embody the 25 percent progress each year. That is the
4 basic standard in the plan, and if that is the reference that
5 we can make, then I do not think we will have a problem.

6 I think that is, in my view, substantial progress, if
7 you look at it today. And if that is not satisfactory, I do
8 not know what we should be looking out for guidance as to
9 what those words mean.

10 Senator Byrd. Would you refresh my memory on this?
11 Let us assume that New York City does achieve a balanced
12 budget. What about its outstanding obligations now? What
13 does it have? What longterm debt does it have?

14 Mr. Craswell. Now it has \$14.5 billion.

15 Senator Byrd. \$14 billion equal to a year's operating
16 cost?

17 Senator Moynihan. About, roughly.

18 Senator Byrd. No provision is being made to curtail
19 that indebtedness, I assume?

20 Senator Moynihan. A balanced budget means that you are
21 paying interest and principal on that debt.

22 Senator Byrd. It does not mean that the debt would be
23 retired.

24 Senator Moynihan. There is a payment of principal in the
25 balanced budget, yes.

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1 Senator Byrd. There is a payment of principal?

2 Senator Moynihan. Yes.

3 Senator Bentsen. One of the things that concerns me,
4 as I recall, on the New York City plan, do they not also
5 anticipate certain action being taken by the Federal govern-
6 ment to take over an additional amount of the welfare program
7 and that sort of thing?

8 Mr. Shapiro. As I understand it, that is a part of
9 the expectation. One of the points too, I think, when we
10 talk about a plan, you are talking about the city having a
11 four-year plan to have a balanced budget.

12 Some of the concerns the Senators are raising is a
13 realization that not that the plan -- you see, the budget is
14 just a plan that they intend to meet. One of your concerns
15 appears to be that they actually do meet it, that there is
16 a realization --

17 Senator Bentsen. Realistic, and without some new, you
18 know, charitable contribution on the part of the Federal
19 government.

20 Senator Moynihan. Senator, I think I can speak to that.

21 This is the reason, when Mr. Carswell speaks of having
22 reference to the Emergency Financial Control Board's Monitor-
23 ing, it is now the law of New York State that a balanced budget
24 will be achieved by fiscal '82. Is that not right, Mr.
25 Secretary?

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1 Mr. Carswell. That is correct.

2 Senator Moynihan. It is the law.

3 Senator Byrd. I thought that the law of New York State
4 was 1985 or '86.

5 Senator Moynihan. No, sir.

6 Mr. Carswell. They changed the law: In 1975, they were
7 permitted ten years to get back into balance and that has now
8 been reduced to 1982 and the standard has been changed to
9 generally accepted accounting principals.

10 Senator Byrd. When was that done by the New York State
11 legislature?

12 Mr. Carswell. Two or three weeks ago.

13 Senator Moynihan. To follow that point and to answer
14 Senator Bentsen's point, the city's financial plan anticipates
15 certain Federal revenues, as it must do, not any huge,
16 great change, but some things.

17 The Senator's plan also understands that if those revenues
18 are not forthcoming, then the city will, by that amount, have
19 to reduce its expenditure. That is explicitly understood.

20 The Mayor testified before Senator Proxmire's committee
21 that they have a list of what goes first and what goes next
22 and what goes after. There is as much realism in this as
23 you will get in the city's finances.

24 Senator Bentsen. Let me say, in trying to move this along,
25 Mr. Chairman, that I think that Mr. Shapiro understands what

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1 I am trying to achieve here and that I want those standards
2 as objective as they can be and the assistance of the outside
3 auditors and the Secretary to have that responsibility.

4 And I am willing to see if we cannot draft language to try
5 to accomplish that and tighten it up a little so that
6 Secretary Carswell knows, or has some definition, on which
7 the bonding houses will be able to operate.

8 Mr. Shapiro. I think we understand the concerns that
9 the Senators have, and I think that we can appreciate what
10 the Secretary has indicated. We will try to work those out
11 and work with the Treasury in providing objective standards
12 which carry out the Senators' concerns and the Secretary's
13 objectives.

14 Senator Talmadge. Let us see if we can move along.

15 Senator Byrd. Mr. Chairman, I do not want to delay this,
16 but I do want to try to understand it a little bit. I have
17 no objection to the two aspects of the proposed bill. It is
18 not yet a bill, so we do not have a text before us, is that
19 correct?

20 Senator Bentsen. It is pretty much so. You have P.L.
21 94-236.

22 Senator Byrd. I just asked counsel for a bill and he
23 said we do not have a bill. I have no objection to continuing
24 the existent law.

25 Senator Bentsen. It is that plus my two amendments to

1 toughen it up.

2 Senator Byrd. I favor toughening it up, as you expressed
3 it, Senator Bentsen. I favor that. I do not want to get
4 locked in, however, to supporting undefined standards which
5 have not yet been ascertained or written down and I do not
6 want to get locked into a 1982 date.

7 Senator Talmadge. Let us see if we can act.

8 Senator Moynihan, do you modify your proposal to include
9 the two Bentsen amendments?

10 Senator Moynihan. I do.

11 Senator Talmadge. The question arises on the Moynihan
12 proposal as modified by the Bentsen amendments. All in favor,
13 please say aye?

14 (A chorus of ayes.)

15 Senator Talmadge. Opposed, no?

16 (No response)

17 Senator Talmadge. The ayes have it.

18 Senator Byrd. Mr. Chairman, I withheld my vote. I want
19 to say that I desire the right to amend this proposal or try
20 to amend the proposal on the Floor if the standards are not
21 what Senator Bentsen believes them to be, or hopes them to
22 be, and what the Senator from Virginia hopes it will be.
23 I would like to reverse the right.

24 Senator Talmadge. The Senator, of course, has that
25 right.

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1 Senator Bentsen. That is fair.

2 One of the standards, and an easy one to define, is
3 certainly that the deficit ought to be reduced each year, as
4 you work towards it.

5 Mr. Shapiro. That is what the Secretary has indicated
6 too, that he would like to have that as an objective standard
7 without having to make that determination. We will work with
8 the Secretary in working that out.

9 Mr. Stern. Mr. Chairman, this is a revenue measure, and
10 therefore would not be a Senate bill. Would it be the
11 Committee's desire to offer this as an amendment to the
12 Banking Committee bill, or as an independent bill that you
13 would offer as an amendment to a House bill? We have the
14 House revenue bill, that is a shell where the substance has
15 already been enacted, H.R. 4007, which dealt with home
16 designation and travel expenses for state legislators. The
17 substance of that has been enacted on another bill, so if
18 you simply want to put it out as a separate bill on the
19 Senate calendar --

20 Senator Moynihan. I think the latter preserves the
21 distinction as a Finance Committee matter and I think that
22 might be in the general interest of the Committee.

23 Senator Talmadge. If there is no objection, that will
24 be done.

25 Do we not have a matter that is expired on fugitive

1 fathers, on October 1, that the Committee has acted on
2 favorably?

3 Mr. Galvin. Section 709 of H.R. 7200 provides for the
4 continuation on a permanent basis of Federal funding. It
5 expires October 1, 1978 under present law.

6 The problem arises in the states --

7 Senator Talmadge. We made that permanent in S. 7200?

8 Mr. Galvin. Yes.

9 Senator Talmadge. We recovered over \$800,000 last year
10 under that Act.

11 Mr. Galvin. That is right.

12 Senator Talmadge. Is there any objection to also adding
13 that amendment to the one that Mr. Stern suggested?

14 Without objection, so ordered.

15 Senator Ribicoff has a request to call up a matter
16 requesting additional funding to study the potential benefits
17 and costs of the multi-lateral trade negotiations. That is
18 before you as staff document H.

19 Senator Ribicoff. Mr. Chairman, as all of us know, by
20 July 15th we anticipate that there will be presented to this
21 Committee a statement of general principles on multi-lateral
22 trade negotiations, probably one of the most important pieces
23 of legislation affecting our economy for the next ten years.

24 A group of members of the Finance Committee went to
25 Geneva and, to our chagrin, we found that there were no figures,

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1 no statistics, no information, as to what was involved in
2 the multi-lateral trade negotiations.

3 We have checked since and we find that neither the
4 Special Trade Representative, Commerce, Agriculture, State
5 or Treasury has undertaken an assessment of potential costs
6 and benefits which would accrue to the United States through
7 the trade agreement.

8 We are going to have to act on a measure that will affect
9 all agriculture, all labor, all industry and the consumers
10 of this country.

11 Last year our general trade was in the nature of \$280
12 billion.

13 Senator Talmadge. Mr. Ribicoff, would you suspend
14 momentarily?

15 I would remind our visitors that you are here as guests
16 of the Committee. Please refrain from conversation in order
17 that the Senator may be heard.

18 Senator Ribicoff. Consequently, the main obligation is
19 going to have to be on this body to make the determination,
20 is this a good agreement for the United States. I am rather
21 shocked that the Executive Branch -- no place in the Executive
22 Branch will these very important negotiations have anything
23 to show us.

24 We have an obligation under the Constitution in trade
25 matters and we should make sure that we should inform our

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1 colleagues in the Congress and the people in this country
2 what the impact of that trade agreement will be. I have
3 asked Mr. Cassidy and the Majority and Minority staff to make
4 an appraisal of what will have to be done to get this infor-
5 mation. They have made a survey and they indicate that by
6 getting independent experts to bring this information to us
7 would be in the nature of about \$200,000. This Committee
8 has \$40,000 for experts, but it has been committed in studies
9 on Social Security, health insurance and welfare and it has
10 been all committed.

11 I would assume that if we saw fit to vote these funds,
12 I would suggest that there be consultation with the House Ways
13 and Means Committee who will share this responsibility, to see
14 if they might not share the general costs. But even if they
15 do not, I think that this Committee does have an obligation to
16 have the facts to present to the Senate, to the Committee, and
17 to the people of this country.

18 Senator Curtis. Will the distinguished Senator yield?

19 Senator Ribicoff. I am pleased to yield.

20 Senator Curtis. I support Senator Ribicoff's proposal.

21 I think this is a very important matter. In the overall expen-
22 diture of the government, this is tiny. This should enable
23 us to act more wisely on these multimillion dollar involvements.

24 While I have the floor, I want to say that this help is
25 needed. I have been impressed by the great amount of time and

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1 the devotion to detail, the dedicated work of the distinguished
2 Chairman of the Trade Subcommittee, Senator Ribicoff, and I
3 think that he should be supported in this matter.

4 Senator Talmadge. Any objection to the resolution?

5 Without objection, the resolution will be reported.

6 Now we will get back to Medicare and Medicaid.

7 Senator Roth. Mr. Chairman?

8 Senator Talmadge. Senator Roth?

9 Senator Roth. We do have at least one matter I would
10 like to raise today, Senate Resolution 475 which expresses the
11 sense of the Senate that the IRS reorganization plan to stream-
12 line the District Offices in 12 states should not be implemen-
13 ted.

14 Senator Talmadge. That is Item G of the staff document.

15 Senator Roth. Mr. Chairman, this resolution has been
16 co-sponsored by Mr. Chaffee, Mr. Dimineci, Mr. Garns, Hansen
17 of this Committee, McGovern, MacIntyre, Melcher, Pell, Smith,
18 Stafford, Wallop and Young.

19 Very frankly, what we are trying to do is prevent from
20 happening what was essentially proposed back in 1970 as well
21 as 1963. My predecessor, Senator John Williams, was success-
22 ful in blocking it in these earlier cases.

23 Under the proposal, several taxpayer service functions
24 would be eliminated in the twelve offices of these smaller
25 states and transferred to IRS offices in other states. Very

1 candidly, we are concerned that this reorganization will
2 result in reduced services for the taxpayers of our affected
3 states,

4 I have had a number of meetings with Commissioner
5 Kurtz and others. Hearings were held. And I think it is
6 significant that there is opposition to this reorganization
7 from all of the states affected.

8 What they are going to do is eliminate a number of func-
9 tions and, as one witness from Rhode Island who is a practi-
10 tioner, a former Democratic State Senator and also serves as
11 the Rhode Island representative on the Internal Revenue
12 Service, he said that he endorses it.

13 This demonstrated quite clearly that the citizens feel
14 alienated, distant from their governments, and are insistent
15 upon a more personal and direct connection with it. It is
16 particularly important that this reality be addressed by the
17 Internal Revenue Service, for under our self-assessment
18 system of taxation, any alienation of taxpayers can be
19 expected to have an adverse impact upon the effective determina-
20 tion and collection of the revenue.

21 They are going to eliminate such positions as four
22 division chiefs -- that includes the administrative division,
23 collection and taxpayers service division, audit division
24 and intelligence division.

25 Very frankly, what it means, for example, in the case of

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1 Ms. Halperin. Senator, I am Anita Halperin, Assistant
2 Commissioner for Planning and Research of the Internal
3 Revenue Service and I am prepared to answer any questions
4 that might be helpful to the Committee.

5 Senator Talmadge. Are there any questions?

6 Senator Nelson. What services would be reduced? What
7 is the objective of the reorganization and what are the
8 economies, and so forth?

9 Ms. Halperin. Senator Nelson, we believe that the
10 proposals we have set forth will not reduce any essential
11 services to the taxpayers in any state of this nation. That
12 includes the 12 states that have been known as the stream-
13 lined states.

14 We will, we hope, we do believe that the reorganization
15 will result in a more efficient, effective operation for the
16 Internal Revenue Service. There are annual savings of some
17 \$4 million a year that will accrue in this streamlining
18 effort.

19 In reply to some of the criticisms that have been, and
20 observations that have been lodged in terms of the reorganiza-
21 tion, what we are doing in the streamlined districts is to
22 renew middle-management positions. We are not removing the
23 services that come under those middle-management positions.

24 In effect, the district directors remain, The district
25 directors of those twelve states will make all of the

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1 decisions, are fully in control of the operations.

2 The audit function, the taxpayer service function, the
3 collection function, the intelligence function goes on as it
4 is going on today. No first-line operational people who are
5 interacting with taxpayers in any of these states will be
6 removed. It is merely middle management positions that we
7 find are just overhead and not justified in these particular
8 states because of their size.

9 The only two operations that will be moved to what we
10 call prime districts is an internal operation of the review
11 function and that is for quality review of our audit cases.
12 There is no interaction with taxpayers there, or there should
13 not be.

14 The other function is administrative services, the kinds
15 of services that are involved in personnel, training, supply
16 services, space, that sort of function.

17 Senator Roth. Mr. Chairman, I have to respectfully
18 disagree with the witness. I do not think that you can say
19 these are middle management positions.

20 You have, of course, the Director and four of the
21 positions immediately below him that are going to be removed,
22 the four division chiefs in charge of the Administrative
23 Division, Collection and Taxpayers' Service Division, Audit
24 Division and Intelligence Division.

25 What it means, while technically the Director will remain

1 in control, that he will have to refer these problems to
2 another office.

3 In the case of Delaware, it would be Philadelphia; in
4 the case of Rhode Island, it would be Hartford. It is going
5 to unnecessarily delay, create problems.

6 We, in Delaware, as one of the fifty states, feel that
7 we are entitled to have full service and, while we applaud
8 efforts to try to become more efficient, very candidly I
9 think the kind of service we are giving to taxpayers is
10 inadequate and we are moving in the wrong direction.

11 I would like to quote again the Senator from Rhode
12 Island, Mr. Arcaro, who pointed out, and I think very right-
13 fully: "In my judgment, no statistics, rhetoric or repre-
14 sentations can hide the reality that those who are close to
15 the situation that this reorganization is a first step towards
16 total elimination of smaller districts and indeed, implementa-
17 tion of that initial step will serve to further justify and
18 support the ultimate elimination of Providence as a District."

19 They tried to do that back in 1963. The man who made
20 the study this year was also very active in the recommenda-
21 tions of 1971 which is very close to what they are proposing
22 this time.

23 I think that it is about time that the people in the
24 Washington Bureaucracy recognized that the service should
25 be close to the people, that the people of Delaware pay a very

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1 high percentage of taxes for the number of people and are
2 entitled to have full service there, and not to be dependent
3 on individuals who are transferred up to Philadelphia.

4 There is no question that you transfer much of this
5 internal work to Philadelphia, that we are going to be second-
6 rate citizens. They are going to take care of those in
7 Philadelphia first. We have had this happen time and again in
8 different areas.

9 I strongly oppose any effort to downgrade our service.

10 Senator Talmadge. If the Senator would yield, this is a
11 Senate Resolution and not binding by law?

12 Senator Roth. Yes.

13 Senator Talmadge. Any further discussion?

14 Senator Curtis. If the Senator would yield, I do not
15 represent a state that is small geographically, but our popula-
16 tion is small and we, through various organizations in the past
17 years, have had activities taken away from us.

18 I think that there is something worth preserving within
19 our state lines. I think that, as heavy taxes as our citizens
20 bear, to go out of the state for any part of their transac-
21 tion, unless it is an appellant thing, creates an undesirable
22 situation.

23 It is easy -- and I do not question their hopes -- to put
24 an estimate of how much such a proposal will save, but I do
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1 not think that there is very much hope that the cost of
2 operating the Internal Revenue Service is going to go down.

3 There are other factors that come into it.

4 Somewhere, we have to make a stand for the right of
5 people to have complete service within their state.

6 I would support the resolution.

7 Senator Talmadge. Are you ready for the vote, gentlemen?

8 Senator Nelson. Are there, in terms of processing, any
9 problem that a taxpayer may have resolving any differences
10 or disputes, personal services, directly for the taxpayer?
11 Do you foresee any delay in that over what would occur in any
12 other state?

13 Ms. Halperin. No, sir, none whatsoever.

14 Senator Roth. That is the position of the Internal
15 Revenue Service, but the fact is that the decision-makers
16 are going to be in another state and another area. They are
17 not going to develop the expertise of the state in which I
18 reside, or the other eleven states.

19 There is no question that it is going to delay decision-
20 making. Every witness that appeared before us, including
21 Democratic Senators, including practitioners, testified that
22 it was necessarily going to end up in delay and that it would
23 mean, as far as savings are concerned, additional expenses,
24 both from the standpoint of the government in transportation
25 between the two different points and, particularly for the

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1 taxpayer.

2 But again, I think it is about time that we recognize
3 that we ought to be giving better service to the taxpayer
4 rather than less.

5 Senator Nelson. May I ask a further question? It was
6 my understanding from your statement that none of the decision-
7 making functions in terms of dealing with an individual tax-
8 payer would be delayed, is that correct?

9 Ms. Halperin. That is correct, Senator Nelson. Moreover,
10 the District Director remains in those twelve states. That
11 District Director is still responsible for all decisions
12 regarding all taxpayers in that state and no taxpayer will
13 have to travel to any other state for any kind of a decision
14 or for any tax matter.

15 Senator Nelson. Are any of those functions that those
16 personnel who have some responsibility who are transferred,
17 would they be involved in direct decision-making respecting
18 individual taxpayers?

19 Ms. Halperin. No, sir. It is strictly internally serving
20 the needs of Internal Revenue Service employees. They have
21 no responsibility to the taxpayers.

22 Senator Roth. Well, that is a difference. It is true
23 that they have no direct contact with the taxpayers, but in
24 the decision-making, the very critical decisions are within
25 the Agency itself. So the people in the Wilmington Office,

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1 whether it is the Director, instead of turning to his Chief
2 there who has some expertise in what is going on in Delaware
3 will have to refer the matter up to Philadelphia.

4 There is no question that, many times, this is going to
5 cause delay and that to say so is just contrary to fact.

6 Senator Nelson. Are any of those people being transferred
7 who have that kind of decision-making function now?

8 Ms. Halperin. Any questions that require decisions will
9 be deferred to the District Director of the District, not
10 to anyone in Philadelphia.

11 Senator Roth. That is not the point. The final decision
12 may be his responsibility, but the advisors on whom he is
13 relying -- it is all very easy to say that this is all going
14 to be turned over to the Director and he has ultimate respon-
15 sibility. The President of the United States has ultimate
16 responsibility for the Executive Branch, but that does not
17 mean that there are not key steps in making that decision-
18 making.

19 We are taking one of these steps in this decision-making
20 from the state and it will mean that there is less specializa-
21 tion. There is bound to be delay because, as a practical
22 matter, there is no way you can avoid it. They are going to
23 give top priority to the other states.

24 Let me quote what Senator Pell says on this. "In fact,
25 I think there is a high probability that services in Rhode

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1 Island will, in fact, be less satisfactory in the reorganiza-
2 tion. For example, the return review process for Rhode
3 Islanders will be conducted outside of Rhode Island in Hart-
4 ford, where IRS has greater specialization is possible.
5 I doubt that IRS will find, in the Hartford Office, reviewers
6 with familiarity or specialized knowledge of the jewelry
7 industry or fishing industry, both of which are very important
8 in Rhode Island, but minimal in Connecticut."

9 Senator Nelson. Are the personnel being transferred
10 those that make that kind of decision?

11 Ms. Halperin. Well, the Division Chiefs of the various
12 divisions certainly do make decisions, yes, but there are --
13 we are looking to the District Director in the District, just
14 as we look to the District Director in all Districts, those
15 that are being streamlined and those that are not, to make
16 the ultimate and final decisions for all matters falling
17 within the jurisdiction of that district. And this is not
18 being changed.

19 A District Director can seek the advice and assistance
20 of anyone. They do today, not only in these districts as they
21 are currently comprised, but also in other districts that
22 are not being streamlined. They go to the Regional Office for
23 advice and assistance. They will come to Washington for
24 advice and assistance and, in fact, in so far as certain
25 industries are concerned, like oil or insurance, they will go

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1 to other districts where such specialization exists.

2 This is not unusual. This is being done today, with
3 absolutely no delays and no sacrifice to the taxpayer. The
4 District Director, in all instances, is the point of final
5 decision.

6 Senator Talmadge. Are you ready for the vote?

7 All in favor, say aye.

8 Senator Nelson. Mr. Chairman, I know this is not a
9 large matter, but we all keep talking about economies. I
10 think that the case by IRS is very specific. I would like
11 to have a roll call. I want to be recorded against it. We
12 are all giving speeches on the Floor -- I have not yet -- on
13 the Floor of the Senate about how you have to cut back in the
14 budget. Everytime a proposed efficiency comes along, the
15 same people who are arguing for the cuts in the budget are
16 the same people saying, but do not cut it here.

17 I would like a roll call.

18 Senator Dole. How do we know it is efficiency?

19 Senator Nelson. I guess you could raise that question
20 about anything.

21 Senator Talmadge. The Clerk will call the roll.

22 Mr. Stern. The question is on Senate Resolution 475.

23 Mr. Talmadge?

24 Senator Talmadge. Aye.

25 Mr. Stern. Senator Ribicoff?

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1 Senator Ribicoff. No.
2 Mr. Stern. Mr. Byrd?
3 (No response)
4 Mr. Stern. Mr. Nelson?
5 Senator Nelson. No.
6 Mr. Stern. Mr. Gravel?
7 (No response)
8 Mr. Stern. Mr. Bentsen?
9 (No response)
10 Mr. Stern. Mr. Hathaway?
11 (No response)
12 Mr. Stern. Mr. Haskell?
13 (No response)
14 Mr. Stern. Mr. Matsunaga?
15 (No response)
16 Mr. Stern. Mr. Moynihan?
17 Senator Moynihan. No.
18 Mr. Stern. Mr. Curtis?
19 Senator Curtis. Aye.
20 Mr. Stern. Mr. Hansaen?
21 Senator Curtis. Aye.
22 Mr. Stern. Mr. Dole?
23 Senator Dole. Aye.
24 Mr. Stern. Mr. Packwood?
25 (No response)

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1 Mr. Stern. Mr. Laxalt?

2 Senator Laxalt. Aye.

3 Mr. Stern. Mr. Danforth?

4 Senator Danforth. Aye.

5 Mr. Stern. Mr. Chairman?

6 (No response)

7 Senator Talmadge. Seven ayes and three nays. The
8 absentees can make a difference. I suggest we poll the
9 absentees.

10 Now, let us get down to Medicaid and Medicare.

11 Senator Dole. What about the fringe benefit resolution?
12 I do not think there is any controversy over that.

13 Senator Talmadge. Do you want to take that up now?

14 Senator Dole. There are three different proposals. I
15 think perhaps Senator Moynihan's is the best.

16 Senator Moynihan. I believe, Mr. Chairman, that mine is
17 closest to the House measure that is in Committee. Senator
18 Ribicoff has an amendment he would like to make to our
19 proposal.

20 Senator Ribicoff. I have a minor amendment. It just
21 so happens that Connecticut State Police on instructions
22 from the IRS paid their taxes taking into account what they
23 paid out for meals.

24 Senator Talmadge. Mr. Shapiro, would you like to explain
25 the bill?

1 Mr. Shapiro. Yes.

2 The House Ways and Means Committee has reported a bill
3 which has not been taken to the House Floor yet that does
4 suspend the authority of the Internal Revenue Service to
5 issue regulations on fringe benefits to the end of next year
6 through December of 1979, in order to give Congress an oppor-
7 tunity to have legislative guidelines for any fringe benefits
8 that they believe that the IRS should deal with.

9 In addition to that, the House added two other amendments
10 to that bill which relate to extending the prohibition on
11 expenses, a regulation that continues a provision passed by
12 the House and the Senate, H.R. 9251, which is pending before
13 the Conference which suspends that through April 30 of this
14 year.

15 That suspends it, also, to the end of next year.

16 An additional matter that was added to it deals with the
17 state troopers which Senator Ribicoff had reference to. That
18 is that the Supreme Court case settled that issue from the
19 standpoint of whether or not the meals allowances would be
20 treated as income. The Ways and Means Committee put that on
21 a prospective basis which, in effect, said on the retroactive
22 period back to when the Internal Revenue Service dealt with
23 that issue with regard to state troopers they would not provide
24 for collections and, therefore, it would apply, in effect,
25 the Supreme Court decision on a prospective basis.

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Senator Talmage. The Committee has approved it. It is up to the Chairman.
Senator Ribicoff. Which is the more effective way?
Mr. Stern. It would be the faster way of doing it.
Senator Curtis. Let's instruct the Chairman to proceed as he sees fit.

Senator Talmadge. That is a fine suggestion. Let's tell the Chairman that we have ordered the bill reported, and he can proceed as he sees fit.

Now, let's get back to Medicaid and Medicare.

Mr. Constantine, I believe we acted on Section 10.

Mr. Constantine. Yes, sir.

Mr. Chairman, on Tuesday we started with Section 10 and the Committee approved Section 10. There were discussions of Section 11 and Section 12, with no decisions made on those provisions.

Then there was an additional staff briefing Tuesday afternoon. Yesterday morning, at your suggestion, there was an additional briefing for those Senators who could attend yesterday morning. Most of the discussion yesterday morning was with respect to the hospital section.

The briefing was not concluded at that time. It was agreed to by the Senators present that today that the Committee would probably do best to proceed with the Sections from 11 forward rather than working on the hospital provisions.

1 Is that your understanding, Senator Curtis?

2 Senator Curtis. All right.

3 Senator Nelson. I did not follow that. What document
4 are we dealing with?

5 Mr. Constantine. This is the summary, Senator, which
6 suggested changes, and the bill itself. E.

7 Senator Nelson. Let me ask a question here. There is
8 the Administration bill which was jointly referred to the
9 Human Resources Committee and the Finance Committee. Then
10 there is, when the Human Resources Committee marks up the
11 bill, it has to be a joint -- that bill has to be reported
12 jointly, as I understand it.

13 In looking at the bills before us, this one, the Rogers
14 bill in the House and the Administration bill, and having
15 sat through the hearings and the mark-up, it is clear to me
16 that the one which does something significant about saving
17 money is the Administration bill, and I think that we ought
18 to have that before us.

19 The Administration bill makes an economy of \$22 billion
20 in the year 1983 and an accumulated savings of almost \$60
21 billion from '79 to 1983 and I think that the cap is too high,
22 I think we were too liberal, but that was the best that we
23 could do.

24 We were allowing an increase of one and one-half times
25 the cost of living for hospitals and all of their ancillary

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1 services.

2 This is the third biggest industry in America. The
3 inflation rate is going up the fastest. There are no cost
4 controls; there is no competition. It is a disaster area.

5 In looking at the Administration bill, it saves \$2.205
6 billion in the year '79. The pending bill saves zero; the
7 Rogers bill \$750 million.

8 Then you go to 1980. The Administration bill, which was
9 carefully considered and acted upon by the Human Resources
10 Committee saves \$5.2 billion in 1980. The Talmadge bill,
11 \$14 million, Rogers \$3 million.

12 By the year 1983, you are saving \$22.635 billion under
13 the Administration bill, \$303 million total under the Talmadge
14 bill, \$9.9 million under Rogers.

15 I think we ought to be looking at the Administration bill.
16 I would like it if we could put the cap on a little tighter.
17 There is no way in the world that we really can justify the
18 liberal limitations that the Administration bill has got, let
19 alone going the route of the pending bill here or the Rogers
20 bill.

21 It seems to me we ought to be dealing with the Administra-
22 tion bill.

23 Mr. Constantine. As a technical matter, CBO disagrees
24 with the estimates of the Administration on the savings on the
25 Talmadge proposal. The Administration -- these estimates here,

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1 of course, relate -- one of those two bills, the Kennedy bill
2 and the Rogers bill cover all hospitals and all payers. The
3 Talmadge bill deals with only Medicare and Medicaid. The
4 estimated savings on routine costs which the Administration
5 shows are the subject of disagreement with the Congressional
6 Budget Office. The CBO says, at a minimum, the Talmadge bill
7 on routine costs in fiscal 1980 would save \$200 million.
8 That is just the hospital provision.

9 The suggestion has been made to authorize extension of
10 the Talmadge bill to cover ancillary services and that was
11 intended under the original proposal as well. If ancillary
12 services are brought in, obviously the savings would be substan-
13 tially more, assuming the voluntary effort.

14 Under the Talmadge approach in fiscal 1980, what is
15 suggested; if the voluntary effort, the joint effort of the
16 American Hospital Association, the AMA succeeds, that there
17 would be no limit on Medicare and Medicaid. If the voluntary
18 effort does succeed, there would be substantial savings.

19 In part, you are comparing a bill which deals with a
20 much more limited area and where there is disagreement on
21 estimates. CBO is working on a different one.

22 Senator Nelson. A limited area?

23 Mr. Constantine. Medicare and Medicaid.

24 Senator Nelson. You know the problem with that, of course,
25 New York just did a study. You limit Medicare and Medicaid

1 and put a cap on that, it does not reduce the hospital's
2 income at all. They raise the price on the other third-party
3 payers.

4 The New York study showed that where they controlled Blue
5 Cross, the Knox Hill in Manhattan, the daily rate under Blue
6 Cross-controlled, \$240. The daily charge where it is not
7 controlled, same hospital, \$442.

8 All they do when you controll Medicare and Medicaid, then
9 the other people get the price boosted up.

10 Huntington, Long Island: \$150 under the control price;
11 same hospital, \$227 if an individual goes in. So you are not
12 controlling the hospital's income by controlling part of the
13 payers.

14 I think it is a very dangerous concept. What I am basic-
15 ally saying is that I think that the Administration bill is
16 too liberal, too liberal. We are allowing those costs to go
17 up too fast. But that was the best we can do in the Human
18 Resources Committee, but it certainly is much more dramatic
19 control and it is a place where we can cut costs to the
20 individual taxpayer, to the Federal government and to the
21 state governments more dramatically than anyplace else. If
22 we cannot bite this bullet, we can bite nothing.

23 Mr. Constantine. In the bill, Senator, you are right.
24 The problem of shifting costs is always present. That is the
25 problem today. When Blue Cross reimburses hospitals on a cost

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1 basis, Medicare reimburses on a cost basis, and Medicaid on
 2 a cost basis. That potential is there, and obviously the
 3 potential is aggravated when you increase the amount of cost
 4 not subject to reimbursement. That is, as the allowances
 5 increase, that is the shift to other payers, if you could.

6 There is a specific provision in the bill and the state
 7 insurance departments that presumably have the capacity to
 8 review that and assure that there is not any payment. The
 9 present provision makes the requirement on hospitals in 1470
 10 not to increase the amounts due from any individual or agency
 11 in order to offset reductions made in the section moderating
 12 the costs, and so on.

13 And the same provision applies to Medicaid.

14 Obviously, to some extent, that is hortatory language.
 15 It is kind of hard to enforce. However, as a part of another
 16 bill you enacted, the anti-fraud and anti-abuse bill, you
 17 now require that they be uniform accounts, uniform allocations
 18 of cost, uniform reporting and an audit trail to facilitate
 19 the tracing of any unlawful or inappropriate cost shifting.

20 Finally, Senator, if you desire -- and it is a potential
 21 problem and it is real, and to nail it down, you could say,
 22 to avoid that, that you simply say that you require the Chief
 23 Administrative Officer of the hospital plus the person
 24 responsible for the bookkeeping practices and accounting
 25 practices to certify under criminal penalty that, to their

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1 knowledge, no cost-shifting occurred other than that which
2 was otherwise authorized.

3 Senator Curtis. Yesterday we had some conversation
4 about CBO's estimate and the Administration's estimate of the
5 bill we are talking about. It was suggested to see if they
6 can be reconciled.

7 Has anything happened on that?

8 Mr. Constantine. Well, the Administration, you know,
9 they went to work and doubled the cost savings under the Tal-
10 madge bill from \$5 million in 1979 in S. 1470, under the
11 hospital thing as introduced, not as with suggested modifica-
12 tions, from \$5 million to \$10 million the first year.

13 Senator Curtis. When did they do that?

14 Mr. Constantine. Yesterday.

15 Senator Curtis. If we wait three or four days --

16 Mr. Constantine. Yes, sire, they are moving. The CBO
17 however, we talked to them last evening. They are working
18 away and they say, at a minimum, fiscal '79, \$200 million.
19 They think the savings will be substantially more.

20 Senator, we believe there is a key difference between the
21 two approaches that the Committee should be aware of. The
22 Talmadge bill, 1470, was not designed to suddenly bring down
23 hospitals. It was designed to moderate the rate of increase.
24 In the drafting process, and in accordance with Senator
25 Talmadge's instructions, it was sought to balance the penalties

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initially and the incentives so you came out very close to a zero thing initially. The point is that the operation of the system itself would lead to moderation over time. There is a racheting effect.

As the people whose costs are disallowed moderate their operations, as they have to because they are not getting reimbursed for their excess costs, that brings the average down, and so on. And the rate of increase, it was not only a cost-cutting approach, it was a cost-moderating approach, and obviously the hospitals felt a lot more uncomfortable, and it sought to differentiate between hospitals.

It is a different approach but, in answer to Senator Nelson, it does not cover all hospitals. It is limited to reimbursement under Medicare and Medicaid.

Senator Nelson. I think that the provision that is in Senator Talmadge's bill which makes a differentiation is a sound approach, that is classifying hospitals, because it is true that there is a cost differential between teaching hospitals and various kinds of hospitals. I certainly think that is a good provision.

The problem, as I understand it from HEW, is that they will not have the adequate data base to make that differentiation for another three or four years.

Nonetheless, the legitimate criticism you could make of the Administration bill is that it applies a limitation on

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all hospitals, and the limitation is the same, whether it is an efficiently run hospital that has done a good job in holding down costs or whether it is an inefficient one that has not. And you have to get at that down the road a little ways.

But the fact of the matter is that it is the run-off, so that the efficient hospitals can live with it and the inefficient hospitals who are too high already are getting more benefit than they should get.

So we should aim it down the road, taking care of that differentiation, but not saying that we are not going to have really effective controls on all of them because it is too hard to do, or something like that. We went through it in great detail over in the Human Resources Committee. I do not think there is any hospital in the country worth a damn that cannot meet this cost increase that is in the Administration bill.

Mr. Constantine. Senator, when Secretary Califano testified last year on the bill, he claimed that 20 percent of hospitals had lived within the Administration's 9 percent, which was then worked out to 9 percent or less -- Johns Hopkins, and others, as examples of frugal facilities.

And therefore, other hospitals could live with it. Obviously, there is variation from year to year. You cannot say one year, you can have a wage increase one year

1 which distorts your experience.

2 Senator Nelson. There is a pass-through.

3 Mr. Constantine. Yes, sir.

4 When the Committee asks for the pattern of hospitals
5 that had 9 percent or less, the ceiling for two years, so
6 you eliminate some of the distortions. After a lot of work,
7 it turned out it was something like 3 percent of the hospi-
8 tals or 2 percent of the beds, were able to maintain that
9 performance over a period of time.

10 On the complexity of S. 1470, it just depends on who
11 you talk to. We have been assured that it could be on line
12 by -- the basic classification and so forth -- could be on
13 line by July of next year when, at Senator Talmadge's direc-
14 tion, we would explore with the Administration whether it
15 would be feasible to use this for Medicare and Medicaid and
16 ultimately expand it to all payers in the event that there
17 is an overall revenue limitation applied.

18 We were told, yes, it was feasible in a joint memorandum
19 which was given to the Administration a year ago.

20 What we did want to say, you may want to offer an amend-
21 ment. Two things that the Committee should understand.

22 Number one, as we pointed out yesterday, the staff is
23 unanimous. All of us, plus the CRS. If you adopt something
24 like S. 1470, the hospital reimbursement approach, there would
25 be no need for Congress to make a decision on a mandatory

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program affecting all payers this year. You could make that decision next year.

The reason for that is the CBO expectation of the voluntary effort will meet its target from virtually all the bills other than the bill as originally introduced by the Administration. It recognizes the voluntary effort and its objectives, Mr. Roskenkowski's proposal, the Rogers proposal, and so on.

The assumption is that the voluntary effort will make it in 1978. The earliest that the voluntary effort can fail will be in 1979 which means that any kind of overall mandatory limitation would not become operative until 1980.

If the S. 1470 approach for Medicare and Medicaid, the methodology were in place in July '79, the bulk of it in place, you could then make the decision, because it is relatively easy to expand that methodology to an overall limitation on all hospitals and all payers, if Congress decided to do that next year.

What we are saying is that the decision can be made next year rather than this year in terms of a mandatory approach.

The other thing that we believe the Committee ought to understand is that, under present law, it is our opinion that under Section 223 of Public Law 92-603, which allows the Secretary to establish reasonable limits, that HEW, by regulation, could order the implementation of everything in



1 Section 2 of the Talmadge bill, with the exception of the
2 incentive payments.

3 It is also our understanding that there has been some
4 exploratory discussion within the Department. If they do
5 it by regulation, you do not have the ability to modify it,
6 moderate it, put in softening, and whatever Congress wants
7 to do.

8 They do have our authority, in our opinion, under Section
9 223, to put everything in except the incentive payments.

10 Anyway, that is just by way of background.

11 Senator Nelson. And we pass a resolution telling them
12 not not do it. I think that there are some very good provi-
13 sions in Senator Talmadge's bill but I think that they can
14 be melded together. It seems to me that we have to cover
15 all hospitals, all payers.

16 It seems to me that the Administration bill ought to be
17 before us. It is the most comprehensive one. I think it has
18 been the most carefully thought out. I think that the Human
19 Resources Committee went through it very carefully.

20 I think, to repeat myself, that it is a very good bill
21 that does something significant about controlling costs,
22 really significant, and that we ought to be dealing with it.

23 Senator Talmadge. If you want to, at an appropriate
24 time, you can offer that as a substitute, Senator Nelson.

25 Senator Nelson. On the cost question, I would like to

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1 have that clarified, if CBO has differences, but it does
2 seem to me that, as a matter of such tremendous consequence
3 which, if the Administration's figures are within the ball-
4 park that there is an opportunity there to make dramatic,
5 very dramatic, savings. It would be the biggest budget cuts
6 for state governments, Federal governments, and cost cuts
7 for individual taxpayers of any proposal that will be before
8 this Congress anytime that I can think of.

9 We should not lose the opportunity.

10 Senator Curtis. Has this Committee held any hearings
11 on the Administration plan? I know you are familiar by reason
12 of the other Committee.

13 Senator Nelson. I do not know.

14 Mr. Constantine. Yes, sir. We held a day and a half.
15 Secretary Califano -- I believe it was the beginning of
16 October.

17 Senator Curtis. In connection with the Talmadge hear-
18 ings?

19 Mr. Constantine. Hospital cost containment in the bill
20 before us.

21 Senator Curtis. A day and a half total?

22 Mr. Constantine. Total. Not on the Talmadge bill. The
23 Talmadge bill had had four days in June and the predecessor
24 five days in 1976. A day and a half on, essentially, the
25 Administration bill in October, with Secretary Califano

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testifying.

Senator Curtis. Who else testified, besides Califano?

Mr. Constantine. Blue Cross -- I am being coached here.

Senator Talmadge. State government people?

Mr. Constantine. We will get a list.

Senator Laxalt. Mr. Constantine, do you agree with the observation of Senator Nelson to the effect that the Administration approach is going to result in far more savings than the Talmadge approach?

Mr. Constantine. Yes, sir. It depends on how you define savings.

Theoretically, you could cut anyone's budget by one-third and save that much. The question is the rationality. Is it savings without reduction in service? That is the kind of issue that you have to decide, whether you are moderating the costs that much by bringing it down that much, are you doing it at the expense of patient care, closing down, and so on.

Senator Laxalt. Fundamentally, for my edification, what do you think the philosophical difference is essentially between the Administration approach and the Talmadge approach?

Mr. Constantine. In the Talmadge approach, the government is a payer. The Federal government and the state governments in Medicare and Medicaid. The system we now have for

1 reimbursement under Medicare and Medicaid is inflationary
2 and uncontrolled. We have no effective means of moderating
3 costs. We pay reasonable costs, no effective definition of
4 reasonableness.

5 The more you run up the cost, in essence, the more we
6 pay.

7 In Talmadge S. 1470, it is designed to say here is a
8 more rational approach in how we spend taxpayer's dollars
9 directly. Whether it achieves it is for something else. That
10 is for you gentlemen to decide.

11 It is designed to sort out hospitals, classify them,
12 compare them, say the determination of one hospital's
13 reasonableness of cost is made relevant to other similar
14 hospitals providing similar services, that we penalize only
15 those that are inefficient relative to their peers and reward
16 those who are efficient, relative to their peers.

17 Senator Laxalt. At that point, do you concede the
18 Administration approach to be broad-stroked and the Talmadge
19 tends to be more selective by way of the classification
20 procedures?

21 Mr. Constantine. Yes, sir.

22 Senator Laxalt. That is a fundamental philosophical
23 difference in the two approaches?

24 Mr. Constantine. Yes, sir. But frankly, as the legisla-
25 tion has evolved, there has been more and more recognition of

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the kinds of things in Talmadge and the legislation evolving in the House.

I think, in the Commerce Committee, they are trying to determine classifications and in the bill as reported by Human Resources, they said, at some time when you can classify, and so on.

Senator Talmadge. Bringing it down to the lowest common denominator, you take a highly-efficient hospital where they might charge \$80 to \$100 for a bed and one that is very inefficient that would cost \$300 a day for a bed, you would put a flat arbitrary 9 percent cap. The efficient hospital would be penalized and the inefficient would be rewarded. We do not think that that is the best way of legislating in this field.

What we are trying to do is compare similar hospitals with similar hospitals, reward the efficient hospitals, penalize the inefficient hospitals.

You remember, we had wage and price controls imposed and it was a disaster and this is doing that in one field only, health care.

Mr. Swoap. If I might respond further to Senator Laxalt, Mr. Constantine made the point that the Administration bill in the House has been incorporating many elements of the Talmadge bill as it has been moving alone. Similarly, I think it must be observed that the bill introduced now by

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Senator Talmadge with the modifications proposed by the staff is moving more closely in the direction of the Administration proposal by broadening its controls and establishing additional mechanisms that were not present in the original Talmadge legislation.

Senator Curtis. What is wrong with taking a whole new look at this thing? Why not do it like private insurance companies do? They have a schedule. You look at it. They pay \$75 a day if you are in the hospital. That is somebody else's worry, where to get the rest of it.

As long as we underwrite, we will pay whatever the adding machine figures up in the hospital. There will be no end to this.

The one thing about putting a cap of 9 percent on everybody, as the Chairman said, the more you raise it, the more you multiply your 9 percent by. The only difference between that and the Talmadge bill, you take a little smaller area in the nation, you compare similar hospitals, but that is a statement that is wide.

We are never going to get out of the woods as long as we operate on the system that we are on, reimbursing them for all the costs. I do not think -- what is wrong with the idea of the Federal government saying here, we will help you with your medical problem up to X dollars for certain things, like a pension policy. The people who have no money, they



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1 still have Medicaid and local governments to go to.

2 I think anything else we would do would not work.

3 Senator Laxalt. If I may ask one more question, in your
4 analysis of your problem -- I know you have lived with it
5 probably longer than any of us --

6 Senator Curtis. He is a pretty old man.

7 Senator Laxalt. What do you consider to be the principal
8 reason why these hospital costs are out of control?

9 Mr. Constantine. A variety of reasons, Senator. We are
10 in good part responsible for it, with the governmental pro-
11 grams, going back to Medicare and Medicaid.

12 Senator Laxalt. Lack of proper controls in the adminis-
13 tration of these programs?

14 Mr. Constantine. We have had problems with the adminis-
15 tration of these programs at the Federal, state and local
16 levels. It is sort of like Topsy. It got built, and we
17 kept building on it on an increasingly inflated base.

18 It was out of hand from the beginning. It has nothing
19 to do with the validity of the programs.

20 Frankly, my own feeling is that we just have a tremendous
21 incapacity in this country to effectively administer large-
22 scale health-care programs.

23 Senator Talmadge. They say what the reasonable cost is,
24 and the government pays it. They give us a blank check and
25 we sign it.

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1 Mr. Constantine. In terms of reasonableness of controls,
2 there are a lot of subjective elements in health care. It
3 is very hard to say that you are over the limit here when you
4 say our case is somewhat different. It just does not lend
5 itself to objective judgments.

6 It is one of the reasons that we suggested to Senator
7 Talmadge, and Mr. Rogers liked the idea, and it is one of
8 those things that were not in the Administration's proposal,
9 this Health Care Facilities Cost Commission as an added
10 provision in the Talmadge bill, primarily to get people with
11 expertise, governmental and outside, as the state of the art
12 changes, to develop refinements in the classification and
13 comparison on an ongoing basis.

14 As we said yesterday at the meeting, a lot of it would
15 depend on the quality of those people. You could have people
16 who are so-so and you would get very poor results. It was
17 an alternative to having the Secretary of HEW doing it.

18 That was the only reason for putting that in. We dis-
19 cussed that with the private hospitals, the Federation of
20 Hospitals. We discussed it with state governmental people.
21 They all liked the idea of at least having a vehicle for
22 input that is visible.

23 It is a means of recognizing that we really do not have
24 all the answers. Maybe we only have a third of the answers.
25 A lot of this has to be evolved. The problems are real, and

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1 they are now.

2 Senator Laxalt. I have pretty much come to the conclu-
3 sion that perhaps the third-party payers are a substantial
4 part of the country. What we are ending up with in this
5 country, nobody else has the responsibility for a bill.
6 Somebody else is paying it. There is no inherent financial
7 discipline on the part of the consumer. I have a suspicion
8 that that is much of the problem. Do you agree with that at
9 all?

10 Mr. Constantine. Yes, sir. I think a large majority
11 of the people do not identify with the high cost of hospital
12 care. They will gripe about their Blue Cross premiums going
13 up, but they are once removed. A lot of the taxpayers are
14 removed from the hospital care. Those on Medicare and Medi-
15 caid do not see it. There is no direct identification.

16 Similarly with private health insurance, not a one-to-
17 one relationship.

18 Senator Talmadge. Mr. Fullerton?

19 Mr. Fullerton. I might add a couple of facts because
20 I think the analysis of Senator Laxalt is pretty much correct.
21 Actually, about 92 percent of hospital in-patient revenues
22 are covered by some form of third-party payer. Medicare and
23 Medicaid is a very large portion of that. The disciplines
24 are lacking.

25 I want to be sure that the members understand that the

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1 Administration favors the general-type Talmadge approach and
2 the Secretary so testified. It also believes that hospital
3 costs are rising so rapidly that you have to get ahold of
4 these costs now, until we can develop the system, and that
5 is why we proposed what we did more than a year ago now.
6 Those costs are still rising very rapidly.

7 We are not sure, in the Administration, that the volun-
8 tary effort is going to make it this year. We still believe
9 that we need some back-up legislation behind that that would
10 help make the voluntary effort.

11 I want to be sure that you understand that, as far as
12 the Administration is concerned.

13 Mr. Swoap. I would like to make one additional point,
14 as well in response to Senator Laxalt. Jay indicated that
15 it has nothing to do with the validity of the programs. I
16 am assuming by that he is referring principally to Medicare
17 and Medicaid.

18 Nonetheless, I think it does need to be pointed out that
19 there is no real effort to reform the Medicare and Medicaid
20 programs themselves since their inception and, much like
21 the Social Security program, we have had a system that has
22 grown in the last 12 years that has placed a great deal of
23 undifferentiated demand upon limited supply.

24 It seems to me that all of the proposals that are before
25 the Congress at the present time have the common characteristic

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of attempting to deal with the result, but not really dealing with the basic cost of the character of Medicare and Medicaid.

Mr. Constantine. As a personal thing, Mr. Fullerton who is working with me, and my counterpart under Mr. Mills in the Ways and Means Committee, there was a bill called H.R. 1 on which this Committee worked for years and we had hearing after hearing and investigations. The Committee worked under John Williams. Senator Williams did a lot of work. The whole Committee was involved, and really labored trying to come up with reforms.

Those people here from Congressional legislative counsel know how many months and months went into that and quite a few changes were made. Some of those changes have worked, some have not. There may be basic changes, but the Congress can administer the programs. You can put in the best statutory language and statement of intent in the world and there is no way you can administer the law.

It also depends not only on good law, but effective administration.

In response to your earlier question, I truly believe that, regardless of the validity of the program or the needs out there -- because we have a lot of needs -- we just do not seem to have the capacity to effectively administer large-scale health-care programs at the Federal, state and local level.



1 Mr. Fullerton. Secretary Califano, in one of his
2 earliest actions, adapted one of the provisions administra-
3 tively that is in the Talmadge bill today, to establish the
4 Health Care Financing Administration. One of the rationales
5 for that, as I understood it at the time -- and still do --
6 was to increase the effectiveness of the administration of
7 these programs.

8 I think I can say, speaking personally, we are working
9 on several fronts to do that. We did find problems in admin-
10 istration when we came there a year ago, but we are taking
11 a lot of variety of steps to meet some of those problems.

12 We do need some changes in the law in order to do them
13 better, but we cannot do a lot under present law.

14 Jay points out that Section 223, we are going to be
15 making the section work more than it has been working in the
16 past, to reduce payments under Medicare and Medicaid to
17 hospitals. We are going to be extending it to other kinds
18 of payers as well.

19 Senator Curtis. What portion of hospital costs is
20 non-professional labor costs.

21 Mr. Constantine. Nonprofessional labor, labor costs --
22 the wage component, Senator, is a little over 50 percent.

23 Mr. Fullerton. To answer your question, it is 40 percent.

24 Mr. Constantine. The other 10 or 11 percent is profes-
25 sional.

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1 Senator Curtis. Which would include the nurses?

2 Mr. Constantine. Yes, sir.

3 Senator Curtis. So if you get all this delegation of
4 power and all of these other things, you will only have control
5 of half of the program, because of the pass-through. Is that
6 right?

7 Mr. Constantine. Under the Administration bill, to the
8 extent that wage costs rose and brought the hospital over
9 the limit.

10 Senator Curtis. Do not all the bills have the pass-
11 through?

12 Mr. Constantine. Only to the extent that the wage
13 increases bring the hospital above whatever limit is applica-
14 ble.

15 Mr. Fullerton. In the original Administration bill the
16 wage pass-through applied to the wages of nonsupervisory
17 employees only in the case where the increases were above
18 the Federal limit of 9 percent. All the Committees have
19 been modifying that provision in a variety of ways since.

20 Senator Danforth. I would like to ask either you or
21 Jay, whoever would like to take a crack at it, about this
22 classification and averaging concept. I do not understand
23 the reason for it, very frankly. I do not understand why
24 we should be in the business of classifying hospitals. I do
25 not understand why the amount we are willing to pay should

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1 get around the problem that Senator Nelson has with the
2 Administration's proposal that tends to reward inefficiencies
3 with the 9 percent cap.

4 It seems to me to give the most economical possible
5 use of the Federal dollar and creates real competition.

6 Senator Curtis. If the Senator will yield, I think you
7 have got something there. It seems to me, if we would agree
8 that Medicaid, instead of being the cost of the hospital
9 bed, would pay X dollars, I think we could even provide that
10 within certain regions if the cost of living index met
11 certain standards, we could increase the amount by that per-
12 centage.

13 As long as we say to anybody we will reimburse you for
14 the costs, you are going to have plenty of costs. I think
15 it is the difference between sending someone off to college
16 and saying let us know what all your bills are, and saying
17 here is so much, sink or swim.

18 Senator Nelson. I just wanted to make clear that the
19 Administration does support the concept in the Commerce bill
20 when you get the data base evaluating some differentials in
21 cost. I kind of like the idea, Senator Danforth's idea,
22 but it is true that teaching hospitals do have higher costs
23 than a rural hospital someplace that does not have all of
24 those facilities, or a cancer unit or a heart unit.

25 I do not know enough about it. There may be valid reasons

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1 for some general classifications, not too many.

2 But that should be in the bill and the Administration
3 supports the Talmadge concept. And the question of rewarding
4 the inefficient while penalizing the efficient, if you are
5 going to start with a program, you have to start someplace,
6 and after extensive hearings and consideration, it did set
7 a 9 percent cap and the efficient hospitals, and one and one
8 half times the inflation rate.

9 The efficient hospitals can meet it. That is still the
10 most dramatic cut in costs of any bill that is before the
11 Congress. We ought to start there and then follow on with
12 the differential and deal with the inefficient hospitals
13 thereafter, because we have to start someplace. But if we
14 start and all we do is cover Medicare and Medicaid hospitals,
15 we have not done anything about this terrible inflation rate.

16 I think we have to cover them all. I think that that
17 inflation rate in the Administration bill is a sound one. I
18 would like to see it lower. But it is the best that we can
19 do, and the savings are very, very dramatic to states,
20 individuals and the Federal government.

21 Senator Danforth. Mr. Chairman, what difference does
22 it make to us from the standpoint of Medicare and Medicaid that
23 it is a teaching hospital or not? I do not understand.

24 If we want to subsidize teaching hospitals, why do we
25 not have a program to subsidize teaching hospitals? Why do

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1 it through Medicare and Medicaid?

2 Mr. Constantine. The staff argued that in 1970, that

3 you have a separate subsidy for educational programs.

4 Senator, the services are more complex. Often you have

5 standby capacity in certain hospitals. Hopefully, rationally,

6 this hospital has this capacity as opposed to that one.

7 Hospitals get together to agree that one hospital is going

8 to have this equipment and the others do not, but they are

9 still getting paid the same amount.

10 You have all sorts of variations on when a hospital was

11 built, its debt service.

12 Senator Danforth. Why should that be of any concern to

13 us? Why should not our sole concern be to be paying for the

14 treatment of human beings, and the cheapest way we can get

15 the job done is the way that we want to do it. Then, if

16 somebody wants to go into a palace and check into one of these

17 very fancy hospitals, fine. But we just are not going to pay

18 for that.

19 It seems to me that we have already reached that theoret-

20 tical decision when you are talking about limiting it to 115

21 percent of the average. That reaches that decision that we

22 are not going to pay the limit, that we are not going to pay

23 every cost that a hospital can conceivably load on its

24 patients.

25 That is the whole reason for hospital cost containment,

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1 so why not just look at the purpose of Medicaid or Medicare
2 to it, to make it possible to treat people who are sick for
3 their ailments and pay for that and, if you can do it at a
4 very reasonable cost at some low-cost hospital, that is what
5 we should be doing. I do not understand why we have to use
6 Medicaid and Medicare to subsidize teaching hospitals or
7 hospitals with this very advanced equipment if it does not
8 have anything to do with this particular patient, and if this
9 particular patient could be treated just as well at a very
10 low cost.

11 Mr. Constantine. Senator, I guess partially on the
12 equipment and so on there is the standby value, there is some-
13 one who may need the quipment. That is one point.

14 In rural areas, for example we pick up the cost of unused
15 beds for standby capacity which may be an additional cost, not
16 available someplace else. You run into all of these refine-
17 ments and differences, but most importantly, it is the physi-
18 cian who chooses the hospital and not the patient.

19 Senator Danforth. I am saying it is possible, and maybe
20 we want to do this. I think we are doing this now. For us
21 to pay all of the costs of a person's medical care. Then we
22 do not have to make any choices at all. Then the physicians
23 and the hospitals can make all of the choices.

24 But what we are saying, and the whole concept of cost
25 containment is, we are tired of it, that we are not just going

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1 to write checks to anybody who submits them.

2 What I do not understand is why are you pegging it to
3 the average rather than to the lowest cost?

4 Mr. Constantine. First, I want to reassure you that we
5 can guarantee you that the approach you are suggesting would
6 save more money than the Administration proposal. The reason
7 the average was chosen was simply trying to say that hospital
8 costs are not necessarily identi-al. They do not necessarily
9 purchase the same mix of goods and services that other elements
10 of the economy do. They do it on a different weighted basis.

11 It is difficult to compare similar hospitals providing
12 similar services to determine reasonableness. It was an index.
13 The average was chosen, adjusted for prevailing wage differ-
14 ences. You have the prevailing wage factor operating as well,
15 simply to determine where you are. If you are below the
16 average, relative to your peers, it is the presumption that
17 you are efficient. If you are above the average, you may be
18 in a band. If you are sufficiently above the average, you
19 are inefficient.

20 We felt this was reasonable on the size of the hospital.
21 The pediatric hospitals, Senator, will come at you that their
22 needs are different, their costs are different, their services
23 are different. The same service in a pediatric hospital is
24 not the same as that service in a general hospital, may not
25 be the same. Those are the kinds of distinctions that need



1 to be made.

2 My personal view is that your proposal would save one
3 hell of a lot of money. I do not think that it could be
4 enacted.

5 Senator Danforth. Supposing I wanted to get my appendix
6 removed. Why should I feel free to check into Burns Hospital
7 in St. Louis that will charge me for a medical school and
8 charge me for CAT scanners and charge me for everything else?

9 Why should I not check into the lowest-cost hospital
10 in the community and then have the government pay that cost,
11 if I am on Medicaid?

12 Mr. Fullerton. If I may comment on that, I think I am
13 personally attracted to your idea also, but I could point
14 out, under Section 223 to which Jay referred to before, one
15 of the very rationales of that section is the very kind of
16 point you are bringing out -- that is, we should not be paying
17 the extra. If it is a luxury situation, the government should
18 not be paying for it. If the patient wants it, he should be
19 paying for it himself.

20 As a matter of fact, there is a provision in the present
21 law that says the hospital in a luxury-type situation can
22 impose the charge on the patient if it is more than Medicare
23 will pay.

24 The problem has been in carrying out Section 223, we
25 did not move as rapidly as we could have. One of the largest

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1 problems has been the situation with wages. Even if you
2 wanted to pay for exactly the same product, you are now
3 providing that product in central Missouri, for example, it is
4 going to cost you less than for that product in St. Louis or
5 Kansas City.

6 Then we would have to make some differential. People
7 would argue right away on just the wage costs that they pay.
8 If you want to cover a Medicare patient --

9 Senator Danforth. That is a purely geographic distribu-
10 tion and that can be worked out.

11 Mr. Fullerton. Yes, sir, and we are working on it, and
12 when we get more wage data coming to us, we will be able to
13 make those distinctions better and use 223 to save even more
14 funds.

15 Senator Curtis. Why does the concept of assisting people
16 with their hospital and medical bills have to be on the basis
17 of reimbursing somebody for their costs? Why can we not do
18 it like the private insurance companies?

19 Mr. Fullerton. In the first place, many insurance
20 companies do divide the payments, so many dollars a day, but
21 many policies do pay for all the charges that the hospitals
22 impose.

23 You could argue that their system of reimbursement --

24 Senator Curtis. With the exception of Blue Cross-Blue
25 Shield.

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1 Mr. Fullerton. Even some of the commercial insurance
2 companies will pay all of the costs now. Some still sell
3 policies.

4 Senator Hansen. I would not buy stock in it.

5 Mr. Fullerton. The Federal Employee's Program, for
6 example, has that kind of a situation, even in a plan admin-
7 istered by the Aetna Insurance Company -- that is, the pay-
8 ment of full charges. They will base it on the charge of
9 the hospital and not so many dollars a day.

10 Senator Curtis. Co-insurance?

11 Mr. Fullerton. Co-insurance, but 20 percent of whatever
12 the charges are, for example, not the first dollar amount,
13 and then the patient has to pay the balance. It is just
14 not as typical in commercial insurance as it once was.

15 Frankly, you put your finger on a very good problem.
16 That is what has accounted for the rapid increases in
17 hospital costs, that is the patients, 92 percent of them, do
18 not have very much stake in what that total hospital cost
19 might be. The doctor does not. And the hospitals, of course,
20 are going to react to that kind of situation, if you spend
21 more, you get more.

22 Senator Curtis. The doctor is faced, and very justifiably
23 so, with the threat of a malpractice suit. Instead of passing
24 on the question of his own judgment, and if it is necessary
25 in order to protect him when he gets in court, to have four

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1 or five additional tests made, why, he has to make them.

2 That is why I question the estimate that the malpractice
3 problem is only adding 3 percent to our malpractice costs.

4 I think that it is a big element.

5 Mr. Constantine. Senator Danforth is correct in one
6 regard -- and you are, too -- that one of the things being
7 actively worked on is the case mix approach for reimbursement.
8 It was developed at Yale and tested at New York's Cornell
9 Hospital and is now being administrated in New Jersey by
10 Medicare to see whether reimbursement by type of case, by the
11 type and nature of the diagnosis, saying so much per case is
12 the way to go.

13 The dilemma has been, as Bill made clear yesterday again,
14 that very often with older people you have multiple diagnoses,
15 a lot of secondary complications and other things, and it is
16 hard to sort that out and say that you are comparing apples
17 with apples when you say this case is similar to that.

18 That is being done, Senator, by diagnosis.

19 Senator Danforth. If you did it by the lowest cost
20 rather than by the average cost, you would not even have to.

21 You could put off the case-mix thing, could you not?

22 My understanding of the problem of the case mix --

23 Senator Nelson. Carl, before you go, I just want to
24 say one thing.

25 Senator Danforth. The problem of the case mix situation,

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1 as I understand it, is the state of the art is not yet to
2 the point at which it can be used, but if you are going to
3 average costs, it is no great difficulty in determining what
4 the lowest cost is, is there?

5 We are at that state of the art that we can go proposition
6 two --

7 Mr. Constantine. The Talmadge bill works to bring the
8 average down over time, so you are coming to that. It
9 certainly is not the lowest.

10 Senator Talmadge. Here is the problem with the lowest
11 cost. The lowest cost hospital might be a little rural hospi-
12 tal in Georgia with very limited facilities. Then you have
13 Johns Hopkins.

14 If a fellow wants an appendectomy in Baltimore, he is
15 not going to go to Georgia to get the lowest cost for it.

16 Senator Danforth. What you could do on that, you could
17 differentiate geographically.

18 Senator Talmadge. You have these high-cost urban centers.

19 Senator Danforth. Some are high-cost and some are rela-
20 tively low-cost. You could determine where a person could
21 reasonably go in his community rather than differentiating
22 by type of hospital and once you did that, you take the
23 second step. Instead of paying out the average plus 15
24 percent, you would pay out the lowest cost.

25 Senator Nelson. Before Senator Curtis goes, if you do

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1 not mind, I have a bias simply because the only bill that
2 I have been through in any detail is the one from the Human
3 Resources committee, the Administration bill which I think is,
4 overall, a very good one.

5 Nonetheless, there are good provisions in Senator
6 Talmadge's bill and good suggestions made by Senator Danforth
7 and Senator Curtis.

8 I am wondering if it would not be fruitful to ask staffs
9 of the Human Resources Committee, this Committee and HEW to
10 sit down and go through and see if we can come up with a
11 package to deal with taking the best elements of all of these
12 bills.

13 Senator Talmadge. We had been doing that for some time.

14 Mr. Constantine. We have tried, Senator. Lord knows,
15 we have tried.

16 I am not sure -- unless it is a formal motion, I think
17 the Committee should understand, Senator Nelson, that what
18 you are really saying is that you want the Finance Committee
19 staff to cooperate in the development of an overall cost
20 containment approach.

21 Senator Nelson. Yes.

22 Mr. Constantine. That is what I thought.

23 Senator Nelson. Exactly. I would like to have the
24 Administration proposal considered, which is more dramatic
25 than any of the others. I would like to have the provisions

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1 of Senator Talmadge's bill considered, the suggestions of
2 Senator Danforth and Senator Curtis, and see if we could not
3 get together.

4 Senator Talmadge. How long have we been doing this?

5 Mr. Constantine. We have been working since February,
6 I guess. We came up with an approach that we believe was
7 equitable; Mr. Fullerton -- we might as well get that out
8 in the open -- was designated by Secretary Califano and
9 I was designated by you to see whether there was a possible
10 middle ground between building on the Talmadge approach to
11 the overall thing.

12 Mr. Fullerton agreed with the staff, and about a month
13 ago that we had something that was feasible if we wanted to
14 do it. He was taking it to his principals at the Department
15 and the White House to see whether they could approve it as
16 a possible mutually-agreeable approach, building on the
17 voluntary effort, and so on.

18 No word ever came back at that time. My own personal
19 view is that the reason that they could not make a decision
20 was because they are still dealing with Paul Rogers, Mr. Rogers
21 in Commerce and Mr. Rostenkowski in Ways and Means, and they
22 would obviously not endorse another approach before they had
23 resolved those gunfights.

24 Senator Talmadge. You also worked with the staff of
25 Mr. Rostenkowski and Mr. Rogers?

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1 want to take Senator Talmadge's suggestion, then, and offer
2 the Administration bill as a substitute so that at least we
3 have it before us. In the meantime, I assume we are going
4 to get some additional statistics from the Congressional
5 Budget Office and we will have them both before us and deal
6 with that.

7 Senator Talmadge. Mr. Champion?

8 Mr. Champion. I would like to speak briefly to the
9 Administration's position in these negotiations. They did
10 proceed. We had thought they were still proceeding, given
11 the fact that there was also legislation being worked on in
12 the House and it therefore came as a surprise to us that
13 legislation covering only Medicare and Aedicaid was being
14 advanced at this time, because our hope was that ultimately
15 something would come out that applied to all payers.

16 I think a lot of progress was made in those negotiations
17 and we have made suggestions, as have your staff. We think
18 that that is a continuing productive way to go and that they
19 are matters, basically the differences resolved how early
20 the timing of getting a voluntary cap, of which the Talmadge
21 principals might work, would be achieved.

22 And it is, therefore, from the Administration's point of
23 view, highly desirable to have those continued. We do not
24 regard those negotiations as fruitless. We think they have
25 a real chance of succeeding.



1 Senator Talmadge. We understood that we are making
2 progress in that direction, but we could not get a final
3 answer from the White House or anything specific from HEW.

4 Mr. Constantine. Mr. Chairman, I might also point out
5 that, subsequent to submitting that, and those discussions
6 which began, we really believed, Mr. Chairman, that the
7 second part of what we were negotiating, the possibility
8 of Talmadge being expanded to encompass all payers in the
9 event that the voluntary effort failed, is, as we mentioned
10 earlier, not necessary for Congress to decide this year.

11 We believe that if you proceeded with the Medicare and
12 Medicaid approach, Mr. Chairman, that you could then, next
13 year, decide. You would have a basis, a mechanism and
14 methodology that could, if Congress were shocked at any
15 continuing rate of rise, could then decide what should be
16 applied to all hospitals.

17 I think that is the change in our perspective, and from
18 the time we started working, we did not believe, at this
19 point in time, that it is necessary, unless you feel that it
20 is important, to approve a mandatory program covering all
21 payers. We think that Congress can defer that decision until
22 next year.

23 Mr. Champion. Mr. Chairman, we have now had this bill
24 for 15 months, during which hospital costs have gone up
25 billions of dollars more. What is behind the voluntary

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1 trigger, if, in fact, they should continue to rise as they
2 have and there is nothing mandatory in place behind it
3 next January 1, it means nothing can be done until January
4 1, 1980.

5 It may be that the voluntary effort will be successful.
6 If that is true, then this effort would not take effect. It
7 would take effect only when and if that amendment took place.

8 If Congress would have acted, it would have put a lot
9 of the teeth in the current voluntary effort to make them
10 much more interested in the problem, and it would have the
11 salutary situation of not going through a number of, 15
12 months of, arguing basically this same set of questions.

13 We could take the current discussions, bring them to a
14 conclusion, and have something in place.

15 Senator Talmadge. Well, it is a little after 12:00.
16 We had had a lot of discussions; no decisions.

17 Senator Dole. Maybe we need some containment on that.

18 Senator Talmadge. Would the Committee like to meet again
19 this afternoon or tomorrow?

20 Senator Dole. Tomorrow, we have a meeting on trade.

21 Mr. Stern. Yes, there is a briefing session of the
22 Trade Subcommittee scheduled for tomorrow morning.

23 Senator Talmadge. We might as well recess and check with
24 Senator Long as to when we can meet again and see if we can
25 make some further decisions.

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Without objection, we will stand in recess, subject to the call of the Chair.

(Thereupon, at 12:05 p.m., the Committee recessed to reconvene at the call of the Chair.)

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