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TREATMENTS FOR AN AILING ECONOMY: PROTECTING HEALTHCARE COVERAGE AND INVESTING IN BIOMEDICAL RESEARCH

HEARING

BEFORE THE

SUBCOMMITTEE ON HEALTH

OF THE

COMMITTEE ON ENERGY AND COMMERCE
HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

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TREATMENTS FOR AN AILING ECONOMY: PROTECTING HEALTHCARE COVERAGE AND INVESTING IN BIOMEDICAL RESEARCH

THURSDAY, NOVEMBER 13, 2008

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HEALTH,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, DC.

The subcommittee met, pursuant to call, at 10:00 a.m., in room 2123 of the Rayburn House Office Building, Hon. Frank Pallone, Jr. (chairman) presiding.

Members present: Representatives Pallone, Towns, Green, Burgess, and Blackburn.

Staff present: Bridgett Taylor, Purvee Kempf, Jessica McNiece, Bobby Clark, Andrew Shin, Brin Frazier, Lauren Bloomberg, Hasan Sarsour, Ryan Long, Aarti Shah, Brandon Clark, and Chad Grant.

OPENING STATEMENT OF HON. FRANK PALLONE, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Mr. PALLONE. The meeting of the subcommittee is called to order.

Today we are having a hearing on "Treatments for an Ailing Economy: Protecting Healthcare Coverage and Investing in Biomedical Research." I thank you all for being here today and I will recognize myself initially for an opening statement.

Medicaid, as you know, provides 59 million Americans with access to medical care and specialized support and services. It protects our most vulnerable populations, the poor, disabled and elderly. It also accounts for nearly half of all nursing home care. The NIH is America's leading medical research agency and the foremost biomedical research institute in the world. It is through the work of NIH that we are living longer and healthier lives and may some day soon find cures for the epidemics of our time like cancer and diabetes, and it will be through the NIH that we are protected from those that wish us harm through bioterrorism.

No doubt the effects of the current economic crisis are on the forefront of everyone's mind. Americans are facing uncertain times and wondering how they are going to pay for basic necessities like food, fuel and healthcare. Others are just hoping to hold on until they are lucky enough to find a job, and as this crisis hits both Wall Street and Main Street, Washington must act because the sit-

uation in the States, as I know we are going to hear from Governor Napolitano, is certainly dire. Due to shrinking State revenues, States may cut coverage and restrict new enrollment, which means millions of Americans may lose access to the healthcare coverage they desperately need and those who have lost their jobs will lose healthcare coverage also. Right now more than 10 million people are actively seeking work but are unable to find it. The unemployment rate is 6.5 percent, which is the highest level since 1994. In each month this year our economy has shed more jobs than it has created. To date, 1.2 million jobs have been lost.

A study conducted by the Kaiser Family Foundation found that increasing the national unemployment rate by one percentage point increases Medicaid and SCHIP enrollment by 1 million people. Such a change would increase state spending by approximately $1.4 billion at a time when States are already struggling to balance their budgets, and to make matters worse, the State Medicaid programs, they not only impact Medicaid-eligible individuals with the cuts but they also adversely affect the healthcare job market. Medicaid cuts translate into healthcare job losses. Therefore, such cuts only contribute to the State's unemployment rate and can exacerbate a worsening fiscal crisis.

Now, earlier this year I introduced a bill with my colleagues, Chairman Dingell, Mr. King and Mr. Reynolds, to temporarily increase each State's Federal Medical Assistance Percentage, what we call FMAP, during this economic downturn, to ensure that States can continue to provide critical services instead of cutting them. A similar provision was included in the recovery package that the House passed in September and I hope that this FMAP increase will be included in any economic recovery package that is crafted during a possible lame-duck session which, as you know, is likely to occur next week.

As we explore the possibility of another economic recovery package, we should also discuss providing additional assistance to States in creating jobs by investing in biomedical innovation and research. While there is no question regarding the importance of the research NIH conducts to improve our health, it also provides real direct economic benefits at the local level including increased employment, growth opportunities for universities, medical centers, local companies and additional economic stimulus for the community.

In 2007, NIH grants and contracts created and supported more than 350,000 jobs that generated wages in excess of $18 billion in the 50 States, and these are good paying jobs. The average wage was $52,000 a year. According to Families USA, if the amount NIH awards to the States were to increase by 6.6 percent, the national economic benefit would add up to $3.1 billion worth of new business activity, 9,185 additional jobs and $1.1 billion in new wages. We have a proud tradition in this country of persevering through tough times by investing in American innovation and ingenuity. What better way is there to tap into that great American spirit and industry than by investing in research to combat disease and lead the world in that noble endeavor.

At a time of great economic uncertainty, Washington, in my opinion, must act. Last month Federal Reserve Chairman Ben

Bernanke voiced his support for an economic recovery package during testimony here on Capitol Hill. Some economists are saying that we need to pass a more robust package. I was reading Mr. Sperling's testimony and I think he talked figures of $300, $400 billion. Each day we hear about more job losses and troubling economic trends. I would hope these headlines would serve as a wakeup call to the White House. House Democrats are prepared to work with President Bush and the Senate to pass another economic recovery package, probably last week, if the President finally recognizes the need for such action.

I would like to thank each of our witnesses for being here today. I especially would like to welcome Arizona Governor Janet Napolitano. I told her before that I have a lot of relatives. I don't know, it seems like people from New Jersey when they retire often go to Arizona, so I have been out there a lot to see my mother-in-law and my brother-in-law. Thanks for being here today. It is also nice to see Gene Sperling, who has been to many of our message meetings over the last year to talk about where we are going on various economic issues, but I look forward to hearing all the testimony from all of our panelists today.

Mr. PALLONE. I now recognize Mr. Burgess, who is our ranking member for the day. Welcome.

OPENING STATEMENT OF HON. MICHAEL C. BURGESS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. BURGESS. Thank you, Mr. Chairman, and I will be brief because we do have a lot of witnesses to go through today and I have an opening statement that is prepared and I will submit it for the record. But I am grateful that we have such a varied panel of witnesses here in front of us today. I think it always speaks well for this committee that we do have such varied witnesses come and speak to us. I am a little concerned. I am grateful to be able to meet the acting head of the National Institutes of Health, but other than that individual, we have no practicing physician. Even with that individual we have no practicing physician in front of us, and I think it would be good to hear from a member of the provider community as we tackle these tough issues because they are obviously impacted by any increase in funding or any growth of the State Medicaid programs. It is all going to affect our physical communities across the country in ways that most of us frankly do not understand or do not care to understand. We heard from a pediatrician from Alabama last year who got my attention because she went into practice the same year that I did, 1981, so now after nearly 30 years of medical school, residency and practice, she had a practice that was 70 percent Medicaid and was borrowing from her retirement fund to keep her office open because as we all know, Medicaid pays about 30 to 40 percent of the cost of delivering the care, and I will tell you from my past as a practicing physician that if you are losing a little bit of money on each patient, it becomes very, very difficult to make it up in volume. One of the great concerns we had during the SCHIP expansion arguments last year was the fact that moving children off of private insurance onto SCHIP was subsequently going to have a very deleterious effect on the practicing pediatrician.

We heard testimony in this committee earlier in the fall from Mr. Jim Frogue from the Center for Health Transformation who asked if we were going to give more money into the system, which maybe we needed to do, but we shouldn't give more money without asking for increased transparency and accountability. Now, we always at this committee are quick to harshly judge the physician community for being slow adopters on electronic medical records but I recall back in 1996 being required to purchase all kinds of computer equipment because electronic claim submission was now going to be required. In fact, that is what led to the HIPAA regulations that we now live with every day but at the same time there is no mechanism across the States for a hospital to identify who is responsible for covering for a patient. As a consequence, we end up with a situation where a Medicare patient may also be eligible to be covered by their private insurance but no one knows because that information is not readily available, and as a consequence, the Medicaid system itself unfairly has to pay for that which rightly should be paid by a private insurance company and the hospital and physician are reimbursed again at that 30 percent of the cost of delivering care that Medicaid provides.

And then the other issue that we are not addressing today and that really just cries out for us to address is the issue of the lack of efficiency and the presence of fraud within the system. The GAO has uncovered this. A New York Times article, albeit this is several months old, from July of 2008, quoting here, "New York's Medicaid program, once a beacon of the great society, has become so huge, so complex, so lightly policed that it is easily exploited." This is the New York Times. Again quoting, "Though the program is a vital resource for 4.2 million people who rely on it for their healthcare, a yearlong investigation by the Times found that the program has been misspending billions of dollars annually because of fraud, waste and profiteering. A computer analysis of several million records obtained under the Freedom of Information Act revealed numerous indications of fraud and abuse and the State had never investigated." Now, they go on to say later in the article New York's Medicaid program is by far the most expensive and the most generous in the Nation. It spends nearly twice the national average, roughly $10,600, and that is more than any other State on each of its 4.2 million recipients, one of every five New Yorkers, and that was from 2005. I suspect that number would be a little higher today. The Kaiser Family Foundation last fall said that the average employer-sponsored insurance is $8,800. We could buy everyone a gold-plated insurance policy in New York on the Medicaid program for what we are spending today and at the very least our providers would be reimbursed more fairly and perhaps we would have less providers leaving the system.

I am grateful that we have some representatives from the private sector here today. I am especially interested in hearing the comments that I read in the testimony about association health plans. Certainly we have multi-state corporations that are allowed to sell insurance across State lines but we don't give the same break to the little guy, and I frankly do not understand that. In the NFL, for example, if a player is traded from Washington to Dallas, 2 months ago I would have said it was an upgrade, but nevertheless,

if a player is traded from Washington to Dallas, their insurance goes with them. If a fan follows his favorite player from Washington to Dallas, he has got to start all over again, and that is a fundamental unfairness of our insurance system and really it is the obligation of this Congress or the next Congress to correct that.

Thank you, Mr. Chairman. I will yield back.

Mr. PALLONE. Thank you. I like the football analogies.

I next recognize for an opening statement the gentleman from Texas, Mr. Green.

OPENING STATEMENT OF HON. GENE GREEN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. GREEN. Thank you, Mr. Chairman, and I appreciate the football analogy also, but since I am from Houston, I wouldn't want anybody to be traded to Dallas but I will be glad to talk about the transferability of State-regulated insurance but I know Governor Napolitano, having served 20 years in the State legislature in Texas, and dealing with State health insurance, I am not so sure folks living in Arizona would be best served by our State agency regulating the policies that are sold in Arizona. With that, I will get into my remarks.

Mr. Chairman, I thank you for holding the hearing today. As we know, the current economic state in this country is taking its toll nationally and at the state level. Many individuals are losing their jobs and the rate of unemployment is rising as is the number of uninsured in our company adding to the 46 million uninsured we already have in the United States. Unfortunately, when individuals lose their job, they often cannot afford medical care and often forego it. This leads to these individuals showing up in emergency rooms when their problems are much worse and more costly to treat and placing a larger burden on the system because they are uninsured. During the last economic downturn in 2003, President Bush provided a 2.5 percent increase in the States' Federal Medical Assistance Percentage to help assist them in the rising number of individuals needing Medicaid coverage. In turn, the States agreed not to reduce their current standards for Medicaid eligibility. In order to avoid State deficits, many States will reduce their standards for Medicaid eligibility which will actually increase the number of uninsured. An increase in the FMAP funding would avert this potential problem and allow States to continue to provide Medicaid coverage to its uninsured population. I have supported providing the increase in FMAP in the past. In fact, Chairman Pallone introduced H.R. 5268, which would have increased FMAP by 2.95 percent, and I supported that bill.

I also supported increased NIH funding. The NIH is the world's leading biomedical research institute. It is one of the great success stories of the Federal Government. Our investment in lifesaving research has lead to advances that have profoundly improved the length and quality of life of millions of Americans. Information gained from NIH research is revolutionizing the practice of medicine and future directions of scientific inquiry. Without a doubt, the work performed at the NIH is invaluable. The groundbreaking research supported by NIH has provided a lifeline of hope to count-

less Americans whether it be diabetes, cancer, HIV/AIDS and many other illnesses.

Unfortunately, for the fifth consecutive year, NIH has received flat funding. The NIH employs thousands of researchers and generates wages in excess of $18 billion in 50 States. The economic benefit of funding the NIH is something that could help both the States and our medical research. While funding the NIH and increasing FMAP are not the answer to our financial situation, they are healthcare-related funding that can provide relief to the States. It is my hope that if Congress moves an economic stimulus next week, that it includes both FMAP increase and additional NIH funding.

Again, Mr. Chairman, I thank you for calling this very timely hearing if we have a lame-duck session next week. Thank you.

Mr. PALLONE. Thank you.

Next for an opening statement, are we going to get the Nashville music analogies?

OPENING STATEMENT OF HON. MARSHA BLACKBURN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TENNESSEE

Ms. BLACKBURN. Well, I could sit here and give you lots of wonderful Nashville music analogies. The CMAs were last night, the Country Music Awards, and if you missed the show, you missed a tremendous show, and Kid Rock came out wearing a Titans jersey, which I thought was terrific. He had a great presentation, and I will say to my colleague from the Houston area, sorry you lost your Oilers, but your Tennessee Titans are now just having the greatest year that they have had. And to the guys from Dallas, all the Texans are coming back to Tennessee. It wouldn't have been a Texas without us so everything——

Mr. GREEN. Will the gentlelady yield?

Ms. BLACKBURN. I will yield.

Mr. PALLONE. I started this. It is my fault.

Ms. BLACKBURN. With great sympathy I will yield.

Mr. GREEN. Well, being a country western fan, I am glad George Strait, a good Texan, is still at the top and king of the CMAs but I also know I gave away all my Oiler paraphernalia to a predecessor from Nashville and said okay, we ended up keeping the owner and you got the team. It was supposed to be reserved. You all were supposed to get the owner and we kept the team but——

Ms. BLACKBURN. Reclaiming my time.

Mr. GREEN [continuing]. Congratulations on the Titans success but the Texans are rebuilding every year.

Ms. BLACKBURN. Your Oiler paraphernalia could probably be sold on eBay and you could reap a tidy sum, and George Strait is the king of country right now but the goodness in his career has happened out of that wonderful Nashville creative community. So we welcome all Texans to Tennessee and we welcome all of our guests here today coming in. We thank you for taking time to come before us and to work with us on this issue.

We are all concerned about healthcare and the economy and the interface of the two and preserving that access to healthcare, and Mr. Chairman, as we are talking about spending more money, I

find it very interesting that over the past year the Administration and the Democrat-led Congress has chosen to spend about $1 trillion bailing out financial institutions and then after having waived the PAYGO rules, the Democrat-led Congress spent $283 billion in new spending and we know that has not been the cure for the economy.

As we look at healthcare and the relationship between what is one-seventh of our Nation's economy and the economic structure that we have, the chairman spoke very appropriately about the spirit of industry, the American spirit of industry that exists in this country, and our focus should be on what we do to energize that spirit of industry because we are the most creative people on the planet. We seek ways to solve problems that are laid in front of us and we are very good at it, and what the decisions that we make should be here to energize and create the right growth environment for small businesses, for science and medical research firms, to solve some of the problems that we have, for technology firms to solve some of the problems of data transfer and of records that can be kept and owned by individuals, and I would hope that as we look at tax policies and how it applies to healthcare, how it applies to innovation that we are going to do that. I will say, Mr. Chairman, I was a little bit concerned to learn that Judiciary is looking at moving intellectual property away from a subcommittee and just having it considered by the full committee because intellectual property is the basis of which all these innovators that are going to resolve the health IT problems, the biomedical research problems, that are going to deal with how industry provides healthcare for employees. They find their basis in that.

So my hope is that as we look at the interface between healthcare and that being a seventh of our economy, that our course of action is not going to be throw some money at it and wait for government to solve it but our focus is going to be how we address the healthcare needs of individuals and create the right environment so that indeed innovators can innovate and find a way to help solve some of the healthcare issues, the health IT issues, the access issues that exist today, and with that, I yield back.

Mr. PALLONE. Thank you.

Before we proceed to the panel, let me ask a unanimous consent to include in the record first a statement of the American Hospital Association, and second, two letters from the National Governors Association supporting a temporary increase in FMAP and a new report released by the National Governors Association today on economic recovery. Without objection, so ordered.

[The information appears at the conclusion of the hearing.]

Mr. PALLONE. Okay. That completes our opening statements, and we are going to turn to our witnesses on our first panel. I want to welcome all of you, and let me introduce the first panel. First is the Hon. Janet Napolitano, who is the Governor of the State of Arizona, and next is Gene Sperling, who is the Senior Fellow for the Center for American Progress Action Fund, and then we have Mr. Craig Zolotorow, a Medicaid beneficiary from Maryland, and then we have Mr. Raymond Pinard, President and Chief Executive Officer of 48HourPrint, and he is from Boston, and last is Dr. Alan Viard, who is a Resident Scholar with the American Enterprise In-

stitute here in Washington. We have 5-minute opening statements. They become part of the hearing record. But each of you may in the discretion of the committee submit additional brief and pertinent statements in writing for inclusion in the record.

I will start with the governor. Thank you for being here today.

STATEMENT OF HON. JANET NAPOLITANO, GOVERNOR, STATE OF ARIZONA

Governor NAPOLITANO. Thank you, Mr. Chairman, members of the committee. Given the colloquy that just occurred, I have to put in a word for the Arizona Cardinals. We are four games ahead in the division and we look forward to meeting Tennessee later on in the year.

I am here to testify about FMAP. I am the two-term governor of Arizona, and the reason I mention that is because I was governor the last time Congress addressed FMAP in the context of state deficits so I can speak directly to its effect on medical care in our States and also its effect on our State economies.

There are two different issues pending before the Congress where States are concerned, two major ones today. In another committee they are hearing testimony on the need to invest in physical infrastructure, on projects that are ready to go that have cleared all the environmental impact statement requirements and the like as a means of stimulating jobs and job creation. That is very important and the governors on a bipartisan basis are in support of that. The letter you just incorporated into the record from the National Governors Association, which is a bipartisan organization as well, addresses FMAP, which is another major issue, and it deals, of course with the federal share of Medicaid payments. This is a very, very easy and efficient way for the Federal Government to work in partnership with the States to make sure that healthcare continues to be provided to most in need, and indeed, in a way is its own economic stimulus into the healthcare provider community.

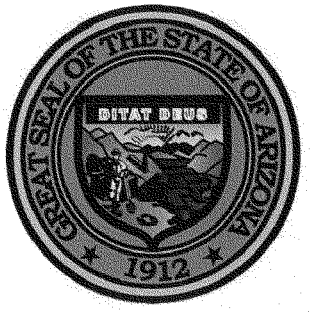
Let me give you a sense of what the condition of the states is today. Forty-nine States are required by law to have balanced budgets every year. Approximately 30 States now are already in deficit. We expect by the end of the year that will rise to 40 States. They expect cumulative deficits of over $140 billion by fiscal 2010. State fiscal years are different than federal. State fiscal years are generally July 1 to June 30 as opposed to the October 1 federal year. The States have been in this position now for some period of time so any easy options available to them have been exhausted. I will use Arizona as an example. Arizona was one of the first States to experience the economic downturn because of the heavy prevalence of the housing industry in our State. During the last few years we had set aside money for a rainy day fund. We had $750 million set aside to use in case of an economic downturn. By the end of our next special session, we will have totally depleted that fund. It is also important to note that State budget deficits tend to lag behind recovery so that whatever you do today, it needs to be done in the context of a timing cycle. It needs to be a 2-year approach and not simply a 1-year approach.

Now, let me turn directly to Medicaid with my remaining few minutes. An increase in the federal Medicaid match allows us to

do two things. One is, it recognizes that when State economies are hurt, when revenues are down, the demand for enrollment in Medicaid goes up. More people simply become eligible. You are not expanding eligibility, you are not changing your program in any way whatsoever, you just simply have more people who aren't making as much money as they used to. By way of example, in September of this year 13,000 more Arizonans qualified for Medicaid than in August. About 8 months ago we had 900,000 people on Medicaid in Arizona. Now we are approaching 1.15 million. That is a very tremendous rate of growth. In addition, what you find is, if you provide an FMAP correction now, you compensate for the way FMAP is calculated. As you know, FMAP is calculated with a 3-year rolling average, and what that means is that you have States that are currently in deficit now that are actually seeing their FMAPs decreased because they are experiencing the effect of the rollover average and so by way of example, you have at least nine States that next month will experience a decrease in their FMAP percentage even though they currently are in deficit. And so by looking at FMAP now, you can assist States with keeping on the rolls those who need healthcare, you can provide healthcare dollars into the healthcare system and you can make sure that States who have already used up their easy options do not have to either raise taxes or cut other spending in order to cover Medicaid which in a period of recession would be contraindicated. That would add to the recession, not help our Nation get out of the recession.

So the Nation's governors believe that this is an appropriate time to reemphasize FMAP. It is an easy calculation to do. It is efficient. You don't need to invent a new program. We know it works. We have done it before. The need for this couldn't be more serious than the present time. Thank you, Mr. Chairman.

[The prepared statement of Governor Napolitano follows:]



Testimony of Janet Napolitano
Governor of Arizona

Submitted to the Subcommittee on Health, House Committee on Energy and Commerce

"Increased Federal Investment in Federal-State Partnerships as an Effective Economic Stimulus"

November 13, 2008

Chairman Pallone, Ranking Member Deal, and Members of the Subcommittee – thank you for this opportunity to testify on the current fiscal condition of the states, and on how Congress can stimulate the economy through supporting existing federal-state partnerships.

My name is Janet Napolitano and I am the two-term governor of Arizona. I am also a former Chair of the National Governors Association, a bipartisan organization representing all of the nation's governors.

Amid discussion in Congress about the need for another stimulus package, my message today is simple: One of the wisest and most effective things Congress can do now to speed a national recovery is to invest in the federal-state programs that Americans rely on during a downturn. Congress can stimulate the economy, provide enormous relief to state budgets, and ensure the most vulnerable Americans have a health care safety net to rely on during difficult times – a win-win-win.

The position of the states in the economic downturn is a paradox created by the countercyclical demands on state budgets: By law, 49 states must balance their budgets every year, so during a recession, when most states will be in deficit, they either must increase taxes or cut benefits – either of which would worsen the national recession. Without greater federal investment in federal-state partnerships, states will be forced into this kind of action early next year — just at the time when most economists expect unemployment to continue to rise. But on the other hand, increased federal investment with the states is a surefire way to provide a boost to the economy.

Increased federal investment in federal-state partnerships, particularly in health care and infrastructure (including highway, transit, water, and border projects) is an efficient and effective way for Congress to stimulate the economy and create jobs while easing the dire fiscal conditions of the states. Congress has done this before to great effect, and I urge you to act again, while taking into consideration some more permanent changes.

In addition to infrastructure, many governors think a stimulus package should also include adjustments to the Federal Medicaid Assistance Percentage (FMAP), food stamps, unemployment benefits, and an initiative on green-collar job creation. In my testimony today before this Health Subcommittee, I will focus primarily on Medicaid.

I would note that providing additional infrastructure funding helps our capital budgets and creates jobs. However, we have to balance our operating budgets — which is where the FMAP and other benefit programs come into the mix. We need *both* the infrastructure funding as well as funding for these key benefit programs.

States' Fiscal Condition

A recent survey of state fiscal conditions found that more than 30 states are currently projecting budget shortfalls in FY 2009, totaling $26 billion. This number is

growing rapidly; 35 to 40 states will ultimately face shortfalls in 2009. These states will accumulate deficits of at least $140 billion through FY 2010.

States have already acted to close the original 2009 budget deficits, but they are quickly running out of easy options to close the new 2009 deficits and the projected 2010 deficit. States are not flush – and when states face successive years of shortfalls in which deficits can't easily be rolled over, they are forced to look at cuts to important state programs like education and health care. In Arizona, for instance, we will deplete our rainy day fund in the next round of budgeting, from a high-water mark of $700 million less than two years ago — and still will have to make cuts. In short: States do not have easy options in front of them.

It's also important to note that state budgets lag behind economic downturns. During economic slumps, the fiscal conditions of states often continue to worsen even after the recession is deemed over. This will probably be the case in the next two years. We certainly expect continued state deficits into the 2011 fiscal year.

The State Role in Stimulating the Economy

In sum, the nation is looking at poor fiscal situations for the states not just this year, but well after any economic recovery has started.

But one of the most efficient mechanisms the federal government can use to speed a national recovery is to invest further in existing programs where it partners with the states. By investing resources in state programs, Congress can lessen the effects of a recession.

In October, the National Governors Association sent a letter to Speaker Pelosi, Majority Leader Boehner and leaders in the Senate to request that Congress invest in states as part of any national recovery strategy. There are two basic, but equally necessary, categories of federal-state programs with the greatest potential to assist with recovery efforts:

- Infrastructure programs with ready-to-go projects that will create new jobs; and
- Countercyclical programs where the federal government can help offset proposed budget cuts by increasing the federal share of key federal-state programs, such as Medicaid, special education, food stamps, and unemployment insurance.

Infrastructure

Investing in America's infrastructure is a course of action that is critical to our current economic recovery, will yield many long-run benefits, and is especially important to states like Arizona.

The construction industry employs 7 million people nationwide and represents over $1 trillion in economic activity. In Arizona alone, the construction industry is worth more than $34 billion. But in the past few years, the construction industry experienced

first the burst of the housing bubble, and later the credit crunch, both of which have dried up demand for construction. In Arizona, housing prices have declined 36% in the Phoenix metro area over the past few years, compared to 18% nationally. From September 2007 to September 2008, Arizona lost 38,600 construction jobs – more than 17 percent of the jobs in one industry just in a year. Arizona was one of the nation's fastest employment-growth states in the past few years – it ranked second in the nation in 2003, 2004, and 2005 – but in 2008, it is just 46th in job creation.

Clearly, this is a sector of the economy in need of a stimulus.

We need new infrastructure both for short-term stimulus and long-term economic growth. But the economic downturn has diminished states' capital budgets, while the credit crunch has resulted in less beneficial borrowing terms that inhibit states' abilities to use financing to build new infrastructure.

An infrastructure stimulus would have a quick effect on the economy. An infusion of federal infrastructure funding would stimulate the critical construction sector immediately because many infrastructure projects are already planned, and just need funding. Nationwide, 3,000 highway projects representing about $18 billion in funding could be awarded and start construction within 90 days of federal stimulus legislation; in addition, there are probably about $10 billion of ready-to-go water infrastructure projects.

Lastly, the Department of Homeland Security has identified $500 billion worth of border security projects to be completed over 10 years; that schedule could be accelerated to help create jobs now while we build the infrastructure we need.

The long-term benefits are clear: According to the U.S. Department of Transportation, every $1 in highway infrastructure investment yields $5.40 in economic benefits.

Congress should not just write a blank check, however. For assurance that a significant infrastructure package is working – and putting people to work – I recommend Congressional oversight, and provisos that states must obligate this money within a defined period, say six months. In other words, use it or lose it. I also recommend that Congress designate an ombudsman for the states within agencies like the GSA in order to help speed the construction approval process.

With infrastructure investment, Congress has a golden chance: Assist states, put people to work, and improve our nation's infrastructure for the long term. It is a win-win-win.

Medicaid

States experience economic downturns in a cascade of pressures from both ends – decreased tax revenues and increased demand for services. First, sales tax revenues decline, because reductions in personal consumption often lead off downturns. Then

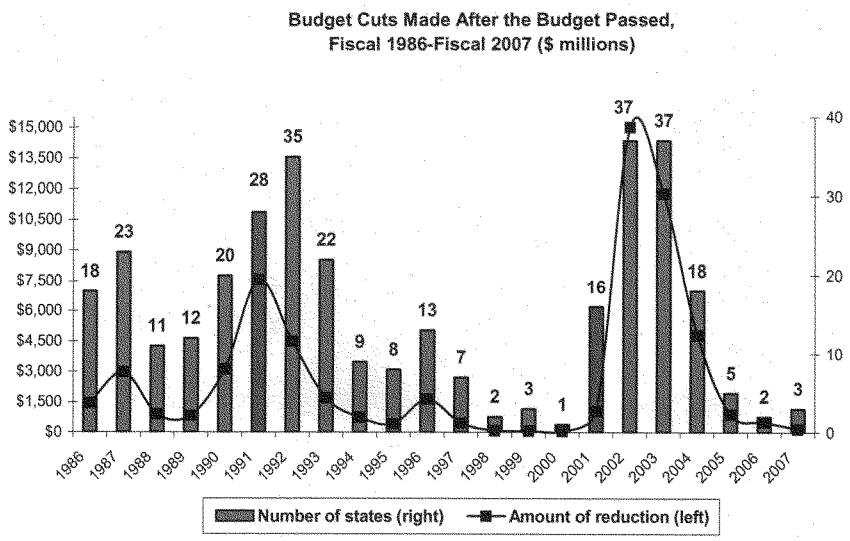
unemployment rises, which reduces personal and corporate income tax revenues. Higher unemployment then leads to increased demand for food stamps, unemployment benefits and especially Medicaid payments – which currently comprise about 23 percent of state budgets. Further Medicaid growth from women and children coming onto the rolls tends to occur even later in the cycle. And remember – 49 states must have balanced budgets.

Most states are now looking at Medicaid enrollment growth beyond what they projected. In Arizona, for instance, between August and September, we saw growth on our Medicaid rolls of more than 13,000 just in a month.

The lag effect on state budgets was evident in each of the last two recessions. The recession that ended in 1991 resulted in 28 states cutting budgets that year. But states continued to experience the recession's impact after that; in 1992, 35 states cut budgets.

Similarly, in 2001, when the most recent recession ended, 16 states cut budgets. However, 37 states cut budgets in each of the next two years — 2002 and 2003. (See Chart 1, Budget Cuts Made After the Budget Passed). If the current downturn continues and follows the path of past recessions, 35 to 40 states will face budget shortfalls in 2009, and some experts say those numbers will be more than 40 states with cumulative deficits of $140 billion by 2010.

Chart 1



One of the most effective ways to aid in a national economic recovery is temporarily to increase the Federal Medical Assistance Percentage (FMAP), or the share of the Medicaid program paid for by the federal government.

State FMAPs are recalculated each year, and the new FMAPs are applied at the start of the federal fiscal year. Small changes in a state's FMAP can have a significant impact on state budgets. Any reduction during a downturn will squeeze states to a greater degree than they already are squeezed.

Currently, the FMAP is based on a three-year rolling average, which means some states are already experiencing reductions: In federal FY 2009, which began October 1, 2008, 17 states experienced FMAP declines over their federal FY 2008 FMAP. Twelve of these states had also experienced FMAP declines in the previous fiscal year. Fourteen states are projected to have FMAP decreases in federal FY 2010, beginning October 1, 2009.

Right now, the FMAP is based on economic conditions that existed several years ago. But what states truly need is a FMAP that corresponds to what's occurring in the economy *right now*.

The 2001-02 recession forced almost every state to seek serious cutbacks in Medicaid costs. In response, Congress approved $10 billion to temporarily enhance FMAPs for every state by 2.95 percentage points for five fiscal quarters in 2003 and 2004. In addition, during the last FMAP alteration, Congress implemented a hold-harmless provision that prevented scheduled FMAP decreases for the same period.

The FMAP enhancements during the last downturn were a success. Studies conducted by the Government Accountability Office (GAO) and other experts found that temporarily increasing all states' FMAP levels provided immediate fiscal relief to states and prevented cuts to programs that residents were relying upon during the economic downturn.

Regardless of their particular form, FMAP enhancements will be most effective if they begin at the onset of an economic downturn, and last long enough for states to meet anticipated increases in Medicaid costs as long as the downturn lasts. This time around, to achieve the maximum effect, the funding should be close to half of the state shortfalls – or no less than $25-35 billion per year over the next two years.

Both the timeframe and the amount are critical. The 24-month timeframe includes the year after the recession will probably end, so it covers the lag period when state budgets will still be in deficit. And anything less than $25 billion per year for two years would limit the countercyclical effect.

The way that the House targeted this investment in the last bill is sound, providing the greatest assistance to the states in the greatest need – the ones that are feeling the effects of the economic downturn most acutely. Not all states are the same, and not all

budget deficits are created equal – the states where the deficits are worst are probably also the states most in need of the most economic stimulus.

Permanent Statutory Solution

Apart from the stimulus package, Congress should make counter-cyclical stimulus a permanent part of the Medicaid statute when it undertakes wider health care reform.

There is broad consensus that an early enough, long enough stimulus during an economic downturn can ameliorate some of the downturn's worst effects. There is also consensus that temporary FMAP increases are one of the best ways to stimulate the economy. But it gets tiresome for Congress to make legislative changes to FMAP during every recession – and it also means that effective action may not occur soon enough. Congress would have to give great care to determine the appropriate triggers for an enhanced FMAP. But building such a mechanism into the statute would save time and resources that would otherwise go to re-creating the concept during every downturn. A countercyclical FMAP would likely kick in far earlier than if Congress has to act. This would help avert state cuts when the economy is weakening. Remember the GAO said the 2002 fiscal relief was good, but came too late in the downturn.

SCHIP

I would also like to note that the current extension for SCHIP lapses on April 1, 2009, and therefore Congress needs to renew its commendable efforts to pass a full 5-year reauthorization. This is a very high priority for the nation's governors, and we do not want to see a number of short-run extensions starting on April 1, 2009. States are going to see increased demand for SCHIP and if there is one area where states must be able to move forward, it is providing children with the health care they need during difficult economic times. The best solution would be to have a complete reauthorization as part of the economic recovery package.

Conclusion

To summarize, Congress is encountering an intersection of needs that it can act decisively to address. Americans need to be able to rely on a health care safety net in difficult times. States need to balance their budgets in difficult times. The economy needs a stimulus during difficult times. Congress can address all of these needs.

Mr. Chairman, thank you again for the opportunity to appear before the subcommittee. I am happy to answer any questions.

Mr. PALLONE. Thank you, Governor. Thank you very much.

Mr. Sperling.

STATEMENT OF GENE SPERLING, SENIOR FELLOW, CENTER FOR AMERICAN PROGRESS ACTION FUND

Mr. SPERLING. I guess in the spirit of this hearing, I have to note that I was born and raised in Michigan. My family still lives there. I am a Detroit Lions fan. We are 0 and 8.

Ms. BLACKBURN. Mr. Chairman, speaking if I may——

Mr. PALLONE. Yes.

Ms. BLACKBURN. Thank you for yielding.

Mr. SPERLING. I know about Thanksgiving, Congressman.

Ms. BLACKBURN. I am so glad that you do and we welcome so many Michiganders who have moved to Spring Hill, Tennessee, the southern area of my district. They are welcomed, they are at home there, and the Spring Hill Saturn plant is doing very well, and we are converting them daily to Titan fans. I yield back.

Mr. SPERLING. Well, her undefeated team plays my winless team on Thanksgiving. The University of Michigan, which is usually our bright spot, is 3 and 7, so I am collectively 3 and 15 for the football season. I hope that will be seen as a sign of character and loyalty and not poor judgment that would make you disregard the rest of my statement.

I think we have to start with the notion that we are in a demand crisis, and I think with the headlines every day on how the TARP is working, the financial crisis, liquidity crisis, capital market crisis is all appropriate, but I think we have to have an adjustment in our thinking. We have a demand crisis, and what I mean by that is, that as important as it is to fix our capital market crisis, it will not do the trick if nobody wants to buy or spend or borrow or expand. In my professional life, I have never been more worried about a coming economic year than the next year. The overwhelming amount of spending that has happened in the last seven years has been driven off people extracting equity from their home mortgages with rising prices. That energy is depleted. It is gone. But what scares me the most is I have never seen a moment where when you look out at the private sector and the American consumer and even the global economy, I can't see where demand is coming from next year.

In October, tens of millions of American families recognized that they had taken a significant hit in their home prices, in their home wealth and their mortgage wealth. Among the tens of millions of American families having conversations around their kitchen table right now, there is only one conversation going on: what are we going to cut back on. That may make sense for every single family but if 50 million families are making that decision at once, that is going to hurt spending and the businesses who see that are going to project that and lay people off and you are going to have that downward cycle. We were hopeful before that with a weak dollar that we might get a burst from manufacturing exports to the rest of the world that would hopefully be growing. There was a little while where that looked like that might be promising. Those hopes are dashed. The dollar is up. Europe is projecting virtually no growth, all of Europe. The IMF is almost projecting a global reces-

sion, and exports in the last few months, manufacturing in the last few months has gone to some of the greatest falls we have seen. So the question is, what is going to jumpstart this economy?

I think again in my professional life, I have never seen a moment where I thought there was a greater case for a very large fiscal stimulus, and let me say, I understand that that would be subject to political tack. I understand. I understand that we have an extremely high deficit, and for 1 year that would make the deficit higher, but I don't see where else the demand is coming from, and I encourage people to put aside their preconceptions and think about what I call the Powell Doctrine approach to stimulus, to come at this with overwhelming force, because the risk of being too slow, too small, too incremental are so much greater for our people than the risks of being too bold for a year. The pain of 8 or 9 percent unemployment for a year or 2 years would be far too great for our economy and would end up hurting the deficit even worse. I think as we look forward, we need to have not only a bigger stimulus, we need to be tough on stimulus, we need to make sure that it actually measures the get out during the period that will increase demand but I think, as Governor Napolitano said, we need to probably look at a longer window. We need to make sure that we are looking at how to get demand going over probably an 18-month or even longer period. I think this also means we should be looking for those areas where those short-term investments are win-wins. They are also down payments on long-term priorities. When possible, that should be our aspiration.

Now, I believe that in that context, a significant increase in the FMAP makes an enormous amount of sense because I think that if you are trying to expand growth to have federal policies that ignore that as you are giving money with one hand, States are being forced to not only cut back on healthcare but to contract, to lay off people, to raise taxes is to have a policy that is going to lead to contraction at the State level. Increasing the FMAP is one of the quickest ways to inject demand. It helps the people who are often the innocent victims of the recession who have lost their healthcare, and I think it is one of those important things that we can do for demand and keeping States out of this, I think, very bad choice they will face, which is either to restrict the Medicaid coverage and see more people lose their healthcare, moving our country backwards, or to protect that and then have to cut back and do painful cuts or tax increases that will be harmful to the economy and their people in other ways. I believe that a very significant FMAP increase of over $35 billion is justified in this context and again I ask people to look at how risky the economy is last year and not look at this through its normal lens. I would never have been here in the previous two discussions on stimulus talking about this much. I think we are just in a very, very different situation.

I also believe that if you are doing an SCHIP expansion, that while a permanent SCHIP expansion should have offsets to ensure that it protects against the deficit going up, in the short term for the first couple of years or so, it would again make sense to do this, to waive those pay-fors so that you are getting the full stimulative effect possible.

And then finally, I would just say that I would not let any of this prevent us from going forward on universal healthcare reform that includes with it the kind of tough measures and smart measures that would help us bring down our long-term healthcare costs. I think that is the way that we can marry an increase for a year or two to help in this period of recess with a long-term strategy to not only cover all Americans but start bringing down national healthcare cost growth, which is the best way to bring down the larger cost of Medicare and Medicaid growth which is obviously our greatest long-term entitlement challenge.

Thank you.

[The prepared statement of Mr. Sperling follows:]

Statement of Gene B. Sperling
Senior Fellow for Economic Policy, Center for American Progress Action Fund
Before the House Energy and Commerce Subcommittee on Health
November 13, 2008

Chairman Pallone, Ranking Member Deal, and distinguished Members of the Subcommittee, I thank you for the opportunity to testify on the topic of economic stimulus and healthcare. I am speaking today in my role as Senior Fellow for Economic Policy at the Center for American Progress Action Fund. Previously, I served in the Clinton Administration as Deputy Director and then Director of the National Economic Council and National Economic Advisor. The ideas I am expressing here are solely my own and do not necessarily reflect those of any institutions or people whom I work with or advise.

My testimony today focuses on six main points:

1) **A Demand Crisis.** Today we must understand that in addition to a financial and capital market crisis, we face a demand crisis in the real economy both in the United States and globally.

2) **A Powell Doctrine for the Stimulus Package.** The breadth and potential depth of that demand crisis require us to undertake a bolder "Powell Doctrine" on stimulus in which $300 - $400 billion – or at least 2 percent of GDP – should be the starting point with an understanding that more could be needed and that we will need to call for a coordinated global stimulus.

3) **High Bang for the Buck for Long Duration.** The depth of the potential demand crisis requires us to enact a stimulus with a higher percentage of high-bang-for-the-buck elements than in the previous stimulus. While much of it should be fast-acting, it also should be capable of adding demand for a 12-18 month duration.

4) **Aim for More Win/Wins on Stimulus and Long-Term Priorities**. We should be looking for win/wins: places where investments can both have a strong stimulative impact and be an important down payment on major long-term priorities. We should be looking for sweet spots that can both jumpstart jobs and jumpstart the future.

5) **Triple Benefit of Addressing Health Care**. Health care initiatives can be a triple-benefit in this context. First, increases in the Federal match for Medicaid can be one of the quickest and most effective means to stimulate the economy. Second, an expansion of SCHIP can be a win/win in that it can provide stimulus while moving us forward on the path to universal coverage. Third, an upfront investment in health information technology can also provide stimulus and be a down payment on the goal of reducing long-term health care costs.

6) **A Grand Bargain on Fiscal Discipline**. While Congress and the new administration should seek to marry long term fiscal discipline with short-term stimulus, the wrong way

to do this is by simply doing less on crucial national priorities like universal health care, climate change and education. A far better way to proceed is through a "grand bargain on fiscal discipline," in which we move forward on major provisions yet do so in the context of addressing long term entitlements like Social Security and lowering health care costs.

I. **The Demand Crisis in the United States is Deepening**. From 2001-2007 sound consumer spending was driven less by wage and income gains of low and middle income families and more by people extracting wealth from their rising home values. Wages and household incomes have actually been very flat. Real average hourly wages actually declined by 19 cents from the end of the recession in December 2001 to October 2008. Real weekly wages are down $14.90 over that same period. (Real hourly wages were $18.22 an hour in October 2008 and $18.41 in December 2001; real weekly wages were $627.80 in December 2001 and $612.90 in October 2008) Median working-age household incomes have declined $2,010 from 2000-2007, after increasing $7,748 from 1993-2000.

- **Rising Home Prices—Not Wages—Fueled Spending Earlier this Decade**. Despite such disappointing wage performance, annual consumer spending growth averaged a solid 2.94 percent between 2001 and 2007 due in part to increased household debt, but most likely to the "wealth effect" of rising home prices, which grew a whopping 71.5 percent from December 2001 to their peak in July 2006. What was striking during this period was the degree to which Americans seemed to use their homes as ATMs—not simply spending a few cents more on the dollar because they felt wealthier, but participating in an explosion of mortgage equity withdrawal. Indeed, according to former Federal Reserve Chairman Alan Greenspan and Fed economist Jim Kennedy, mortgage equity withdrawal grew 800 percent, from 1 percent of GDP in 1995 to 8 percent of GDP by the fourth quarter of 2005. Even "active mortgage equity withdrawal" – the amount of home-equity extraction and cash-out refinancing that excludes equity reinvested in a new home—grew from $37 billion annualized in 1995 to $532 billion at the end of 2005, a 14-fold increase.

- **The Crisis Will Dramatically Hurt Consumer Spending:** The degree that consumer spending appeared to be based on exceptional rising home prices suggests that even if we had not faced the historic capital market crisis, there was a significant danger that a moderation or fall in home prices could have a severe impact on consumer spending as people realized they have overestimated their wealth or realized they had spent equity that they did not in fact possess. This danger to consumer spending and economic demand was only multiplied by the financial crisis and its severe impact on equities and pension wealth. Unfortunately, as we entered October tens of millions of American families were hit with the realization that both their home wealth and their pension savings had taken a major reduction. The Case-Shiller home price index is down 16 percent from a year ago, and Goldman Sachs

expects prices to decline to a total of 30 percent below year-ago levels before hitting bottom.[1] Eighteen percent of Americans are now in negative equity—with homes valued less than their outstanding mortgage debt—and another 5 percent are within five percentage points of negative equity. Some believe the percentage could go over 30 percent. As a result, net mortgage equity withdrawal fell to only $9.5 billion, or 0.3 percent of disposable personal income, in the second quarter of 2008, a decline of 96 percent from its 2004 high. Even those who held diversified wealth have seen declines. Christian Weller of the Center for American Progress found that $4.5 trillion in real household wealth was destroyed from September 2007 to June 2008.[2] Jack VanDerhei of the Employee Benefits Research Initiative has projected workers nearing retirement could replace 13.4 percentage points less of their pre-retirement income when they retire thanks to the financial crisis.[3]

- **As we look out into 2009, we face a significant demand crisis.** The signs of a demand crisis and a downward economic spiral are already present. The US economy has lost 1.2 million jobs since January and unemployment stands at 6.5 percent, a 14-year high. If the same percentage of the workforce was actively seeking work as was the case in 2001, the unemployment rate would be 7.4 percent. Retail sales declined by one percent from September 2007 to September 2008, the first year-over-year decline since 2002, and only the third decline since 1991. Absent a significant stimulus, Moody's predicts that retail sales will not turn positive until the second quarter of 2009.[4] Business spending is just as problematic; Business fixed investment increased 4.9 percent in 2007, but Goldman Sachs projects it will increase only 2.9 percent in 2008 before declining 7.6 percent in 2009. Perhaps even worse than these signs of a temporary recession is the lack of indication as to where increased demand would likely come from. For tens of millions of families who are observing a weakening labor market and dual hits to their home wealth and pension savings, there is only one conversation going on around these millions of kitchen tables: What are we going to cut back?

- **If the broad US middle class is taking understandable measures to restore their personal balance sheets, where exactly is a surge in economic demand likely to come from in 2009?** For those who have previously speculated that the spark to US growth would be a combination of a falling dollar, cheaper exports and strong demand for American products in Europe and elsewhere, those hopes have been dashed. American manufacturing exports are anemic. The Institute for Supply Management's New Export Orders index fell 11 points in October to 41, the lowest level in decades.

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[1] "GS Skinny: Home Prices." Goldman Sachs, 10/28/08
[2] Christian Weller, Testimony to House Education and Labor Committee, 10/7/08, http://www.americanprogressaction.org/issues/2008/better_retirement_plans.html
[3] Jack VanDerhei, Testimony to House Education and Labor Committee, 10/7/08, http://www.ebri.org/pdf/publications/testimony/t156.pdf
[4] "Retail Sales Tumble; No Rebound in Sight." Moody's Economy.com, 10/15/08

Without exports to prop up manufacturing, the headline ISM index fell from 50.2 in June to 38.9 in October, well below the threshold of 50 that indicates a contraction in the manufacturing sector. Those who hoped there would be a decoupling as the US economy went down have seen the opposite. The International Monetary Fund, which defines 3 percent real annual growth as the global recession threshold, now projects FY2009 growth at 3.03 percent—barely above that mark. Its outlook for European economies shows only 0.55 percent growth in 2009. Even the Chinese economy is projected to possibly see its GDP growth drop from over 10 percent this year to as little as 6 percent in FY2009.[5]

II. **A "Powell Doctrine" on Stimulus**. This demand crisis compels us to consider a stimulus that is fundamentally different than the two previous calls for stimulus in 2001-02 and 2008. In both of those earlier cases, the medicine that appeared appropriate was a quick injection of fiscal stimulus for a few months to provide a shot in the arm in the economy to increase confidence and help moderate a downward spiral. The previous stimulus packages were in the range of $150-$165 billion, or 1 percent of GDP. They were targeted to be spent out over a single year, with a larger effect in the quarters in which they were released and had a heavy focus on tax relief. We face at this moment a more severe and more potentially long-lasting crisis. In the United States and globally, demand is unlikely to come solely from the private sector without a potentially long and painful period of retrenchment.

This certainly creates painful decisions for policymakers who care about fiscal responsibility. Some estimate the deficit for FY 2009 at $750 billion to even $1 trillion even without a stimulus. Nevertheless, this is a situation where the risks of being careful, slow and moderate are far greater than the risks of moving boldly even at the expense of a higher short term deficit. I see three key design elements for this stimulus:

- **$300 - $400 Billion as the Minimum**. The risks to the US and global economy require a "Powell Doctrine" approach in which we seek to bring overwhelming stimulus force to combat a serious global recession. For the United States, the minimum that should be initially sought is $300 - $400 billion or at least 2 percent of GDP— this should be the minimum amount with the understanding that more may be necessary.[6]

- **Temporary Deficit Effect but Longer Duration**. As with previous stimulus efforts, to have an immediate demand effect without ballooning long-term deficits (thus hurting long-term growth), it is important that the stimulus be fast acting and temporary. Yet, in this case it is also important that the injection in demand will be maintained for a 12-18 month period to provide

[5] Wall Street Journal, 10/11/08; http://online.wsj.com/article/SB122634761261114745.html?mod=testMod

[6] Goldman Sachs Weekly US Analyst, 10/24/08

confidence for employers to halt further cutbacks and layoffs. Without that confidence, it could fuel a deepening downward spiral in the labor market and overall economic growth.

- **Globally Coordinated.** By leading with a strong stimulus package, the United States will increase its leverage to call upon other major global economies also to provide significant stimulus. Newspaper accounts already report that China is implementing a stimulus of more than a half a trillion dollars and industrialized nations are considering aggressive action of their own. An understanding in the global economy is that $1 - $2 trillion of simultaneous government injected demand would boost confidence.

III. **Importance of Stimulus that has a Strong Demand and Multiplier Effect**. I have previously supported and will continue to support well-fashioned tax cuts as part of economic stimulus, particularly tax cuts that go to low- and middle-income families most likely to spend them quickly. These pro-growth and progressive kinds of tax cuts help families to improve their balance sheets, increase their personal savings and boost spending. Yet it is also known that there are other forms of stimulus that can hit the economy quicker and have a higher payoff than such broadly-based tax relief. In the prior 2008 stimulus package, the tax cut portion was about 70 percent. In a $300 - $400 billion package, there could still be sizable tax cuts while the majority of the stimulus could be of the most high-impact forms of direct government investments. For example, a $75-$100 billion package of tax rebates would still allow up to two-thirds of the package to be the highest-multiplier elements that can impact demand within a 12-18 month target window.

- **Higher Mix of Most Effective Stimulus Elements.** While my purpose here today is not to spell out the exact details of the best stimulus package, there is significant evidence that certain policies will have a greater effect per dollar spent. Generally, Dimitri Papadimitriou, Greg Hannsgen and Gennaro Zezza of the Levy Institute find that well-designed government spending has an impact of 130 percent on GDP.[7] The Congressional Budget Office cites extending unemployment insurance benefits and food stamps as the most effective type of stimulus—sure-fire measures that are fast-acting and have a high bang for the buck. Mark Zandi of Moody's Economy.com published an oft-cited analysis suggesting that federal aid to states, infrastructure spending, food stamps, and extending unemployment benefits all have multiplier effects of greater than 130 percent.

IV. **Looking for Win/Win Stimulus**. Due to the magnitude of an effective stimulus in our current economic environment, there is a greater imperative to search for stimulus proposals that are win/wins – policies that are both effective stimulus

[7] Dimitri B. Papadimitriou, Greg Hannsgen and Gennaro Zezza. "Fiscal Stimulus: Is More Needed?" Levy Institute, 5/22/08; http://www.eurointelligence.com/article.581+M5309b28e442.0.html

measures and yet can also be down payments on our long term priorities. Finding this "sweet spot" is challenging but is often doable.

One of the challenges in finding the sweet spot is that some important down payments on long-term priorities may start and have a high-payout during the period of stimulus yet go on beyond it. One way to deal with this dilemma is to waive pay fors in the first year or two to ensure a strong stimulus effect, yet have provisions or an understanding that long-term extension requires off-setting savings.

- **Green Jobs and a Down Payment on a Green Infrastructure**: There has been enormous and appropriate enthusiasm and interest in a "green recovery" – the degree to which an investment in green jobs can be a strong immediate stimulus and yet still jump-start long-term energy and climate change goals. The challenge here is finding the right mix. A focus only on projects that can be started and completed within an 18 month window can produce a strong stimulus, but could be a less effective down payment than measures that might require a much longer investment. This may be a case where it would make sense to push for a down payment on crucial long-term green infrastructure investments under a framework where the first 18 months is done as pure stimulus, but where there will be off-setting savings to pay for the permanent or long-term extension of the investments. Bracken Hendricks and Benjamin Goldstein of CAPAF have a number of suggestions that could potentially achieve the win/win for green stimulus. For instance, they suggest that tripling the Energy Efficiency and Conservation Block Grant program—a $6 billion investment for one year—could provide down payments to communities for long term retrofit projects through a proven funding stream, an investment that the US Conference of Mayors estimates could be fully spent within a year. Another win/win would be accelerating investment in Smart Grid technology, which has the potential to coordinate energy production and delivery in a way that lowers costs and reduces carbon emissions. The Energy Independence and Security Act of 2007 already authorized smart grid investments; CAPAF believes that at least 1.3 billion in smart grid matching funds, research and demonstration projects could be funded immediately, with a broader investment to follow.[8][9]

- **School modernization**. Especially in urban and poor areas, modernizing schools and making them energy efficient is not only a way to move our long term priorities of saving on energy costs and improving our children's health, but it is also good stimulus. Schools have long lists of deferred maintenance

[8] Bracken Hendricks and Benjamin Goldstein. "A Strategy for Green Recovery." Center for American Progress Action Fund, November 10, 2008; http://www.americanprogressaction.org/issues/2008/pdf/green_recovery_memo.pdf

[9] Robert Pollin, et al. "Green Recovery: A Program to Create Good Jobs and Start Building a Low-Carbon Economy." Center for American Progress and UMASS-Amherst Political Economy Research Institute, September 2008.

projects—from brick repairs to window replacements—ready for approval; the Los Angeles Unified School District alone has a backlog of $5 billion in deferred repairs, according to the Economic Policy Institute. EPI's President Larry Mishel testified that the New York City school system completely spent $1 billion in only twelve months to modernize buildings in 2005 and could easily do the same today given the maintenance needs outstanding.[10] EPI suggests an investment of $20 billion to eliminate some of the long-term backlog, but also because it predicts that doing so would increase demand for materials by $6 billion and would generate 250,000 skilled jobs.[11] The Center for American Progress Action Fund has pointed out that there are already $7.25 billion in authorized but unfunded school modernization grant programs that could jumpstart the school modernization investment as soon as Congress chooses to appropriate the funds.[12] School modernization could thus be a job-creating stimulus that props up the ailing construction sector in the short term and also enhances our long-term goal of providing safe, clean and efficient schools for our kids.

- **Programs for Disadvantaged Youth.** One of our most pressing long-term goals is to help poor and disadvantaged youth to succeed in school, and to help those who have left to return to the classroom. But the infrastructure for programs such as Youth build, a Green Job Corps and summer enrichment scholarships already exists and has the capacity to deploy increases in funding quickly. Youth build, for instance, has an immediate $40 million shortfall this year that could be plugged and put toward developing a program in green construction, a down payment on the long term goal of creating green jobs.[13] Investments in successful youth empowerment and after school programs could be good stimulus, help with educational goals and help maintain strong nonprofit organizations whose giving is likely to be impacted by the economic downturn.

- **Infrastructure.** While our major infrastructure goals need to be part of the long term budget, there should be strong openness to make those projects that can be fast tracked part of the stimulus. Projects such as preventative maintenance, repairs and homeland security upgrades may be quick acting. Other projects may already be in the pipeline and can be accelerated. Where things go far beyond the period of stimulus they need to be part of a long term bill that includes offsets.

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[10] Lawrence Mishel, testimony to the Joint Economic Committee, 1/16/2008; http://www.epi.org/webfeatures/viewpoints/testimony-mishel-20080116.pdf

[11] "$20 billion in Federal investment in school infrastructure would provide major boost to education, economy." Economic Policy Institute, April 29, 2008.

[12] Bracken Hendricks and Benjamin Goldstein. "A Strategy for Green Recovery." Center for American Progress Action Fund, November 10, 2008; http://www.americanprogressaction.org/issues/2008/pdf/green_recovery_memo.pdf

[13] John Podesta, Laura Tyson and Sarah Rosen Wartell. "A Practical and Progressive Economic Stimulus and Recovery Plan." Center for American Progress Action Fund, 1/17/08.

V. **The Triple Importance of Healthcare in the Current Economic Crisis:** In recognition of the jurisdiction of this committee, I would like to focus the rest of my remarks on why health care is a win / win for stimulus and our long term priorities. I advocate a three-pronged approach: Increased FMAP payments to states, a jumpstart on the implementation of health information technology and putting a down payment on the expansion of the State Children's Health Insurance Program (SCHIP).

- **Increasing FMAP Payments is Critical.** Today, states are faced with an increasingly bad set of options on how to deal with rising demands for health care in a struggling economy. As the labor market weakens, more people lose their jobs and their health insurance, putting a greater strain on Medicaid. In 2002, MIT economist Jonathan Gruber found that every percentage point rise in the unemployment rate increases the rolls of the uninsured by 1.2 million people. The Kaiser Family Foundation and Urban Institute determined that the same percentage point increase in unemployment increases Medicaid and SCHIP demand by one million, but also causes state General Fund revenue to underperform expectations by 3-4 percent as payroll and income taxes decline. The inevitable problem, then, is that at the very time states should be spending more on Medicaid to cover these newly uninsured, they are feeling fiscal pressure instead to cut back their funding and eligibility criteria.

  Without additional federal assistance on Medicaid, states in this situation will be forced to make painful choices that will have a contractionary effect on their economies – at the exact time that stimulus is desperately needed. If states try to maintain their current Medicaid eligibility standards and take on what can add up to hundreds of thousands of additional recipients, their fiscal situation deteriorates further, causing states to pull back in other areas such as education and infrastructure or even to raise taxes. In surveying 14 state-level reports on Medicaid, the Kaiser Family Foundation concluded unequivocally that "reductions in state and federal Medicaid will lead to declines in economic activity at the state level."[14]And just as bad, if states seek to cut back on Medicaid eligibility, millions of the most hard-pressed and vulnerable Americans will be denied health care. This outcome is morally unacceptable and moves us backwards– not forward – in our nation's efforts to reach universal access to health care.

  The data coming out of the states in the current crisis shows this Medicaid squeeze scenario is only getting worse. In October, the unemployment rate jumped four tenths of a percent to 6.5 percent, a 14-year high. This news, combined with the plunging home prices I mentioned above contributed to the fact that 37 states faced FY2009 budget gaps totaling $72 billion. According

[14] "The role of Medicaid in state economies: A look at the research." Kaiser Family Foundation, April 2004. http://www.kff.org/medicaid/upload/The-Role-of-Medicaid-in-State-Economies-A-Look-at-the-Research-Policy-Brief.pdf

to Iris Lav of the Center for Budget and Policy Priorities (CBPP), "judging from the rate at which revenue is deteriorating and the history of prior recessions, the 2010 gaps are likely to be in the $100 billion range." CBPP notes that 17 states have cut or are considering cuts to low income child and family health care programs and at least 15 states are cutting care for the elderly and those with disabilities. These numbers are likely to grow over the coming months.[15]

The main fiscal mechanism the federal government has to address this health coverage vs. economic contraction dilemma is to increase the match it provides the states for the Medicaid program as a fiscal stimulus. That match rate is known as the Federal Medical Assistance Percentage (FMAP). States with lower per-capita income have a higher federal match rate than wealthier states. Temporarily increasing the FMAP becomes a powerful stimulus policy for three reasons:

1) It targets workers who have been hardest hit by an economic downturn, preventing a recession from leading to loss of health care and further devastation of families. Medicaid rolls swelled from 35.7 million in December 2001 to 41.8 million in December 2004, an increase of 17 percent. Rolls would have increased upwards of 20 percent had 1 million people not been dropped from eligibility by state Medicare plans before the 2003 FMAP stimulus.[16]

2) FMAP allows states to expand Medicaid enrollment without requiring other contractionary policies and has one of the highest multiplier effects of any form of economic stimulus. A 2004 study by Families USA found that a 2.95 percent increase in the FMAP rate would bring a return of $3.85 million in business activity for every $1 million in Medicaid investment, a multiplier of 385 percent.[17]

3) FMAP is among the quickest acting stimulus possible. As Gruber found, Medicaid demand is highly responsive to the unemployment rate, so economic downturns show up very quickly in the form of Medicaid applications. Medicaid spending is calculated on a monthly basis so, in terms of logistics, a stimulus program could get up and running very quickly.

In light of the demand crisis our economy is likely to face in 2009 and even into 2010, the projections of rising unemployment and the need for bold, fast-acting

[15] Elizabeth McNichol and Iris Lav. "State Budget Troubles Worsen." Center on Budget and Policy Priorities, 10/24/08.
[16] Iris Lav, testimony to House Budget Committee, 10/20/08. Data from Kaiser Family Foundation State Health Facts
[17] "Medicaid: An important part of a stimulus package." Families USA, 1/28/08; http://www.familiesusa.org/assets/pdfs/medicaid-coalition-stuff/families-fmap-economic-stimulus-jan-28_1.pdf

and high bang-for-the buck stimulus, there is a compelling case for a major one-time increase in FMAP to stimulate the economy, prevent backward movement on our long-term goal of universal coverage and to prevent unnecessary suffering by hard-working families. In this light, the $10 billion FMAP increase seen in 2003 appears to be highly inadequate. I believe – depending on the size of additional state fiscal relief – that an FMAP increase in the range of $35-50 billion will be required over the next 12-18 months. Indeed, Lav testified that $30 - $35 billion in increased FMAP payments—along with a ban on states reducing Medicaid eligibility—is needed to prevent an additional 4 million Americans from becoming uninsured. Perhaps we should analyze how FMAP could, in the future, be structured to serve more as an automatic stabilizer, but for now we need a strong FMAP increase to be part of a broader $300 - $400 billion or more stimulus package. As my colleague Jeanne Lambrew explained, "Medicaid is the largest source and the best conduit of federal funds to states. Maintaining state spending is key to preventing a deep recession. Medicaid not only supplies the greatest amount of federal funding to states, but sustains state spending since it is a matching program. The federal matching rate in Medicaid can also be adjusted quickly: an increase can occur immediately, and can be turned off when the need subsides."[18]

- **An SCHIP Expansion Would Be an Important "Win/Win"for Stimulus and Putting a Downpayment on Long-Term Health Priorities.** Expansion of the State Children's Health Insurance Program (SCHIP) presents a win/win scenario in terms of providing strong stimulus while also providing a down payment on a long-term priority: universal coverage, starting with all children. Like FMAP, SCHIP funds can go out quickly and be spent by states that already have programs in place. All federal appropriations for SCHIP expire in March 2009, so this will be an issue the Congress is forced to address or risk eliminating coverage for over 7 million children. Indeed, an increase in the federal FMAP match will not be as effective unless there are additional funds provided for SCHIP.

  The struggle to pass an SCHIP reauthorization with important expansions and incentives for states to enroll more eligible children such as so-called "Express Lane" enrollment, relaxed documentation requirements and enhanced outreach grants has been frustrated in recent years by Presidential vetoes and threats of vetoes, as well as the White House guidance in August 2008 that stopped a number of state expansions from going forward. I know that as we speak there are significant discussions going on over how to extend and expand SCHIP to cover the increased demand for health coverage that our current economic recession will bring. As the health community and this Committee structure the exact package, I would recommend the following: One, while long-term and permanent expansions require appropriate off-setting savings, there is a strong

[18] Jeanne Lambrew, "Healthy Stimulus." Center for American Progress 1/28/08; http://www.americanprogress.org/issues/2008/01/healthy_stimulus.html

case to be made on stimulus grounds for waiving the off-sets for about the first couple of years of the reauthorization when the economy would still be in a slow-growth period. Two, it would make sense to seek an expansion of outreach efforts during the period of economic downturn. Doing so would put thousands of people to work at a time of economic weakness, while also laying the foundation and infrastructure needed for achievement of our moral imperative to ensure universal coverage for all children – and hopefully for all Americans of any age. While President Obama works with the Congress on a comprehensive health care bill, boosting SCHIP can be a temporary and well-targeted stimulus plan, prevent millions of children from losing coverage they already have and move us closer to achieving universal coverage.

- **Investigating One-Time Health Information Technology as a Stimulus:** There is wide agreement coming from leaders ranging from Congress and the new Administration to the Business Roundtable that major advances could be made on our economic and fiscal imperative to lower the rapid growth in health care costs through a one-time implementation of advanced information technology in our hospitals and doctors' offices. Implementing advanced health IT will be a large one-time cost to bring healthcare into the 21st Century. The Rand Corporation conservatively estimates savings of $77 billion per year if most hospitals and doctors' offices adopt health IT, reducing unnecessary hospital stays, eliminating wasted time on paperwork, and efficiently allocating drugs.[19] The Business Roundtable estimated the savings to be $165 billion per year, or about $2,200 for a typical family. Administration and Congressional policymakers should undertake an immediate investigation of the viability of implementing a portion of the health information technology quickly over the next 12-18 months. If there is a possibility for such quick action, this could fit into the win/win area of investments that can both jumpstart jobs and jumpstart creating the health and fiscal future we aspire to.

VI. Final Note: Universal Health Care Reform as Part of a Fiscal Discipline "Grand Bargain." Some have recently questioned whether, in light of the high deficit and large stimulus needed to revitalize economic growth, we can afford to move forward on major universal health care legislation. I believe this is the wrong perspective.

- **Cost of Inaction is Too High:** Rather than seeing a movement toward health care reform to cover all Americans, improve quality, and bring down the growth of health care costs as an expensive luxury to be deferred, I believe the largest cost would be the cost of inaction. Not only does inaction delay us from our moral imperative as a nation to ensure health care to all of our people, but it allows a status-quo to remain in place that is hurting our

[19] Richard Hillestad, James Bigelow, Anthony Bower, Federico Girosi, Robin Meili, Richard Scoville, and Roger Taylor, "Can Electronic Medical Record Systems Transform Health Care? Potential Health Benefits, Savings, And Costs," *Health Affairs*, September/October 2005; 24(5): 1103-1117

competitiveness and leading to high growth in our long-term entitlement bill concerning health care. It makes no sense from an economic perspective to allow our national health care bill to remain exceedingly large and growing simply because the steps to greater national efficiency require a temporary shifting of some costs for the uninsured to the public ledger. The serious reforms that can only take place with a major health coverage bill – reducing cost-shifting while expanding prevention measures, chronic care management, health information technology and eliminating the tens of billions of dollars spent on excluding and discriminating against those with pre-existing conditions – are among the measures most needed to reduce the growth of health care costs, which are also driving our largest long-term entitlement challenges concerning Medicare.

- **A Grand Bargain on Fiscal Discipline: Do More, Not Less, On The Nation's Long-Term Priorities.** Rather than responding to the large deficits the new President will inherit by pushing only for incremental change, the "grand bargain on fiscal discipline" should be to go forward with bold efforts on stimulus, universal health care and climate change. Those concerned about our long-term fiscal future should not call for abandoning plans for universal health care, but rather for ensuring it is done in a way that is effective in lowering the growth of health care costs. And with the partial privatization of Social Security dead and buried, there could be a new opening for a Social Security reform plan that is progressive, does more for widows and other elderly women, locks-in Social Security as a rock-solid guaranteed benefit, and is part of a package that includes a universal 401K as well as defined benefit plan protections.

  This grand bargain would mean that we seek to marry stimulus and long-term priorities with fiscal discipline not by seeking less bold change, but more.

Mr. PALLONE. Thank you really for your testimony, and I am going to have some follow-up questions later specifically on some of the points you mentioned.

I think your name is actually spelled wrong there. It is Zolotorow?

Mr. ZOLOTOROW. Zolotorow, Z-o-l-o-t-o-r-o-w.

Mr. PALLONE. Oh, so it is correct there.

Mr. ZOLOTOROW. It is right there.

Mr. PALLONE. All right. Thanks. I recognize you for an opening statement. Thank you for being here.

STATEMENT OF CRAIG ZOLOTOROW, MEDICAID BENEFICIARY

Mr. ZOLOTOROW. Good morning and thank you to Chairman Pallone, Ranking Member Deal and members of the subcommittee for having this hearing and for inviting me to speak to you today. I come before this committee as a proud and grateful enrollee in Maryland's Medicaid program. I am a student at Howard Community College. Right now I am only taking one class but I also work at the school newspaper as an advertising manager, copy editor and staff writer. I hope to major in journalism so that one day I can work for the Washington Post or for the Baltimore Sun. Medicaid has been a lifesaving program for me, allowing me access to critical healthcare services that my family would not otherwise have been able to afford. I am here today to ask you to help States preserve Medicaid coverage for the millions of people like me in this country who rely on it daily.

I did not always rely on Medicaid. Until the age of 12, I had family health insurance coverage through my mother's employer, and thank goodness I did. My numerous chronic illnesses started in 1987 with the diagnosis at age 2 of common variable immunodeficiency, which is a mild form of the "boy in the bubble" syndrome, causing continuing serious viral infections. In 1995 at age 10, I was diagnosed with Hodgkin's lymphoma. I am now a proud 13-year cancer survivor. Because of my diagnoses, my family faced $50,000 in medical bills, which is 20 percent of medical bills totaling $250,000, and our family income, I became eligible for SSI, which automatically made me eligible for Medicaid.

In 1997, 2 years after cancer treatment, I reached my lifetime maximum of $250,000 on my mother's health insurance, so I became reliant on Medicaid to cover the costs of chronic sinusitis, which required two surgeries, meningitis, three grand mal seizures, a life-threatening adrenocorticotropic, or ACTH endocrine deficiency, hypothyroid, anorexia, bipolar disorder, Asperger's syndrome, colitis, growth hormone deficiency, hypertension, anemia, renal disease, nephrogenic diabetes insipidus, and fevers of up to 105 degrees. With this many chronic conditions, it was essential that I receive ongoing medical attention. Luckily, my Medicaid coverage in Maryland allowed me to receive the care I needed to cope with my health challenges.

Unfortunately, individual insurance is not accessible to somebody like me who is disabled because of various health problems. These plans simply do not offer coverage to someone with healthcare issues as extensive and expensive as mine. And even if I am lucky enough to reach my dream and work for a big newspaper, em-

ployer-sponsored coverage will probably not be enough. Just as I reached my lifetime limit on my mother's employer-based coverage, I would likely quickly reach the limit on any coverage I receive through a future employer or be denied coverage due to preexisting conditions. Luckily, my Medicaid coverage in Maryland allowed me to receive the care I needed to cope with my health challenges. Medicaid is an irreplaceable lifeline for me.

Given all my diagnoses and the treatment that I needed, I don't know what I would have done without Medicaid. During my cancer chemotherapy in 1995, while still on my mother's employee insurance, I was discharged from the hospital after a 1-week stay. I returned just 5 hours later with a fever of 104. The insurance company had refused to pay for any more days for that hospitalization. Medicaid never discharged me before my medical team felt it was appropriate. Instead, I was able to get the medically necessary care I needed.

Medicaid will be covering my treatment for occupational and physical therapy. As a child, I never had the opportunity to just go out and play and build up my muscles like the other kids in the neighborhood did. The muscles in my hands are so weak that I cannot type as much as I should for school or in the future for work. I started college this fall and hope these therapies will increase my stamina and help me sustain the rigors of college and pursue a future career. In many States I would be in danger of losing access to these important services and that would put me at a severe disadvantage both in terms of my education and my future career prospects.

As Congress considers how to protect Medicaid in these tough economic times, I hope you will think of the millions of people like me who rely on Medicaid and can see their lives significantly harmed if we are unable to receive the care we need through this important program. Now is the time for Congress to increase federal support for Medicaid to prevent States from making any further cuts.

Thank you.

[The prepared statement of Mr. Zolotorow follows:]

STATEMENT OF CRAIG ZOLOTOROW

Good morning, and thank you to Chairman Pallone, Ranking Member Deal, and members of the Subcommittee for having this hearing and for inviting me to speak to you today. I come before this committee as a proud and grateful enrollee in Maryland's Medicaid program. I am a student at Howard Community College. Right now I am only taking one class but I also work at the school newspaper as an advertising manager, copy editor, and staff writer. I hope to major in journalism so that one day I can work for the Washington Post or the Baltimore Sun. Medicaid has been a life-saving program for me, allowing me access to critical health care services that my family would not otherwise have been able to afford. I am here today to ask you to help states preserve Medicaid coverage for the millions of people like me in this country who rely on it every day.

I did not always rely on Medicaid. Until the age of 12, I had family health insurance coverage through my mother's employer. And thank goodness I did. My numerous chronic illnesses started in 1987 with the diagnosis, at age 2, of Common Variable Immunodeficiency, a mild form of the "Boy in the Bubble" Syndrome, causing continuing serious viral infections. In 1995, at age 10, I was diagnosed with Hodgkins Lymphoma. I am now a proud 13 year cancer survivor. Because of my diagnoses—my family faced $50,000 in medical bills (20 percent of medical bills totaling

$250,000)—and our family income, I became eligible for SSI, which automatically made me eligible for Medicaid.

In 1997, two years after cancer treatment, I reached my lifetime maximum of $250,000 on my mother's health insurance, so I became reliant on Medicaid to cover the costs of: Chronic Sinusitis (requiring two surgeries), Meningitis, three Grand Mal Seizures, ACTH Deficiency, Hypothyroid, Anorexia, Bipolar Disorder, Asperger Syndrome, Colitis, Growth Hormone Deficiency, Hypertention, Anemia, Renal Disease, Nephrogenic Diabetes Insipidus and fevers up to 105 degrees. With this many chronic conditions, it was essential that I receive ongoing medical attention.

Unfortunately, individual insurance is not accessible to someone like me, who is disabled because of various health problems. These plans simply do not offer coverage to someone with health care needs as extensive—and expensive—as mine. And even if I am lucky enough to reach my dream and work for a big newspaper, employer sponsored coverage will probably not be enough. Just as I reached my lifetime limit one my mother's employer based coverage, I would likely quickly reach the limit on any coverage I receive through a future employer. Luckily, my Medicaid coverage in Maryland allowed me to receive the care I needed to cope with my health challenges. Medicaid is an irreplaceable lifeline for me.

Given all of my diagnoses and the treatment that I needed, I don't know what I would have done without Medicaid. I have been followed by 12 different specialists at the Johns Hopkins Children's Center and now in adult medicine for 20 years. During my cancer chemotherapy in 1995 while still on my mother's employee insurance I was discharged after a one-week hospital stay. I returned just 5 hours later with a fever of 104. The insurance company had refused to pay for any more days for that hospitalization. Medicaid never discharged me before my medical team felt it was appropriate, instead I was able to get the medically necessary care I needed.

Medicaid will be covering my treatment for Occupational and Physical Therapy. As a child, I never had the opportunity to just go out and play and build up my muscles like other kids in the neighborhood. The muscles in my hands are so weak that I cannot type as much as I should for school or, in the future, for work. I started college this fall and hope these therapies will increase my stamina and help me sustain the rigors of college and pursue a future career. In many states, I would be in danger of losing access to these important services, and that would put me at a severe disadvantage both in terms of my education and my future career prospects.

Some services-including physical and occupational therapy as well as prescription drugs, dental services, and other important benefits-are optional under Medicaid. That is, although states must provide Medicaid to certain people, there are certain benefits they are not required to offer or that they can cut. Because states are facing such dramatic revenue declines and budget shortfalls in the coming year, many have enacted or are considering cuts to Medicaid, including to these so-called "optional services" that people like me rely on.

Medicaid is an excellent program that provides excellent medical care to the most vulnerable Americans. It needs to be protected, particularly now when many states might be looking to make cuts. If my state cut had to cut Medicaid, I would be at risk of losing critical health care services that help me live, and that will allow me to achieve my potential and lead a productive life.

As Congress considers how to protect Medicaid in these tough economic times, I hope you will think of the millions of people like me who rely on Medicaid and could see their lives significantly harmed if we are unable to receive the care we need through this important program. Now is the time for Congress to increase federal support for Medicaid to prevent states from making any further cuts.

Mr. PALLONE. Thank you.

Mr. Pinard.

STATEMENT OF RAYMOND E. PINARD, PRESIDENT AND CHIEF EXECUTIVE OFFICER, 48HOURPRINT

Mr. PINARD. Good morning, Chairman Pallone, Ranking Member Burgess and the committee. I am Ray Pinard, president and CEO for 48HourPrint.com, an 85-employee small business specializing in online commercial printing. We are headquartered in Boston and have state-of-the-art print shop facilities located in Cleveland and Phoenix. Because we are a multi-state operation, I am not taking

a position today on endorsing any one particular football team. I am also here on behalf of the U.S. Chamber of Commerce and serve as a member of its board of directors and Council on Small Business and Corporate Leadership Advisory Council.

I believe the best way to treat an ailing economy and to protect healthcare coverage is for Congress to incentivize private sector job creation by providing tax cuts for businesses and making commonsense changes to the healthcare system that will help contain costs and promote small business pooling so more of those jobs will include healthcare as a benefit.

At 48HourPrint.com, we responded to the tax incentives provided by the first stimulus package by jumpstarting spending on capital equipment. We purchased a 40-inch offset printing press at a cost of $2.25 million. The bonus depreciation provision for the stimulus package resulted in $300,000 of bonus depreciation in 2008, which we are able to plow back into further capital equipment and providing jobs. This purchase could have been delayed to a future date but the investment incentives provided by the stimulus package made this purchase possible in 2008. Taxes do matter. Low taxes and incentives like these have helped me grow my business and provide 85 well-paying jobs with healthcare benefits in the 5 short years that we have been operating. I think also when we look at healthcare benefits, we should look at benefit packages as a whole. We also provide healthcare insurance, we provide dental insurance, we provide life insurance, we provide short-term and long-term disability insurance, and we also provide a $10,000-a-year educational stipend for any employee who wants to go to college. For companies our size, I think this is a tremendous benefit package.

48HourPrint.com's story of utilizing the tax incentives provided by the first economic stimulus bill is just one example that represents thousands of similar actions taken by small businesses throughout the United States to invest in their companies. My decision and the decisions of many other business owners to make capital investments in our companies are directly the result of the tax incentives in the first stimulus package. As Congress moves forward in its consideration of a possible new stimulus plan, I would strongly encourage you to be mindful of this reality.

I understand that Congress is facing very difficult decisions on what items to include in the second stimulus package. I am here to tell you today that the best way to protect healthcare benefits and to reduce healthcare costs incurred by States is to provide incentives for the private sector to create jobs. Creating private sector jobs is a win-win scenario for everyone: the employee, the employer and the government. As an employer, I feel that you will get more bang for the buck by considering a second round of tax incentives crafted for small businesses to invest and expand. This would further encourage employers to do what they do best: grow our businesses and create jobs. And as you know, most of the job creation in America is done by small- and mid-sized businesses with 80 percent of net new jobs being created by businesses with less than 500 employees. In my written testimony, you will find a list of suggested tax incentives.

One of the most basic elements to fostering economic prosperity is creating a private sector job and there is nothing more rewarding

to an employer than to be able to accompany that job with private sector healthcare benefits. If Congress could couple the tax incentives I have suggested with some commonsense healthcare reforms, not only would States have more money flowing into their coffers through increases in payroll rosters and resulting revenues but by making it easier for employers to provide healthcare benefits, they will also experience less need for Medicaid funding by reducing the rolls of the uninsured.

Small businesses need more options to choose from when purchasing health insurance and a free enterprise system should ensure that affordable healthcare is available to everyone. A small business should not be penalized for its lack of size or diversity of workforce. Every small business owner I know wants to offer affordable, dependable health insurance to our employees and we need the type of flexibility that will keep up competitive in our respective marketplaces. To ensure this, we call upon Congress to help.

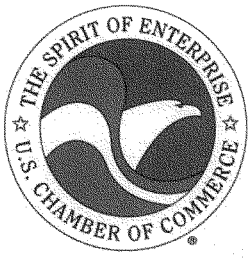
With regard to a comment made by Congressman Burgess in his opening remarks, for years the chamber and businesses like mine have pushed for legislation that would provide relief by letting small businesses pool together across State lines to provide cost-effective and accessible insurance through trade and professional associations. In our situation, because we operate in three States and we offer three levels of medical coverage to our employees, we essentially offer nine different plans. It would be much easier if we could deal in our case with the printing industry and offer three different plans that span across all 50 States. By being part of a larger group, small businesses would have greater negotiating power and would also reduce costs by having uniform standards from State to State. The Congressional Budget Office has found that allowing this would cost nothing and in fact save money for the government while helping more Americans get insurance.

Mr. PALLONE. Mr. Pinard, I just wanted to point out, you are a minute over so if you could kind of wrap it up?

Mr. PINARD. In conclusion, being in the printing industry, I am very proud to quote one of the world's most famous printers, founding father Benjamin Franklin. He once said, "Watch the pennies and the dollars will take care of themselves." I cite this quote knowing full well that in discussing tax policies and possible stimulus ideas, you may be considering a package with a price tag in the billions, which is hardly pennies. But Franklin's message does resonate in the sense that if Congress acts wisely in how it handles the pennies through reasonable tax incentives and commonsense market-based healthcare reforms, the ensuing investment and economic growth, the tax dollars generated by businesses across our Nation will be exponential.

Thank you for this opportunity and I would be happy to answer any questions.

[The prepared statement of Mr. Pinard follows:]



Statement of the U.S. Chamber of Commerce

ON: **Hearing: "Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research"**

TO: **THE HOUSE COMMITTEE ON ENERGY AND COMMERCE, SUBCOMMITTEE ON HEALTH**

DATE: **November 13, 2008**

The Chamber's mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector, and region.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance – is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 105 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Statement on
"Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research"
Hearing before the
THE HOUSE COMMITTEE ON ENERGY AND COMMERCE
SUBCOMMITTEE ON HEALTH
on behalf of the
U.S. CHAMBER OF COMMERCE
by
Raymond Pinard
President & CEO
48HourPrint.com
November 13, 2008

Chairman Pallone and Ranking Member Deal, members of the Committee, I am Ray Pinard, President and Chief Executive Officer of 48HourPrint.com, an 85 employee small business specializing in on-line business to business commercial printing. We are headquartered in Boston, Massachusetts and have state-of-the-art print shop facilities located in Cleveland, Ohio and Phoenix, Arizona. I am pleased to be able to submit the following testimony for the record. I am also here on behalf of the U.S. Chamber of Commerce and serve as a member of its Council on Small Business and Corporate Leadership Advisory Council. The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector and region. Over ninety-six percent of the Chamber members are small businesses with fewer than 100 employees. I commend the Committee for its interest in holding this hearing on reviving our economy and for acknowledging the challenges facing small and mid-size businesses in the United States.

Company Background

48HourPrint.com was launched in July 2003. While headquartered in Boston, Massachusetts, we opened a facility in Cleveland, Ohio in 2004, and a facility in Phoenix, Arizona in 2006, allowing us to have coast-to-coast coverage. According to *Printing Impressions*, which provides the industry's most comprehensive ranking of the leading printing companies, we ranked as the 219th largest printer in 2007 in the United States out of approximately 30,000 print shops nationwide.

Since its inception, 48HourPrint.com has grown and positioned itself as the leading business-to-business online printing company in the nation. We are 100% internet based, and have built our reputation by delivering the business quality printing that businesses need, with fair pricing and guaranteed turnaround. We strive to deliver 100% customer satisfaction, and are committed to ensuring that the needs of our customers are the driving force behind every decision we make.

At 48HourPrint.com, we know how critical it is for businesses to receive their printed materials on time. We are the only print company to offer 48 hour turnaround on all of our products. On September 1, 2005, we took this pledge one step further and made it our guarantee. 48hourprint.com guarantees that we will ship a customer's print order within 48 hours of the time they approve their proof or their order is free.

In 2007, we completely reengineered our ordering and check out process, making it more intuitive and easier to order the products our customers need. We employ the latest in printing technology and proprietary software utilities, all focused on providing our clients with the tools they need to reach their business goals. Our company was built on innovation and creativity and it is going to continue to grow based on those very same ideals. We are excited about our future and what it means for our employees and our customers.

Stimulus I & 48HourPrint.com

While the National Bureau of Economic Research has yet to officially label the U.S. economy as in recession, we are clearly in very trying economic times. With the unwinding of the housing market, a severe liquidity crisis, and the general deleveraging of the financial markets, many pundits would say that the economy has succumbed and already entered into a recession. The weakened economy threatens to slow further, making credit even less accessible to Main Street businesses.

The overarching concern I have, which is shared by many business owners across our nation, is that this downturn will potentially last longer and run much deeper than either of the last two. Before turning to a discussion of what I believe are the best ways to stimulate the economy moving forward, I want to first review the bipartisan action taken earlier this year by Congress and the Administration to revive the economy and its real world implications for my business.

In February 2008, Congress approved and the President signed the Economic Stimulus Act of 2008, a $168 billion package to help the flagging U.S. economy. This stimulus bill focused primarily on increasing consumption and investment. The bill provided a tax rebate to individual taxpayers with the goal of increasing consumption while another key component of the legislation was encouraging businesses to make investments through tax incentives. This was achieved by increasing the Section 179 expensing limit to $250,000 and providing 50 percent bonus depreciation for capital investments made in 2008.

At 48HourPrint.com, we responded to the tax incentives in the first stimulus by jump starting spending on capital equipment. We purchased a 40-inch offset sheet-fed printing press at a cost of $2.25 million including installation. The bonus depreciation provision of the stimulus package resulted in $300,000 of bonus depreciation in 2008 for our company. This was a purchase that could and very likely would have waited until a

future date, but the investment incentives provided by the stimulus package made this purchase possible in 2008.

The increased technological advantage from the new press will afford our company additional capacity and throughput, which are very necessary in meeting our customers' demands for a 48 hour turnaround time. We have also purchased another, smaller, printing press and are considering adding a line of digital presses, allowing us to move into entirely new markets.

48HourPrint.com's story of utilizing the tax incentives provided by the first economic stimulus bill is just one example that represents thousands of similar actions taken by small businesses throughout the U.S. to invest in their companies, expand operations and create jobs. During a meeting at the White House in April 2008, I heard first-hand about fellow Chamber members' plans to use the tax incentives. These included the President of a heavy equipment manufacturer in Texas who decided to purchase new forklifts and machine tools; the CEO of a Virginia company that designs web-based educational products who purchased new computers and related equipment; and the President of a Minnesota-based precision machining company who purchased a robot, a grinder, a machining center and an advanced system for quality measurement.

My decision and the decisions of these and many other business owners to make capital investments in our companies are directly the result of the tax incentives in the first stimulus package. As Congress moves forward in its consideration of a possible new stimulus plan, I would strongly encourage you to be mindful of these examples which underscore the importance of providing incentives to businesses to invest, grow and create jobs and become more competitive in the short-term and beyond.

Efforts to Revive the Economy Moving Forward

I understand that Congress is again facing very difficult decisions on what items to include in a possible second stimulus package in order to revive our sluggish economy. I am here to tell you today that the best way to protect health care benefits and reduce health care costs incurred by states is to provide incentives for the private sector to create jobs. Creating private sector jobs is a win-win scenario for everyone – the employer, the employee and the government. I am also aware that some of the proposals you are entertaining are helping states with their Medicaid obligations or providing additional funding to NIH for research. While these are interesting proposals, as an employer I feel that you will get more bang-for-the-buck by considering a second round of tax incentives crafted for small businesses to invest and expand instead. This would further encourage employers to do what we do best—grow our businesses and create jobs. In addition, if Congress could couple this with some common sense health care reforms, such as reducing insurance mandates and allowing for association health plans across state borders, not only would states have more money flowing into their coffers through increases in payroll rosters and the resulting revenues, but by making it easier for employers to provide health care benefits, they will also experience less need for Medicaid funding by reducing the uninsured rosters.

One of the most basic elements to fostering economic prosperity is creating a private sector job, and there is nothing more rewarding for an employer than to be able to afford to accompany that job with a private sector health care benefit. Most of the job creation in America is done by small and mid-size businesses with 80 percent of net new jobs being created by businesses with less than 500 employees. These businesses truly are the backbone of our nation's economy and, therefore, must be a top priority for lawmakers. It is imperative that Congress incorporate measures into any legislation that will further incentivize business owners, like me, to expand and invest in our companies and our employees while also recognizing challenges to our long-term competitiveness. As an employer I must be empowered by Congress to be part of the solution.

Tax Incentives to Stimulate Job Growth and Investment

1. Federal Individual Income Tax Rates

48HourPrint.com is a privately owned business organized as a Subchapter S Corporation for federal income tax purposes. This means that 48HourPrint.com's profits are not taxed at the corporate level, but instead are passed through to our shareholders who must then report the income (or loss) on their own individual income tax returns. While I and our shareholders pay personal income taxes on 48HourPrint.com's profits, the reality is that only a portion of the income generated by the business actually makes its way to our personal bank accounts. Much of that income we are being taxed on is actually reinvested in our company in the form of new equipment and technologies.

Raising or lowering the individual federal income tax rates directly impacts the cost of capital for small and mid-size business formed as "pass through" entities. Currently, for every dollar of income 48HourPrint.com realizes, approximately 40 cents goes to pay income taxes. If Congress were to raise the individual income tax rates, capital would cost more and we, and business owners like us, would have less money to invest in our companies. In contrast, by keeping taxes low small and mid-size businesses can invest and grow and have greater ability to create jobs and help expand our economy.

As you conclude the 110th Congress and look to the 111th, I recommend that Congress make permanent the existing federal individual income tax rates for small business owners as an avenue to create more investment in their businesses. I would also urge Congress not to raise these rates or allow these rates to increase, including the higher brackets with current rates of 35 percent and 33 percent. As I have highlighted, doing so would increase the cost of capital, diminish investment opportunities and ultimately make small businesses less competitive, thus hamstringing job creation and leaving our nation less prosperous.

2. Research and Development (R&D) Tax Credit

As the President and CEO of 48HourPrint.com, one of my most important duties is to think strategically and evaluate how best to respond to the challenges facing our

economy and our industry. We have become an industry leader by leveraging and investing in technology. It is clear to me that growth in today's knowledge-driven global economy is increasingly driven by innovation. Often times this innovation is directly born of business investments in research.

Innovative ideas come to fruition when businesses of all sizes in America make a strong commitment to invest in research and development. And there can be no doubt that this innovation process is critical to our nation's continued future prosperity as it sparks additional capital investment, job creation and spillover activities in other industries.

We need a tax policy that fully supports the critical nature of R&D. Far too often, the R&D tax credit has lapsed making it necessary to retroactively extend it, detracting from the stability of the benefit. Lapses and retroactive extensions of this crucial tax credit leave businesses in uncertain circumstances and make it difficult to effectively develop their research budgets and plans. R&D projects are rarely "stop and go" and the tax credit should not be either.

Congress and the next Administration need to make the R&D tax credit permanent to provide stability and enhance its incentive value since businesses could reliably count on it for multiyear projects. A permanent R&D tax credit will empower companies to bring to the marketplace more products and services, increase employment and raise the standard of living in our nation. Failing to address this issue only increases the likelihood that businesses will locate R&D facilities and the high-paying jobs associated with them in other countries with friendlier, more stable tax policies.

3. Important Short-Term Tax Provisions

In the short-term, I recommend that Congress consider including, in any new stimulus legislation, provisions such as the following, which I believe would have an immediate positive impact on the economy:

- Extending bonus depreciation and increased §179 expensing provisions, and adopting a temporary investment tax credit would promote investment during the current economic downturn and would stretch scarce capital by lowering the cost of undertaking new investment.
- Reducing the corporate capital gains rate to 15% would unlock appreciated assets held by companies, generating substantial tax revenues and at the same time providing much needed capital that could be redeployed more efficiently into the economy.
- Extending the reduced tax rate on dividends and capital gains would give taxpayers greater incentives to save and invest, which will add to our capital stock and increase productivity.
- Extending the carryback period from two years to five years would enhance the liquidity of businesses with current losses.

- Issuing rebate checks which would infuse cash into the economy, putting money in workers' pockets and stimulating consumption.

Stimulating More Small Business Health Care Participation

I am proud of the 85 jobs we have created over the last five years and the benefits that I have been able to offer our employees. 48 HourPrint.com offers its employees health insurance, life insurance, long-term and short-term disability. We provide our employees a $10,000/yr stipend to pursue college or trade related education. We also provide dental benefits. Even in an environment in which health care costs have increased dramatically, we have been able to split the costs of some of these benefits with our employees.

But small business owners need more options to choose from when purchasing health insurance, and the free enterprise system should ensure that affordable health care is available to everyone. A small business should not be penalized for its lack of size or its diversity of workforce. Every small business owner I know wants to offer affordable, dependable health insurance to our employees, and we need the type of flexibility that will keep us competitive in our respective marketplaces. To ensure this, we call upon Congress to help.

For years the Chamber and businesses like mine have pushed for legislation that would provide relief by letting small businesses pool together – across state lines – to provide cost effective and accessible insurance through trade and professional associations. By being part of a larger group, small businesses would have greater negotiating power and would also reduce costs by having uniform standards from state to state. The Congressional Budget Office has found that allowing this would cost nothing and in fact save money for the government, while helping more Americans get health insurance. Many in Congress support allowing Medicare to negotiate the price of prescription drugs – why not support allowing small businesses to really negotiate with insurance companies?

Another proposal with merit would be to create a national market for health insurance that would allow employers and individuals to buy insurance from a state other than their own, which would help with unnecessary state mandates and regulation. Small businesses need the freedom to purchase plans that meet their employees' needs, which means fewer mandates, less bureaucracy, and more flexibility. Employees at a print shop need very different insurance options than perhaps a landscaping or construction business would need; one-size-fits-all and "minimum benefits packages" just cannot work. I also want to mention a newly introduced proposal called the "Small Business Cooperatives for Healthcare Options to Improve Coverage for Employees Act of 2008 (CHOICE)." The CHOICE Act provides a new approach by using a reinsurance concept to spread risk, lower premium volatility, protect the solvency of primary insurers, and help control costs for small businesses.

Congress should also consider proposals that would provide tax credits to small businesses to help them provide insurance. Another positive step Congress could take would be to level the playing field for individuals and the self-employed by giving them deductibility of health insurance premiums. Congress can also take a look at improving Health Savings Accounts, to which more than 6 million Americans have already subscribed. Giving more flexibility to funding and using these accounts will make the products, which are an affordable alternative to traditional PPO plans, more attractive to employers and employees. I am also supportive of legislation that would amend the Internal Revenue Code to allow small businesses to set up simple cafeteria plans to provide nontaxable employee benefits to their employees, to make changes in the requirements for cafeteria plans, flexible spending accounts, and benefits provided under such plans or accounts.

Lastly, I encourage Congress to take note of the success that many employers and employees are experiencing by changing our focus from "sick care" to true "health care" through preventative health care. The Chamber believes that this is the only way to achieve true savings in our health system. Proposals that would offer tax credits to employers who provide comprehensive wellness programs for their employees would be a great help in promoting these efforts. Toward that end, the Chamber is leading efforts to encourage maximum business participation in wellness programs that enhance healthy lifestyles of employees and their dependents through the establishment of the U.S. Workplace Wellness Alliance, an alliance of more than 60 organizations that have joined forces to encourage greater focus on comprehensive wellness.

Stimulating Growth Through Increased Exports

Many of my peers on the Chamber's mid-market and small business councils are succeeding in the international marketplace by exporting their goods and services to customers around the globe. International trade has been a bright spot during these difficult economic times and that is good news for small and mid-size businesses which comprise 97 percent of all U.S. exporters.

To help stimulate the U.S. economy immediately and in the long-term, I recommend that Congress approve the trade agreements with Colombia, Panama, and South Korea to open up these foreign markets and allow America's small and mid-size businesses to increase export growth and compete on a level playing field. In the future, I would also encourage the next Administration and Congress to pursue new trade agreements that reduce barriers to U.S. goods and services, level the playing field for U.S. businesses and workers, and increase the opportunity to grow our exports.

Awaiting Congressional action are three bills that together would provide a significant stimulus for the U.S. economy at a very modest cost to the American taxpayer. A recent analysis by the U.S. Chamber of Commerce estimates that enacting pending trade agreements with Colombia, Panama, and South Korea would boost U.S. exports by more than $42 billion within five years. Additionally, the cost for this

"stimulus" would be modest -- foregone tariff revenue that is measured in millions, not billions, of dollars.

Conclusion

Being in the printing industry, I am very proud to quote one of the world's most famous printers, Founding Father Benjamin Franklin. He once said, "Watch the pennies and the dollars will take care of themselves." I cite this quote knowing full well that in discussing tax policies and possible stimulus ideas, you may be considering a package with a price tag in the billions – hardly pennies. But Franklin's message does resonate in the sense that if Congress acts wisely in how it handles the "pennies" through reasonable tax incentives, commonsense market-based health care reforms and more export opportunities, the investment and economic growth – "the dollars" – generated by businesses across our nation will be exponential.

Thank you for the opportunity to testify today. As a business owner, I look to you to champion and put in place policies that unleash the innovative ability and entrepreneurial spirit of America's job creators – our small and mid-size businesses. I know that the window of opportunity for action this year on a second stimulus bill is small. Therefore, I encourage you to move forward in a deliberative and constructive approach that is grounded in policies that encourage immediate investment and further the prospects for long-term economic growth. And as we look ahead to a new administration and Congress, I would hope that your actions as we work together to thoughtfully address the challenges facing the U.S. economy, would be guided by the premise that to revive growth we need policies that encourage investment, job creation and more opportunity.

Mr. PALLONE. Thank you.
Dr. Viard.

STATEMENT OF ALAN D. VIARD, PH.D., RESIDENT SCHOLAR, AMERICAN ENTERPRISE INSTITUTE

Mr. VIARD. Thank you, Mr. Chairman, Mr. Ranking Member, members of the subcommittee. It is an honor to appear before you today to discuss this important and pressing topic.

The U.S. economy is in a severe downturn. Although we do not yet have an official declaration to that effect, there can be no doubt that the downturn is a full-fledged recession. The severity of the economic difficulties that we are facing has understandably prompted calls for a fiscal stimulus package. I will submit today, however, that the case for a fiscal stimulus package is still quite uncertain and that if a fiscal stimulus package is adopted, the inclusion of an increase in Medicaid matching rates is an ineffective way to stimulate aggregate demand. I will also urge the subcommittee to continue to think about the need to promote long-run growth, even as we simultaneously address the short-run difficulties that we are facing.

I would like to begin, Mr. Chairman, by clarifying the potential role of fiscal stimulus. Increases in aggregate demand by increasing the category of some public or private spending cannot permanently boost the level of output. In the long run, an increase in spending in one part of the economy creates jobs there but it displaces spending elsewhere in the economy, reducing employment in that sector. In the long run, the level of output in the economy is determined by the number of workers who are available, the labor market institutions that allow them to work, the supply of natural resources and the supply of capital and the availability of technology. We therefore need to be wary of arguments that increased spending on any particular item, whether it be Medicaid or defense or alternative energy, will permanently increase jobs. Instead, arguments for particular category of spending should always be based upon the output that that is expected to provide to the American people in the form of beneficial services. So it is perfectly reasonable to argue in favor of Medicaid spending on the grounds that it will provide healthcare to those who are in need or to argue in favor of defense spending because it will make the Nation more secure or to argue in favor of alternative-energy spending because it will give us a better, more reliable source of energy but that is quite a different matter from arguing for it on the notion that it will permanently create jobs.

Of course, in the short run, increases in aggregate demand can increase employment and output, but what it effectively does is to borrow that output from the future. When spending decreases in some other item, we do experience an output loss. Obviously none of us would want to increase output at some random date and then later reduce it at some other random date. What we would like to do is of course to increase output in conditions like today's when we clearly have a desperate need for more economic growth, even if we know that we need to pay it back at some future date. But to accomplish that goal, aggregate demand needs to be managed in a very careful manner.

Now, economists of all persuasions, liberals and conservatives, have long argued that in most cases the best ways to manage aggregate demand are through monetary policy and through the automatic fiscal stabilizers that are built into our economy. Monetary policy, of course, has already responded aggressively to the current downturn with interest rates having already been slashed by 425 basis points. The Federal Reserve does still have a little bit of room to move further on monetary policy, although to be sure, it will soon begin to encounter the zero lower bound on interest rates. Monetary policy does take some time to work but the interest rate cuts began 14 months ago and so we will still see their impact. Automatic fiscal stabilizers are also an important part of today's economy. In any recession, there are automatic reductions in tax receipts and automatic increases in government spending, and we have already seen that response in this downturn as we have in earlier ones.

Now, there is always the possibility, Mr. Chairman, of supplementing these types of stabilization with some type of fiscal stimulus package, and that is one of the issues that you are considering today, but as the economists that I quote in my testimony, economists from the Brookings Institution note, that a fiscal stimulus package has to be designed carefully and that, Mr. Chairman, I submit probably does not include a temporary increase in Medicaid matching rates. An increase in Medicaid spending by the Federal Government does not directly increase aggregate demand. It is a transfer from the Federal Government to the State governments, and as such, is does not directly increase aggregate demand any more than would a transfer of money from one of the Federal Government's bank accounts to another of its bank accounts. Of course, it will increase aggregate demand if state governments respond to that increase in federal aid in a manner that boosts spending and the economy. It is a little unclear to me, Mr. Chairman, exactly what effects are envisioned from this increase in the FMAP percentage. If States increase their Medicaid spending or avert their cuts that they otherwise would adopt, there may be some increase in aggregate demand but it is hard to see a substantial one. Recipients might be able to consume somewhat more medical care which as a result would be good in its own right but it is hard to imagine it being a large stimulus to aggregate demand. An increase in provider payments will of course increase the incomes of those providers but it is hard to imagine that they would increase dramatically their consumption in response to a temporary increase in incomes.

It also is important to look at how the money would be distributed. An across-the-board increase in FMAPs rewards those States with the largest Medicaid programs. Allowing States to use an outdated FMAP percentage in place of the new FMAP percentage for a given fiscal year actually rewards those States that have had the fastest per capita income growth, which seems antithetical to targeting aid towards those States in need. Of course, any of these proposals would increase spending on a program that has grown unsustainably and that is projected to continue growing unsustainably. So Mr. Chairman, I don't see an increase in Med-

icaid matching rates as being a useful part of a fiscal stimulus package.

In closing, I would also urge the subcommittee to keep in mind the need that even as we address the short-term difficulties we face to also keep part of the focus on the need to promote long-run economic growth, particularly through tax-and-spending policies that will promote private business investment.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Viard follows:]

Testimony Submitted To

Subcommittee on Health

Committee on Energy and Commerce

The United States House

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Alan D. Viard

American Enterprise Institute

Alan D. Viard is a Resident Scholar at the American Enterprise Institute. The views expressed in this testimony are solely his own and do not necessarily reflect the views of the American Enterprise Institute or any other institution or person.

Chairman Pallone, Ranking Member Deal, and members of the subcommittee, it is an honor to appear before you today to discuss "Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research."

The U.S. economy is in a severe downturn. (Although the National Bureau of Economic Research has not yet made an official determination, it will almost certainly declare, at some point, that the economy entered a recession in late 2007 or sometime in 2008.) The severity of the downturn has prompted calls for a fiscal stimulus package to boost aggregate demand. It is far from clear, however, that a fiscal stimulus package is necessary or useful, since monetary policy and automatic fiscal stabilizers are generally better suited to serve the goal of economic stabilization. Even if a stimulus package is adopted, increases in the federal Medicaid matching rate should not be included because they are an ineffective means of boosting aggregate demand. Even as Congress addresses the current economic difficulties, it is also important to foster long-run growth through tax and spending policies that promote private business investment.

1. Increases in aggregate demand cannot permanently increase the levels of jobs or output, but can play a role in stabilizing the economy.

Fiscal and monetary policies can boost aggregate demand by increasing consumer spending, residential and business investment, government purchases, or net exports. These policies are intended to boost output and create jobs by prompting firms to produce more goods and services for purchase by consumers, homebuyers, businesses, and foreigners. It is important to realize, however, that such policies cannot permanently boost output. In the long run, the level of output is determined by the supply of productive resources – the number of willing workers, the functioning of the

labor markets that enable them to work, the supply of capital and natural resources, and the availability of technology.

It is tempting to argue that increased spending on a specified item – medical care, alternative energy, defense, business investment, or anything else – will create jobs. It is always easy to see the large number of workers who will be employed to produce the specified item. But, it is also necessary to see the jobs displaced elsewhere in the economy, as an increase in spending on the specified item forces a reduction in spending on other goods and services. Attempting to spend more on everything simply bids up prices and interest rates without increasing total employment.

It is therefore a serious mistake to support spending on renewable energy on the ground that it will create "green jobs" or to support business investment because workers will be employed to construct the investment goods or to support defense or Medicaid spending because it will create jobs. It is quite a different matter, of course, to support renewable energy spending because it will provide cost-effective energy resources or to support business investment because it will expand the capital stock and make workers more productive (as discussed below) or to support defense spending because it will make Americans more secure or to support Medicaid spending because it provides health care to people in need. Those arguments must be evaluated on their own merits.

Increases in aggregate demand can boost output in the short run. Firms that experience a higher demand for their products may initially expand output and hire more workers rather than raising their prices. This short-run effect fades away as prices and interest rates adjust.

A sustained increase in any category of public or private spending generates only a temporary increase in output and employment. Because it is unlikely that spending would be boosted for all of eternity merely to obtain a short-run boost to output, it is more meaningful to consider a temporary boost to spending. A temporary increase in a category of public or private spending boosts output when the spending increase occurs, but reduces output when spending returns to normal. In other words, fiscal stimulus measures that boost public or private spending do not "buy" us extra output – they merely "borrow" it from the future. There is no free lunch.

Although it is not useful to boost output at one random date and lower it at a later random date, it may be useful to boost output when the economy is in a recession and lower it when the economy is booming. For example, boosting output during the current downturn may be useful even though we will have to "pay back" the output gains at some later date.

Although aggregate demand policies cannot permanently boost output, they can help stabilize the economy. The best policies are not those that permanently increase aggregate demand in a futile attempt to permanently increase output, but those that alter aggregate demand over time in a way that offsets the business cycle.

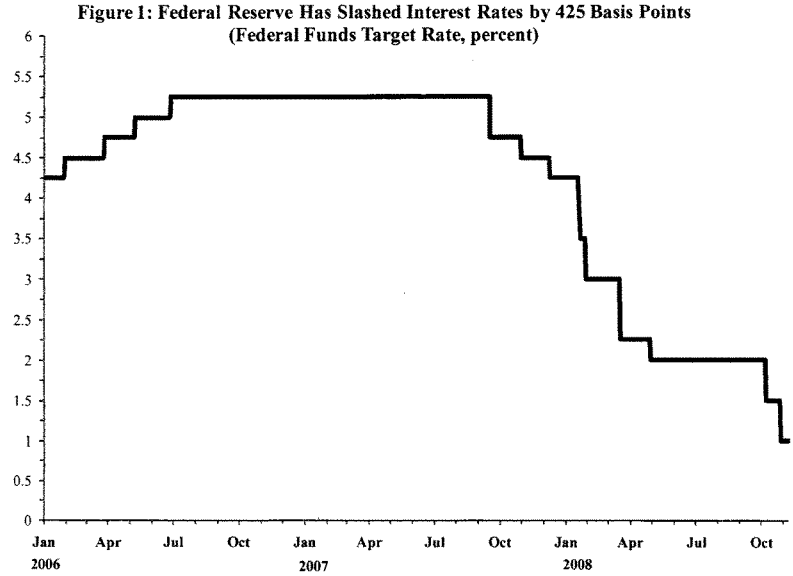
2. Monetary policy and automatic fiscal stabilizers are generally more effective than discretionary fiscal stimulus.

Monetary policy and automatic fiscal stabilizers are two important policy tools for managing aggregate demand in a way that stabilizes the economy. Monetary policy can change aggregate demand by changing interest rates, altering the amount of spending that people and firms desire to do. Automatic fiscal stabilizers boost

disposable income during downturns and dampen it during expansions, potentially changing the path of desired spending.

Monetary policy has responded aggressively to the current slowdown, as shown in **Figure 1**. From September 18, 2007 to the present, the Federal Reserve has lowered the federal funds target rate by 425 basis points, from 5.25 percent to 1 percent. Because monetary policy usually works with a lag, the full effect of the monetary easing has not yet been felt. Although interest rates cannot be reduced below zero, the Federal Reserve still has some further room to reduce rates and has left open the option of doing so.

Figure 1: Federal Reserve Has Slashed Interest Rates by 425 Basis Points (Federal Funds Target Rate, percent)

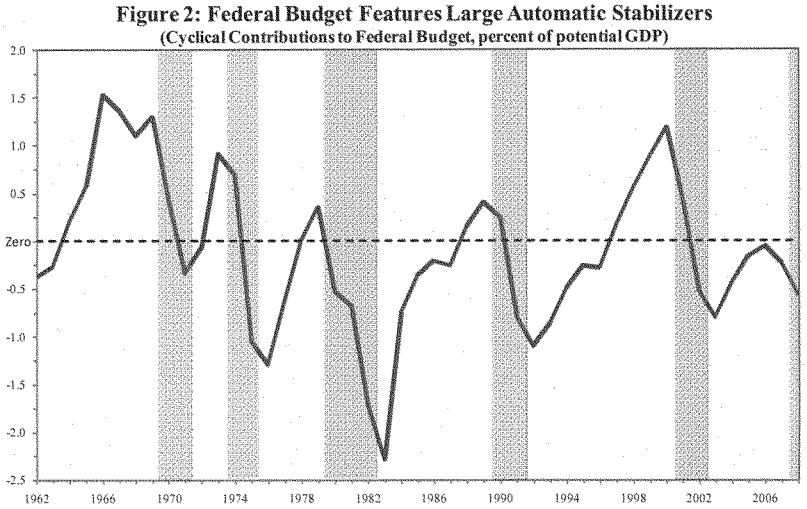


Source: Federal Reserve Bank of New York

Automatic fiscal stabilizers can also be significant. When the economy weakens, tax receipts automatically fall and outlays on social insurance and anti-poverty programs automatically rise. **Figure 2** shows the cyclical component of the federal budget deficit or surplus (the change in budget balance that results automatically from business cycle

conditions) as estimated by the Congressional Budget Office (CBO). Positive values indicate that business cycle conditions are reducing the federal budget deficit (or increasing the surplus) and negative values indicate that business cycle conditions are expanding the deficit (or reducing the surplus). Recessions, shown by the shaded areas in the chart, have been associated with significant cyclical increases in deficits, often about 2 percent of GDP. The chart further shows that automatic stabilizers are already responding to the current downturn.

Figure 2: Federal Budget Features Large Automatic Stabilizers
(Cyclical Contributions to Federal Budget, percent of potential GDP)



Source: Congressional Budget Office, "The Cyclically Adjusted and Standardized Budget Measures," October 2008, pp. 12-13, Table 5 (https://www.cbo.gov/ftpdocs/97xx/docs/9769/10-03-StandaBudget.pdf).
Note: 2008 value is projected by CBO. Fiscal years that included one or more months of recession are shaded. Chart assumes that a recession began during fiscal year 2008, although the National Bureau of Economic Research has not yet made an official determination.

Most economists agree that economic stabilization is generally best achieved through monetary policy and automatic fiscal stabilizers. This consensus is reflected in a January 2008 article by Brookings Institution economists Douglas Elmendorf and Jason Furman (Furman later served as a senior economic adviser to Senator Barack Obama's successful presidential campaign):

> Economists believe that monetary policy should play the lead role in stabilizing the economy because of the Federal Reserve's ability to act quickly and effectively to adjust interest rates, using its technical expertise and political insulation to balance competing priorities … monetary policy should generally be the first line of defense against an economic slowdown … Economists almost universally support the automatic stabilizers that do not require any legislative action, like mechanical reductions in tax payments and increases in unemployment insurance payments when incomes fall and unemployment rises.[1]

The advantages of monetary policy and automatic fiscal stabilizers should be considered carefully before considering discretionary fiscal policy. Discretionary fiscal policy seeks to offset the business cycle by altering particular categories of public or private spending, either boosting such spending during recessions or restraining it during booms. The February 2008 stimulus package, which combined tax rebates with temporary investment incentives, was an example of discretionary fiscal policy.[2]

Most economists approach discretionary fiscal policy with some degree of wariness, as Elmendorf and Furman note:

> During the past several decades, the idea that Congress should make legislative changes to tax or spending policies to counter the business cycle has fallen into disfavor among economists … the shift is based on very important political and administrative challenges to countercyclical fiscal policy, especially with regard to the timing and design of the stimulus … fiscal policy generally responds to

[1] Douglas W. Elmendorf and Jason Furman, "If, When, How: A Primer on Fiscal Stimulus," *Tax Notes*, January 28, 2008, pp. 545-559, at pp. 545-546.
[2] Public Law 110-185, 122 Stat. 613 (enacted February 13, 2008).

> changes in economic conditions with considerable lags, due both to the time needed to enact a stimulus bill and the time needed for the bill to be implemented and the spending increases or tax reductions to actually reach the pockets of consumers. As a result, the effect of fiscal stimulus on household and business spending may be poorly timed.[3]

Despite the limitations of discretionary fiscal policy, most economists recognize that it can play a useful role in some circumstances. As Elmendorf and Furman explain, fiscal stimulus can sometimes operate more quickly than monetary easing, fiscal stimulus remains available when interest rates approach zero and further monetary easing is impossible, fiscal stimulus can operate in situations when spending is insensitive to interest rates, and fiscal stimulus can avoid interest-rate reductions that might (in some cases) be considered undesirable. Also, uncertainty about the economic impact of stimulus may be lower with a combination of fiscal and monetary stimulus than with either type alone.[4] These authors therefore reach the following conclusions:

> There are several circumstances in which fiscal stimulus can be helpful or even crucial … these circumstances are potentially relevant today … However, it would be better not to have a fiscal stimulus at all than to have tax cuts or spending increases that are poorly timed, badly targeted, or permanently increase the budget deficit.[5]

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[3] Elmendorf and Furman, p. 546.
[4] Elmendorf and Furman, pp. 547-548.
[5] Elmendorf and Furman, p. 545.

In summary, fiscal stimulus proposals should be approached with caution and awareness of their inherent limitations. Stimulus proposals cannot permanently increase output; they can only stabilize it, boosting output during recessions and reducing it during expansions. In this regard, stimulus proposals play, at best, a supporting role to monetary policy and automatic fiscal stabilizers. If a stimulus package is to be adopted at all, it should be well designed. These principles should be kept in mind when evaluating proposals to increase Medicaid matching rates as a form of stimulus.

3. Increases in Medicaid Matching Rates Have Been Proposed as Stimulus.

Medicaid is operated by the states and the District of Columbia, which receive matching grants from the federal government. For each state, the Federal Matching Assistance Percentage (FMAP) equals 100 percent minus the state share. The state share is proportional to the square of the state's per capita income, with a value of 45 percent for a state with per-capita income equal to the national average. However, that the FMAP is at least 50 percent, meaning that the state share may not exceed 50 percent, even for states with the highest per-capita incomes. Also, the District of Columbia is assigned a 70 percent FMAP. For fiscal year 2009, the state FMAPs (based on 2004-2006 per capita incomes) range from 50 percent for thirteen high-income states to 75.84 percent for Mississippi.[6] The five overseas possessions also participate in Medicaid with FMAPs of 50 percent.

Temporary increases in FMAPs have recently been proposed as a form of fiscal stimulus. Such increases were also adopted as a stimulus measure in 2003.

Section 3001 of H.R. 7110, as approved by the House on September 26, 2008, would increase FMAPs for the fourteen-month period from October 1, 2008 through

[6] 72 *Federal Register* 67304 (Nov. 28, 2007), corrected by 72 *Federal Register* 69285 (Dec. 7, 2007).

November 30, 2009. Each state would be allowed to use its fiscal 2008 FMAP in fiscal year 2009 if it is higher than its 2009 value; each state would have a similar option to use its fiscal 2009 FMAP in the first two months of fiscal year 2010. In addition, all FMAPs would be increased by one percentage point. States would also be awarded additional increases of up to 3 percentage points if they have experienced, over the preceding two years, declines or slow growth in nonfarm payroll employment, increases in food stamp participation, or increases in the fraction of mortgages in foreclosure. To obtain the higher FMAPs, states would be required to maintain their July 1, 2008 Medicaid eligibility criteria. CBO has estimated that these provisions would increase federal outlays by $12.2 billion in fiscal year 2009 and by $2.5 billion in fiscal year 2010.[7]

Section 3001 of S. 3604, as introduced in the Senate on September 26, 2008, would provide FMAP increases for the fifteen-month period from October 1, 2008 through December 31, 2009. Each state would be allowed to use its fiscal 2008 FMAP in fiscal year 2009 if it is higher than its 2009 value; each state would have a similar option to use its fiscal 2009 FMAP in the first quarter of fiscal year 2010. In addition, all FMAPs would be increased by four percentage points. To obtain the higher FMAPs, states would be required to maintain their September 1, 2008 Medicaid eligibility criteria. States would be prohibited from using the additional aid to increase their reserve or rainy day funds.

The Jobs and Growth Tax Relief Reconciliation Act of 2003 provided for FMAP increases for the fifteen-month period from April 1, 2003 through June 30, 2004. Each state was allowed to use its fiscal 2002 FMAP in the last two quarters of fiscal year 2003

[7] Congressional Budget Office, "Estimated Cost of H.R. 7110, The Job Creation and Unemployment Relief Act of 2008, As Introduced on September 26, 2008" (http://www.cbo.gov/ftpdocs/98xx/doc9816/hr7110.pdf).

if it was higher than its 2003 value; each state had a similar option to use its fiscal 2003 FMAP in the first three quarters of fiscal year 2004. There was also a 2.95-percentage-point increase in all FMAPs. To obtain the higher FMAPs, states were required to maintain their September 2, 2003 Medicaid eligibility criteria.[8]

4. Temporary FMAP increases would be an ill-designed and ineffective way to stimulate aggregate demand.

Counter-cyclical increases in Medicaid matching rates would function poorly as a stimulus tool because any boost to aggregate demand would be limited and indirect. It is important to stress that financial transfers from the federal government to the states do not directly boost aggregate demand because they do not directly increase consumer spending, business or residential investment, government purchases, or net exports. A transfer from the federal government to state governments does not directly boost aggregate demand any more than would a transfer from one of the federal government's bank accounts to another of its bank accounts.

To be sure, aid to state governments can indirectly boost aggregate demand if the aid causes a change in state tax or spending policy. But, the size of the boost depends on the nature of the state tax or spending change. In a January 2008 report, CBO noted:

> In general, the extent to which federal aid to state and local governments helps arrest the decline in demand depends on the degree to which those governments alter their behavior. If they cut spending less or raise taxes less as a result of federal aid, the policy will help keep demand from falling as much in the economy. The cost-effectiveness of federal aid to states and localities will also depend on exactly how the recipients use the aid. Policies can have very

[8] Public Law 108-27, section 401(a), 117 Stat. 764 (enacted May 28, 2003).

> different effects on the economy and the principles of an effective federal stimulus that were discussed earlier generally apply to stimulus carried out by states and localities as well. The cost-effectiveness of the aid could also depend on who it is distributed geographically and on whether the aid is accompanied by maintenance-of-effort requirements ... Additional federal aid to states that are facing fiscal pressures or are already in recession would probably stimulate the economy. However, federal aid to states whose budgets are relatively healthy may provide little stimulus, especially if those states use the aid to build up their "rainy-day" funds instead of increasing spending or reducing taxes.[9]

In a table summarizing stimulus options, CBO lists "Providing General Aid to State and Local Governments" as having "medium" cost-effectiveness and a "medium" lag from enactment to stimulus, with "large" uncertainty about the effects. The uncertainty arises because it is hard to know how states will alter their tax and spending policies. That uncertainty is present in full force in the FMAP context.

It is far from clear that states would actually change their Medicaid spending in response to a temporary increase in FMAP. States would be unlikely to adopt legislated increases to the program in response to the FMAP increase, as they would have to either cancel the increase when the FMAP increase expires or permanently bear the financial costs without the benefit of the higher FMAP. The only plausible story for why the FMAP increase might temporarily boost Medicaid spending above what it otherwise would have been is that the FMAP increase might allow states to avoid temporary

[9] Congressional Budget Office, "Options for Responding to Short-Term Economic Weakness," January 2008, pp.18- 19 (http://www.cbo.gov/ftpdocs/89xx/doc8916/01-15-Econ_Stimulus.pdf).

Medicaid cutbacks that otherwise would have adopted during the downturn in response to state balanced-budget requirements. It is far from clear that this effect would be significant. A study by the Rockefeller Institute of Government found that states generally avoided cutting Medicaid during the economic weakness of fiscal 2004 and that those decisions were generally not driven by the temporary FMAP increase in effect at that time.[10] On the other hand, a study by the Henry J. Kaiser Foundation concluded that states adopted a variety of Medicaid cutbacks during that downturn.[11]

If a temporary increase in Medicaid spending occurred, it would be unlikely to significantly boost aggregate demand. While a temporary relaxation (or avoidance of a temporary tightening) of eligibility criteria could prompt an increase in the consumption of health care, it is doubtful that the effect would be large. Furthermore, any temporary change to Medicaid spending would probably take the form of temporary increases (or avoidance of temporary reductions) in provider reimbursement rates, which would have economic effects largely similar to those of temporary transfer payments to the providers. This relatively high-income group would probably not increase its consumption sharply in response to temporary transfer payments.

If a temporary increase to Medicaid spending did not occur, the aggregate demand impact of the FMAP increase would become even more uncertain. If the federal aid prompted states to cut taxes or to increase non-Medicaid spending (perhaps by averting tax increases or spending cuts that would otherwise be required by balanced-

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[10] James W. Fossett and Courtney E. Burke, *Medicaid and State Budgets in FY 2004: Why Medicaid is so Hard to Cut*, Rockefeller Institute of Government Federalism Research Group, July 2004 (http://rockinst.org/pdf/health_care/2004-07-medicaid_and_state_budgets_in_fy_2004_why_medicaid_is_hard_to_cut.pdf).

[11] *Few Options for States to Control Medicaid Spending in a Declining Economy, Kaiser Commission on Medicaid and the Uninsured*, Issue Paper, April 2008 (http://www.kff.org/medicaid/upload/7769.pdf).

budget constraints), there could be a boost to aggregate demand. As CBO noted in its January 2008 report, however, many types of tax cuts and spending increases, whether done at the federal or state level, do not provide effective and timely stimulus. There is no mechanism to ensure that states would respond to the FMAP increase in a way that would provide effective stimulus. Indeed, some states might not cut taxes or increase spending in response to the FMAP increase, but might simply narrow their budget deficits, which would not boost aggregate demand at all.

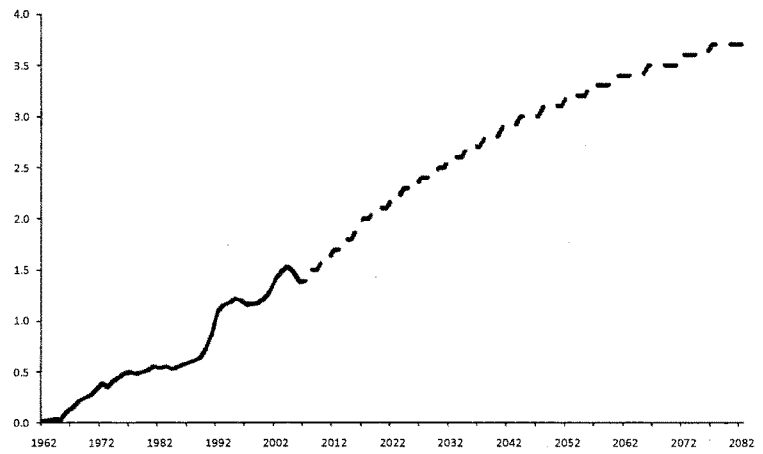
Even if an increase in aggregate demand occurred, it might not be timely. Setting aside the lag before Congress enacts the FMAP increase, a further unpredictable lag may occur before state legislatures actually increase spending (on Medicaid or other programs) or cut taxes.

CBO also notes that aid to states is a more effective stimulus if it is targeted at states that have been hard hit by the recession. The provisions of H.R. 7110 that target aid to states with economic weakness address this concern. In contrast, the across-the-board FMAP increases in H.R. 7110 and S. 3604 provide the largest aid to states with the largest Medicaid programs. The provisions in those bills giving states the option to use their fiscal 2008 FMAPs (based on 2003-2005 per capita incomes) in place of their fiscal 2009 FMAPs (based on 2004-2006 per capita incomes) directs federal aid toward states that experienced rapid growth of per capita income between 2003 and 2006, an approach antithetical to helping states that have been hit by economic weakness.

The ineffectiveness of the FMAP increase as a fiscal stimulus makes it all the more important to consider its other policy implications. The most striking feature of an FMAP increase is that it would boost, if only temporarily, federal spending on a program

that is already growing at an unsustainable pace and is projected to continue doing so, as shown in **Figure 3**. Furthermore, the increase in FMAP perpetuates the fundamental flaws of the FMAP formula, notably its well-documented tendency to provide the greatest aid to the states that already have the greatest economic resources.[12]

Figure 3. Unsustainable Medicaid Growth Projected to Continue
(Percent of GDP)



Source: Congressional Budget Office, http://www.cbo.gov/budget/data/historical.pdf (accessed 11/10/2008); Congressional Budget Office, *The Long-Term Budget Outlook, December, 2007*, http://www.cbo.gov/publications/bysubject.cfm?cat=0 (accessed 11/10/2008).

5. Long-run growth can be promoted by tax and budget policies that increase private business investment.

The government exists to serve both the short-run and long-run needs of the American people. Meeting the short-run needs of the American people involves monetary easing and automatic fiscal stabilizers. At the same time, Congress must not lose sight of the need to promote long-run growth.

[12] See General Accounting Office, *Medicaid Formula: Differences in Funding Ability Among States Are Often Widened*, GAO-03-620, July 2003 (http://www.gao.gov/new.items/d03620.pdf) and the July 22, 2008 testimony of Robert B. Helms before this subcommittee (http://energycommerce.house.gov/cmte_mtgs/110-he-hrg.072208.Helms-Testimony.pdf).

The current tax treatment of business investment impedes long-run growth. Corporate investment returns are typically subjected to corporate income tax and also to individual tax (at a 15 percent rate) on dividends and capital gains. As a result, savers cannot capture the full returns from their decision to postpone consumption. Reducing or eliminating the taxation of investment (financed by spending cuts) would allow an expansion of the capital stock, which would boost output and wages. Such tax relief could be financed by slowing the growth of entitlement spending. Another desirable approach is a revenue-neutral fundamental tax reform in which the income tax system is replaced by a progressive consumption tax, such as the Bradford X-tax.

Conclusion

Our economy is in a severe downturn, but the case for a fiscal stimulus package is problematic. Even if some type of stimulus is warranted, a temporary increase in Medicaid matching rates would be ill-designed and ineffective.

Mr. PALLONE. Thank you, Dr. Viard.

Now we will have questions and I will start with myself for 5 minutes. I wanted to start with Mr. Sperling. This is very complex and yet because of the economic downturn and the dire situation, we obviously have to get it right, and I was very interested in your comments because I read an article within the last few days, I guess it was in the New York Times, I forget who it was by, that was talking about Herbert Hoover and Franklin Roosevelt, dare we go back to those days, and saying that part of the problem, everyone assumes that when Roosevelt came into office that automatically he started this big stimulus package and got the government going again, I should say got the economy going again, but in reality, it was very much the opposite. He was reluctant to have a huge stimulus. He was worried about the debt. He actually increased taxes and it wasn't that successful in the first few years and it wasn't until World War II came along and so much money was being spent that the economy actually started to turn around in a significant way, and the advocate, I forget who it was, one of your colleagues was essentially saying you need a huge stimulus, we are just not talking enough money here. And in September I think we did a $60 billion package. We have talked about $150 billion. I think the FMAP part of that was only 14 or 15. You were using figures much larger, 300, maybe I thought you said 60 for FMAP. Maybe I got that wrong. But at the same time the issue, particularly to this subcommittee, is the FMAP part of it so part of it is, how big should the stimulus be and then, as Dr. Viard said, how effective is the FMAP part of this in terms of the total picture. So I guess I wanted to ask you those two questions again. I know you kind of got into it. What do you say to those, some of my colleagues, and I am not trying to distract from them, seem to be implying that well, what about the debt. Marsha mentioned PAYGO. What about all that? Do we just not worry about the debt, do we not worry about PAYGO because this is such a dire circumstance that we just have to spend and spend? And then the second thing, maybe responding to Dr. Viard, how effective is the FMAP part of this, if it becomes robust, in actually stimulating the economy?

Mr. SPERLING. First of all, on the fiscal side, obviously my position and I believe the policies we had in the 8 years in the Clinton Administration were very strong on the importance of long-term fiscal discipline. I think Haines basically say that smart fiscal policy kind of leans against the wind. In other words, you are expansive when demand is very weak. The government is willing on a short-term basis, just on a short-term basis, a year or 2 years, to allow the deficit to go up to stimulate the economy and part of the thought too is that if you allow a deep recession to happen, the fall in revenues and the rise in automatic stabilizers would end up increasing the deficit anyways but with a worse economy. Now, the other side of that is to lean against the wind the other way, that as the economy is doing stronger, you want to increase savings, and I think we are learning that one of the reasons why you want to have good long-term fiscal policy is so that when you do come to a time of war or a time where you need a stimulus, you are in a position that you can do that for a year or two at less risk to the economy.

Again, I never in my life before advocated for a stimulus above around $150 billion. I am just extremely, extremely worried. I have never seen a situation like this where I just worry there is going to be such a broad cutback in spending, and if you look at the projections for 2009 in the rest of the global economy, I think this is a moment where you would actually like world leaders in the way that you do coordinated monetary policy to all say that they are going to do a significant fiscal stimulus. It absolutely is not a way to permanent job creation. What you are trying to do is stop an incredibly painful downward cycle with a temporary injection of demand, and I guess I would—and in that light, you do have to think more expansively, how could you get $300 billion or more into the economy. It sounds very large but it is really just around 2 percent of GDP. If you are worried that you are going to be in negative growth for an entire, that in and of itself is not an excessive amount. Now, I think having some smart small business tax cuts, extending the 179 expensing, those type of kind of use-it-or-lose-it tax incentives for businesses makes sense. I think giving tax cuts to ordinary people and hope they spend makes sense. I do think that the evidence does not suggest that you get quite as high of a bang for the buck as those measures but I have still supported them in the past and I still support them now but I think in this context, I am worried that people are hurting so bad and the economy will be so weak, it might not inject, inspire, incent the spending that you want. So I think there is a degree of what you have to kind of almost make sure there is going to be more spending and I think you do have to be tough. I think if you are looking at even things I support like green jobs or infrastructure, you do have to ask, is the money coming to come out in that 18-month window where you are trying to stimulate the economy? And if not, then you have to say it is a good measure but you have to do it as long-term policy and figure out how you pay for it. But if you can do some things that are good for the future and stimulate the economy in 18 months, you should have a hearing. One should give that a hearing and see if people can find things that would be good for energy independence or good for infrastructure that could spend out fast enough. If they can't, they shouldn't be part of a stimulus. If they can, we should be open to it. But in this environment, you do want to do some things that are surefire successes in getting demand out. And the truth is that things like unemployment insurance and food stamps and the FMAP are among, I believe economists think, among the most successful. Dr. Viard said you want to have automatic stabilizers but this is essentially an automatic stabilizer. Unemployment insurance goes up in a weak economy. Medicaid spending should go up in a weak economy. So essentially when you are increasing FMAP, you are simply making up for the fact that we don't have Medicaid as an automatic stabilizer anyways. So by that very logic, we recognize that as unemployment goes up, you have both State pressure on other things and you have more people coming on the rolls. It is a terrible choice for States. I worked for 2½ years for a governor during the 1990 recession. It is a terrible choice. You have less revenue and more demand, and I think the cutbacks that you make in those situations are contractionary, they hurt the economy, and because they are in

such things often as cutting back teachers, police officers, they are bad and they are also I think very damaging for consumer confidence.

So the FMAP is one of the quickest, most automatic things that you can do right away to get stimulus in the economy, and I have to object to one thing. It is not a transfer of the Federal Government. The Federal Government can borrow. States have balanced-budget requirements. So States don't have the opportunity to provide this temporary stimulus. This is the reason why you look to the Federal Government in a case like this to do temporary borrowing so that you can deal with the pain and distress but do so in ways that money will go out quickly. So in this context, I believe we need to think about a much larger FMAP, both because of the distress I see and because I think it is one of the most effective stimuluses. Mark Zandy, others who looked at what gets out the quickest and what has the highest multiplier effect find aid to State relief I believe among the top three. So this isn't an all-or-nothing thing. We can have smart tax incentives for people like Mr. Pinard and we have some consumer tax cuts but I think what is different this time around is we are just going to have to do more to directly get money into the economy because it may be so weak that we may have trouble incenting people to get there alone. That is why I think things like FMAP and State aid make a lot more sense this time around than in the past.

Mr. PALLONE. Thank you.

Dr. Burgess, I want to hear from Governor Napolitano so I will give you the same amount of time because this is important and I want to make sure we get everything out here. I wanted you to respond to the same thing, Governor, but in addition to that, if you will, you talked about being governor in 2003 when we did have the FMAP pass, but my understanding is that it took time to accomplish that, in other words, while we were working to do that, many families lost their Medicaid coverage, and one of the issues is, would it be preferable to have an automatic trigger for increases based on economic indicators, in other words, rather than just do this piecemeal. But I also wanted to hear if you wanted to respond to the same thing that Mr. Sperling was talking about.

Governor NAPOLITANO. Thank you, Mr. Chairman. Let me answer the second question first. I think having sort of an automatic trigger built into Medicaid makes a lot of sense. How that is constructed requires some care but the fact of the matter is, it is a device that does help stabilize and is somewhat countercyclical so that instead of having to have these kinds of things every down cycle, if there was some automatic triggers, that would, I think, improve the Medicaid program.

Mr. PALLONE. See, the other thing too, and you can comment on this as well, is that one of the reasons why a lot of people are saying the stimulus needs to be bigger is because they figure that as States cut back, whatever stimulus we do may be essentially eaten up by those State cuts and so that is why it needs to be larger. But anyway, go ahead. I want to hear from you rather than commenting myself.

Governor NAPOLITANO. Well, thank you, Mr. Chairman, and I think it is important to understand, as Gene said: States cannot

borrow. We must balance our budgets every year. We have three basic functions we pay for: we educate, we medicate, and we incarcerate. And the medication part is Medicaid. Education is by far the largest part of State budgets and then incarceration costs. When you have a shortage of revenue as the States do now, you have to take that from somewhere. So unless there is an increase in FMAP, you have choices. You can either remove people from the Medicaid rolls and increase the number of uninsured, which has huge social costs beyond the offload of costs onto the healthcare provider community. You can cut back on education, and you began the hearing with a statement about the importance of investment in knowledge and biomedical research as long-term economic stimulus. Well, the largest discretionary item in the Arizona budget below prisons, if you call them discretionary, which I don't, but are universities. So you have 40 States looking at large cuts to university budgets unless they get some help on the FMAP side of things. And beyond that, you are at a situation where States have already, as I mentioned before, already taken drastic measures. We have hiring freezes, we have laid off people, we have instituted moratoriums on school construction in a State that has the fastest growing 0-5 population of any State in the country. We have deleted optional State services like adult dental coverage for poor seniors. All those things have been done. So you are really down to the basics and now if you don't do the FMAP, what you are going to have to do is force States either to do these cuts countercyclical, doesn't help our Nation get out of a recession or to raise taxes, also countercyclical because I agree with several of the speakers here. I think some targeted tax cuts for small business make a lot of sense in a national economy such as we have today in order to stimulate, and it is all about stimulating demand and getting deals going again, getting business going again, getting job creation going again.

So in a sense what you have is a program before you that has worked before in the short term. What I am suggesting is do it again. Our calculation is, it needs to be at least $25 billion for each of the next 2 years to really work and then to absolutely look at the Medicaid statute and structure itself so that we build in some economic triggers for future purposes.

Mr. PALLONE. Thank you very much.

Dr. Burgess.

Mr. BURGESS. Thank you, Chairman.

Dr. Viard, we heard Mr. Sperling just answer a question and he talked about the FMAP increase being one of those automatic stabilizers and your testimony seemed to be at odds with that. Do you have any further comment to make on that?

Mr. VIARD. Yes. Thank you. The FMAP increase of course that we are considering today is not an automatic increase precisely because we are here holding hearings about it, which is one of the things that makes it problematic I think in a couple respects, Mr. Congressman. One is, of course, that we can't be certain that we will get the timing right, and the other is that unlike the automatic stabilizers, which are automatically targeted to those parts of the country that are in the greatest distress, the FMAP increase that we are considering today doesn't have that characteristic. I think

that some of the ideas that have been put forward in this hearing concerning setting up some type of automatic adjustment does make sense and I think there is a variety of things that could be explored. We could have a system set up where FMAP does automatically rise during weak economic conditions and automatically fall during strong economic times. We could have options available to States that in order to maintain their eligibility criteria during a downturn which would of course be sound policy that they could avail themselves of a temporarily higher FMAP if they accepted a temporarily lower FMAP when the economy recovered. But I think the proposals that we are considering today are really quite different, an increase in FMAP with no offsetting reduction later and a lack of targeting to those States that are in need.

Mr. BURGESS. In the interest of full disclosure, I did vote in favor of the FMAP increase in 2003. I think I am the only person here who did. Did you vote for the FMAP increase in 2003? That was that $250 billion tax cut that you guys opposed so badly?

Mr. PALLONE. I don't remember.

Mr. BURGESS. I think you voted against it. But I voted for it and I just want the record to show that.

Dr. Viard, before we depart this subject, now on the next panel we are going to hear about NIH and funding in biomedical research as a form of economic stimulus. We don't get an economist on that panel so I am going to impose upon you to be the adult in the room for the next panel and give us just a preview of what your feeling is about the increase in NIH funding being used as an economic stimulus as well.

Mr. VIARD. Of all the types of spending that one might want to consider manipulating for purposes of stabilizing the business cycle, it really seems to me that biomedical research would be at the absolute bottom of the list. Now, let us be clear from the outset that it is a completely separate question of what value biomedical research may have because of course biomedical research could have enormous benefits in terms of promoting the health and the well-being and the longevity of the American people, but as a tool to stabilize the business cycle, I think it is completely ill suited. To use it for that purpose would imply that the budget for research would be increased during every recession and would then be cut back during every expansion, which would be absolutely identical to the notion of a long-run research strategy.

I think that the comments that the Congressional Budget Office made with respect to a slightly different category of spending would apply here. CBO commented in a January report some of the candidates for public works such as grant-funded initiatives to develop alternative energy sources are totally impractical for countercyclical policy regardless of what other merits they may have. I think that comment absolutely applies to biomedical research. I think that biomedical research should be funded based upon the benefits that it can bring to the American people in terms of the research and the business cycle consideration should be completely divorced from that funding decision.

Mr. BURGESS. Thank you.

Mr. Sperling, let me just ask you, because we just had a presidential election. You may have heard. And during the run-up to

that election, there were several debates, and at least in the last debate, if I recall correctly, both candidates talked about the need for reducing spending and the need to move—I think the question was posed by Mr. Schieffer, are you going to pursue a balanced budget, and both indicated that they would. Senator McCain said he would do so by across-the-board cuts. Senator Obama, President-elect Obama said that it would be more surgical, but the only cut that he ever mentioned specifically was a cut to Medicare Advantage. Do you think we can cut Medicare Advantage enough to cover the expense of the increased FMAP and are we going to have to rely on that, for the cutting in Medicare Advantage to pay for other things or is the concept of PAYGO and cutting spending to offset any of this increased spending, is that just completely out the window at this point?

Mr. SPERLING. Well, I think the idea of a stimulus is actually that you are not offsetting during that short window, and I think that it is an unfortunate situation that we have such a high deficit that the next administration will inherit such a large deficit, and in that context, you would normally not want to have to do a stimulus. So I think you call for such a large stimulus like this or I am, not because you want to but I feel that we have to. I do believe that a stimulus is not a get out of fiscal responsibility, free card forever. So in other words, the idea of a stimulus should be that you are letting the deficit go up for that period of time in which you are trying to get more spending into the economy but only for that period of time. So I do think, I may disagree, I have a slightly different attitude than Dr. Viard in the following way, but I think this is where I am sure we both agree, which is that money has to go out during that period to be a stimulus. If you pay for it, then it is not actually stimulating the economy, it is neutral, but on the other hand, if you call for a stimulus for 2 years and the money doesn't spend out to year 3, it has obviously failed to meet its purposes. Now, I do think one thing you can do is let us say you had an investment that you thought was very wise over a 5-year period. Now, somebody might come in and say well, and this is, to be honest, what many of us criticize the previous administration for. They would say well, we are in a recession, we don't have to pay for all of it, and we would say well, no, you don't have to pay for it for the year or two that you are trying to stimulate the economy but in the long term you do. So for example, if you were doing a 10-year extension of SCHIP, I might think it might make sense for the first 2 or 2½ years to waive the offsets for those 2½ years because you are trying to stimulate the economy at that point but it wouldn't be an excuse to never pay for it or have offsetting savings. So I think you really have to distinguish between the fact that you are allowing a short-term deficit and therefore it does add to the debt but it is just for that 1 year but you shouldn't use it as an excuse, which is what I fear we did too much in the previous 7, 8 years of using it as a way to do long-term permanent increases.

Now, for me, what I would do on healthcare is, I would use the FMAP because I think even though it is not an automatic stabilizer right now, it kind of should be and it operates that way so I think having an increase right now would be helpful to stimulate the economy. It would mean temporary borrowing to help stimulate the

economy. For the long term what I would do is, I would encourage bipartisan work on a universal healthcare plan that would cover everybody but would also at the same time take on much broader issues of the waste that happens from people trying to discriminate against people with preexisting conditions, where there are negative incentives, the cost shifting, all of those things. Those are the broader things I think you have to do to bring down the growth of Medicare and Medicaid costs in the future. If you do that together in 2009, 2010, than you can say we are increasing healthcare costs temporarily to help us get out of this recession but we are also working on a long-term package to cover all Americans, make healthcare more efficient and thereby bring down the cost of healthcare.

Mr. BURGESS. If I could just interrupt you for a moment, ever under the most optimistic of scenarios, to take on that second piece, it is $160 to $480 billion a year for the plan that was outlined by Senator Obama or President-elect Obama during the run-up to the campaign, so we have increased the debt limit three times this year. We are barely a month into the fiscal year and we have got a $1 trillion deficit on top of a $3.2 trillion budget. The Chinese won't loan us any more money. Where do you propose that we get this if we are not going to restrain spending in some other quarter?

Mr. SPERLING. Well, what I would argue personally is that as you are trying to do universal healthcare, you try to rationalize the healthcare system. Let me just tell you on an economic point of view——

Mr. BURGESS. Well, but I want to get back to Mr. Pinard before I run out of time, so very quickly. Go ahead but very quickly.

Mr. SPERLING. Well, President-elect Obama has clearly talked about using offset from not extending the tax cut for people over $250,000 as a way of getting $100 billion or so savings, I believe to——

Mr. BURGESS. But in fairness, though, the Congressional Budget Office has already figured that in. The Bush tax cuts have expired as far as the Congressional Budget Office in their budget predictions for the next 10 years.

Mr. SPERLING. Well, this is one place where the President-elect and the current President agree, that the baseline calls for extending that. It is still a choice and you are doing that for savings, but my point——

Mr. BURGESS. But that still becomes new spending.

Mr. SPERLING. But my point is, and I just encourage you to think about it this way. Right now what hurts our country, the competitiveness, the costs to competitiveness for businesses, for people, is the rising cost of healthcare generally. To not try to fix that, to allow our national healthcare spending to grow so great and just feel comforted that you are keeping the public ledger part of it lower is just no comfort. Governor Schwarzenegger is the one who says very eloquently that when you allow massive uninsured Americans, that they end up getting too late expensive coverage which then ends up being a hidden tax on the premiums of all Americans. Now, you can feel comforted that that is not publicly on the ledger but I think that if you can have an upfront cost in subsidies for Americans and healthcare information technology but it is in part

of a plan that does have some touch medicine, we are slowing the growth of healthcare that in the long term for our long-term Medicare entitlement growth, a universal healthcare plan that brought down the growth of national healthcare spending overall——

Mr. BURGESS. But it won't, and we have a graph somewhere in this packet that shows a projection in the increase in Medicaid spending over time which I think the term that is used is unsustainable. I do want to get to Mr. Pinard because you were so kind to come to the panel. I want to give you a chance to at least discuss this for just a moment. Now, we have heard the argument for universal insurance, and in the interests of full disclosure, I was a surrogate for Senator McCain during the campaign so, yes, I know McCain's plan pretty well but as a consequence of being in 15 cities in the last 2 months, I also know President-elect Obama's plan pretty well also. If we go to a system where there is now a new like Medicaid, like Medicare, there is a new national health insurance patterned after the FEHBP that as a business you either are going to show credible coverage or your employees are going to be covered under this new national plan. What is the inclination there? You are offering a pretty generous package of benefits right now and I commend you for doing that. I had a small business and I had about the same number of employees as you so I fully know how expensive it is to provide those benefits. So if you look around you and you see your competitors, credible coverage, I can't keep up with it, I will just pay the fine and get into the national plan, do you think that that is likely to—I know it is hard to project human behavior but do you think that that is likely to be a sentiment shared by some of your competitors and might that not also put pressure on you to look at that as well?

Mr. PINARD. My fear in a universal plan of that nature, if it was a single system and everybody had to participate, sooner or later we are going to end up trying to satisfy everybody, and you may satisfy 1 percent with this coverage but 100 percent have to pay into it because you have to assume that the larger percentage is going to participate. So I think the costs involving in administering a national universal healthcare system I would imagine would have to be astronomical. So I think the system would be very burdensome and not attractive to private employers. I feel that with private employers that I deal with, they would prefer to preserve the free market healthcare system that currently exists as it exists today or even in a more free market with the AHPs to allow them to choose the coverages they want that best fits their employee profile. As you know, young technology companies have certainly a very different demographic than a machine shop that has been in business for 60 years and they require different kinds of coverage and different emphasis. So the private sector, as far as I know with the people that I deal with, prefer to see that there is a private sector healthcare system that is maintained that they can choose from and choose who their carrier is going to be and so on.

Mr. BURGESS. From a competitive standpoint, what does it do to your printing business if you look around and every other printer in the cities in which you work have said oh, to heck with it, I will just pay the fine or the tax, whatever we call it and I will be in the national plan and yet you are obviously by nature very gen-

erous and you are providing your employees with the Elysian Fields of benefits that you now spread before them. Are you going to have to rethink that?

Mr. PINARD. Well, that would make us very uncompetitive because, for instance I believe in Massachusetts the fine is $250. Two hundred and fifty dollars doesn't go anywhere towards providing somebody with healthcare for the year. So it takes a lot of $250 checks to fund that system, and as you know, Governor Patrick is having a devil of a time up there trying to deal with this. But it makes us uncompetitive if we elect to provide a more fuller, generous health insurance plan. It is an employee benefit and it is a job attraction tool. We would try to maintain our benefit plan so that we can attract better employees.

Mr. BURGESS. Very good. I just wanted one comment to our friend from Maryland. I went to medical school in Houston. I didn't know David but I knew of David and our medical school class was allowed to see him one day so I certainly appreciate the difficulties with which you have existed and obviously done very well. As a father who paid for a journalism degree for my middle daughter, I do wonder about your selection of a profession. I fully expect you to complete your studies, having heard from you today. I am not sure the Washington Post and the Baltimore Sun will still be there when you emerge on the other end.

I will yield back, Mr. Chairman.

Mr. PALLONE. Such optimism. You sound like me. Listen, first of all, let me thank all of you for being here today. I know we just had the questions from the two of us but I think it was very worthwhile and I appreciate your input as we move forward on this, and as you know, we are probably going to deal with the legislation next week so it is very timely that you were here today. Thank you very much. Thank you all.

Mr. BURGESS. Mr. Chairman, as we go to our next panel, can I ask unanimous consent that the report "Why Government Spending Does Not Stimulate Economic Growth" from the Heritage Foundation be submitted into the record? The report is dated November 12, and points out that every dollar the government injects into the economy is first taxed or borrowed out of the economy. In fact, it doesn't create new purchasing power, it simply redistributes existing purchasing power, and I will submit this for the record.

Mr. PALLONE. Without objection, so ordered.

[The information appears at the conclusion of the hearing.]

Mr. PALLONE. I will ask the second panel to be seated. Before we go to the second panel, I have a unanimous consent request also. These are the remarks by Mr. Towns, who had to leave, and also three items: the testimony by the governor of New York, Mr. Paterson, before the House Ways and Means Committee on October 29, which discusses New York's dire need for at least a 5 percent increase in the FMAP through 2011; second, a November 12, 2008, New York Times article entitled "Brooklyn Lab as Part of City's Goal to be a Biotech center," which discusses a new HIV/AIDS lab in the Brooklyn Army Terminal section of the city and how it is the precursor to the city's initiative to make New York City a biotech hub; and third, a letter to the Speaker, to Nancy Pelosi, from more than 230 patient groups, scientific and medical societies

and research institutions, urging support of increased NIH funding in the economic recovery package. Without objection, so ordered.

[The information appears at the conclusion of the hearing.]

Mr. BURGESS. And Mr. Chairman, I would also like to ask unanimous consent that the statement of the California Healthcare Institute, which was submitted to the House of Representatives, Energy and Commerce Subcommittee on Healthcare, for our hearing today.

Mr. PALLONE. And without objection, so ordered.

[The information appears at the conclusion of the hearing.]

Mr. PALLONE. Would the second panel be seated? Okay. Welcome. Thank you for being here on this important issue today, and let me introduce each of you. Starting from my left is Dr. Raynard Kington, who is Acting Director of the National Institutes of Health, and then we have Mr. Ron Pollack, who is Executive Director of Families USA, and Ms. Rachel King, who is Chief Executive Officer of GlycoMimetics, Inc. from Gaithersburg, Maryland, and lastly is Dr. Joachim Kohn, who is Director of the New Jersey Center for Biomaterials and he is a Professor at Rutgers University in my district in Piscataway. Thank you all for being here. I think you know the drill. We have 5-minute opening remarks. They become part of the record, and each of you may in the discretion of the committee submit additional statements in writing for inclusion in the record, and we will start with Dr. Kington.

STATEMENT OF RAYNARD S. KINGTON, M.D., PH.D., ACTING DIRECTOR, NATIONAL INSTITUTES OF HEALTH

Dr. KINGTON. Good morning, Chairman Pallone and Dr. Burgess, I am Raynard Kington and I am the acting director of the National Institutes of Health, and it is a pleasure to be here to testify before you today on the potential role of NIH in stimulating the economy during the current financial crisis of the country.

The economic downturn, as we all know, is complex in its origins and its recovery process will be multifaceted, and stimulation of the economy is critical to this process. We believe that biomedical research can play a significant factor in stimulating the economy while more importantly advancing the discoveries to improve the health of the public. NIH has a unique ability to provide an influx of funds to an established network of research institutions across the country and this can be accomplished literally within weeks. With a long history of success in scientific discovery, the best peer review system in the world and the trust of Congress and the American people, our impact on public health is well known and is exemplified by substantial reductions in mortality from such diseases as heart disease, many infectious diseases, cancer. It is fueled by new advances such as the sequencing of the human genome, and we are poised to enter an era of personalized medicine that will allow us to accurately predict and then preempt the development of disease.

Although our mission is and must remain first and foremost dedicated to seeking scientific knowledge to improve the health of all, our mechanisms for supporting research are ideally suited to stimulating the economy. NIH is a granting and contracting agency providing awards to research institutions that are an integral component of local economies, many of whom are the largest employers

in their communities. These awards support local economies by creating jobs, building infrastructure and conducting research that leads to new technologies and therapies. In turn, discoveries leads to patents and new businesses producing additional economic benefits, and you will hear more about this from other witnesses.

In fiscal year 2007, NIH funded 47,000 grants worth approximately $20 billion across the country. As you know, recent analyses indicate the NIH grants have a multiplier effect on the economy of up to 2½ times their value and you will hear more about this later. In addition, there is a leveraging effect of 35 percent from the NIH budget in terms of additional private sector investments in medical research stimulated by NIH funding. NIH grants support jobs. We estimate NIH funding supports more than 300,000 jobs in the United States, approximately seven positions for each grant. In addition, through its training programs for Ph.D., postdoctoral, and clinical scientists, NIH supplies a major portion of the human capital required for U.S. biomedical enterprises to remain globally competitive.

To determine the long-term effect of NIH-supported research, we recently reviewed the outcome of approximately 30,000 grants awarded in fiscal year 2000. These grants resulted in over 30,000 invention disclosures, 17,000 non-provisional patent applications and more than 7,000 full patents. At least 17 percent of all drugs approved by the FDA between 1982 and 2006 cited NIH funding as a factor, and we believe that is an underestimate of the importance of NIH funding, especially basic science funding in the development of new drugs. NIH-supported research and training is key for U.S. global competitiveness in the biomedical industry. In today's global environment, large pharmaceutical and biotech companies can choose to locate anywhere in the world. NIH-supported world-glass laboratories filled with the best scientists in the United States based at our universities and other research institutions offer the biomedical industry a tremendous resource in the form of valuable collaborators as well as a pool of the leading scientists to draw upon, a critical incentive to do these businesses in the United States.

Failure to sustain the biomedical research enterprise in this country will have negative implications for science, medicine and public health as well as producing financial stresses on the research institutions that have already leveraged NIH funding with billions of dollars of their own to expand the research capabilities of a nation. With a flat NIH budget over the past 5 years, we have failed to sustain the NIH investment in the U.S. economy. The inability to sustain current levels of funding of scientific opportunity is quantifiable by the percentage of successful grant applications submitted to NIH. The historic norm for success rates has been about 30 percent. Five years of budgets that did not keep pace with medical research inflation have contributed to reductions in the success rate to about 20 percent, and if this trend continues, the success rate will continue to drop.

During fiscal year 2008, NIH identified 14,000 scientifically meritorious research applications that could not be funded. These grants have already undergone peer review process and have been approved by our public advisory councils. With additional funding,

we would focus on these projects and others to fund important new science that otherwise would not be supported. Distribution of funds to many of the projects across the country could occur literally in a matter of weeks. The awards could be made with virtually no increase in NIH's administrative costs through existing processes and mechanisms. Among the underfunded areas of research are clinical trials involving genomics research in multiple disease areas, translational research in heart disease and stroke, AIDS vaccine research, asthma research, health disparities research, research on mental illness and addiction and kidney diseases, advances in imaging and other areas of research. These critical areas of research among others could be immediately funded and expanded for the benefit of the economy as well as for the benefit of the long-term health of this country.

NIH proposes two issues for Congress to consider as it struggles with current economic crisis. One is the potential effectiveness of biomedical research in directly stimulating the economy. The other is the consequence of failure to sustain the research enterprise in the United States at a time when so many important scientific opportunities have been identified. Investment in NIH is an investment in the U.S. economy and more importantly an investment in the future health of our nation.

I thank you again for this opportunity to testify, and I will be happy to answer any questions you might have.

[The prepared statement of Dr. Kington follows:]

Testimony
Before the
Subcommittee on Health
Committee on Energy and Commerce
United States House of Representatives

The Role of Biomedical Research in the Economic Stimulus

Statement of
Raynard S. Kington, M.D., Ph.D.
Acting Director
National Institutes of Health
U.S. Department of Health and Human Services

For Release on Delivery
Expected at 10:00 a.m.
Thursday, November 13, 2008

Good morning, Chairman Pallone and Members of the Subcommittee. I am Dr. Raynard Kington, the Acting Director of the National Institutes of Health (NIH). It is a pleasure to testify before you today on the economic impact of NIH funding. My testimony is intended to provide you information about NIH funding, not to request additional resources above and beyond the President's FY 2009 budget.

With a long history of success in scientific discovery and the best peer review system in the world, we at NIH are the proud stewards of federal funds supporting biomedical research. Our impact on public health is well known, exemplified by substantial reductions in mortality from such threats as heart disease, infectious disease, and cancer. Fueled by new advancements such as the sequencing of the human genome, we are poised to enter an era of personalized medicine that has the potential to predict, preempt, and prevent disease.

Our mission is, and must remain, dedicated to seeking scientific knowledge to improve the health of all citizens. NIH is a grant making and contracting agency, providing awards to research institutions. NIH awards go primarily to non-profit organizations in the private sector. These awards support conducting research that lead to new technologies and therapies. In turn, discoveries may lead to patents and new businesses producing additional economic benefits over the long term. NIH grants are dispersed widely, to all 50 States and covering 90 percent of congressional districts.

In Fiscal Year (FY) 2007, NIH provided 47,000 grants worth $20.4 billion. These grants support salaries, equipment, and infrastructure.

We estimate NIH grant funding supports 300,000 jobs in the United States, approximately seven positions for each grant. To determine the long-term effect of NIH-supported research, we reviewed the outcome of 31,144 grants awarded in FY 2000. The outcomes included 30,477 invention disclosures, 17,341 non-provisional patent applications and 6,909 patents. Seventeen percent of all drugs approved by the Food and Drug Administration from 1982 to 2006 cited NIH patents as a factor. The biotechnology industry that was spawned in the United States in the late 1970s played an important role in the revolution in molecular biology that occurred as a result of Federal funding for brilliant new and continuing investigators. The biotechnology industry has been a major driver of the United States economy over the past 3 decades.

The FY 2009 Budget includes over $3.5 billion for nearly 9,800 new grants. In total, the FY 2009 Budget supports more than 38,000 grants. Enactment of the FY 2009 Budget would enable NIH to focus on priority research areas, including: clinical trials involving genomics research in multiple disease areas; translational research in heart disease and stroke; AIDS vaccine research; asthma research; health disparities; hearing loss; mental illness; addiction; kidney disease; advances in imaging; vaccines; and cancer. These critical areas of research, among others, could be immediately funded and expanded for the benefit of the health of the people here and around the world. The development of new infrastructures for emerging technologies involving

genomics, proteomics, nanotechnology, and systems biology are required to speed new discoveries leading to the next generation of therapeutics. The investment in new research infrastructures will stimulate the acquisition of reagents and supplies necessary to advance these new fields of biomedical science.

Thus, NIH highlights an important issue to consider in regard to the current economic crisis: the potential effectiveness of medical research on the economy. Thank you, and I would be happy to answer any questions you may have.

Mr. PALLONE. Thank you, Doctor.
Mr. Pollack.

STATEMENT OF RONALD F. POLLACK, EXECUTIVE DIRECTOR, FAMILIES USA

Mr. POLLACK. Thank you, Mr. Chairman. Dr. Burgess, I also want to thank you. When you spoke to Mr. Viard on the previous panel and said he would be the grownup to speak before this one, I want to thank you for recognizing my youth. I appreciate it.

My testimony this morning will focus on how additional funding for NIH, America's leading medical research agency and the foremost biomedical research institute in the world, can help the American economy. I do want to say one quick word, however, about the discussion you had in the prior panel. I think that an FMAP increase is critically important. If you look at the last Census Bureau report, it shows that there was a significant continuing drop over the last few years in terms of employer-sponsored insurance, and the fact that we actually had a reduction in the number of people uninsured was attributable to increases in enrollment in Medicaid and the Children's Health Insurance Program. There are at least 18 States that are in the process of significantly cutting back the Medicaid program, and if we don't provide an FMAP increase, we are going to be digging a much bigger hole because as fewer people have coverage in the employer sector, we are not going to have a public safety net to pick them up and the States do not have the ability to do so. At the last pages of testimony, we cited some of the States in terms of what they are doing to cut back. It would make the economy a whole lot worse.

Others on this panel are going to speak to the enormous importance that NIH plays with respect to medical breakthrough, as Dr. Kington just did. I want to testify about the positive economic force that NIH plays with respect to local economies including job creation. Between 80 to 90 percent of NIH's approximate $29 billion budget funds extramural research that takes place in universities, medical research centers, hospitals and other research institutes. We tried to gauge what the economic impact is and we used as a tool for that the so-called RIMS II model that is created by the Department of Commerce, Bureau of Economic Analysis. Our report, which I hope can be entered into the record in your own backyard, describes this in greater detail, but I want to provide you with the most salient findings.

In 2007, NIH awarded almost $23 billion in grants and contracts to universities and research institutions in the 50 States. This funding generated a total of $50.5 billion in new business activity in the form of increased output of goods and services. NIH funding created and supported more than 350,000 jobs, and I want to emphasize that the average wage associated with those jobs was approximately $52,000. These are not jobs that provide really low wages. It is about 25 percent higher than the average U.S. wage.

Let me just exemplify that by what happened in New Jersey. In New Jersey, NIH provided grants and contracts of $280 million in 2007. This generated $631 million in new business activity. It led to the creation of over 3,700 jobs. The average wage in New Jersey that was supported by these new jobs was $57,720, and this oc-

curred as a result of major awards to institutions like the University of Medicine and Dentistry of New Jersey and Rutgers University. In my written testimony, we described what those grants and contracts supported.

In 14 States, NIH funding generated over $1 billion in new business activity. Those states are California, Illinois, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Texas, and Washington. In 10 States, each dollar of NIH funding generated at least $2.26 in economic activity, including in the State of New Jersey. In six States, more than 20,000 jobs were created, including in Texas. In seven States, the average wage per new job exceeded $55,000 including, as I mentioned before, New Jersey. This is all very important because as you heard in the testimony, NIH performs an enormously important service but it has done so with less than a flat budget. If you look at the budget compared to cost of living in real dollar terms, the budget has declined, so it is important that we increase funding for NIH both for the key medical purposes it serves and for the benefit of the economy. Thank you.

[The prepared statement of Mr. Pollack follows:]

FamiliesUSA
The Voice for Health Care Consumers

Statement for the Record
Of
Ron Pollack, Executive Director
Families USA
Before the Committee on Energy and Commerce, Subcommittee on Health
November 13, 2008

Treatments for an Ailing Economy:
Protecting Health Care Coverage and Investing in Biomedical Research

Good morning, and thank you to Chairman Pallone, Ranking Member Deal, and members of the Subcommittee for having this hearing and for inviting me to speak to you today. Families USA is a not-for-profit consumer advocacy organization. We are dedicated to achieving high-quality, affordable health care for all Americans. Among the issue areas we address, we advocate for improvements in health nationally as well as globally through expanded funding for research and development for new tools to fight global diseases.

Families USA is pleased to submit this testimony on the important role of biological research, specifically research funded through the National Institutes of Health (NIH), in stimulating local economies throughout the United States and in fostering economic growth for our nation.

NIH is America's leading medical research agency and the foremost biomedical research institute in the world. The members of the Subcommittee are well aware of the extraordinary advances in health nationally and worldwide that can be traced to NIH funded research, from decreases in death from cancer, heart disease, and stroke to dramatic increases in life expectancy for patients with diabetes and HIV/AIDS. We are here today to speak to another, less well known, contribution that NIH makes to our nation. We are here to testify to NIH's role as a positive economic force in communities across America, and to discuss how NIH stimulates growth and creates jobs in every state.

Between 80 and 90 percent of NIH's $29 billion budget funds "extramural research," research that takes place in universities, medical research centers, hospitals, and research institutes across the country. That money clearly offers a direct benefit to the institutions that receive those funds through NIH grants or contracts. However, it also brings a broader economic benefit to the larger communities of which these institutions are a part.

NIH funding flowing into communities across America represents a new source of spending from outside the state. Spending that comes from outside of the state has a larger impact on the state economy than new spending from within the state alone, through what economists call the

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"multiplier effect." As new spending enters a state, successive rounds of spending occur. The new funds are earned by local businesses and residents who then spend these earnings on purchases from other state firms or residents. By bringing new federal dollars into a region, NIH funding promotes new spending that would otherwise not exist in a state.

In June 2008, Families USA published a report quantifying the economic impact of NIH funding on the economy of each state and nationally. That report, entitled *In Your Own Backyard: How NIH Funding Helps Your State's Economy,* used data on NIH's fiscal year 2007 grants and contracts to each state to measure the broad economic benefit that states receive from NIH funding. A copy of that study is submitted along with this testimony.

Measuring the Benefit of NIH Funding on State Economies

Families USA used the Regional Input-Output Modeling System (RIMS II) created by the U.S. Department of Commerce, Bureau of Economic Analysis to determine the overall impact of NIH funding on each state's economy. The RIMS II model measures, within a region, the extent to which an investment in one industry affects all other industries in that region, and ultimately, the region's economy. RIMS II can be used to estimate the impact of a variety of different projects, such as development of new retail establishments, construction, and university expenditures. The RIMS II model includes hundreds of economic multipliers to measure the impact of new spending in different industries.

For its analysis, Families USA used the RIMS II multipliers for the scientific research and development (R&D) industry, as the industry measure that would most accurately reflect the impact of NIH's biomedical research funding. RIMS II multipliers are specific for each state, based on an analysis of each state's economy and industry structure. The RIMS II model allowed us to estimate three economic impacts that NIH funding would have in a state.

- The first is economic output, or the value of goods and services produced in the state. RIMS II measures the increased demand in a state for goods and services supplying the research activity.

- The second is employment, or the number of jobs created in the state by the change in demand.

- The third measure is employee earnings, or the wage and salary income associated with the affected jobs.

NIH Funding: A Direct Contribution to Economic Growth

Our analysis showed that NIH spending has a significant impact on state economies. In fiscal year 2007, NIH awarded approximately $22.8 billion in grants and contracts to universities and other research institutions in the 50 states. Seven states received more than $1 billion in funding from NIH. On average, each dollar of NIH funding going into a state generated more than twice as much in state economic output. Nationally, the investment of $22.8 billion from NIH generated a total of $50.5 billion across the states in new business activity in the form of increased output of goods and services.

NIH funding also contributes to state job creation. In fiscal year 2007, NIH funding created and supported more than 350,000 jobs that generated wages in excess of $18 billion in the 50 states. NIH funding not only created new jobs, but it created high-paying jobs. The average wage associated with the jobs created was $52,000, nearly 25 percent higher than the average U.S. wage of $42,000.

Although the value of NIH awards varies widely from state to state, institutions in every single state received NIH grants or contracts. As a result, NIH funding contributed to business growth and job creation in every state.

For example, in New Jersey, $280 million in NIH funding in 2007 generated $631 million in new business activity and led to the creation of 3,738 new jobs. The average wage associated with those jobs was $57,720. NIH funds benefited a cross section of New Jersey universities, hospitals and businesses. Major award recipients included the University of Medicine and Dentistry of New Jersey, which received over $120 million to support research, training, and clinical trials at the University and its affiliated teaching hospitals; and Rutgers University, which received over $60 million to support research at multiple campuses.

In Georgia, $374 million in NIH funding generated $883 million in new business activity in the state, creating 6,774 new jobs with an average wage per job of $46,924. The state's award recipients truly spanned from A to Z, from Agnes Scott College to Zygogen, an Atlanta company that offers technology supporting clinical research. Major recipients of NIH funding included Emory University, receiving over $225 million; the University of Georgia, with over $33 million in awards; and Morehouse School of Medicine, with over $22 million in funding from NIH in 2007.

Looking more broadly at the impact of NIH funding on business and job growth nationally, this is a snapshot of the positive impact of NIH funding on state economies.

- The amount of new business activity generated ranged from $8.39 billion in California to $13 million in Wyoming.

- In 14 states, NIH funding generated over $1 billion in new business activity. Those states are: California, Illinois, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Texas, and Washington.

- In ten states, each dollar of NIH funding generated at least $2.26 in economic activity: Texas ($2.49); Illinois ($2.43); California ($2.40); Georgia ($2.36); Colorado ($2.34); Pennsylvania ($2.32); Tennessee ($2.32); Utah ($2.30); Ohio ($2.29); and New Jersey ($2.26).

- In six states, more than 20,000 new jobs were created. Those states are: California (55,286 new jobs); Massachusetts (30,864); New York (27,877); Maryland (21,299); Pennsylvania (21,262); and Texas (20,148).

- In seven states, the average wage per new job created exceeded $55,000: Connecticut ($60,285); Massachusetts ($58,801); Delaware ($57,960); New Jersey ($57,720); Nevada ($56,664); California ($56,268); and Illinois ($55,566).

Substantial Indirect Benefits

In addition to the substantial economic growth that can be measured through the RIMS II modeling, NIH funding contributes to the economic health of communities across the country in other ways that are less readily quantified.

Helping Universities Grow. NIH awards help universities, medical schools, and other research institutions to expand their programs and to attract funding from additional sources. The level of federal research funding that a university receives—of which NIH grants are a key component—is one of the criteria used to rate universities by sources as divergent as think-tanks, such as the Center for Measuring University Performance, to popular rating systems such as U.S. News & World Report. Higher ratings can translate into more applicants and a growing student body. This is critical to the economic health of the many communities nationwide where universities are a major sources of jobs, tax revenue, and area growth.

Helping Businesses Grow. While the bulk of NIH funding goes to universities, medical colleges, and research institutes across the country, some funding is directed to businesses. A state-by-state review of NIH grants shows that funding recipients include a mix of academic institutions, hospitals, research centers, and large and small businesses. NIH also helps businesses grow through non-grant resource sharing arrangements. NIH's Cooperative Research and Development Agreements (CRADAs) and Material Transfer Agreements (MTAs) allow resources, facilities, and expertise to be shared between NIH and industry. From 1985 to 2004, NIH entered into more than 400 CRADAs. From 1991 to 2004, at least 15 drugs and vaccines approved for use were developed through NIH/industry relationships.

Improving Local Health Care and Quality of Life. NIH funding can also have a positive impact on local health care by improving the quality of medical services available in communities across the country. For example, NIH funds help out schools that are affiliated with hospitals, and as a result these hospitals perform better. Of the 20 highest-ranked hospitals, 19 were affiliated with one of the 25 top NIH-funded medical schools. Additionally, studies have found a facility's participation in clinical trials—one of the research components that NIH funds—is positively correlated to health outcomes. In 2007, NIH spent $3 billion on clinical trials. Much of that funding went to medical centers across the country, contributing to better health outcomes. Better health outcomes can translate into improved worker productivity and economic growth.

Helping Local Economies and Improving Health Globally. NIH funds research addressing health problems of a global scale. This includes research on "neglected infectious diseases" such as malaria, tuberculosis, and a host of tropical diseases—diseases that are most prevalent in low-income countries, and that are insufficiently researched by the drug industry. For example, NIH has awarded $23.7 million to Emory University in Atlanta over seven years to evaluate new vaccines and therapies for infectious diseases; $7.8 million to Texas A&M University to research tuberculosis drugs; and $4.8 million to the University of North Carolina's Carolina Vaccine Institute for research into vaccines for dengue fever.

These types of awards not only support growth in the U.S. communities that receive the research funding, but also help the United States show leadership in addressing major health problems globally—problems that, if better addressed, will contribute to economic growth internationally, which, in a global economy, translates to growth here at home.

Economic Benefits at Risk Due to Funding Stagnation

For the last five years, NIH's budget has been steadily declining. This has compromised the agency's capacity to fund medical research across the country and has hurt universities and other institutions that depend on NIH funding. In turn, that has hurt the communities where these institutions are an integral part of economic growth.

As part of its study of NIH's impact on state economies, Families USA used the RIMS II multiplier to estimate the impact that a 6.6 percent increase in NIH funding would have on state economies. We chose 6.6 percent because that level of increase is needed to offset past flat funding and to adjust for current inflation. For illustration purposes, we applied that hypothetical increase evenly across all states when making our calculations.

If the sum of all NIH awards to the states was increased by 6.6 percent—roughly $1.4 billion—the economic benefit of that increase would be an additional $3.1 billion in new business activity, 9,185 additional jobs, and $1.1 billion in new wages. There would also be the additional economic benefits that are difficult to measure. Those are the benefits of college and university growth, business development, and improved community health care.

Investment in NIH Stimulates Economic Growth

As the Congress looks at our investment in health care and ways that investment can stimulate economic growth, it should keep in mind the interrelated set of benefits that flow from NIH funding. The government's investment in NIH is an investment in the physical and economic health of our communities and our nation. An NIH budget that fails to keep up with inflation and that fails to foster scientific growth hurts labs, hospitals, universities, businesses, communities, and America's standing as a world leader in medical research. On average, every dollar invested in NIH generates more than twice that amount in state economic output. That is an excellent investment—it is an investment that can stimulate state economies while helping ensure that we maintain our preeminence in biomedical research.

Other Investments in Health Care

With the economy continuing to decline, further economic stimulus is important to states. While there are many ways to stimulate the economy, one of the most effective ways is to temporarily increase the federal matching rate for Medicaid, otherwise known as the Federal Medical Assistance Percentage (FMAP). If the federal government pays a larger share of Medicaid costs through a temporary increase in the FMAP, states can sustain their programs—rather than cutting them when families most need help—while simultaneously facilitating national economic recovery. In fact, Families USA has data that show—on a state-by-state basis—that temporarily increasing the FMAP is an effective and proven way to stimulate the economy, and it provides

immediate relief to state and local economies. We are happy to share these data with the Subcommittee.

Without help from the federal government, states would be forced to reduce spending (often by cutting Medicaid). This further aggravates an economic downturn. Unfortunately, many states across the country have already made significant cuts to their Medicaid programs in the face of this economic crisis. At least 18 states have made or are proposing cuts for the current fiscal year and beyond. Many of these states made cuts this past cycle as they struggled to fill budget deficits in order to pass their Fiscal Year 2009 budgets. As the economy has continued to decline over the past few months, state revenues have fallen well below projected amounts. As a result, a number of states—including several that already made cuts and others that just barely averted cuts in developing their current budgets—are now making or considering mid-year budget cuts. Medicaid programs across the country are facing significant funding cuts.

Cutting Medicaid has a real and significant impact on individuals and families. As a result of the cuts states have made and are currently considering, fewer people will qualify for Medicaid, and it will be harder for many to enroll. For those who are enrolled, it will be more costly to get health care services, and fewer services will be covered. And it may be more difficult to find a provider who takes Medicaid, because several states are cutting reimbursement rates for health care providers. For example:

- In its fiscal year 2009 budget, California implemented enrollment barriers, increased cost-sharing, and cut provider reimbursements. Needing to fill a mid-year budget gap, the state is now proposing making further cuts, including eliminating coverage for some parents; cutting benefits; increasing cost-sharing for the aged, blind, and disabled; and reducing funds to public hospitals.

- Rhode Island eliminated coverage for some parents and increased cost-sharing. Even more troubling, in order to delay significant Medicaid cuts, Rhode Island is asking the federal government to give it additional Medicaid funds "up front" in exchange for an agreement that would put a hard cap on the amount of federal Medicaid funding the state could spend on Medicaid over a 5-year period. Essentially, Rhode Island is asking the federal government to "block grant" its Medicaid program. This will have a serious detrimental affect on Rhode Islanders in the future.

- Maine implemented an enrollment fee for some parents, which will deter many from being able to attain coverage.

- New Jersey cut charity care funding to hospitals, which will limit its ability to treat Medicaid and uninsured patients.

- Utah recently made mid-year cuts by eliminating some benefits and cutting provider rates.

- Nevada implemented an enrollment cap for its CHIP program to the approximate number of current enrollees; many uninsured and eligible children will now be left without access to health care. The state also increased cost-sharing, eliminated coverage for almost 100

pregnant women, and implemented stricter eligibility standards for elderly and disabled individuals needing institutional care.

- New York cut payments to managed care organizations and delayed implementation of a Medicaid enrollment center. The Governor is proposing billions of dollars in additional cuts from the Medicaid program, including reducing the rate of budget growth from 4 percent to 1.7 percent, and significantly cutting funding for hospitals and nursing homes. These cuts will have a detrimental effect on Medicaid beneficiaries.

These are just a few examples of the harmful Medicaid cuts taking place in the states. As states grapple with looming budget deficits resulting from the bad economy, more cuts are likely to happen.

But Congress can prevent more harm from coming to the low-income and vulnerable people who rely on Medicaid for access to critical health care services. A temporary increase in the FMAP can help state Medicaid programs sustain their Medicaid spending and avoid or minimize further cuts. Temporarily raising the FMAP has proven to be a useful tool that helps states avoid Medicaid cuts and helps them meet the increasing enrollment demands that arise during an economic downturn. Medicaid enrollment rose by 8.6 percent between 2001 and 2002 because of the recession. Congress passed the Jobs, Growth, and Tax Relief Reconciliation Act of 2003, which temporarily increased the FMAP. As a result, states received $10 billion in federal funding, which was instrumental in helping states such as Minnesota, Missouri, and Ohio avoid or postpone cutbacks in eligibility and benefits.

Not only will an FMAP increase protect Medicaid beneficiaries, it will also buffer states' economies. This injection of new federal dollars into state economies has a measurable effect on states' business activity, wages, and jobs. The new dollars pass from one person to another in successive rounds of spending, generating additional business activity, jobs, and wages that would not otherwise be produced. Economists call this the "multiplier effect." Increasing federal Medicaid spending amplifies this effect.

Conclusion

Investments in health care can provide a stimulus that benefits communities across the country. But they can do even more. Investments in NIH bolster U.S. medical and scientific leadership. A temporary increase of the FMAP is a way to preserve Medicaid, support access to medical care for our most vulnerable citizens, and boost state economies during this time of economic crisis. Families USA supports both.

Mr. PALLONE. Thank you.
Ms. King.

STATEMENT OF RACHEL KING, CHIEF EXECUTIVE OFFICER, GLYCOMIMETICS, INC.

Ms. KING. Thank you very much, Chairman Pallone and Dr. Burgess. I am delighted to be here today. I am the CEO of GlycoMimetics, which is a biotechnology company, and our lead product is in clinical trials today for the treatment of sickle cell disease. I am here today representing the Biotechnology Industry Organization where I serve as a member of the board of directors as well as chair of the emerging company section, and I am really happy to be here today to discuss policies that Congress can implement both to spur the economy and to ensure the continuation of biomedical research.

Federal funding of the National Institutes of Health is clearly one of the most important things that we believe can be done both to stimulate the economy and to provide that critical research support, and BIO fully supports any and all efforts to do this. An increase in NIH funding though is just one of the things that Congress can do to invigorate the economy and to spur biomedical innovation. While some of these additional proposals may not fall directly within the jurisdiction of the Committee on Energy and Commerce, it is our hope that Congress will consider them as part of any stimulus package as they would have a meaningful impact on the ability of biomedical innovation to continue during these tough economic times.

The biotechnology industry holds tremendous promise for the future of healthcare. The industry has already delivered over 250 FDA-approved therapies, many of which address important areas of unmet medical need or are first in class treatments. Biomedical research and innovation and the development of new treatments and therapies are key economic drivers. Life science R&D, as has been mentioned, provides high-tech, high-wage jobs at both public research institutions and at the biotech companies that typically locate close to these centers of academic research. However, in this economic crisis, many biotechnology companies are now struggling for survival. In October alone, over 20 companies publicly announced layoffs. Many other companies are making programmatic adjustments such as shelving important research to conserve financial resources and to reduce cash burn rates. These companies are struggling because the financial markets are effectively closed to public biotechnology companies. Public market investors have been unwilling to participate in initial public offerings, and without strong governmental policies, the outlook for these companies remains dire.

Increasing federal funding for biomedical research is a critical first step to alleviate the financial uncertainty that the industry is facing. An increase in NIH-supported research will yield more basic scientific findings and can also advance clinical and translational knowledge associated with the diagnosis and treatment of disease. NIH-supported research can potentially advance the early stages of development of new biotechnology products and thereby reduce the R&D burden on industry. The NIH also plays a critical role in the

transfer of technology through which the fruits of NIH intramural research are transferred to industry, ultimately where they can be developed into preventative, diagnostic and therapeutic products that will advance our ability to improve public health.

Since completion of the doubling of the NIH budget over the 5-year period from 1998 to 2003, annual appropriations for the agency have fallen below the rate of biomedical research inflation. Congress has been able to provide incremental funding increases, however, we fall well short of the costs associated with biomedical research and technology development inflation. To maintain research grants at current funding levels, annual increases of at least 3½ to 5 percent are required. The funding of the last 5 years has effectively resulted in a 17 percent decrease in spending power on research for the NIH, and this is a serious challenge to the biotechnology industry. BIO strongly supports an additional $1.9 billion in funding for the NIH. This increase in funding would put us on the track of sustainable growth that is necessary to realize the full potential that we see.

While I acknowledge that this committee does not have jurisdiction over tax policy, I want to take this opportunity to highlight some potential proposals that would infuse much-needed capital into the industry at this critical juncture. For example, corporate tax proposals allowing loss-making companies to immediately utilize their accumulated tax assets such as net operating losses and research development tax credits would infuse much-needed capital into emerging biotech companies. Additionally, the enactment of certain investor tax proposals, a short-term stimulus for investments such as reductions in the capital gains rate, capital gains rollover or reduced capital gains specifically for funds invested in our industry would also serve to encourage investment.

While the current crisis has substantially impacted the industry, I do remain optimistic that the biotech industry will triumph by working closely with the Congress, the Administration and by important institutions like the NIH we will be able to continue to support biomedical innovation by increasing these government investments as well as enacting financial policies that will incentivize investment in the industry.

Thank you very much.

[The prepared statement of Ms. King follows:]

HEARING TESTIMONY

RACHEL K. KING

CHIEF EXECUTIVE OFFICER
GLYCOMIMETICS, INC.
ON BEHALF OF

THE BIOTECHNOLOGY INDUSTRY ORGANIZATION

HOUSE ENERGY AND COMMERCE HEALTH SUBCOMMITTEE HEARING:

"TREATMENTS FOR AN AILING ECONOMY: PROTECTING HEALTH CARE COVERAGE AND INVESTING IN BIOMEDICAL RESEARCH"

NOVEMBER 13, 2008

Chairman Pallone, Ranking Member Deal, Members of the Subcommittee: I am Rachel King, Chief Executive Office or GlycoMimetics, Inc., and I am appearing before this subcommittee on behalf of the Biotechnology Industry Organization (BIO) where I serve on the Board of Directors and as Chair of the Emerging Companies Governing Board. It is my privilege to testify before the Subcommittee today to discuss policies Congress can implement to spur the economy and ensure the continuation of biomedical innovation in the United States. Of course one way to both spur the economy and provide support for biomedical research is increasing Federal funding of the National Institutes of Health (NIH). BIO fully supports any and all efforts to do this. But an increase in funding for NIH is just one thing the Congress can do to invigorate the economy and biomedical innovation. My testimony will also cover other recommendations

the Congress should undertake to accomplish these worthy goals. While these additional proposals may not fall technically within the jurisdiction of the Committee of Energy and Commerce, it is our hope Congress will consider them as part of any stimulus package, as they would have a meaningful impact on the ability of biomedical innovation to continue during these tough economical times.

I have been the Chief Executive Officer of GlycoMimetics, Inc. located in Gaithersburg, MD since 2003 and part of the biotechnology industry for 20 years. GlycoMimetics currently has 20 employees who are developing carbohydrate mimics representing an important new class of drugs. We have developed a specialized platform technology which is producing first-in-class drug candidates with an initial focus on inflammation, cancer and infectious disease. Our lead compound, currently in Phase I clinical trials, will provide treatment for patients suffering from sickle cell disease, an area of substantial unmet medical need.

Importance of Investing in Biomedical Research

Biomedical research and innovation, and the development of new treatments and therapies are key economic drivers, especially as we work to strengthen our economy in the face of a recession. Life sciences R&D provides high wage jobs at both public research institutions and in the biotech companies that typically locate near centers of academic research. The indirect effects of increased research funding on the regional economy is significant. For example, sponsored biomedical research directly generates jobs in the host institutions, and indirect and induced job creation in the region amounts to additional job growth. In fact, the nation's 1.2 million bioscience jobs generate an additional 5.8 million jobs in the Unites States, resulting in a total employment impact of 7 million jobs. Additionally, wages for bioscience

workers have increased 6.4% since 2001 compared with only 1.4% increase in real earnings for the average U.S private sector worker. As economic development becomes more competitive locally, regionally, and internationally, biomedical sciences that have always been intrinsically valued gain extrinsic value.

However, lack of investment by either the government or the private sector discourages the next generation of young scientists. Decreasing research and job opportunities for young scientists threatens the nation's competitive edge in the global economy – we risk losing the best new scientific minds to other fields, or research programs in other countries.

Federally-supported biomedical research builds the foundation of scientific and clinical knowledge that is widely communicated and used to improve the development of diagnostics, treatments and cures. The Federal government funds biomedical research in the United States primarily through the National Institutes of Health (NIH). An increase in NIH-supported research will yield more basic scientific findings and can also advance clinical and translation knowledge associated with the diagnosis and treatment of diseases. NIH-supported research can potentially advance the early stages of development of new biomedical products and thereby reduce the R&D burden on industry. The NIH also plays a critical role in the transfer of technology through which the fruits of NIH intramural research are transferred to industry to be developed ultimately into preventive, diagnostic, and therapeutic products that advance our ability to improve public health. Additionally, companies that market advanced laboratory research tools also obviously benefit from and increased investment in the federal biomedical research effort.

The NIH is the nation's premier research agency for the study of human health conditions, diagnostics, and treatments. However, for the past five years the NIH budget has been flat or declining in real-dollar terms. This is happening at a time of unprecedented capacity for research, as well as an unprecedented demand for new healthcare solutions. The NIH research infrastructure is simply unable to meet the growing demand for project grants, and many important well-designed research projects are going unfunded. Moreover, there is no private sector alternative for much of the basic research that NIH supports. Adequate funding for NIH is necessary to sustain the public-private collaboration that is transforming biomedical discoveries into innovative treatments for patients.

Since completion of the doubling of the NIH budget over the five-year period, 1998-2003, annual appropriations for the agency have fallen below the rate of biomedical research inflation. Congress has been able to provide incremental funding increases, however we fall well short of the costs associated with biomedical research and technology development inflation. To maintain research grants at current funding levels, annual increases of at least 3.5-5% are required. The funding of the last 5 years has effectively resulted in a 17% decrease in spending power for the NIH. This is a serious challenge to the biotechnology industry. BIO strongly supports an additional $1.9 billion in funding for NIH. This increase in funding will put us on the track of sustainable growth that is necessary to realize our potential.

Financial State of the Biotechnology Industry

The biotech industry holds great promise for the future of health care, and has already delivered over 250 FDA-approved therapies, many of which address areas of unmet medical need or are first-in-class treatments. Unfortunately, though, the financial crisis facing our nation

continues to have a profound impact on biotech companies and threatens biomedical innovation and U.S. competiveness. The U.S. biotech industry is the unquestioned world leader, and this is an industry that has started and been built in our country. However, the economic crisis we face is having a dramatic impact on our companies.

On average, it takes more than a decade and $1 billion to develop a new molecule for approval. As a result, biotech companies go for years without revenue, instead relying on financing from investors. Emerging biotech companies – comprising over 85% of the industry – are therefore highly dependent on well-functioning capital markets to finance their long term, capital-intensive research and development projects. Over the past 14 months, the credit markets have seized up, making less capital available for investors to put at risk; and the capital that is put at risk is dedicated to shorter-term, lower-risk options other than biotechnology. Since biotech investing is higher-risk and longer-term in nature, while some areas of the economy have seen a slowdown, biotechnology has seen a near-freeze.

With financing generally coming from equity investments, both public and private biotechnology companies have been adversely impacted by the economic crisis. The financial markets are effectively closed for public biotech companies. Public market investors have been unwilling to participate in initial public offerings (IPOs) or follow-on (secondary) financings. Compared with 2007, IPOs for the first 9 months of 2008 have fallen 96% and follow-on/secondary offerings have fallen 50%. Without strong governmental policies, outlook for these companies remains dire at best. Ninety-nine companies are operating with less than six months' worth of cash, which accounts for 25% of all public U.S. biotech companies. Likewise, the number of public biotech companies that are presently valued at less than their cash-on-hand

has risen nearly ten-fold over the past 24 months. There has been a dramatic slowdown in private investments as well, and overall, the total capital raised by the industry has fallen by a considerable 56% in the last year.

What does this mean for many emerging biotechs? The current economic crisis puts them in a precarious situation where they must continue their development projects, but are unable to attain additional financing from investors. Many of these companies, like my own, are in the development phase, do not have product revenues, and therefore are net cash burners. The bottom line is that these companies are experiencing uncertain financial situations and cannot postpone raising capital indefinitely

As other countries try to mimic the U.S. model, and make massive investments in biotech, our industry faces challenges unlike those we have seen in the past. Equally important, as this financial crisis impacts our companies, biotech companies with promising therapies are facing the need to shelve promising therapies or delay their development to conserve cash, postponing the availability of new therapeutic options for patients.

Emerging Biotechnology Companies Face Difficult Business Decisions

Challenged by these financial realities, many emerging biotech companies are struggling for survival and forced to continually make operational adjustments, unfortunately at an accelerating pace. Such difficult operating decisions include postponing development of new therapies or laying off employees to reduce operating expenses. In October alone, over 20 companies publicly announced layoffs. Many other companies are making programmatic

adjustments, such as shelving important research to conserve financial resources to reduce cash burn rates.

Critical Point in U.S. Biotechnology Innovation

The economic crisis jeopardizes the current U.S. competitive edge over the rest of the world. The biotechnology industry can serve as an engine to build an innovation-based economy and help create economic growth by (1) creating high-value, high-wage U.S. jobs; (2) continuing U.S. leadership in innovation; and (3) addressing and advancing solutions to pressing healthcare, global warming, environmental, energy security and agricultural issues.

As you look for solutions to the economic crisis, it is critical to consider legislative and regulatory policies that will improve the investment climate for the competitiveness of U.S. emerging biotech companies. Any stimulus legislation should include proposals that will help emerging companies to shore-up their balance sheets and provide incentives to attract and retain investment in our industry.

Corporate and Investment Incentives for Emerging Biotech Companies

While I acknowledge this Committee does not have jurisdiction over tax policy, I would like to take this opportunity to highlight some potential proposals that would infuse much needed capital into the industry at this critical juncture in innovation. Congress should consider capital formation tax provisions as part of an economic stimulus package and tax reform legislation.

Corporate tax proposals allowing loss-making companies to immediately utilize their accumulated tax assets, such as Net Operating Losses (NOLs) and research and development (R&D) tax credits, would infuse much-needed capital into emerging biotechs. Also, any reforms

to the current rules limiting the use of NOLs upon a substantial change in ownership would encourage investment.

1. ***Refund of NOLs in Lieu of Other Tax Benefits to Sustain Critical R&D***

   Allowing a taxpayer to temporarily elect to receive a refund of their NOLs at a discounted rate to offset qualified research expenses and in lieu of claiming other tax benefits for those expenses, such as the R&D tax credit. This policy would extend and expand opportunities for loss-making companies. Under this proposal, a company would permanently forgo all accumulated NOLs involved in computation of a refund. Furthermore, NOL refunds would be reinvested in investments that would qualify as research expenses.

2. ***Refund of R&D Credits Modeled on Recently-Enacted R&D/AMT Provision***

   A provision in the July 2008 stimulus legislation provided for companies to claim a refund of the R&D and AMT credits in lieu of claiming "bonus depreciation" to offset capital expenditures. While this legislation was helpful for a number of biotechs, extending this provision for 2009 and 2010 and expanding the provision would allow emerging biotechs to receive much needed capital infusion for investments in U.S. employees and lab supplies. Specifically, it would also be beneficial to temporarily allow a taxpayer to claim a refund of the R&D and AMT credits in lieu of claiming "bonus depreciation" AND "qualified research expenses" at a discounted rate.

3. ***Suspension of Section 382 NOL Limitations Upon Substantial Change in Ownership***

Another proposal that could serve to encourage mergers and acquisitions in the biotechnology industry is ensuring that the Code Section 382 limitations on the use of NOLs are not triggered by successive rounds of equity financings, or a business-driven merger of companies. Congress should look at reforming Section 382 rules at least on a temporary basis—as the Treasury Department has recently done for the financial industry during this economic crisis.

4. ***Encourage Investments in Biotechnology***

Additionally, the enactment of certain investor tax proposals would encourage investments in the biotech industry. For example, Congress should consider short term stimuli for investments such as a zero capital gains rate, capital gains rollover, or reduced capital gains for funds invested in our industry.

Long-Term Outlook for Biotechnology Remains Strong

While the current crisis has substantially impacted the industry, I remain optimistic that the biotech industry will triumph by working closely with Congress and the Administration to ensure policies are enacted that will support U.S. innovation in biomedical research by increasing government investments, as well as creating financial policies that will stabilize emerging biotechnology companies and incentivize private sector investment in the industry. I believe the long-term outlook for the biotech industry remains strong.

Thank you for the opportunity to testify before you today on the very important matter of both stimulating the economy generally, and more specifically stimulating biotechnology investment. I'm happy to answer any questions you may have.

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Mr. PALLONE. Thank you.
Dr. Kohn.

STATEMENT OF JOACHIM KOHN, PH.D., DIRECTOR, NEW JERSEY CENTER FOR BIOMATERIALS AND PROFESSOR, RUTGERS, THE STATE UNIVERSITY OF NEW JERSEY

Mr. KOHN. Thank you very much, Mr. Chairman, Congressman Burgess and members of the subcommittee. My name is Joachim Kohn and I am pleased to address this committee about the economic value to the nation of investment in the NIH.

As a Rutgers professor, I hold the title of Board of Governors professor of chemistry. I am also the director of the New Jersey Center for Biomaterials and an adjunct associate professor for orthopedics. I am testifying here today because of my dual experience as an NIH-funded academic researcher as well as an entrepreneur who has started three companies and whose inventions have become FDA-approved medical products.

I would like to make two key points. First, NIH funding has obviously an immediate short-term stimulating effect on the economy. This short-term effect has been well described in the report by Families USA. I would like to confirm that I agree with the findings of this report. My second key point is that NIH funding has a pronounced long-term effect on the economy and the well-being of our Nation. I describe this long-term benefit as economic leverage. Simply stated, the investments made by NIH-funded researchers are the basis of a substantial amount of economic activity relating to the translation of these inventions to medically useful products.

In my personal experience, the economic leverage has been tremendous. As little as $4.5 million in NIH support for my research activities at Rutgers resulted in technology commercialization efforts in four startup companies. Briefly, TyRx Pharma, REVA Medical, Lux Biosciences, and Renova Biomaterials have licensed my NIH-derived inventions and have since then raised a total of $132 million in private equity and I have now created over 100 high-paying jobs, all paid for by private funding without further NIH support. Let me emphasize again that without NIH funding, none of these companies would be in existence today.

The NIH investment of $4.5 million made throughout the 1990s continues to bring benefits to our economy today. TyRx Pharma has obtained FDA market clearance for two products and continues its research and marketing operation in New Jersey. REVA Medical is testing a revolutionary coronary stent in clinical trials in Germany and Brazil with the expectation to start extensive clinical trials in the United States sometime in 2009 in the middle of our economic crisis. Lux Biosciences is completing phase III clinical trials of Voclosporin for the treatment of major and common diseases of the eye such as dry eye syndrome, uveitis and age-related macular degeneration. And Renova has just now been incorporated and has already attracted $1.2 million in its first round of financing. Renova has now started to operate in Somerset, New Jersey. This level of economic activity has been made possible by private follow-up investments which have so far leveraged the original government funding at a staggering ratio of 29 to 1.

Finally, in terms of the total benefit to society, I can see one additional economic incentive for the government's investment, which I refer as the indirect health dividend. By this I mean the value of the improvement in the health of the Nation as well as the reduction in healthcare costs derived from new products developed with NIH funding. I can illustrate the health dividend best with a personal experience again. Macular degeneration threatens my aging mother with blindness. Twice a day a nurse has to come by my mother's house to administer her prescription eye drops. My mother at age 84 is simply too frail to administer these drops herself. In response to this need shared by millions of disabled and elderly Americans, I am collaborating with Lux Biosciences to develop a new fully bioresorbable drug delivery system that can be inserted into the eye and that will deliver a variety of ophthalmic drops for 6 to 12 months continuously, eliminating the need for daily nurse visits. The polymers we are using to develop this drug delivery system were invented as part of an NIH-funded research project in my lab.

An additional example of the indirect health dividend is provided by the antimicrobial sleeve developed by TyRx Pharma to protect patients with cardiac implants such as pacemakers from infection. This product alone has the potential to reduce the national healthcare costs by $240 million each year as outlined in my written testimony.

In conclusion, Mr. Chairman, the NIH stimulates our economy in many ways. In the short term, we can quantify these economic benefits in terms of the direct stimulatory effect as well as the significant multiplier ripple effect that is felt throughout the Nation. In addition, in the long term, I believe that the grants and contracts provided by the NIH have a disproportionately large and lasting impact on our economy through the significant leverage of NIH funding by private capital and through the health dividend. I am firmly convinced that increasing the NIH budget whether in a near-term stimulus package or as part of future funding bills will pay off both now and in the long run. I encourage you to take this comprehensive view, and I thank you for the opportunity to testify.

[The prepared statement of Mr. Kohn follows:]

SUMMARY
Testimony of Joachim Kohn, Ph.D
Board of Governors Professor of Chemistry and Chemical Biology
Rutgers, the State University of New Jersey

Before the

Subcommittee on Health of the Committee on Energy and Commerce
10:00 am, Thursday, November 13, 2008
2123 Rayburn House Office Building

Hearing entitled "Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research."

Joachim Kohn, Ph.D., Board of Governors Professor of Chemistry at Rutgers, the State University of New Jersey and Director of the New Jersey Center for Biomaterials, describes the economic value to the nation of investment in the National Institutes of Health via four mechanisms: 1) The immediate (direct) stimulatory effect of a cash infusion into the research community and its local economy; 2) the (indirect) ripple effect of growth opportunities for universities, medical centers, and local companies; 3) the long term economic benefits relating to the leverage of the original NIH investment by private sector funds aimed at the translation of NIH inventions into medically useful products, services and new therapies; and 4) the health dividend derived from the clinical use of the new products and services.

NIH investment of $4.5 MM in the Kohn laboratory has so far generated $132 MM of private venture investment in four companies that are developing implantable medical products using innovative biomaterials invented under NIH support at Rutgers. Two products developed by TyRx Pharma, Inc. are in clinical use to reduce infection following hernia repair operations and implantation of cardiac rhythm medical devices. A revolutionary coronary stent developed by REVA Medical Inc is in clinical trials in Germany and Brazil with the expectation to start clinical trials in the US sometime in 2009. Clinical trials by Lux Biosciences are also underway for ophthalmic drug therapies targeting major diseases of the eye, such as "dry eye syndrome", uveitis, and (age related) macular degeneration.

In summary, these economic activities created high paying jobs, provided a 29-fold leverage of government funding by private funding, and promise to yield significant reductions in our national health care costs.

Professor Kohn stated his firm conviction that increasing the NIH budget, whether in a near-term stimulus package or in future funding bills will pay off both now and in the long run.

Testimony of Joachim Kohn, Ph.D
Board of Governors Professor of Chemistry and Chemical Biology
Rutgers, the State University of New Jersey

Before the

Subcommittee on Health of the Committee on Energy and Commerce
10:00 am, Thursday, November 13, 2008
2123 Rayburn House Office Building

Hearing entitled "Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research."

My name is Joachim Kohn and I am pleased to be able to address this committee about the economic value to the nation of investment in the National Institutes of Health.

At Rutgers, the State University of New Jersey, I hold the title of Board of Governors Professor of Chemistry and Chemical Biology. I am also the Director of the New Jersey Center for Biomaterials, and an Adjunct Associate Professor of Orthopedics at the University of Medicine and Dentistry of New Jersey. One of my most significant current activities is my leadership in the Armed Forces Institute of Regenerative Medicine (AFIRM) - a DoD-funded national effort to advance medical research rapidly into the clinic to benefit severely injured military service members.

Over the course of my studies, I have not only published more than 200 scientific manuscripts, but also have made numerous inventions which have resulted in a portfolio of about 40 issued US patents (and a commensurate number of related international patents and patent applications). As part of my entrepreneurial activities, I have founded three spin-off companies (Vectramed, TyRx Pharma, and Renova) and participated in the successful negotiations for a total of eight technology transfer licenses (Integra, Vectramed, Surmodics, Osteotech, TyRx Pharma, Lux Biosciences, REVA Medical, and Renova). I have received the prestigious Thomas Alva Edison Award for Best Patent in New Jersey twice, and have been inducted into the New Jersey Biotechnology Hall of Fame. I have had the honor of being an invited speaker on several occasions both in Europe and at home, on the topic of the technology transfer process in the US and the commercialization of University inventions. Since joining the faculty at Rutgers in 1986, I have received NIH awards continuously through a variety of funding mechanism ("First

Award", "Career Development Award", multiple R01 awards, SBIR awards, and a P41 Award). Thus, through my work as an NIH funded academic researcher and a successful entrepreneur, I have significant personal experience relating to the impact of NIH funding on our economy.

In my testimony today, I would like to make two key points:

First key point: Immediate economic impact of NIH funding

NIH funding directly contributes to economic activity. In my experience, each dollar of grant or contract funding awarded by the NIH to an academic laboratory buys about 70 cents of salary support for students, postdoctoral researchers and faculty, and about 30 cents worth of supplies and equipment which are purchased predominantly from US-based suppliers. I have read the June 2008 report by Families USA entitled "In your own backyard: How NIH funding helps your State's economy". To the best of my knowledge, this report accurately describes the immediate economic impact of increased NIH funding. Families USA describes this impact in terms of "real, direct economic benefits at the local level, including increased employment; growth opportunities for universities, medical centers, and local companies".

The findings of the Families USA report include a description of the "multiplier effect" - successive rounds of spending emanating from the original stimulus like successive ripples in the surface of a pond after a stone has been thrown into the water. The immediate economic impact, together with the substantial "multiplier effect" described in the Families USA report, provide, in my opinion, strong justification for the inclusion of NIH funding in any new economic stimulus package. However, I also believe that the Families USA report underestimates the full impact of NIH on the economy. In addition to the "multiplier effect", there is a second, longer-term benefit to the economy. I would like to describe this longer-term benefit as "economic leverage" of the original government investment in the NIH as well as the "indirect health dividend" derived from the scientific discoveries made as part of NIH-funded research programs. These longer-term benefits of NIH funding are the focus of the second key point of my testimony.

Second key point: Longer-term benefits to the economy: "Economic Leverage" and "Indirect Health Dividend"

NIH funding has a measurable and significant secondary effect on the economy, which I refer to as the "economic leverage". Simply stated, the scientific knowledge gained by NIH-funded researchers and the inventions made in the course of their studies are the basis of a substantial amount of economic activity relating to the translation of NIH inventions into medically useful products, services and new therapies. Furthermore, these new products, services, and therapies can reduce our nation's health care costs significantly. This is the "Indirect Health Dividend".

In my personal experience, the "economic leverage" has been tremendous: About $4.5 million in direct NIH support for my research activities at Rutgers resulted in technology commercialization efforts in four start-up companies (REVA Medical, TyRx Pharma, Lux Biosciences, and Renova) which, over the last three years alone, have attracted almost $120 million in private equity funding (Table 1). As a consequence of these investments, these companies have created over 100 high-salary jobs. Additional outcomes from these high-tech private equity investments include:

1) TyRx Pharma has obtained FDA market clearance for two products (hernia repair devices and antimicrobial protective sleeves for coronary implants)
2) REVA Medical is testing a revolutionary coronary stent in clinical trials in Germany and Brazil (with the expectation to start clinical trials in the USA sometime in 2009)
3) Lux Biosciences is completing Phase 3 Clinical Trials of Voclosporin, a new derivative of Cyclosporin A, for the treatment of major diseases of the eye, such as "dry eye syndrome", uveitis, and (age related) macular degeneration.

Table 1 – Private Leveraging Investments Raised by Companies Licensing Technology Developed with NIH funding in the Kohn Laboratory at Rutgers

Company and Location	Private Investment Raised
TyRx Pharma Inc., *Monmouth Junction, NJ*	about $40M (5/1998 to 2/2008)
REVA Medical Inc., *San Diego, CA*	$42M (12/2007)
Lux Biosciences Inc., *Jersey City, NJ*	$49M (7/2006)
Renova Biomaterials Inc., *Bridgewater, NJ*	$1.2M (10/2008)

Let me describe the "economic leveraging effect" in more detail. I will also explain how my collaborations have produced this significant leveraging of the government's investment in the NIH by private capital.

When I was a newly-appointed assistant professor in 1986, I was fortunate to receive grants from the NIH that enabled me to establish my laboratory and develop a program of research about synthetic biomaterials. My NIH-funded research studies led to the invention of several classes of new polymers. With the help of the Rutgers technology transfer office, I was able to apply for patents to protect that intellectual property. Some of my seminal inventions were made in the period of 1990 to 1996 - almost exclusively based on research supported by the NIH awards listed in Table 2. In terms of a time line, funding received in the early 1990s is the foundation for much of the significant economic leveraging in the early 2000s - with the full value of NIH's investment in my laboratory becoming apparent only over the next five years, e.g., about 15 years AFTER the original grants were awarded.

Table 2 – NIH Awards to the Kohn Laboratory at Rutgers (exclusive of center and training grants)

NIH Funding Received	Date	Total amount awarded
First award - Structurally new biopolymers derived from alpha-L-amino acid	1/88 to 12/92	$350,000
New biopolymers dervied from alpha-L-amino acids	1/90 to 6/95	$267,840
Polymers designed for biomedical applications	8/93 to 7/97	$624,904
Structurally new biopolymers derived from alpha-L-amino acids	4/97 to 3/02	$934,367
Combinatorial approach to biomaterial design	7/98 to 6/04	$960,919
Radio opaque resorbable polymers for vascular application	9/03 to 7/09	$1,313,537
Total grant amount awarded		**$4,451,567**

In terms of the total benefit to society, I can see one additional economic incentive for the government's investment in the NIH which I refer to as the "indirect health dividend": the significant improvement in the overall health of the nation. Often, advances in medical technology can lead to increases in health care costs. However, in the field of biomedical engineering, I believe that many of the NIH-funded research projects have

the potential to reduce the overall health care costs. A personal experience relates to the problem of macular degeneration that threatens my aging mother with blindness. Twice every day, a nurse has to come by my mother's home to administer her prescription eye drops. My mother, at age 84 is too frail to administer these drops herself. In response to this need, shared by millions of disabled and elderly Americans, I am collaborating with Lux Biosciences to develop a new, fully bioresorbable, drug delivery system that can be inserted into the eye and that will deliver a variety of ophthalmic drugs for 6 to 12 month - eliminating the need for daily administration of eye drops (Figure 1). The polymers we are using to develop this drug delivery system were invented as part of an NIH-funded research project. In addition, I believe that many of the scientific advances needed to conceptualize such drug delivery systems can be traced back to NIH supported research in numerous laboratories throughout the nation. While I lack the expertise to estimate the total value of the "indirect health dividend", I believe that it is very substantial.

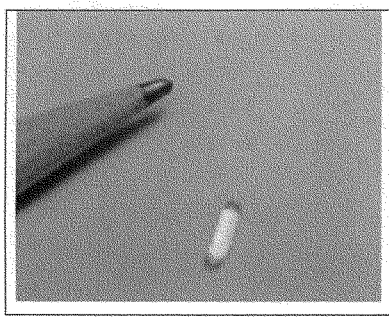

Figure 1: Prototype of a new drug delivery system, designed to be inserted under the eye. This device will deliver ophthalmic drugs for 6 to 12 months continuously while slowly degrading. The elimination of the need to administer eye drops several times daily will not only increase patient compliance and improve clinical outcomes, but will also reduce the health care costs for millions of disabled or elderly patients who require assistance with the administration of conventional eye drops.

During the remainder of my testimony, I shall describe the "economic leveraging effect" and the "indirect health dividend" in more detail using TyRx Pharma and their antimicrobial sleeve as a specific example. In addition, I will highlight the way NIH funding as contributed to the creation and success of three additional companies: REVA Medical, Lux Biosciences and Renova.

A detailed example for economic leverage and indirect health dividends derived from the funding of single NIH grant

People are excited about the potential capabilities of synthetic biodegradable polymers and the effect they will have on the design and function of implanted devices. Whether

they are used to enable an implanted controlled drug delivery system or to regenerate lost tissue, these materials are crucial to the development of a wide range of new medical applications.

TyRx Pharma, Inc., based in Monmouth Junction, New Jersey, is a 10-year old company that came into existence when a venture capital fund agreed to underwrite the effort to commercialize a class of new biomaterials called "tyrosine-derived polyarylates". These materials were invented by me and one of my students as part of an NIH funded research project in my laboratory. I received the Thomas Alva Edison award for best patent in New Jersey for this invention. TyRx Pharma focuses on the development of new drug-eluting medical devices. In January last year, FDA cleared for marketing TyRx's new hernia repair device (Figure 2a), incorporating one of our new biodegradable tyrosine-derived polyarylates.

For the next generation of this product line, TyRx Pharma added antibiotics that elute into the body as the polymer degrades over time. This new device addresses an important medical need: In the US alone, about 700,000 patients annually need a hernia repair device, about 5% of which tend to fail due to infection. An infected hernia repair device is painful and potentially life-threatening for the patient and very costly to replace. By reducing the number of patients suffering from infected hernia repairs, the TyRx device has the potential to reduce hospital and health care costs.

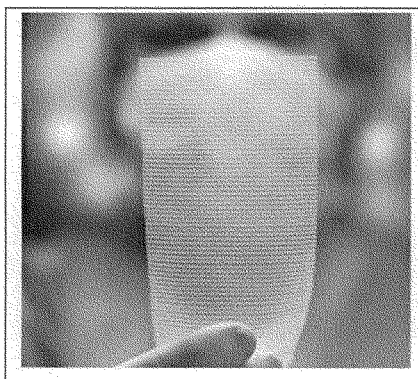

Figure 2a: The TyRx hernia repair device (Pivit™). Photograph from http://www.tyrxpharma.com

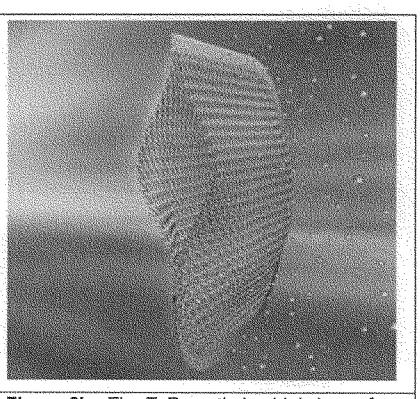

Figure 2b: The TyRx antimicrobial sleeve for prevention of infection of cardiac devices (AIGIS™). Photograph from http://www.tyrxpharma.com

A second line of TyRx products (Figure 2b) targets the problem of infected cardiac rhythm management devices. In a public press release (February 27, 2008), TyRx Pharma announced that

> "more than 400,000 cardiac rhythm management devices (CRMDs) are implanted each year in the U.S. According to a recent study presented during the Heart Rhythm Society (*Heart Rhythm 2006 Scientific Sessions, Boston*), the University of Pittsburgh Medical Center noted that the 2003 national incidence of CRMD implant infection was estimated to be 5.8% for pacemakers and 3.7% for implantable cardioverter defibrillators (ICDs). Furthermore, according to Infection Control Today (8/2003), the average cost of each infection related to invasive medical devices varies from $34,000 to $56,000."

If every CRMD patient would use the TyRx product[1], the extra cost of the devices would be about $400 MM annually, compared to the potential savings of over $640 MM annually in health care costs due to the prevention of infection. To the best of my knowledge, I believe that the TyRx AIGIS product alone has the potential to result in a $240 MM annual "indirect health dividend"[2]- brought about by the government's investment of only $624,904 in NIH funding for the grant entitled: "Polymers designed for biomedical applications", which was awarded in August 1993. This grant supported the invention of the tyrosine-derived polyarylates which are at the foundation of the TyRx Pharma products.

In the same press release, TyRx Pharma also announced a new $25 MM private equity investment that further leverages the original NIH investment made in August 1993. Over its 10-year history, TyRx has raised about $40 million to commercialize products using "tyrosine-derived polyarylates". In this example, the specific NIH grant mentioned above, resulted in a 64-fold leveraging of the government's investment by private equity funding. I am unable to calculate the substantial economic impact of this single NIH grant, but I believe that the sum of the "direct economic impact", the "multiplier" as described by Families USA, the "economic leveraging effect", and the "indirect health

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[1] I have heard that each antimicrobial sleeve will cost about $1000

[2] This calculation is based on hospital care costs only and does not take into account the costs to the economy due the patient's lost productivity.

dividend" must be staggering - making this grant probably one of the very successful government investments.

Highlights promising additional high-impact economic benefits from NIH investment

I will briefly touch on three other companies that are licensing technology developed in my laboratory. They each have products in clinical trials or in development.

REVA Medical Inc.

The San Diego based company REVA Medical, Inc. came to our laboratory with a new structural design for a cardiovascular stent – the small tubular device used to keep coronary arteries open after transcutaneous balloon angioplasty. To fabricate the REVA stent, the company was looking for a biodegradable material that would have the proper mechanical and chemical properties. We offered them a license to another invention made in our laboratory, the "tyrosine-derived polycarbonates". I believed at that time that the mechanical and chemical properties of our "tyrosine-derived polycarbonates" would be a particularly good match for REVA's design needs.

In this case history, NIH funding had multiple, beneficial effects: First, the original invention of our "tyrosine-derived polycarbonates" can be traced back to NIH funding provided between 1990 and 1995 in the amount of $267,840 under a research grant entitled: "New biopolymers derived from alpha-L-amino acids". Later on, NIH support in the amount of $1,313,537 (from 9/03 to 7/09) allowed us to further refine this family of new biomaterials for use in the cardiovascular system. Finally, REVA Medical received an NIH SBIR grant that allowed them to establish the feasibility of using our polycarbonates as part of their stent design.

The development of a fully resorbable stent is not only a challenging research project but also a high-risk commercial R&D effort. I credit the support provided by the NIH for making this entire effort possible. I believe that the availability of timely NIH support allowed REVA to establish the feasibility of a polycarbonate-based, resorbable stent. Only at that point, did private investors agree to provide about $42 MM which enabled REVA to advance the polycarbonate stent into clinical trials in Germany and Brazil.

In terms of the "economic leveraging effect", about $1.7MM in NIH support was leveraged by $42 million in private equity funding so far, corresponding to a 24:1 ratio of government funding to private funding. Because of this leveraging effect, REVA is a thriving company with 40 employees who contribute to the overall economic activity in the San Diego area. REVA is currently raising additional private funding to conduct clinical trials in the USA. Thus, the economic leveraging effect will certainly increase over time.

The future "indirect health dividend" is exceptionally high. In the US, about 2.4 million patients annually are diagnosed with cardiovascular disease, requiring some medical treatment. Increasingly, that treatment has involved angioplasty followed by the placement of a permanent metal stent. By contrast, the REVA stent is intended to act as a temporary scaffold to support the vessel during the healing process. Once the vessel has healed, the stent will resorb, leaving the patient free of a permanent metal implant. Because of the large number of patients with coronary disease, I believe that the economic impact of any improved treatment option will be staggering.

Lux Biosciences

This example brings me back to my mother, who I mentioned earlier. A Jersey City startup called Lux Biosciences focuses on ophthalmic diseases such as uveitis (eye inflammation), macular degeneration, and dry eye. Like TyRx, they are creating combination products that bring a biomaterial together with an active pharmaceutical agent. The pharmaceuticals they are using are already marketed for non-ophthalmic conditions.

To assemble a unique package of technologies, Lux has licensed the use of a number of advanced drug molecules from pharmaceutical companies, a controlled release technology that was developed by intramural NIH scientists, and the "tyrosine-derived polycarbonates" that were invented in my laboratory. Thus, Lux is leveraging both NIH's intramural research program as well as NIH's extramural research support.

Based on press releases published by Lux Biosciences, uveitis is an inflammatory condition in the eye that affects about 300,000 people in the US. Typically treated with corticosteroids, which produce numerous adverse effects, uveitis is responsible,

according to some experts, for 10% of new cases of blindness. Financially, the market is small but could grow with a truly effective therapy. A much larger market exists with age-related macular degeneration which affects 25 million patients in the US and Europe. Lux's hypothesis is that 90% of these cases result from the accumulation of inflammatory insults. Treatment of age-related macular degeneration could become a major application of Lux' approach to anti-inflammatory ophthalmic therapy. Dry eye is a common condition that can result from numerous causes. It is so common that it is responsible for about 40% of all visits to the ophthalmologist. Lux is exploring both topical and long-term drug delivery systems for dry eye disorders.

The company has so far raised $49 million since 2006 when it started.

RENOVA

Last, I mention Renova Biomaterials, Inc., the third and most recent company I have founded. Renova was incorporated in New Jersey in the summer of 2008. It has so far raised $1.2MM in private equity funding from a group of angel investors, further leveraging the investment made by the NIH in supporting our research on "tyrosine-derived polycarbonates". Renova's technology portfolio is entirely based on inventions made with NIH research support. While it is too early for Renova to have had significant economic impact, it is an example of the entrepreneurial activities that can grow out of NIH funding. I believe that a majority of biomedical start-ups coming out of academic research laboratories can trace the creation of their technology portfolios to NIH funded research programs. For that reason, I believe, that a significant portion of the national pipeline of medical technology innovation and entrepreneurship is tightly linked to the level of NIH support available to underwrite research through grants and contracts.

Conclusion

I want to leave you with the message that government investment in the NIH stimulates our economy by four different mechanisms: In the short term, NIH funding has a direct stimulatory effect, just like any other cash infusion into the economy that results in the consumption of services and products. However, in addition to this direct stimulatory effect, NIH funding has a significant "multiplier" or "ripple effect" that is felt throughout the nation. This was described comprehensively in the Families USA report cited earlier in my testimony. In the long term, I believe that the grants and contracts provided by the

NIH have a disproportionately large impact on our economy through "economic leverage" and the "indirect health dividend". I hope that I was able to show you that NIH support for research can create large multipliers in private investment in biomedical enterprises, enterprises that transform our university research into clinical products that improve the health of our population. On a personal level, I, like many other scientists and clinicians, have received from NIH the resources to pursue interesting biomedical science. Entrepreneurial companies take the next step of commercializing the technologies emerging from our science toward a broad variety of biomedical targets. On the way, both levels of investment – research and commercialization – impact the local economies of their regions. **I am firmly convinced that increasing the NIH budget, whether in a near-term stimulus package or as part of future funding bills will pay off both now and in the long run. I encourage you to take this comprehensive view.**

Thank you for your attention.

Mr. PALLONE. Thank you, Doctor.

I think Dr. Burgess is coming back but I am going to start with the questions here, and I will start with Ron Pollack. The reason we had this panel today is because of obviously a feeling on some of our parts on the committee that NIH funding could be a significant stimulus for the economy. It is not always thought of in that way, in the way that FMAP is though, and so I do want to kind of get into a little more exactly how it would be a significant stimulus. There is also the fact that in Congress many of us feel that innovation in itself is a good thing and that somehow innovation which you know we have been lacking in some respects should be part of the stimulus. So Ron, if you could say specifically about NIH how is this such an ideal mechanism, in other words, how is it that the innovation, the research, why should it be included as opposed to some other things?

Mr. POLLACK. Well, an investment in NIH, which obviously has critically important health consequences, does help the economy in significant ways. Remember that the overwhelming majority of resources that NIH receives from the Congress are spent via institutions like universities and research centers, and they hire people right way. Also in the process, it leverages funds. Funds from the Federal Government attract other money, both at the State level and in the private sector, and so as a result there is an immediate impact in terms of people being hired. When you grant or contract, you have to deliver within time parameters, and so each of these institutions quickly staff up to make sure that they can fulfill the contract, and that has an immediate economic consequence.

Mr. PALLONE. All right. Thank you.

Now, I wanted to ask Dr. Kington sort of a negative and a positive, the negative being because in the past 5 years NIH has not received any increase in funding in real terms, well, actually it hasn't received any increase. If you take the inflation factor, we have actually cut NIH budget for the past 5 years. So do you think you could estimate what our country has lost in economic benefit due to the past 6 years of flat funding? Can you explain what the impact of this level of funding has been on the NIH's ability to spur medical innovation? And finally, your thoughts on what impact this has had on our ability to attract talented and promising young minds. Those are my negatives. Then I will get into the positives.

Dr. KINGTON. Well, clearly we believe that we are at an extraordinary point in biomedical and behavioral science where there are tremendous opportunities, and because of the flat budget, we aren't able to invest in those opportunities to the degree that we think would be optimal for the American people. I think that the drop in the success rates of funding applications is one indicator. Part of that reflects an appropriate reading in the academic community and the university and research community that the country was investing in the enterprise of biomedical research and that led to a priming of the pump. More people were being trained, there were substantial investments by institutions at local levels to strengthen the infrastructure, and just as they were able to do that, they were met by flat budgets with a drop in success rates. One of the greatest concerns of Dr. Zerhouni, whose tenure just ended, was the potentially horrible effect this might have on young investigators, on

new investigators, and we believe that that is a concern and that more and more young, new scientists are thinking long and hard before making investment in a scientific career because the outlook isn't so positive when their success rates are 20 percent. Now, we are doing everything we can to target funds within the agency so that we can invest in new investigators but we have limited options in the face of a flat budget.

Mr. PALLONE. Well, let me do the positive. Let us say we were to take the number used by Families USA and increase funding for NIH by 6.6 percent or $1.4 billion. What would that mean in terms of new grants being funded, and would you be able to fund grants immediately or will it take time?

Dr. KINGTON. We have looked into this. We believe that we could fund several thousand grants within a matter of weeks. For every about $500 million or so, we could fund an additional 1,400 grants that would not have otherwise been funded. We believe that we can do it without increases in infrastructure. We are primed and ready to go. We have 10,000 grants that have already been approved from the last fiscal year that have been found to be scientifically meritorious and that have been approved for funding by our public advisory councils. So it is just a matter of getting these grants out the door. We have established relationships with 3,000 institutions across the country who are ready and primed to receive these funds. We are confident that we can make the investment within a period of 4 to 6 weeks.

Mr. PALLONE. Okay. Great.

Mr. POLLACK. And I want to just emphasize with the figure you used, this would, by the calculation using the RIMS model, would increase over 9,000 jobs over the course of the year.

Mr. PALLONE. Okay. I am waiting for Dr. Burgess, and I am over my time. Let me see if he is coming. He is. Thank you. I yield to the gentleman.

Mr. BURGESS. Let me first just say that this hearing is not about the value of the NIH because there is no one up here who disputes the value of the NIH. You are the crown jewel in the federal government. You are the agency, the system that works when all else fails, so I want to say that up front. Dr. Zerhouni was very good to me during his tenure. I took many field trips out to the NIH. I look forward, Dr. Kington, to getting out and visiting with you. One of the things that Dr. Zerhouni talked about, when I came on the committee two terms ago, it had been years since there had actually been an authorization bill for the NIH, and one of the things Dr. Zerhouni was very concerned about that it was feast or famine one year to the next. He never knew that was going to happen. He asked us for stability. He asked us for flexibility with the translational research, to be sure, but he asked us for some degree of stability in knowing what he could depend on from year to year because my understanding is, many of these grants aren't just a few months' time, they are like 60 months or 5 years, so if we give you something one year and don't continue it the next year, then we have brought a young scientist in, we have staffed up a lab and now we are not continuing, and that is very disruptive obviously to the ongoing research.

We went through an extensive reauthorization process which concluded 2 years ago, December of 2006, right before the end of the 109th Congress, and in that reauthorization bill, and we took a lot of criticism for this, the baseline budget I believe was $29.5 billion and it was to be a 5 percent authorization increase for the next 5 years was what was laid out, and Dr. Zerhouni felt very comfortable with that as a roadmap for going forward. I think, Ms. King, that would fit within your parameters of a 3.5 to 5 percent increase. Now, we were criticized because although the rate of biomedical inflation was 3.5 percent at the time, medical inflation was 7 percent and there were people on this committee who argued that our numbers should be somewhere in between 3.5 and 7 percent, but 5 percent is where we ended up. And then we weren't in charge of the appropriation, and so the next year when Chairman Pallone's guys on the appropriations committee came up with a 2 percent increase and then we didn't do any appropriations at all last year, we did a continuing resolution. We will get to you in February if that is okay. So there is your problem, is the fact that we made a promise to you as authorizers on this committee and the appropriators have not executed that responsibility correctly, and it seems to me that we will be going down the same path that Dr. Zerhouni found bothersome a couple of years ago where we inject—I will agree that we are 6.6 percent behind what we should have been. If we gave you 2 or 3 percent in the fiscal year before and nothing this fiscal year, you should be up 10 percent. So yes, that 6.6 percent figure makes sense but the reality is, that should have been a stable, dependable appropriation coming from a stable authorization that was laid out by this committee in agreement with Dr. Zerhouni, and at the end of December of that year we all clasped hands and said that was a good thing and we refrained from actually getting too much into the business of restructuring the NIH, which several people on the committee wanted to do, some areas where there might be duplication and perhaps the director should have greater authority. I remember those articles when I first came on board, 29 figures without a palm is not a usable appendage.

So I just want to stress that this committee has done its work as far as the NIH is concerned. The problem is that the other committees in Congress haven't followed suit and really I would call upon the chairman to insist with the Speaker that the Appropriations Committee do its work in February when we do finally get around to doing the appropriations for last year and then ongoing during the year that we do the work required in the Appropriations Committee and that we provide you with the funding that we promised, because if we don't do it this fiscal year, yes, now you are down 15 percent of what you were promised of that increase. That is about $1.5 billion a year, and like old Everett Dirksen said, pretty soon you are talking about real money.

So with that, again, I am so grateful that you all are here. I think the NIH is the crown jewel in the Federal Government and it is a national treasure and it is certainly something to be preserved. I am not sold on the idea of it being an economic stimulus engine. I do have to ask, Ms. King, what in the world are GlycoMimetics? Because I should know and I don't and I couldn't

find it in your testimony and I didn't look it up on Google last night.

Ms. KING. They are mimics of functional carbohydrates. As a physician, I am sure you appreciate it.

Mr. BURGESS. Well, that is what I would infer from the name. And then what is the association with sickle cell disease, if I may be so bold as to ask?

Ms. KING. The adhesive events associated with a sickle cell crisis are mediated by a mechanism that our drugs interfere with. So I will send you more about it.

Mr. BURGESS. That is a fascinating field of study and just indicative of the type of basic research that is so critical for people who are afflicted with very, very onerous diseases and conditions.

And Mr. Pollack, I just have to say, everyone remembers where they were during certain events in their life. I will never forget the night driving home in 1993 after a hard day of seeing patients and hearing you and Donna Shalala talk about your vision for healthcare reform. It made me politically active from that night, so although it was probably not your intention, I thank you for the impetus, and you were the catalyst for me suddenly becoming aware of my surroundings and the impact that Congress on my life.

I am going to yield back, Mr. Chairman, in the interest of time.

Mr. POLLACK. Doctor, I have to say we are delighted that we helped to facilitate a portion of your career.

Mr. PALLONE. I am not sure that was a compliment. But in any case, thank you all for being here today. Again, it is such an important issue, and we would like to include the NIH in the stimulus at some point because I think it has to be part of it in some way. So thank you again.

Let me just remind members that they, well, I should tell you as well that you may get written questions from members and those would be submitted to the clerk within the next 10 days so you may get a notification that we have additional written questions.

But without objection, this meeting of the subcommittee is adjourned. Thank you.

[Whereupon, at 12:15 p.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

PREPARED STATEMENT OF HON. JOHN D. DINGELL

I am pleased that we are having a second hearing on the role of health care as an economic stimulus. With the continued deterioration of the economy, it is clear that quick, decisive action is needed.

Earlier this fall, after the collapse of the housing market and failures of key economic institutions, Congress acted to pass the Emergency Economic Stabilization Package of 2008, which was signed into law on October 3, 2008. However, the continued loss of jobs and revenues for States is underlying the need for a second stimulus package. That package needs to be targeted to include funding for infrastructure, unemployment insurance, and health care in the form of increased federal funding for Medicaid to the States.

The ranks of the unemployed have risen by 2.2 million workers over the last 12 months. Most States are experiencing considerable budget deficits along with declining or flat revenues. A one percentage-point increase in unemployment could raise the number of uninsured by 1.1 million, adding to the already staggering number of uninsured in this country and an increased burden on the States through their Medicaid programs.

Health care spending, in the form of increased funding for Medicaid to the States, must be a critical component of any stimulus package. First, as workers lose their

jobs, so too goes their health insurance. States need additional resources to support the increased demand for services as their revenues are declining. States also need additional resources to prevent cutbacks in Medicaid coverage and benefits that would otherwise be required to help balance their budgets in a time of declining revenues.

Second, additional health care spending acts as an economic booster. Increasing the federal funding of Medicaid is a powerful countercyclical tool; it is direct, immediate, and does not require any additional administrative costs or actions to implement.

Third, increased investment in the National Institutes of Health (NIH) is vital to a successful economic stimulus package. An effective economic stimulus plan must quickly inject and circulate a significant amount of money into the domestic economy to reinvigorate consumer confidence, sustain employment, and contribute to more stable financial markets. The NIH is a proven vehicle to provide maximum economic stimulus effect, plus it offers additional opportunities to accelerate biomedical research, which will benefit all U.S. citizens.

Unfortunately, for the past five years, federal funding for NIH has not kept pace with inflation. In addition to stifling scientific progress, these funding cuts have a negative economic impact on communities across the country. Eighty to ninety percent of the NIH's $29 billion budget funds research that takes place at universities, medical research centers, hospitals, and research institutes in every state in the U.S. The federal dollars that NIH sends out into communities provide direct economic benefits at the local level, including increased employment and growth opportunities for universities, medical centers, and local companies. When NIH funding is cut, communities across the country pay the price.

I look forward to the testimony of today's witnesses, particularly Mr. Zolotorow who will provide a first-hand account of the importance of his Medicaid coverage and what is at stake if Congress does not act to provide States with the resources to ensure that they can continue to provide health care coverage to people, like Mr. Zolotorow, in this time of great need.

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Statement
of the
American Hospital Association
before the
Committee on Energy and Commerce
Subcommittee on Health
of the
United States House of Representatives

"Treatments for an Ailing Economy:
Protecting Health Care Coverage and Investing in Biomedical Research"

November 13, 2008

On behalf of our nearly 5,000 member hospitals, health systems and other health care organizations, and our 38,000 individual members, the American Hospital Association (AHA) appreciates the opportunity to submit this statement for the record as the Health Subcommittee of the Committee on Energy and Commerce examines the need for a second short-term economic stimulus legislative package to stave off a deep economic recession.

A weak economy means fewer jobs with employer-based health care coverage and, consequently, greater numbers of uninsured individuals and families. Medicaid is *the* public program designed to assist vulnerable populations in times of economic hardship. As state revenues decline and Medicaid enrollment increases, state governments will struggle to meet the health care needs of their residents. A fiscal relief package for the states is important, as the economy has worsened, and should include a temporary increase in Medicaid's federal medical assistance percentage (FMAP).

Hospitals are not immune to the pressures of a worsening economy. Any changes to Medicaid and Medicare payments directly impact the health of our facilities and the patients we serve. Therefore, the legislative package also should include a moratorium on two Centers for Medicare & Medicaid Services (CMS) regulations that would negatively impact hospital payments: one that would cut federal funds to state Medicaid programs; and the other related to Medicare payments to teaching hospital.

HOSPITALS AND THE ECONOMY

Hospitals are not immune from economic downturns. Reports are coming in that some hospitals are seeing fewer insured patients, while at the same time more uninsured and underinsured people are showing up at the emergency department. The hospital field also has been negatively impacted by the lack of liquidity in the credit market. Hospitals, like many businesses, use lines of credit to finance utility payments and payroll. In addition, non-profit hospitals are finding it difficult to raise capital through the municipal bond market. With these increased pressures, some hospitals have been forced to lay off workers and delay capital improvements.

FMAP

The demand for Medicaid services increases during a time of economic recession, requiring states to manage the increase in enrollment and funding pressures at a time when most of their budgets are stretched thin. According to an April 2008 report by the Kaiser Commission on Medicaid and the Uninsured, a one percentage point rise in the national unemployment rate would increase enrollment in Medicaid and the State Children's Health Insurance Program (SCHIP) by 1 million (600,000 children and 400,000 non-elderly adults) and cause the number of uninsured to grow by 1.1 million. Medicaid and SCHIP costs would increase by $3.4 billion, including $1.4 billion in state spending, representing a one percent increase in total Medicaid and SCHIP expenditures.

During the last economic downturn, from 2001-2004, states cut spending for services – including Medicaid – in order to balance their budgets. Congress provided a $10 billion temporary increase in the matching rate to assist the states and maintain Medicaid coverage. According to surveys by the Kaiser Commission on Medicaid and the Uninsured and the National Association of State Budget Officers, as many as 25 states used these resources to avoid, lessen, or postpone Medicaid cutbacks; and as many as seven states used these resources to restore previous Medicaid cutbacks or make other program expansions. Once again, the states are seeking assistance due to a weak economy. It is estimated that over the current and next fiscal years, 39 states will face budget shortfalls.

The AHA supports a temporary FMAP increase that would allow states to use such funds to support their Medicaid programs and maintain their current levels of enrollment. This is critical because states have already targeted their Medicaid programs in a search for savings through provider payment freezes or reductions, as well as benefits and eligibility changes. Such cuts will further weaken the already tenuous foundation of the health care safety net, dramatically harming the ability of providers to continue serving our most vulnerable patients.

REGULATIONS THAT SHOULD BE UNDER A MORATORIUM

Given the financial constraints faced by hospitals, the AHA believes two CMS rules should be placed under moratoria: the Medicaid hospital outpatient rule and the Medicare indirect medical education (IME) capital payment cut.

Outpatient Rule. This rule, which will take effect December 8, substantially departs from long-standing Medicaid policy regarding the definition of Medicaid outpatient hospital services. Under the rule, the types of services that are at risk for not being reimbursed through hospital outpatient programs include Medicaid's early and periodic screening and diagnostic treatment dental services for children; physician emergency department services; physical, occupational and speech therapies; outpatient clinical diagnostic laboratory services; ambulance services; durable medical equipment; and outpatient audiology services.

CMS stated that it based its dramatic shift in policy on the need to align Medicaid outpatient policies with Medicare outpatient policies. However, these programs serve very different populations; Medicaid serves a largely pediatric population, while Medicare serves an elderly population. Yet despite these differences, CMS would narrowly define Medicaid hospital outpatient services to align Medicaid with Medicare. The effect of aligning the hospital outpatient policies for these two programs would be to limit Medicaid federal spending for hospital outpatient programs and state Medicaid programs overall and, ultimately, the patients served by Medicaid.

In addition to the 333 states, local government, providers and health care associations that submitted comments to CMS, Congress has spoken repeatedly in bipartisan opposition to the rule. Two Senate bills (S. 2460 and S. 2819) that included a moratorium on the Medicaid outpatient regulation received strong support from members of both parties. By a vote of 349-62, the House overwhelmingly passed legislation (H.R. 5613) that included a similar moratorium. The outpatient moratorium and others contained in H.R. 5613 were part of the *Supplemental Appropriations Act of 2008*, but the outpatient regulation was dropped during negotiations between the White House and House leadership. And before the end of the legislation session, Senators Charles Schumer and Hillary Clinton and Representative Eliot Engel introduced related versions of the PATH Act (S. 3656 and H.R. 7241) which, among other provisions, included a moratorium on the Medicaid outpatient regulation. Given the bipartisan support for preventing the outpatient regulation from moving forward, the AHA believes Congress should institute a moratorium on this rule.

Capital IME Payments. On July 31, CMS released its fiscal year (FY) 2009 final rule for the hospital inpatient prospective payment system (PPS). The final rule took effect October 1. One of the major changes in the rule included a policy to phase out the IME capital payment adjustment to teaching hospitals starting in FY 2009. Given that the impact of this phasing out of payment is significant – a reduction of $1.3 billion over five years – CMS provided the public with an additional opportunity to comment in the FY 2009 proposed rule. Although many commenters, including the AHA, 210 representatives and 51 senators, urged CMS not to proceed with these cuts, the agency announced that it was moving forward with its plans. Therefore, in FY 2009 hospitals will receive half their capital IME adjustment; in FY 2010 and beyond, the adjustment will be eliminated. These unnecessary cuts ignore how vital these capital payments are to investment in the latest medical technology, ongoing maintenance and improvement of hospital facilities and importance of medical education. The AHA believes Congress should reverse these cuts.

CONCLUSION

Hospitals and state Medicaid programs are reeling under the weight of an economic recession, and congressional assistance through another stimulus package is paramount. The AHA believes that the current fiscal crisis faced by states demands immediate and meaningful federal support through an increase in the federal Medicaid matching percentage.

Hospitals are important economic entities for their communities, and their emergency departments are the location of last resort for care for millions of the uninsured, including those that will lose their jobs and their employer based health care coverage. Medicaid and Medicare payment cuts at this time will only place further strain on many financially distressed hospitals. For this reason, we ask that Congress place a moratorium on the Medicaid and Medicare rules that could adversely impact access to much-needed services.

Edward G. Rendell
Governor of Pennsylvania
Chair

James H. Douglas
Governor of Vermont
Vice Chair

Raymond C. Scheppach
Executive Director

October 27, 2008

The Honorable Harry M. Reid
Majority Leader
United States Senate
Washington, D.C. 20510

The Honorable Mitch McConnell
Minority Leader
United States Senate
Washington, D.C. 20150

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
Washington, D.C. 20515

The Honorable John Boehner
Minority Leader
U.S. House of Representatives
Washington, D.C. 20515

Dear Senator Reid, Senator McConnell, Speaker Pelosi, and Representative Boehner:

The slowing economy is resulting in growing unemployment, increased demand for state services and significant declines in state revenues. As governors work to reduce budget shortfalls and plan for the coming fiscal year, we call on you to pass an economic recovery package this session that includes additional funding for Medicaid and investments in our nation's infrastructure.

Specifically, Congress should temporarily enhance the Federal Medical Assistance Percentage (FMAP) for at least two years. Funding for FMAP is a particularly effective countercyclical tool because it immediately allows Governors to eliminate planned budget cuts required to meet balanced budget requirements and continue services for those with the greatest need.

Likewise, investments in ready-to-go infrastructure projects are a cost effective creator of high paying jobs. These investments should include a broad array of infrastructure projects including airports, highways, transit systems, clean water, sewers and broadband. We would welcome the opportunity to work with you on the details of the infrastructure provisions to ensure that funds can be targeted on high priority projects and be obligated and expended quickly by states.

Congress also should consider changes to the federal tax code that can spur economic growth and avoid policies that preempt state authority, shift costs to states or impose new unfunded mandates.

State governments play a vital role in the nation's economy and must be part of any national recovery strategy. We look forward to partnering with you to help stabilize the economy, speed our recovery and serve our citizens during this difficult time.

Sincerely,

Edward G. Rendell

Governor Edward G. Rendell

James H. Douglas

Governor James H. Douglas

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October 27, 2008

The Honorable Harry M. Reid
Majority Leader
United States Senate
Washington, D.C. 20510

The Honorable Mitch McConnell
Minority Leader
United States Senate
Washington, D.C. 20510

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
Washington, D.C. 20515

The Honorable John Boehner
Minority Leader
U.S. House of Representatives
Washington, D.C. 20515

Dear Senator Reid, Senator McConnell, Speaker Pelosi, and Representative Boehner:

As Congress develops a new national economic recovery package, we encourage you to assist state and local governments by including a temporary increase in the federal matching rate for Medicaid and additional funds for infrastructure investment.

Recent surveys indicate as many as 27 states face shortfalls of about $26 billion -- numbers that could double over the next few months as revenues continue to decline. Surveys of local governments show a similar pattern, with property, sales and income taxes down between 3 and 4 percent from last year and the rate of revenue losses accelerating.

During economic downturns, state and local governments are often forced to cut spending and increase taxes to meet balanced budget requirements. These actions can exacerbate the downturn and slow recovery. Already states have made cuts to education, public safety and Medicaid and may be forced to make more as the downturn persists. Providing federal funds directly to state and local governments allows them to reduce cuts and continue services. Most economists agree that this is one of the most effective countercyclical tools the federal government can implement. Even with this assistance, state and local governments will continue to consolidate departments and agencies, streamline services and make government more efficient.

During the last recession, Congress enacted a $10 billion block grant and also provided $10 billion to temporarily enhance Federal Medical Assistance Percentages (FMAP) for every state. The Medicaid component provided immediate fiscal relief to states and helped stabilize the economy by preventing cuts to programs important to vulnerable populations.

As Congress prepares to take action, state and local officials recommend that any recovery package include at least a two-year increase in FMAP and additional federal funding for infrastructure. Investing in infrastructure provides job creation, longer-term stability and helps ensure the nation's safety and competitiveness. Since the nation's infrastructure needs are varied, federal investments should include a broad array of ready-to-go projects, including funds for airports, highways, transit, clean water, sewer and schools.

Our members welcome the opportunity to work with you as active partners in restoring the economy. Investments in state and local governments are effective and efficient ways to speed recovery and help those most directly affected by the economic downturn.

Sincerely,

Governor Edward G. Rendell
Chair
National Governors Association

Speaker Joe Hackney
President
National Conference of State Legislatures

Governor M. Jodi Rell
President
The Council of State Governments

County Supervisor Don Stapley
President
National Association of Counties

Council Member Cynthia McCollum
President
National League of Cities

City Manager David M. Limardi
President
International City/County Management Association

Backgrounder

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Why Government Spending Does Not Stimulate Economic Growth

Brian M. Riedl

In a throwback to the 1930s and 1970s, Democratic lawmakers are betting that America's economic ills can be cured by an extraordinary expansion of government. This tired approach has already failed repeatedly in the past year, in which Congress and the President:

- Increased total federal spending by 11 percent to nearly $3 trillion;
- Enacted $333 billion in "emergency" spending;
- Enacted $105 billion in tax rebates; and
- Pushed the budget deficit to $455 billion in the name of "stimulus."

Every one of these policies failed to increase economic growth. Now, in addition to passing a $700 billion financial sector rescue package, lawmakers have decided to double down on these failed spending policies by proposing a $300 billion economic stimulus bill. Even though the last $455 billion in Keynesian deficit spending failed to help the economy, lawmakers seem to have convinced themselves that the next $300 billion will succeed.

This is not the first time government expansions have failed to produce economic growth. Massive spending hikes in the 1930s, 1960s, and 1970s all failed to increase economic growth rates. Yet in the 1980s and 1990s—when the federal government shrank by one-fifth as a percentage of gross domestic product (GDP)—the U.S. economy enjoyed its greatest expansion to date.

Talking Points

- Washington has already spent hundreds of billions of dollars on economic stimulus bills that have failed to revive the economy. There is no reason to believe the next one will succeed.
- Government spending cannot be stimulative because every dollar that government spending "injects" into the economy must first be taxed or borrowed out of the economy. Rather than create new purchasing power, these policies merely redistribute existing purchasing power.
- Claims that a Department of Transportation study proved that highway spending creates jobs are based on a misreading of the study.
- Economic growth requires increasing the productivity of American workers. Lower marginal tax rates encourage productivity by increasing incentives to work, save, and invest.
- Tax rebates do not help the economy because they are government grants that are not based on encouraging productivity.

This paper, in its entirety, can be found at:
www.heritage.org/Research/Budget/bg2208.cfm

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Cross-national comparisons yield the same result. The U.S. government spends significantly less than the 15 pre-2004 European Union nations, and yet enjoys 40 percent larger per capita GDP, 50 percent faster economic growth rates, and a substantially lower unemployment rate.[1]

When conventional economic wisdom repeatedly fails, it becomes necessary to revisit that conventional wisdom. Government spending fails to stimulate economic growth because every dollar Congress "injects" *into* the economy must first be taxed or borrowed *out of* the economy. Thus, government spending "stimulus" merely redistributes existing income, doing nothing to increase productivity or employment, and therefore nothing to create additional income. Even worse, many federal expenditures weaken the private sector by directing resources toward less productive uses and thus impede income growth.

The Myth of Spending as "Stimulus"

Spending-stimulus advocates claim that government can "inject" new money into the economy, increasing demand and therefore production. This raises the obvious question: Where does the government acquire the money it pumps into the economy? Congress does not have a vault of money waiting to be distributed: Therefore, every dollar Congress "injects" *into* the economy must first be taxed or borrowed *out of* the economy. No new spending power is created. It is merely redistributed from one group of people to another.[2]

Spending-stimulus advocates typically respond that redistributing money from "savers" to "spenders" will lead to additional spending. That assumes that savers store their savings in their mattresses or elsewhere outside the economy. In reality, nearly all Americans either invest their savings by purchasing financial assets such as stocks and bonds (which finances business investment), or by purchasing non-financial assets such as real estate and collectibles, or they deposit it in banks (which quickly lend it to others to spend). The money is used regardless of whether people spend or save.

Government cannot create new purchasing power out of thin air. If Congress funds new spending with taxes, it is simply redistributing existing income. If Congress instead borrows the money from domestic investors, those investors will have that much less to invest or to spend in the private economy. If Congress borrows the money from foreigners, the balance of payments will adjust by equally reducing net exports, leaving GDP unchanged. Every dollar Congress spends must first come from somewhere else.

This does not mean that government spending has no economic impact at all. Government spending often alters the consumption of total demand, such as increasing consumption at the expense of investment.

More importantly, government spending can alter *future* economic growth. Economic growth results from producing more goods and services (not from redistributing existing income), and that requires productivity growth and growth in the labor supply. A government's impact on economic growth is, therefore, determined by its policies' effect on labor productivity and labor supply.

Productivity growth requires increasing the amount of capital, either material or human, relative to the amount of labor employed. Productivity growth is facilitated by smoothly functioning markets indicating accurate price signals to which buyers and sellers, firms and workers can respond in flexible markets. Only in the rare instances where the private sector fails to provide these inputs in adequate amounts is government spending necessary. For instance, government spending on education, job training, physical infrastructure, and research and development can increase long-term productivity rates—but only if government spending does not

1. This originally appeared in Daniel J. Mitchell, "The Impact of Government Spending on Economic Growth," Heritage Foundation *Backgrounder* No. 1831, March 15, 2005, at *http://www.heritage.org/research/budget/bg1831.cfm*. The EU–15 consists of the 15 member states of the European Union before the 2004 enlargement: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom.
2. The Federal Reserve could fund new spending by printing new money, which would only create inflation.

crowd out similar private spending, and only if government spends the money more competently than businesses, nonprofit organizations, and private citizens. More specifically, government must secure a higher long-term return on its investment than taxpayers' (or investors lending the government) requirements with the same funds. Historically, governments have rarely outperformed the private sector in generating productivity growth.

Even when government spending improves economic growth rates on balance, it is necessary to differentiate between immediate versus future effects. There is no immediate stimulus from government spending, since that money had to be removed from another part of the economy. However, a productivity investment may aid *future* economic growth, once it has been fully completed and is being used by the American workforce. For example, spending on energy itself does not improve economic growth, yet the eventual existence of a completed, well-functioning energy system can. Those economic impacts can take years, or even decades, to occur.

Most government spending has historically *reduced* productivity and long-term economic growth due to: [3]

1. **Taxes.** Most government spending is financed by taxes, and high tax rates reduce incentives to work, save, and invest—resulting in a less motivated workforce as well as less business investment in new capital and technology. Few government expenditures raise productivity enough to offset the productivity lost due to taxes;
2. **Incentives.** Social spending often reduces incentives for productivity by subsidizing leisure and unemployment. Combined with taxes, it is clear that taxing Peter to subsidize Paul reduces both of their incentives to be productive, since productivity no longer determines one's income;
3. **Displacement.** Every dollar spent by politicians means one dollar less to be allocated based on market forces within the more productive private sector. For example, rather than allowing the market to allocate investments, politicians seize that money and earmark it for favored organizations with little regard for improvements to economic efficiency; and
4. **Inefficiencies.** Government provision of housing, education, and postal operations are often much less efficient than the private sector. Government also distorts existing health care and education markets by promoting third-party payers, resulting in over-consumption and insensitivity to prices and outcomes. Another example of inefficiency is when politicians earmark highway money for wasteful pork projects rather than expanding highway capacity where it is most needed.

Mountains of academic studies show how government expansions reduce economic growth: [4]

- *Public Finance Review* reported that "higher total government expenditure, no matter how financed, is associated with a lower growth rate of real per capita gross state product."[5]
- The *Quarterly Journal of Economics* reported that "the ratio of real government consumption expenditure to real GDP had a negative association with growth and investment," and "growth is inversely related to the share of government consumption in GDP, but insignificantly related to the share of public investment."[6]
- A *Journal of Macroeconomics* study discovered that "the coefficient of the additive terms of the government-size variable indicates that a 1% increase in government size decreases the rate of economic growth by 0.143%."[7]
- *Public Choice* reported that "a one percent increase in government spending as a percent of

3. This list was influenced by Daniel J. Mitchell, "The Impact of Government Spending on Economic Growth."
4. These studies were originally cited in *ibid.* Many more studies can be found in the supplemental appendix to that paper, at *http://www.heritage.org/Research/Budget/bg1831_suppl.cfm*.
5. S. M. Miller and F. S. Russek, "Fiscal Structures and Economic Growth at the State and Local Level," *Public Finance Review*, Vol. 25, No. 2 (March 1997).
6. Robert J. Barro, "Economic Growth in a Cross Section of Countries," *Quarterly Journal of Economics*, Vol. 106, No. 2 (May 1991), p. 407.

GDP (from, say, 30 to 31%) would raise the unemployment rate by approximately .36 of one percent (from, say, 8 to 8.36 percent)."[8]

Economic growth is driven by individuals and entrepreneurs operating in free markets, not by Washington spending and regulations. The outdated idea that transferring spending power from the private sector to Washington will expand the economy has been thoroughly discredited, yet lawmakers continue to return to this strategy. The U.S. economy has soared highest when the federal government was shrinking, and it has stagnated at times of government expansion. This experience has been paralleled in Europe, where government expansions have been followed by economic decline. A strong private sector provides the nation with strong economic growth and benefits for all Americans.

Three Applications of the Spending Fallacy

The myth of government spending stimulus is often found in debates over tax rebates (which function similar to government spending), highway spending, and federal bailouts of states.

1) Why Tax Rebates Do Not Stimulate

The debate on taxes and economic growth is also clouded with confusion. By asserting that tax cuts spur economic growth by "putting spending money in people's pockets," many tax cutters commit the same fallacy as do government spenders. Similar to government spending, the money for tax cuts does not fall from the sky. It comes out of investment and net exports if financed by budget deficits or government spending if offset by spending cuts.

However, the right tax cuts can add substantially to productivity. As stated above, economic growth requires that businesses produce increasing amounts of goods and services, and that requires consistent business investment and a growing, productive workforce. Yet high marginal tax rates—defined as the tax on the next dollar earned—create a disincentive to engage in those activities. Reducing marginal tax rates on businesses and workers will increase incentives to work, save, and invest. These incentives encourage more business investment, a more productive workforce by raising the after-tax returns to education, and more work effort, all of which add to the economy's long-term capacity for growth.

Thus, not all tax cuts are created equal. The economic impact of a tax cut is measured by the extent to which it alters behavior to encourage productivity.

Tax rebates fail to increase economic growth because they are not associated with productivity or work effort. No new income is created because no one is required work, save, or invest more to receive a rebate. In that sense, rebates are economically indistinguishable from government spending programs that write each American a check. In fact, the federal government treats rebate checks as a "social benefit payment to persons."[9] They represent another feeble attempt to create new purchasing power out of thin air.

Consider the 2001 tax rebates. Washington borrowed billions from the capital markets, and then mailed it to Americans in the form of $600 checks. Rather than encourage income creation, Congress merely transferred existing income from investors to consumers. Predictably, the following quarter saw consumer spending surge from 1.4 percent to 7.0 percent, and gross private domestic investment spending drop correspondingly by 22.7 percent[10] The overall economy grew at a meager 1.6 percent that quarter, and remained stagnant through 2001 and much of 2002.

7. James S. Guseh, "Government Size and Economic Growth in Developing Countries: A Political-Economy Framework," *Journal of Macroeconomics*, Vol. 19, No. 1 (Winter 1997), pp. 175–192.
8. Burton Abrams, "The Effect of Government Size on the Unemployment Rate," *Public Choice*, Vol. 99 (June 1999), pp. 3–4.
9. Frequently Asked Questions, Bureau of Economic Analysis, Department of Commerce, at *http://faq.bea.gov/cgi-bin/bea.cfg/php/enduser/std_adp.php?p_faqid=490* (November 7, 2008).
10. These growth rates are annualized. See U.S. Commerce Department, Bureau of Economic Analysis, NIPA Tables, Table 1.1.1, at *http://www.bea.gov/bea/dn/nipaweb/SelectTable.asp* (November 7, 2008). Consumption and investment spending changed by similar dollar amounts, but because investment spending begins at a lower base figure, its percentage change is larger.

It was not until the 2003 tax cuts—which cut tax rates for workers and investors— that the economy finally and immediately began a robust recovery. In the previous 18 months, business investment had plummeted, the stock market had dropped 18 percent, and the economy had lost 616,000 jobs. In the 18 months following the 2003 tax rate reductions, business investment surged, the stock market leaped 32 percent, and Americans created 307,000 new jobs (followed by 5 million jobs in the next seven quarters).[11] Overall economic growth rates doubled.[12]

Marginal tax rates were reduced throughout the 1920s, 1960s, and 1980s. In all three decades, investment increased, and higher economic growth followed. Real GDP increased by 59 percent from 1921 to 1929, by 42 percent from 1961 to 1968, and by 31 percent from 1982 to 1989.[13]

Yet in a triumph of hope over experience, lawmakers embraced tax rebates over rate reductions again in early 2008. While the economic data are still coming in, it is clear that once again the rebates failed to support economic growth. There is no reason to expect another round of tax rebates to be any more effective.[14]

2) Highway Spending: The Myth of the 47,576 New Jobs

Nowhere is the government spending stimulus myth more widespread than in highway spending. Congress is already rumbling to push billions in highway spending in the next stimulus package. Over the years, lawmakers have repeatedly supported their errant claim that highway spending is an immediate economic tonic by citing a Department of Transportation (DOT) study. This study supposedly states that every $1 billion spent on highways adds 47,576 new jobs to the economy.[15]

The problem: The DOT study made no such claim. It stated that spending $1 billion on highways would *require* 47,576 workers (or more precisely, it would require 26,524 workers, who then spend their income elsewhere, supporting an additional 21,052 workers). But before the government can spend $1 billion hiring road builders and purchasing asphalt, it must first tax or borrow $1 billion from other sectors of the economy—which would then lose a similar number of jobs. In other words, highway spending merely transfers jobs and income from one part of the economy to another. As The Heritage Foundation's Ronald Utt has explained, "The only way that $1 billion of new highway spending can create 47,576 new jobs is if the $1 billion appears out of nowhere as if it were manna from heaven."[16] The DOT report implicitly acknowledged this point by referring to the transportation jobs as "employment benefits" within the transportation sector, rather than as *new* jobs for the total economy.

11. U.S. Commerce Department, Bureau of Economic Analysis, NIPA Tables, Table 1.1.1; Yahoo Finance, "S&P 500 Index," at *http://www.finance.yahoo.com/q/hp?s=%5EGSPC* (November 7, 2008); and U.S. Department of Labor, Bureau of Labor Statistics, "Employment, Hours, and Earnings from the Current Employment Statistics Survey (National)."
12. For more on the Bush tax cuts, see Brian M. Riedl, "Ten Myths About the Bush Tax Cuts," Heritage Foundation *Backgrounder* No. 2001, January 29, 2007, at *http://www.heritage.org/Research/Taxes/bg2001.cfm*.
13. See Daniel J. Mitchell, "Lowering Marginal Tax Rates: The Key to Pro-Growth Tax Relief," Heritage Foundation *Backgrounder* No. 1443, May 22, 2001, at *http://www.heritage.org/Research/Taxes/BG1443.cfm*.
14. Because pro-growth tax cuts are not designed simply to "put money in people's pockets," their proponents do not focus on whether recipients are rich or poor. Tax relief policies should be designed to maximize long-run economic growth, which in turn raises incomes across the board. Thus, raising marginal tax rates on "the wealthy" to finance tax rebates from low-income families may satisfy a redistributive agenda, but it would also reduce economic growth and eventually lower incomes across the board. It is better for everyone to reduce tax rates across the board and encourage all Americans to work, save, and invest.
15. Much of this analysis originally appeared in Ronald D. Utt, "More Transportation Spending: False Promises of Prosperity and Job Creation," Heritage Foundation *Backgrounder* No. 2121, April 2, 2008, at *http://www.heritage.org/Research/budget/bg2121.cfm*.
16. *Ibid.*

An April 2008 DOT update to its previous study reduced the employment figure to 34,779 jobs supported by each $1 billion spent on highways, and explicitly stated that the figure "refers to jobs *supported* by highway investments, not jobs *created*."[17] Similarly, a Congressional Research Service study calculated similar numbers as the DOT study, but cautioned:

> To the extent that financing new highways by reducing expenditures on other programs or by deficit finance and its impact on private consumption and investment, the net impact on the economy of highway construction in terms of both output and employment could be nullified or even negative.[18]

Not surprisingly, highway spending has a poor track record of stimulating the economy. The Emergency Jobs Appropriations Act of 1983 appropriated billions of dollars in highway spending (among other programs) in hopes of pushing the double-digit unemployment rate downward. Years later, an audit by the General Accounting Office (GAO, now the Government Accountability Office) found that highway spending generally failed to create a significant number of new jobs.[19] The bottom line is that there is no reason to expect additional highway spending this year to boost short-term economic growth or create new jobs.

As stated above, resulting improvements in the nation's infrastructure may increase *future* productivity and growth—once they are completed and in use. This is *not* the same as suggesting that the act of spending money on additional highway workers and asphalt is itself an immediate stimulant. Even the hope of future productivity increases rest on the assumptions that politicians will allocate money to necessary highway projects (rather then pork), and that those future productivity benefits will outweigh the lost productivity from raising future tax rates to finance the project.[20]

3) State Bailouts Merely Shift Money Around

Congress is reportedly considering using stimulus funding to bail out states dealing with their own budget shortfalls. This makes little sense as a matter of macroeconomic policy. State spending does not suddenly become stimulative because it is funded by Washington instead of state governments. Either way, any spending "injected" into the economy must first be taxed or borrowed from the economy. It does not matter which level of government is doing the taxing, borrowing, or spending.

Furthermore, sending federal aid to states would not save taxpayers a dime because state taxpayers are also federal taxpayers. Increasing federal borrowing to keep state taxes from rising is like running up a Visa card balance to keep the Mastercard balance from rising. The overall costs do not change, only the address receiving the payment.

Governors typically respond that a federal bailout is preferable because it could be funded with deficits rather than new taxes—currently not an option for the 49 states with balanced-budget requirements. But nobody forced these states to enact balanced-budget requirements, which they are free to repeal. It is disingenuous for a state to enact a balanced-budget amendment, and then demand that Washington bail it out of the consequences of its own policy.

Congress already sends $467 billion to state and local government every year—up 29 percent after inflation since 2000.[21] This is well beyond what is needed to reimburse states for federal mandates. In fact, since 1996, Washington has imposed less than $25 million per state in new unfunded

17. "Employment Impacts of Highway Infrastructure Investment," Department of Transportation, Federal Highway Administration, April 7, 2008. (Emphasis in original.) Report no longer appears on DOT Web site. Contact author for original PDF file.

18. David J. Cantor, "Highway Construction: Its Impact on the Economy," Congressional Research Service *Report for Congress* No. 93–21E, January 6, 1993.

19. U.S. General Accounting Office, *Emergency Jobs Act of 1983: Funds Spent Slowly, Few Jobs Created*, GAO/HRD–87–1, December 1986, at *http://archive.gao.gov/f0102/132063.pdf* (November 7, 2008).

20. Alternatively, the project could be financed by borrowing. However, long-term economic growth requires that the government obtain a higher return on its investment than the private sector would have with those funds.

mandates. (No Child Left Behind is neither unfunded nor mandated.)[22] State health, education, and transportation programs remain heavily subsidized by Washington.

Because states are so dependent on income tax revenues—which are volatile—common sense says to build rainy-day funds during booms to cushion the inevitable recessions. Instead, states keep responding to *temporary* revenue surges with new *permanent* spending programs. Between 1994 and 2001, states flush with new revenues shunned rainy-day funds and instead expanded their general fund budgets by 6.2 percent annually.[23]

All booms eventually end, and these free-spending states left themselves utterly unprepared for the 2002–2003 economic slowdown. Yet instead of sufficiently paring back their bloated budgets, the states demanded and received a $30 billion bailout from Washington in 2003. When government bails out irresponsible behavior, it only encourages more irresponsibility. And that is just what happened: After the 2003 bailout, states went right back to spending—with annual budget hikes averaging 7.2 percent over the next four years.[24] Rainy-day funds were expanded, although not nearly by enough. Thus, another recession has brought another round of state bailout calls.

How will states learn to budget responsibly if they know they can keep returning to the federal ATM?

The biggest losers from a federal bailout are the taxpayers who live in fiscally responsible states. They played by the rules and resisted extravagant new spending programs—and will be "rewarded" with higher taxes to bail out neighboring states that went on a spending spree they could not afford. That is simply unfair. And it encourages responsible states to be less responsible next time—better to be the bailout recipient than the bailout payer.

Congress should resist a bailout and instead instruct state governments to set priorities, make trade-offs, and reduce unnecessary spending. States that insist on deficit spending should reform their own balanced-budget laws rather than demand that Washington borrow for them. Finally, any federal aid to state governments should come in the form of loans to be repaid in full, with interest, within three years.

A Better Way

Government spending has an abysmal track record of stimulating the economy. However, these repeated failures have not stopped lawmakers from proposing and enacting a seemingly endless string of "stimulus" bills. Rather than redistributing money, lawmakers should focus on improving long-term productivity. This means reducing marginal tax rates to encourage working, saving, and investing. It also means promoting free trade, cutting unnecessary red tape, and streamlining wasteful spending that all weaken the private sector's ability to generate income and create wealth. Finally, it means strengthening education—not just throwing money at it. Addressing long-term growth and productivity is more challenging than waving the magic wand of short-term "stimulus" spending—but a more productive economy will be better prepared to handle future economic downturns.

—Brian M. Riedl is Grover M. Hermann Fellow in Federal Budgetary Affairs in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

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21. U.S. Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2009* (Washington, D.C.: U.S. Government Printing Office, 2008), p. 113, Table 8.3, at *http://www.whitehouse.gov/omb/budget/fy2009/pdf/spec.pdf* (November 7, 2008).
22. U.S. Congressional Budget Office, "A Review of CBO's Activities in 2007 Under the Unfunded Mandates Reform Act," March 2008, Appendix C, pp. 55–56, at *http://www.cbo.gov/ftpdocs/90xx/doc9068/03-31-UMRA.pdf* (November 7, 2008).
23. National Association of State Budget Officers, "Fiscal Survey of the States," June 2008, p. 4 at *http://www.nasbo.org/Publications/PDFs/Fiscal%20Survey%20of%20the%20States%20June%202008.pdf* (November 7, 2008).
24. *Ibid.*

REMARKS FOR CONG. EDOLPHUS "ED" TOWNS AT THE SUBCOMMITTEE ON HEALTH HEARING ENTITLED "TREATMENTS FOR AN AILING ECONOMY: PROTECTING HEALTH CARE COVERAGE AND INVESTING IN BIOMEDICAL RESEARCH

November 13, 2008 ROOM 2123 10:00 A.M.

CHAIRMAN PALLONE, RANKING MEMBER, COLLEAGUES, COMMITTEE STAFF AND OTHERS, THANK YOU FOR HOLDING THIS EXTREMELY IMPORTANT AND MUCH NEEDED HEARING ON THE IMPACT OF THE ECONOMIC DOWNTURN ON HEALTH CARE COVERAGE AND ACCESS. I WOULD ALSO LIKE TO ACKNOWLEDGE ONE OF OUR ESTEEMED WITNESSES, THE HONORABLE JANET NAPOLITANO OF ARIZONA.

JUST TWO WEEKS AGO THE GOVERNOR OF MY STATE, THE HONORABLE DAVID PATERSON, GAVE TESTIMONY BEFORE THE HOUSE WAYS AND MEANS COMMITTEE. GOVERNOR PATTERSON'S TESTIMONY, AMONG OTHER POINTS OF CONCERN, ADDRESSED HOW AN INCREASE IN THE FEDERAL MEDICAID ASSISTANCE PERCENTAGE WOULD EFFECTIVELY AND EFFICIENTLY PROVIDE MUCH NEEDED AID TO THE STATE.

LAST WEEK WE REGRETFULLY LEARNED THAT 240,000 JOBS WERE LOST IN OCTOBER. AND, UNEMPLOYMENT RATES JUMPED TO 6.5 PERCENT, A RATE WE HAVE NOT SEEN THE LIKES OF IN NEARLY 15 YEARS.

A COMMONLY USED QUOTE CAUTIONS US TO "HOPE FOR THE BEST, AND PLAN FOR THE WORST". I DESPERATELY HOPE THAT OUR FRAGILE ECONOMY WILL RESOLVE,

HOWEVER GIVEN THE BLEAK UNEMPLOYMENT TREND AND THE FRAGILE STATE OF OUR ECONOMY, NOW IS NOT THE TIME TO HOPE FOR A MIRACLE – WE MUST ACT WITH HASTE.

IN ADDITION TO INCREASES IN FMAP, I WOULD ALSO LIKE TO BRIEFLY DISCUSS THE ROLE INCREASED NIH FUNDING MAY PLAY IN HELPING TO STIMULATE OUR ECONOMY.

AS EVERYONE IS KEENLY AWARE, THE LONGSTANDING "BREAD AND BUTTER" OF NEW YORK CITY'S ECONOMY HAS BEEN WALL STREET. WITH THE RECENT ECONOMIC DOWNTURN, IT IS NOT ONLY PRUDENT BUT IS IMPERATIVE FOR ME TO CHAMPION INCREASED NIH FUNDING IN AN EFFORT TO DIVERSIFY MY CITY'S ECONOMY AND SUPPORT A BOOMING BIOTECH INITIATIVE NATIONWIDE.

BEFORE I CONCLUDE I WOULD JUST LIKE TO ASK FOR CONSIDERATION OF UNANIMOUS CONSENT TO ADMIT THREE ITEMS INTO THE OFFICIAL HEARING RECORD THAT ARE GERMANE TO THIS HEARING:

1) THE TESTIMONY BY THE HON. DAVID PATERSON, GOVERNOR OF NEW YORK BEFORE THE HOUSE WAYS AND MEANS COMMITTEE ON OCTOBER 29, 2008 WHICH DISCUSSES NEW YORK'S DIRE NEED FOR A INCREASE IN THE FMAP. AND,

2) A NOVEMBER 12, 2008, *NEW YORK TIMES* ARTICLE, ENTITLED, "BROOKLYN LAB IS PART OF CITY'S GOAL TO BE A BIOTECH CENTER" WHICH DISCUSSES A NEW HIV/AIDS LABORATORY IN THE BROOKLYN ARMY TERMINAL SECTION.

3.) A LETTER TO OUR HONORABLE SPEAKER NANCY PELOSI FROM MORE THAN 230 PATIENT GROUPS, SCIENTIFIC AND MEDICAL SOCIETIES, AND RESEARCH INSTIUTIONS URGING SUPPORT OF INCREASED NIH FUNDING IN THE ECONOMIC RECOVERY PACKAGE.

THANK YOU MR. CHAIRMAN. WITH THAT, I WOULD LIKE TO YIELD BACK THE BALANCE OF MY TIME.

Statement of the Honorable David A. Paterson, Governor of the State of New York

Testimony before the Full Committee
of the House Committee on Ways and Means

October 29, 2008

Chairman Rangel, Ranking Member McCrery, and distinguished members of the committee, I appreciate the opportunity to testify before you today.

For the second time this decade, New York finds itself at the epicenter of a national emergency. Unprecedented turmoil on Wall Street has left our state in the throes of its most severe economic crisis since the Great Depression. The financial services industry has been shaken to its core, and with it, virtually every aspect of economic life in America.

In just the last month and a half we have seen the largest bank failure in U.S. history; the demise of the independent investment banking model; a credit freeze that is impacting the ability of municipalities to borrow funds needed for urgent infrastructure improvements; and declines in the stock market of over 40 percent—threatening the ability of average Americans to retire and send their children to college. In many ways, the economic consequences of the current financial crisis will likely be deeper and longer-lasting than those that followed the horrific terrorist attacks on Lower Manhattan.

The Failures of the Federal Government

Americans have watched the fabric of our economic system unravel and the values of their 401(K)'s evaporate, leaving them confused, angry, and wondering who is to blame for the near collapse of our financial system.

Certainly, an age of irresponsibility and greed on Wall Street was one of the most important factors behind this crisis. But there is another culprit that is equally culpable -- the lack of oversight and regulation by the federal government. In a moment of commendable candor, Treasury Secretary Henry Paulson recently admitted that he regrets the "failures of our regulatory system." Former Federal Reserve Chairman Alan Greenspan also recently confessed he "made a mistake" by putting too much faith in the ability of the free market to police itself and protect shareholders.

Federal oversight bodies utterly failed in their duty to protect the life savings of millions of Americans and the financial system itself. And because of their failure, our government (federal, state and local) and individuals are left to pick up the pieces—as evidenced by the $700 billion Wall Street rescue package that Congress was forced to pass.

How the Crisis is Impacting States

State governments, just like average Americans, have suffered as result of the failure of our national regulatory system. Tax revenues have plummeted and economic growth has stagnated. According to the Center on Budget and Policy Priorities, at least 39 states are currently experiencing fiscal distress. Twenty-nine states closed budget shortfalls of $48 billion in enacting their 2009 budgets. Since, at least 27 states are experiencing mid-year budget shortfalls for FY09, totaling $12.3 billion, and the projected shortfall for FY10 is $100 billion.

New York State is no exception. In fact, the challenges we face are perhaps more acute than any other state given that Wall Street accounts for twenty percent of our state tax revenue. The New York securities industry has reported $40.9 billion in losses in the last four quarters. Even in the four quarters following September 11, 2001, these firms posted a cumulative profit of $8.4 billion. We are now projecting that Wall Street bonuses will decline by 43 percent, or $20.7 billion, this year, and that capital gains on the sale of stocks and other assets will decline by 35 percent, or $38 billion.

New York's broader economy, like those in states around the nation, is also struggling. Last month, unemployment in our state reached 5.8%, the highest level in more than four years. We project that over 160,000 New Yorkers will lose their jobs during the current downturn and unemployment will reach 6.5 percent in 2009.

There is no doubt we are currently in a statewide recession. And if history is any guide, the recession will be more severe and longer lasting in New York State than it is in the nation as a whole. Indeed, the last five US recessions lasted an average of 11 months compared to 25-months in New York.

Record Deficits and New York's Response

Yesterday, I announced that over the next four years New York State will have to close a staggering $47 billion deficit – the largest in our history. Next year's $12.5 billion budget gap alone represents more than 25 percent of our General Fund

The magnitude of this fiscal crisis will require state governments to make significant spending reductions. When I took office seven months ago, I immediately began this process. I have already worked with the New York State Legislature to make nearly $2 billion in reductions to this year's state budget. I have also asked the State Legislature to partner with me and find $2 billion in additional savings at a special session in November. And when I deliver next year's budget, I will propose the largest spending reductions in state history. Funding for many worthy programs, several of which I personally support, will have to be curtailed dramatically. This is not something I want to do, but it must be done.

But Governors can only cut so much before we begin to jeopardize our fundamental responsibilities to our constituents. The reductions necessary to close these massive deficits will impact the very core of what we do as states – protecting the public's safety, providing health

care for the most vulnerable, educating our children, caring for the needy, meeting the energy needs of our constituents, maintaining our infrastructure, and investing in our economy.

Unfortunately, the cruel irony is that at the time when citizens need their state governments the most, state governments are least equipped to help them because of plummeting revenues. History shows that during economic downturns, Medicaid and Human Services caseloads will increase dramatically. The current fiscal crisis will also impair our ability to make key investments in infrastructure and job creation that are needed to help us emerge from this recession and stimulate long-term economic growth.

When states are hurting, our national economy suffers. State governments are engines of both economic and social progress. They are a key source of job creation in this country, through aid for small businesses, incentives for economic investment, and workforce development programs.

Likewise, investments at the state level both expand our national tax base and lower entitlement pressures on the federal budget. For example, the innovative Federal State Health Reform Partnership (F-SHRP) program provides federal assistance to reform our health care industry and to deliver more cost effective services, which saves money for both levels of government.

An investment in state governments is an investment in the health of both our overall economy and the federal budget. And, while I acknowledge that the federal government is facing fiscal difficulties of its own right now, I submit that avoiding the long-term adverse consequences of failing to aid state governments greatly outweighs any short-term financial costs.

Direct Fiscal Relief to States

In dealing with the current fiscal crisis, New York and other states are holding up their end of the bargain by reducing spending in a proactive and responsible manner. But we also need a partner in the federal government. No single action could re-establish that partnership more quickly than for Congress to pass an economic stimulus bill before it adjourns for the year.

There are a number of important initiatives that should be included in any final negotiated package, such as money for infrastructure improvements, greater unemployment benefits, and a temporary increase in food stamp subsidies. But there is an essential item that rises to the top of the priority list ahead of all others.

As part of a comprehensive second economic stimulus package, ***states need direct and immediate fiscal relief*** to help close their massive budget deficits. The failure of our federal regulatory system has caused too many innocent bystanders to suffer. And now, Washington needs to step up and help states address a problem that was not of their own making. Just like the financial services industry, we need a partner in the federal government in order to help stave off an impending calamity and stabilize our fiscal condition.

Much of the good that would be done through proposals like expanding unemployment or food stamp benefits would be undone if states do not receive necessary federal budget relief. State governments like New York are on the front lines of service delivery for our citizens for

programs like Medicaid, TANF, and other social services. The results of federal inaction could be devastating in every corner of our nation. We would be giving with one hand and taking with the other.

Furthermore, most state budgets dedicate a substantial amount of resources to local assistance payments to municipalities. In New York, seventy percent of our budget goes to local assistance. Massive sudden reductions in state budgets will reverberate across all levels of government from the largest cities to the smallest school districts.

While all states are hurting and deserve support from the federal government, I think it is incumbent on me to note that New York faces unique circumstances with respect to this crisis. First, we are at the epicenter of the crisis on Wall Street, and the failure of financial institutions impacts our revenues and unemployment situation more than any other state. Just as after 9/11, we are asking the federal government to come to our assistance in a time of emergency. Second, New York has been shortchanged for years when it comes to aid from Washington. In 2007 alone, New York sent $86.9 billion more to the federal government in taxes than it received in return – again, more than any other state.

State fiscal relief is most effectively and efficiently provided through a temporary increase in the Federal Medicaid Assistance Percentage (FMAP) and emergency block grant funding. To help support escalating Medicaid costs, a temporary FMAP federal reimbursement rate increase of at least 5 percent should be provided through federal fiscal year 2011 to states hardest hit by the current economic crisis. Next, we ask that Congress again provide emergency block grant funding to states as it did in 2003, which will allow us to preserve a broad array of essential services.

I firmly believe that if it took only took two weeks for the federal government to find $700 billion dollars to bail out Wall Street and bank executives that brought our financial system to the brink of collapse, then we ought to be able to find a fraction of that amount to help preserve essential services at the state level that will help lift up Americans out of poverty, expand opportunity for the middle class, and protect our economic future.

States didn't cause this crisis and we shouldn't be left to deal with it alone. I have no choice but to close the massive deficits I inherited. It is simply a question of how. A rescue package from the federal government will help soften the blow for average Americans. It could make the difference between targeted, surgical spending reductions that will help heal our fiscal condition and massive and wide-ranging cuts that will cause irreparable damage to millions of families.

Other Vital Initiatives to Stimulate the Economy

While stabilizing the fiscal condition of state governments is of immediate importance, you have rightly recognized that there are other critical components that must be included in any new stimulus or recovery package. We must also rebuild our aging infrastructure and provide direct relief to citizens who have been hardest hit by this economic downturn.

- Infrastructure funding for ready-to-go transportation and water improvement projects. Infrastructure spending is one of the most important investments the federal government can make during an economic downturn as it has the dual benefit of modernizing our nation's deteriorating infrastructure while also stimulating the economy through job creation. In fact, analysts estimate that for every $1 billion invested in transportation projects, approximately 35,000 jobs are created.

  The American Association of State Highway and Transportation Officials (AASHTO) estimates that there are over 3,000 transportation projects in over forty states worth more than $18 million 'on the shelf,' waiting to be funded. In New York, with an additional $410 million in funding, we could put people to work immediately on over 40 highway, transit and rail projects that are shovel-ready.

  The conservative cost estimate of repairing, replacing and updating New York's municipal wastewater infrastructure is $36.2 billion over the next 20 years. There are 390 separate projects, with costs exceeding $4 billion waiting for funding. With an additional $715 million in Clean Water State Revolving Funds, New York's share of the proposed $6.5 billion stimulus investment in Clean Water State Revolving Funds we can protect and improve the water quality of New York State and put people to work on 58 wastewater projects this year.

  It is important to note that state budget conditions have deteriorated to the point where any federal dollars received for infrastructure projects must be free from state matching fund requirements. States have already reprogrammed and reprioritized to a point where there is simply nothing left in the budget for the current fiscal year.

  The financial crisis has also forced governors and legislatures to explore new ways to finance and deliver infrastructure projects and effectively make long-term capital investments. Some states have already made hard decisions to increase tolls and implement congestion pricing. In New York, I recently signed an executive order to establish a State Commission on Asset Maximization to study potential public-private partnerships. The Commission will examine the role of PPPs and consider whether this model can benefit New York State. It will also examine whether any specific state assets, such as the multi-billion dollar replacement for the Tappan Zee Bridge, are suitable candidates for such partnerships.

  I would also like to take a moment to remind the members of this committee and Congress about the only portion of the post-9/11 recovery package which the federal government promised New York but has not yet received – the proposal to sunset the existing $2 billion New York Liberty Zone tax provisions, and instead provide tax credits which the State and City of New York will use to fund infrastructure projects with a connection to Lower Manhattan. This provision has been included in the President's budget year after year, and it has been included in multiple pieces of legislation that have passed both the House and Senate more than once. Somehow, though, it has not yet found its way into a bill that has ultimately been signed into law. This is not only a tremendously high priority for me, but also for Mayor Bloomberg and all New Yorkers. I ask you to follow through on this promise to New York.

- An extension of Emergency Unemployment Compensation (EUC) benefits and modernization of the unemployment insurance system. The current EUC program, which took effect on July 6, 2008, provides 13 weeks of benefits to laid-off workers after they exhaust 26 weeks of regular Unemployment Insurance benefits. In New York State, we project that 90,000 laid-off workers will exhaust 13 weeks of EUC benefits by the end of this calendar year.

  Congress should provide for an additional 7 weeks of emergency benefits after the 13 weeks of EUC benefits. Studies reveal that for each dollar in cost, an extension of unemployment benefits generates $1.64 to $1.73 in increased activity. The Congressional Budget Office agrees: its report on short-term economic stimuli found that extending unemployment benefits is among the most cost-effective, potent, yet temporary steps that Congress can take to jump-start our economy.

  Additionally, as Congress gets set to consider a broader economic recovery package it must take action to close the gaps in the unemployment insurance system. Mr. Chairman, I commend you for your Unemployment Insurance Modernization Act proposal, which would help close this gap by making an estimated half-million more low-wage and part-time workers eligible for unemployment benefits. It ties distribution of funds to various changes in state laws to broaden eligibility for unemployment insurance benefits. This could result in over $400 million to New York State over the next five years. This is of critical importance to my state and many others.

- Temporary boost in funding for the Food Stamp program. As the economy declines, more and more Americans are struggling to feed their families. In New York, demand for food assistance New York has increased by 30 percent statewide over the last year. Through our Working Families Food Stamp Initiative, we have enrolled over 100,000 new families in the Food Stamp program. In these difficult economic times, the federal government must act swiftly to help our most vulnerable families by providing a temporary increase in food stamp benefits.

- Moratorium on federal regulations that harm state budgets. At a time when states are so desperately in need of fiscal relief, the last thing we can afford is onerous federal regulations that curtail existing avenues of federal support for critical services. One such regulation is the Outpatient Hospital Clinic regulation that was inappropriately promulgated by the Center for Medicare and Medicaid Services (CMS). This regulation would restrict over $450 million in federal funding to outpatient services to New York State alone. This regulation should be placed under moratorium in the stimulus package.

Conclusion

Last week, Federal Reserve Chairman Ben Bernanke expressed his support for a second federal stimulus package. Chairman Bernanke noted that this congressional effort should be aimed at "redressing specific factors that have the potential to extend or deepen the economic slowdown." I can tell you, most assuredly, that the large budget gaps facing New York and other states, and

their impact on vital services, are just such a factor. Unless states receive fiscal relief, I believe the goal of stabilizing the economy cannot be achieved.

I know that we can partner together to help ensure that, despite the challenges that lie ahead, states like New York can help preserve essential functions of government, grow our economy, create jobs for average Americans, and emerge from this crisis even stronger than before.

Once again, I thank you for the opportunity to provide a state perspective on these important issues, and I welcome your questions.

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November 11, 2008

Brooklyn Lab Is Part of City's Goal to Be a Biotech Center

By PATRICK McGEEHAN

On the top floor of a hulking 90-year-old building on Brooklyn's western waterfront, plasterers and electricians are preparing what city officials hope will be an economic antidote to the implosion of the financial services industry.

In a cavernous warehouse built as a military supply depot during World War I, medical scientists will soon be searching for a vaccine to fight the spread of AIDS. Their laboratory, scheduled for an official opening on Wednesday, will be the first tenant of a section of the Brooklyn Army Terminal that the city has reserved for bioscience companies and organizations.

The center is the newest frontier in the city's long-running campaign to make New York a capital for the biotechnology industry and in Mayor Michael R. Bloomberg's efforts to reduce the city's economic dependence on Wall Street.

The urgency of that effort has only increased as some of the biggest banks in New York have collapsed or laid off hundreds of employees, raising fears that the city's leading industry may permanently shrink.

"This is a down payment on an industry that we think is going to be a major tax generator for both the city and the state for many years," said Seth W. Pinsky, president of the city's Economic Development Corporation.

So far, the city has invested more than $35 million to build or renovate office and lab space for bioscience ventures. About one-third of that is going toward the new quarters for the International AIDS Vaccine Initiative in Brooklyn. The state has pledged an additional $48 million to convert 500,000 square feet of the Brooklyn Army Terminal into space for biotechnology firms.

The Brooklyn project is a prelude to a much more ambitious initiative: the development of the East River Science Park, a $700 million complex under construction on city property adjacent

to New York University Medical Center in Manhattan. The science park, with more than 1 million square feet of office and lab space between East 28th and 29th Streets, is scheduled to be completed in 2010.

Although the metropolitan area has the highest concentration of medical science talent in the country, it lags far behind the Boston and San Francisco areas as a center for turning their ideas into products and services.

"The academic medical centers that are here spin off about 20 companies per year and we're missing out on them," said Lenzie Harcum, vice president for biosciences at the Economic Development Corporation.

Financiers from Silicon Valley have been picking off many of the most marketable ideas for new ventures and persuading their founders to set up shop in established biotech centers where operating costs are significantly lower than in New York City, like San Diego or Cambridge, Mass., local business leaders say.

"The joke here was that venture capitalists came into New York from the West Coast with the three M's — the money, the management and the moving van — and relocated them," said Kathryn S. Wylde, chief executive of the Partnership for New York City, an association of large employers that has invested in some biotech startups. "They either went to the West Coast, some went to New Jersey, a lot went to Massachusetts, some to New Haven."

Ms. Wylde said New York's previous attempts to compete with those places lacked the necessary scale. She cited the Audubon Business and Technology Center, which Columbia University manages in upper Manhattan, as a prime example.

The Audubon center was built in the early 1990s with about $11 million in city funds, according to economic development officials. Standing adjacent to the former site of the Audubon Ballroom, where Malcolm X was assassinated in 1965, it contains about 100,000 square feet of office and lab space for nascent biotech companies.

That is about one-tenth of what the city needs to attract a "critical mass" of biotech businesses, Ms. Wylde said. Having incubators, like the Audubon center and another at the State University of New York Health Science Center at Brooklyn, known as SUNY Downstate, is helpful but not sufficient to keep growing companies in the city, she said. The scientists prefer to be in a cluster where they can share ideas and equipment, but the cost of operating in New York City has been prohibitive for many of them.

"Nobody wanted to start their company here because all they would have to do is move," Ms. Wylde said.

The city is home to the headquarters of some big pharmaceutical companies like Pfizer, but most of their scientists work in labs in New Jersey or farther away. One exception to the rule is ImClone Systems, a company developing cancer treatments that set up research labs on Varick Street in Lower Manhattan in 1986 and grew quickly.

But ImClone's name was tarnished in 2002 when its founder, Samuel D. Waksal, was arrested, and later convicted, in an insider-trading scandal. Martha Stewart, who was a friend of Mr. Waksal, wound up in prison for lying about the circumstances of her sale of shares of ImClone stock. The company's continued presence in the city is in doubt because Eli Lilly, a large drug company based in Indiana, offered last month to buy ImClone for $6.5 billion.

Retaining the next generation of ImClones is the goal behind the city's investment in the East River Science Park and the Brooklyn Army Terminal. The science park, being built by a California developer, will offer new space at competitive rates. The Brooklyn project is aimed at those outfits, like the AIDS vaccine initiative, that cannot afford Manhattan rent.

Seth Berkley, president and chief executive of the AIDS initiative, said his nonprofit organization considered several alternatives around the region when it began to outgrow its space at SUNY Downstate. He estimated it would have cost at least $70 a square foot to move into the science park when it is finished, too much for a nonprofit operation.

"When we negotiated with the city, we said, for the type of stuff we're doing that's not acceptable," Mr. Berkley said.

The Economic Development Corporation was planning to renovate the south end of one of two huge buildings at the Army terminal as a bioscience center. But Mr. Berkley's group, known as IAVI, had a different idea: Because their labs required so much equipment for filtering air and venting chemical fumes, they wanted to take 36,000 square feet of the top floor on the north side of the building.

There, they could install much of the infrastructure on the roof, allowing for maximum use of the floor space, said Stephen Kaminsky, the initiative's director of protein and analytical chemistry. Turning a building that once was the jumping-off point for soldiers headed overseas — including Elvis Presley in 1958 — into a state-of-the-art lab for testing various proteins that could kill the virus that causes AIDS was a challenge, Mr. Kaminsky said. But among the advantages, he said, is that the terminal is so sturdy that the scientists will not have to worry

much about vibrations that could upset their experiments.

The initiative is installing $3 million worth of scientific equipment, some of which was bought with money contributed by the Bill and Melinda Gates Foundation, Mike Goldrich, the organization's chief operating officer, said. But it would not be staying in Brooklyn without the hefty financial assistance provided by the city.

Along with the $12.5 million in public funds to fit out the space, the initiative received a 15-year lease that starts at a below-market rate of $16 per square foot. Only 30 to 40 people will work there at the outset, but city officials hope that number will double over time.

They and the scientists hope that the new lab will not be alone in the terminal for long. Mr. Kaminsky said having other tenants in related fields would help to attract speakers for seminars on recent scientific advances. The vaccine researchers also hope there will be an area in the building to house the monkeys, rabbits and other small animals that would be needed for experiments. And, of course, it would help to have neighbors to borrow supplies from in a pinch.

"There's an advantage to having people who do the same things you do in the same place," Mr. Kaminsky said.

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October 30, 2008

The Honorable Nancy Pelosi
Speaker
House of Representatives
Washington, DC 20515

Dear Madame Speaker:

The undersigned organizations, which represent more than 230 patient groups, scientific and medical societies, research institutions, and industry organizations, strongly urge your support for the inclusion of an additional $1.9 billion for the National Institutes of Health (NIH) in the economic recovery package currently being developed.

Recognizing the challenges facing NIH as a result of six years of funding below the rate of inflation, this proposal will provide immediate funding to support more than 5,000 additional competitively awarded research grants to help find cures for many devastating diseases.

NIH supports groundbreaking research that results in new preventive, therapeutic, and diagnostic measures to improve the health and quality of life for all Americans. In addition, these advances also contribute to the economic strength of the nation by creating skilled jobs, new products, and improved technologies. The medical schools, teaching hospitals, universities, and research institutes where this research takes place are among the largest employers in their respective communities.

According to a study released in June 2008 by Families USA, on average, in fiscal year 2007, every dollar of NIH funding generated more than twice as much in state economic output. This means an overall investment of $22.846 billion from NIH generated a total of $50.537 billion in new state business activity in the form of increased output of goods and services. This same study revealed that in FY 2007 NIH grants and contracts created and supported more than 350,000 jobs that generated wages in excess of $18 billion in the 50 states. The average wage associated with the jobs created was $52,000. We must invest now in the NIH to maximize the benefits of scientific opportunity for our nation's fiscal as well as physical health.

Since FY 2003, NIH has lost more than 14 percent of its purchasing power due to federal funding lagging behind the rate of biomedical inflation. The agency's current budget path hinders the scientific discovery that drives the search for new and better treatments and undermines the nation's leadership in medical research. Approval of the additional funding in the forthcoming economic recovery package would be an important step towards reversing NIH's current funding trend and setting it on a new course, giving patients, their families and researchers renewed hope for the future.

Sincerely,

Academic Pediatric Association
Academy of Radiology Research
Ad Hoc Group for Medical Research
AdMeTech
Administrators of Internal Medicine
Agfa HealthCare
AIDS Action Baltimore
AIDS Project Los Angeles
AIDS Vaccine Advocacy Coalition (AVAC)
Alliance for Academic Internal Medicine
Alliance for Aging Research
Alpha-1 Association
Alpha-1 Foundation
Alzheimer's Association
American Academy of Allergy, Asthma & Immunology
American Academy of Dermatology Association
American Academy of Neurology Professional Association
American Academy of Pediatrics
American Anthropological Association
American Association for Cancer Research (AACR)
American Association for Dental Research
American Association for the Study of Liver Diseases
American Association for Women Radiologists
The American Association of Anatomists
American Association of Colleges of Nursing
American Association of Colleges of Osteopathic Medicine
American Association of Immunologists
The American Association of Neurological Surgeons (AANS)
American Association of Physicists in Medicine
The American Brain Coalition
American Cancer Society Cancer Action Network
The American College of Clinical Pharmacology
American College of Preventive Medicine
The American College of Radiology (ACR)
American Dental Education Association (ADEA)
American Diabetes Association
American Foundation for the Blind
American Gastroenterological Association
American Heart Association
American Institute for Medical and Biological Engineering
American Liver Foundation
American Lung Association
American Osteopathic Association
American Pediatric Society
American Physical Therapy Association
American Psychiatric Association

American Psychological Association
The American Physiological Society
Americans for Medical Progress
American Roentgen Ray Society
American Social Health Association
American Society for Addiction Medicine
American Society for Biochemistry and Molecular Biology
The American Society for Bone and Mineral Research
The American Society for Cell Biology
The American Society for Clinical Investigation
The American Society for Microbiology
American Society for Pharmacology and Experimental Therapeutics
American Society for Reproductive Medicine
The American Society for Therapeutic Radiology and Oncology (ASTRO)
The American Society of Clinical Oncology
American Society of Emergency Radiology
American Society of Hematology
American Society of Nephrology
American Society of Pediatric Hematology/Oncology
American Society of Pediatric Nephrology
American Society of Radiologic Technologists
American Society of Transplantation
The American Society of Tropical Medicine and Hygiene (ASTMH)
American Sociological Association
The American Thoracic Society
American Tinnitus Association (ATA)
amfAR, The Foundation for AIDS Research
Arizona State University
Arthritis Foundation
The Asthma and Allergy Foundation of America
Association for Behavioral and Cognitive Therapies
Association for Clinical Research Training
Association for Psychological Science
Association for Research in Vision and Ophthalmology
Association of Academic Health Centers
Association of Academic Health Sciences Libraries
Association of American Cancer Institutes (AACI)
Association of American Medical Colleges (AAMC)
Association of Educators in Imaging and Radiologic Sciences, Inc.
Association of Independent Research Institutes
Association of Medical School Pediatric Department Chairs
The Association of Pediatric Oncology Social Workers
Association of Professors of Medicine
Association of Schools of Public Health
Association of Specialty Professors
Association of University Centers on Disabilities

American Society of Pediatric Hematology/Oncology
The Association of Women's Health, Obstetric, and Neonatal Nurses (AWHONN)
Autism Society of America
Baylor College of Medicine
Biophysical Society
Biotechnology Industry Organization
Boston University Medical Campus
Brigham and Women's Hospital
Brown University
Case Western Reserve University School of Medicine
Center for Emerging Technologies (CET)
Chronic Obstructive Pulmonary Disease Foundation
Cincinnati Children's Hospital Medical Center
Clinical Research Forum
Coalition for the Advancement of Health Through Behavioral and Social Sciences Research
Coalition for Imaging and Bioengineering Research (CIBR)
Coalition for the Life Sciences
Coalition to Protect Research
The College on Problems of Drug Dependence
Cooley's Anemia Foundation
Columbia University Medical Center
Columbia University TeenScreen Program
Community Anti-Drug Coalitions of America (CADCA)
Community HIV/AIDS Mobilization Project (CHAMP)
Congenital Adrenal Hyperplasia Research Education and Support (CARES) Foundation, Inc.
The Congress of Neurological Surgeons (CNS)
Consortium of Social Science Associations
Crohn's and Colitis Foundation of America
Cystic Fibrosis Foundation
Digestive Disease National Coalition
Duke University Medical Center
Dystonia Medical Research Foundation
EPSCoR/IDeA Foundation
Emory University
The Endocrine Society
Families USA Global Health Initiative
Federation of American Societies for Experimental Biology (FASEB)
First Candle/SIDS Alliance
Friends of Cancer Research
Friends of NICHD
Fujifilm Medical Systems USA
Gamma Medica-Ideas, Inc
The Gerontological Society of America
Harlem United

Harvard University
The Heart Rhythm Society
Hepatitis B Foundation
Hepatitis Foundation International
The HIV Medicine Association
Indiana University
Infectious Diseases Society of America
Intellectual and Developmental Disabilities Research Centers Association
The International Community of Women Living with HIV and AIDS (ICW)
International Foundation for Functional Gastrointestinal Disorders
The International Society for Computational Biology
Invitrogen Corporation
Jeffrey Modell Foundation
Johns Hopkins Institutions
Juvenile Diabetes Research Foundation
LA Gay & Lesbian Center
Legal Action Center
The Leukemia & Lymphoma Society
The Lupus Research Institute
March of Dimes Foundation
Massachusetts General Hospital
Medical College of Wisconsin
Medical Library Association
Morehouse School of Medicine
National Alliance for Eye and Vision Research (NAEVR)
National Alliance on Mental Illness
National Association for Biomedical Research
National Association for Children of Alcoholics
The National Association of Pediatric Nurse Practitioners
National Association of State Alcohol and Drug Abuse Directors
National Caucus of Basic Biomedical Science Chairs
National Coalition for Cancer Research (NCCR)
The National Coalition for Osteoporosis and Related Bone Diseases
National Health Council
National Kidney Foundation
National Marfan Foundation
National Multiple Sclerosis Society
National Organization for Rare Disorders (NORD)
National Primate Research Centers
National Psoriasis Foundation
NephCure Foundation
Neurofibromatosis, Inc.
New York-Presbyterian Hospital
North American Society for Pediatric Gastroenterology, Hepatology and Nutrition
The NYU School of Medicine
The Ohio State University Medical Center

Oregon Health & Science University
Osteogenesis Imperfecta Foundation
The Paget Foundation
Pancreatic Cancer Action Network
Parkinson's Action Network
Penn State College of Medicine
Population Association of America and the Association of Population Centers
The Preeclampsia Foundation
Pulmonary Hypertension Association
Reed Elsevier Inc.
Research!America
San Francisco AIDS Foundation
Scleroderma Foundation
Seattle Children's Research Institute
Sjögren's Syndrome Foundation
Society for Adolescent Medicine
Society for Maternal-Fetal Medicine
Society for Neuroscience
Society for Pediatric Research
Society for Research in Child Development
The Society for Women's Health Research
Society of Computed Body Tomography and Magnetic Resonance
Society of Gastrointestinal Radiologists
Society of General Internal Medicine
Society of Gynecologic Oncologists
Society of Thoracic Radiology
The Society of Toxicology
Society of Uroradiology
Spina Bifida Association
State Associations of Addiction Services
Stony Brook University Medical Center
SUNY Upstate Medical University
The Teratology Society and Environmental Mutagen Society
Therapeutic Communities of America
Toshiba Medical Research Institute USA, Inc
Treatment Action Group
Unite 2 Fight Paralysis
University of Alabama at Birmingham
University of Arkansas for Medical Sciences
University of California, San Diego
University of Maryland, Baltimore
The University of Minnesota Medical School
The University of Nebraska Medical Center
University of Rochester Medical Center
The University of Texas System
University of Washington

University of Wisconsin School of Medicine and Public Health
Vanderbilt University Medical Center
Wake Forest University
Washington University in St. Louis
Weill Cornell Medical College
WomenHeart: The National Coalition for Women with Heart Disease
Yale School of Medicine

C H I
CALIFORNIA HEALTHCARE INSTITUTE

Statement of the
California Healthcare Institute

Submitted to
U.S. House of Representatives
Committee on Energy & Commerce
Subcommittee on Health

Hearing on
Treatments for an Ailing Economy: Protecting Health Care Coverage and Investing in Biomedical Research

Thursday, November 13, 2008

The California Healthcare Institute (CHI) appreciates the opportunity to present our views on the importance of biomedical research as a critical fuel to prime the engine of innovation, job creation, economic growth, and improvements in health care for this important hearing.

CHI represents more than 260 of California's leading biotechnology, pharmaceutical, medical device and diagnostics companies, venture capital firms, research universities, and non-profit research institutions. CHI's mission since its founding in 1993 has been to identify and advocate for policies to promote biomedical research, development, and innovation in the state.

Biomedical research and development in California has advanced scientific knowledge and resulted in new tools, technologies and treatments for serious ailments such as cancer, diabetes, and HIV/AIDS, chronic pain, and cardiovascular, respiratory and infectious diseases. California's life sciences industry is also an important engine of economic growth, employing some 270,000 workers statewide, and leading the nation in terms of both venture capital investment ($3.2 billion) and National Institutes of Health (NIH) research funding ($3.16 billion).

The challenge we face today, in light of the slowing economy and financial markets meltdown, is to identify policies to help jumpstart the economy and

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WASHINGTON, D.C. 1608 Rhode Island Avenue, NW Washington, D.C. 20036 202.974.6313 Fax 202.974.6330 WWW.CHI.ORG

create jobs while also considering the severe fiscal and budgetary challenges we face at the federal, state and local levels.

In light of these circumstances, and recognizing that policies such as extension of the research and development tax credit, net operating loss (NOL) reform, and capital gain rollover, would have a significant stimulative impact on sectors beyond just the life sciences, CHI submits that increasing biomedical research funding, and in particular National Institutes of Health (NIH) funding, would address two goals: promote growth and job creation in an important sector of the high-tech economy AND provide a booster shot to efforts to advance biomedical science and the resulting technologies, tools, and therapies that will help transform medicine and improve health care for all Americans.

Biomedical research, funded primarily by the NIH, forms the foundation of California life sciences industry, and the state's academic research centers stand as the cornerstone of discovery. The birthplaces of ingenuity and breakthrough science, California's biomedical research centers lead the nation in grant funding and commercial licensing agreements – and for good reason. For decades, researchers at these centers have engineered discoveries yielding life saving therapies, diagnostics tools, drug delivery systems and medical devices. The state hosts a community of 100 leading academic research centers, which, fueled by NIH and other federal research funding, breeds groundbreaking research that expands the world's scientific knowledge, spearheads tomorrow's disease treatments, and plants the seeds of company formation and job creation that help drive the economy. Simply put, NIH funds the research upon which the biomedical industry has been built; without this foundation, there is no industry.

Some examples, as reported in the 2008 CHI/PricewaterhouseCoopers report "The National Institutes of Health (NIH): Fueling Healthcare Innovation in California":

- Dr. Mark Kay, professor of pediatrics and genetics at Stanford University School of Medicine and director of Stanford's program in human gene therapy, published the first results demonstrating that RNAi was an effective gene-therapy technique in mice. That finding launched widespread RNAi gene therapy research in both academic and industrial research groups. Dr. Kay was the scientific founder of Avocel, a California-based company since acquired, which employed

RNAi technology to precisely destroy RNA viruses and silence the expression of defective genes. NIH funding supported all of the research that lead to Avocel's founding.

- Researchers at The Scripps Research Institute in La Jolla, California purified the antihemophilic Factor VIII, a coagulation protein lacking in people with hemophilia A. The prescription medication Monoclate, the purified concentrate of Factor VIII, enables hemophiliacs to receive blood plasma that is free of virus contamination.

- University of Southern California researchers made the critical link between inhibiting DNA methylation, a process by which a chemical cluster called a methyl group is attached to the surface of a DNA strand and obstructs DNA transcription, and silencing genes. This research demonstrated the promise of epigenetic therapy and led to the development of two drugs that can inhibit cancer. The FDA has approved Vidaza and related drug Dacogen for the treatment of myeloid dysplastic syndrome, a pre-leukemic condition in older patients.

- NIH-funded researchers at the University of California discovered proto-oncogenes, or normal genes that have the potential to convert to cancer genes. The discovery has transformed the way that scientists look at cancer and is leading to new strategies for detection and treatment.

- Fully 581 life sciences companies have links to the University of California. One in six public biotech companies were founded by UC scientists. One in three California biotech companies were founded by UC scientists.

Certainly, the story illustrating the importance of biomedical research to the founding and growth of the life sciences industry is not exclusive to California. It is one being increasingly replicated throughout the country. NIH-funded research led to the development of the biotechnology cluster around Cambridge, Massachusetts, for example. Similarly, other top recipients of NIH funding – Illinois, Maryland, Michigan, New York, North Carolina, Ohio, Pennsylvania, Texas, Washington State, to name a few – have staked out economic development plans around the establishment and growth of biomedical innovation clusters in their states.

While NIH-funded biomedical research is not the sole driver of life sciences innovation, it is a critical one. Unfortunately, recent NIH funding levels threaten real consequences to the promises offered by advances in biomedical research.

Since the five-year doubling of NIH funding ended in 2003, the agency's budget has suffered dramatically. Although the agency's $28 billion budget for 2004 amounted to a 3.3 percent increase over the prior year, it was flat when adjusted for inflation. The President's FY2008 budget called for $28.9 billion, which was $379 million less than the NIH received in 2007. Moreover, because the president's budget request included a $201 million funding transfer, the actual 2008 research budget decreased by $581 million.

The picture at the ground level is similarly serious. Again, according to the CHI/PwC report:

"...the competition for peer-reviewed grants is rising, and investigators see their proposals undergo successive rounds of submissions before applications are funded. Meanwhile, the value and duration of awards are decreasing. Furthermore, funding constraints prohibit faculty from maintaining sufficiently staffed laboratories and limit them from hiring qualified younger researchers. ***Over time, longer, more tenuous proposal cycles will have negative downstream implications for future local workforce development and, ultimately, sustained innovation.***" (emphasis added)

Thankfully, Congress has begun work to address these consequences. And we are hopeful that further improvements are on the way. For example, lifting of existing federal restrictions on embryonic stem cell research will open the door for promising advances in that exciting and promising area of science. And as the case study of California has shown, biomedical research funding is a proven investment that not only advances scientific understanding, but also promotes innovation, saves lives, improves public health, and helps create jobs and foster economic growth.

Once again, CHI appreciates the opportunity to provide our views for this important hearing.

Thank you.

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