

**EMERGENCY HEARING TO EXAMINE THE
SHORTFALL IN VA'S MEDICAL CARE BUDGET**

HEARING

BEFORE THE

COMMITTEE ON VETERANS' AFFAIRS

UNITED STATES SENATE

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EMERGENCY HEARING TO EXAMINE THE SHORTFALL IN VA'S MEDICAL CARE BUDGET

TUESDAY, JUNE 28, 2005

U.S. SENATE,
COMMITTEE ON VETERANS' AFFAIRS,
Washington, DC.

The Committee met, pursuant to notice, at 11:08 a.m., in room SR-418, Russell Senate Office Building, Hon. Larry Craig (Chairman of the Committee) presiding.

Present: Senators Craig, Hutchison, Burr, Ensign, Thune, Akaka, Jeffords, Rockefeller, Murray, Obama, and Salazar.

OPENING STATEMENT OF HON. LARRY CRAIG, U.S. SENATOR FROM IDAHO

Chairman CRAIG. Good morning, everyone, Members of the Committee, Mr. Secretary. Let me first thank all of my colleagues for their understanding and the recognition of a short notice on this hearing, but we thought it was important to have it today and to move as quickly as we could to address the issue that is before us.

Second, I want to welcome our Veterans Administration Secretary Jim Nicholson and his staff to the Committee and their quick response to our request.

Five months ago, this Committee considered VA's budget proposal for fiscal year 2006. Many of us, myself included, relied on information VA provided and the assumptions the Administration made about the needs for our Nation's veterans when we voted on that budget.

Then only 2 months later, the Senate debated a supplemental appropriation bill for fiscal year 2005. Again, we sought the Administration's advice and many of us relied on that information when we voted on issues concerning the health care needs of our veterans.

Now I sit here, having recently learned that the information provided to me thus far has been disturbingly inaccurate. Needless to say, Mr. Secretary, I can't be very pleased about that. So I asked you to come here this morning to tell this committee four different things: Why VA's assumptions about the budget needs were wrong; when did you know, or when did you find out they were wrong; what the consequences are for transferring money to compensate for these errors; and what is needed to address the problem for fiscal year 2005 and fiscal year 2006 and beyond.

In my opinion, the question of what to do for fiscal year 2006 and beyond is the most important issue of the day. It may be that we are too far into the 2006 appropriation process to consider other alternatives besides simply providing the necessary financial re-

sources to address the shortfall, but if we are going to do that, then we must be accurate about what we do, again, so that we will not have this kind of conversation 6 months from now.

Additionally, we must come face-to-face with the reality that adding funds to the 2006 budget would mean continual annual increases in the funding of VA health care at an average of 10 percent. At that rate, we will double VA's health care budget every 8 years. This, on top of a system that already spends \$82 million every day and over a half-a-billion dollars every week, ladies and gentlemen, that is an extraordinary amount of money even in Washington terms.

While there is a good deal more I could say, I will stop there. I know others of my colleagues have comments before we hear from you, Mr. Secretary. I would hope that we could keep those as brief as possible so we can get to the substance of your statement and how we solve this problem.

I would also ask unanimous consent that I put into the record a letter from Senator Jon Kyl expressing his concern about this issue and addressing it in a forthright way so that our veterans are served as we would expect them to be.

[The letter from Senator Kyl follows:]

JUNE 28, 2005.

Senator LARRY CRAIG, *Chairman,*
Senate Committee on Veterans Affairs, SR-412,
Washington, DC.

DEAR MR. CHAIRMAN: I am writing to express my deep concern about the recently disclosed funding problems within the Department of Veterans Affairs and to commend you for your speedy effort to ensure accountability and devise solutions by inviting VA officials to testify before your Committee tomorrow.

Like you, I was distressed to learn that the information previously provided to the Congress by the Department was incorrect. Like you, I relied on that information and am quite displeased to learn that it was not as accurate as it ought to have been. And like you, I am committed to supporting whatever measures are needed to ensure that veterans' access to the health care services upon which they are depending is maintained—and improved. I trust that your hearing will provide helpful direction to me and to our colleagues in determining how to proceed and I look forward to working with you to ensure that this problem is addressed as soon as possible.

Sincerely,

JON KYL,
United States Senator.

Chairman CRAIG. With that, let me turn to my Ranking colleague, Democrat Senator Danny Akaka. Danny.

**STATEMENT OF HON. DANNY AKAKA, U.S. SENATOR
FROM HAWAII**

Senator AKAKA. Thank you very much, Mr. Chairman. Good morning to everyone.

We all know why we are here, and that is to understand, as the Chairman has said, what went wrong in planning for veterans' health care needs and also to focus on what we must do to fix the problem.

This is not simply about data or assumptions for the planning models. This is about providing vital health care services for our Nation's veterans and we simply must keep focused.

We at least now have an admission that VA hospitals and clinics are in the red, and this is the first step in turning things around.

I, frankly, do not understand why this shortfall comes as a surprise, but we will hear about that. We have been hearing from health care providers all over the country about how dire this situation is. For months now, reports have been coming in that beds are deliberately kept empty or that failing equipment cannot be replaced and that mental health services are being denied. Every day, clinic directors are making arbitrary decisions about which veterans can come in for care. And, of course, this is in violation of the law.

Despite the tremendous pressure to keep quiet, VA's dedicated providers have been forthright about the fact that they were raiding capital accounts just to make ends meet. Using capital funds means that needed clinics like one in America Samoa will never come to fruition.

We raised these issues earlier this year on the Senate floor, Senator Murray, myself, and others, and VA officials denied that trouble was ahead. During our debate on the shortfall in April, we drew attention to the impact that the men and women returning from Iraq and Afghanistan could have on the VA system. This is an influx of patients that VA simply cannot easily absorb in addition to its huge current patient load.

I do think that in light of this crisis, we need to take a fresh look at the proposal to guarantee full funding for VA health care. If we cannot put faith in the current process, perhaps we need another approach.

Finally, Mr. Chairman, let me just say that I am truly committed to working with my colleagues and with you and this Committee to ensure that existing veterans and returning servicemembers get the health care they deserve. I have no doubt that we will restore the funding. In fact, Senator Murray and I are moving to add these funds to the Interior appropriations bill currently on the Senate floor.

Thank you very much, Mr. Chairman.

Chairman CRAIG. Senator Akaka, thank you.

We will proceed in the order with which Members came to the Committee today. We have also been joined by the chairman of the appropriating subcommittee for Military Construction-VA and I will turn to Chairman Hutchison in a few moments. Let me go next to Senator Murray.

**STATEMENT OF HON. PATTY MURRAY, U.S. SENATOR
FROM WASHINGTON**

Senator MURRAY. Thank you very much, Chairman Craig and Senator Akaka, for holding today's hearing, and Secretary Nicholson for joining us today, especially so quickly after last Thursday's announcement that the VA is well over \$1 billion short of funding this year. I especially want to thank Chairman Craig for assuring me he will get to the bottom of this issue, as well as Senator Hutchison for their work in trying to figure out a solution to this.

Like all of the Members here today, I want to find a solution to this problem as soon as possible and I hope this Committee today can have a very open and honest discussion about the VA's needs and the best way that we can now move forward to provide adequate funding. This Committee, as the Chairman said, needs to

know how this happened, and specifically, we need to know how your staff estimated a 2.7 percent increase in the number of veterans accessing VA care when in reality we are, as we all knew, seeing more than a 5 percent increase. This Committee also needs to know when it was clear that the VA had a shortfall, how we can fix this, and how we can prevent this from ever happening again.

During my attempt to include VA funding on the last direct war supplemental, Chairman Craig said that if the VA came forward with an announcement like this, that he would work with me to get the funding the VA needed, and I am grateful for that commitment.

Mr. Secretary, I hope that as you address this Committee you will outline how we got here today and how you plan to meet the needs of our veterans. As this Committee knows, throughout the budget and supplemental appropriations process, I fought to increase funding for care for our Nation's veterans. I used my position on the Budget Committee, on the Appropriations Committee, and on this Committee to get adequate funding for our veterans and I introduced an amendment to the supplemental to provide for our troops by assuring access to quality health care services and benefits when they return home. I took these measures because I have long believed that caring for our veterans is a fundamental cost of war. Unfortunately, each time, my efforts failed.

Secretary Nicholson, in an April 5 letter to Military Construction and Veterans' Affairs Subcommittee Chairman Hutchison, you wrote in this letter, and I want to quote, "I can assure you that VA does not need emergency supplemental funds in fiscal year 2005 to continue to provide timely, quality service that is always our goal," end quote. I would like to ask unanimous consent to include this letter in the record for this hearing.

Chairman CRAIG. Without objection.

[The letter from Secretary Nicholson follows:]

Hon. KAY BAILEY HUTCHISON, *Chairman,*
Subcommittee on Military Construction and
Veterans Affairs Committee on Appropriations,
U.S. Senate,
Washington, DC.

DEAR MADAM CHAIRMAN: Before I begin the main purpose of this letter, I want to take this opportunity to thank you for the consideration and interest you have shown VA through your leadership in this year's appropriation hearing and many other endeavors on behalf of our veterans. I very much appreciate your proactive involvement and commitment to providing for those who have served this country with such dedication.

I write to you today to address certain issues regarding VA's fiscal year 2005 fiscal situation. I know some have said that VA must have emergency supplemental funds to continue providing the services for which veterans depend on us—timely health care and delivery of benefits. Whenever trends indicate the need for re-focusing priorities, VA's leaders ensure prudent use of reserve funding for these purposes. That is just simply part of good management. It does not, however, indicate a "dire emergency." I can assure you that VA does not need emergency supplemental funds in fiscal year 2005 to continue to provide the timely, quality service that is always our goal. We will, as always, continue to monitor workload and resources to be sure we have a sustainable balance. But certainly for the remainder of this year, I do not foresee any challenges that are not solvable within our own management decision capability.

I look forward to continuing to work with you as we strive to provide the very best service possible for those veterans who depend on us the most. Thank you again for your leadership in this important area.

Sincerely yours,

R. JAMES NICHOLSON.

Senator MURRAY. Even during a June 9 hearing before this Committee, under direct questioning, Secretary Nicholson, you did not indicate that your budget was in trouble. Now, less than 3 months after this letter, and just 20 days after that hearing, you are here to testify that we are short over \$1 billion.

When I was fighting to get my veterans' health care amendment passed a few months ago, I warned my colleagues that what was an emergency would become a crisis if we didn't work together to address this problem. With the VA's announcement last week, that emergency has now become a crisis.

Mr. Secretary, as Secretary of Veterans Affairs, you are our Nation's veterans advocate. Your job is to fight for the needs of our veterans. This funding shortfall is yet another indication that the Administration has not taken the issue of veterans' funding seriously.

Mr. Secretary, I know you have probably come here today prepared to tell us how you are going to get through this year. When you and I spoke over the phone last Thursday evening, you told me that you felt you could get through this shortfall by moving more funds from capital accounts to the operations account. You said our VA facilities were in top-notch shape, despite the fact that the VA's own community-based outreach clinics have been stymied due to lack of capital funds, and most of our VISNs have delayed major capital projects for more than 2 years now.

Now, I realize that moving funds between accounts is commonplace at the VA to meet the health care needs of our veterans, but I want to be clear. Any plan to get us through this year based on borrowing funds from future years is fundamentally flawed. Any plan that involves borrowing funds from future years is fundamentally flawed. That type of solution is no solution at all. In fact, it is not any different than any other budgetary gimmick. It is a shell game that will really put us in jeopardy and in future crisis and we cannot afford to do that.

What we really need now, I think is clear, and that is an infusion of cash to stop the bleeding at the VA. If, as you say, this is truly an unanticipated cost, then that is exactly what emergency supplemental bills are for.

I really regret that it has come to this, but now I believe it is time for all of us to come together and provide the needed dollars so our veterans have the quality, accessible care that they were promised and that they deserve. Every indication is that we simply do not have enough funding for our current services, and the VA is increasingly unable to handle the increased number of veterans who are coming home from Iraq and Afghanistan while still providing high levels of service to our previous veterans. It is not right and it is not what our veterans were promised.

Mr. Secretary, I don't know how you couldn't foresee such an enormous shortfall in VA funding, but I do intend to work with my colleagues to find out and I hope that when the President addresses the Nation tonight on the war in Iraq, he addresses this adminis-

tration's plan to take care of the needs of our Iraq war veterans, and I stand ready to work with this Administration, our Republican colleagues and our Democratic colleagues to fix this problem and what I believe the best solution will be, an emergency supplemental that we can enact as soon as possible. That is why I have offered an emergency supplemental as a freestanding bill and why I have filed an amendment to the appropriations bill that is currently pending.

But I do stand ready to work with the Chairman, both Chairmen that are here, as well as the White House to get done what we need to get done immediately for those men and women who have served our country. I know this process requires White House participation. Congress can't do it on its own. I will be looking to the Administration to be serious, I hope, tonight when the President addresses the Nation. The stakes, Mr. Chairman, are just too high to be continuing to kick this can down the road.

Finally, I just want to assure the Chairman that I want to get to the bottom of this problem, as I know he does. From what I have learned, this shortfall is either deliberate misdirection or incompetence, but either way, it is unacceptable for us in Congress to get that kind of information and we need to fix it, and we need to find out how to recover from this and provide the dollars so that our veterans don't face this shortage. Thank you, Mr. Chairman.

Chairman CRAIG. Senator Murray, thank you.

Senator Salazar.

**STATEMENT OF HON. KEN SALAZAR, U.S. SENATOR
FROM COLORADO**

Senator SALAZAR. Thank you, Chairman Craig and Ranking Member Akaka, for holding this very important hearing, and thank you, Secretary Nicholson, for coming here today.

Let me just say that we have a crisis on our hands, and from my point of view, when you have this kind of a crisis on your hands, the question is very simple. One is, how do we fix the problem, and two, how do we make sure that this problem doesn't occur again?

When I look at the numbers that we are talking about, it is something that I believe we all should be very, very concerned about, because a \$1 billion shortfall when we have 3 months remaining in the fiscal year, if you annualize that, we end up with a \$4 billion shortfall, which I understand is somewhere between 12 and 15 percent of the overall health care budget for the Veterans Administration, and so we are looking at a very severe problem in terms of the provision of health care services to our veterans.

So what I would like to hear from you are the responses to the questions that Senator Craig and Senator Akaka and Senator Murray have asked, but in particular, looking ahead in terms of how we are not going to allow this problem to happen again.

Let me also say that I think that this may be one of those issues that, frankly, has been decided above your pay grade, with all due respect, Mr. Secretary, because I remember the hearing that we had here in this Committee where we were talking about the budget. I remember learning about the letter from the VA that basically said that the VA had all the money that it needed. And it seemed to me that at the end of the day, that the decision on the allocation

of money over to the VA is coming out of the White House and out of OMB.

So you are relatively new in this job, and you are a person for whom I have a great deal of personal respect. I think these decisions were, frankly, made outside of your control by people who are above your pay grade, and that is OMB and the White House basically deciding to go ahead and to put arbitrary restrictions on the level of funding for health care for veterans in America.

I think that is the wrong way to go and I am very hopeful that when the President addresses the Nation tonight on the status of Iraq, that he also addresses the question of how we are taking care of our veterans when they are return home. When we look at the fact we have approximately 350,000 veterans coming back from Iraq and from Afghanistan, how we treat our veterans when they return back home is a key component of how we are dealing with this war on terror.

And so I would encourage you, and through this statement encourage the President of the United States tonight in addressing the American people how exactly we are going to address this problem by answering the two questions which I hope you are able to answer here today, how did we get into this mess and how we are going to fix it, and second, how are we going to prevent this from happening ever again.

Thank you, Mr. Secretary, and Mr. Chairman, I have a more formal opening statement that I will submit for the record.

Chairman CRAIG. Without objection, it will become part of the record.

[The prepared statement of Senator Salazar follows:]

PREPARED STATEMENT OF HON. KEN SALAZAR, U.S. SENATOR FROM COLORADO

Thank you, Chairman Craig and Senator Akaka, for moving quickly to address this crisis.

I hope today's hearing will be the beginning of an open and honest accounting of how much more money the VA needs for this year and next year, what went wrong, and what we can do to ensure that it never happens again.

Last week, America's veterans were alarmed by the announcement that the VA was short \$1 billion for health care programs.

EXISTING BUDGET PROBLEMS

I've only been in Washington 6 months, but it doesn't take that long to realize that the VA was in trouble before this announcement. I said it, some Members on this Committee said it, and the Veterans groups all said it—the VA did not have the resources to do its job.

In Colorado, we've already seen the effects of extremely tight budgets. Now, there is a virtual hiring freeze for new nurses at the Denver VA Medical Center. This has led to nurse-to-patient ratios as high 1–15. Patients have to wait hours for scheduled medicines to be administered. Patients suffer the indignity of being bathed less frequently and having their bandages changed less often than they should be.

The staff is heroically trying to fill the void, working overtime and having to actually prioritize the worst patients. As one nurse said, "We are getting frustrated, knowing there is no light at the end of the tunnel." In another sign of budget cuts, we've seen staff cuts at community-based outpatient clinics. It has been clear for some time that VA has been running in the red.

CREDIBILITY GAP

That is what I have been hearing from my constituents in Colorado, but you would not know there were any such problems if you listened to White House officials. Time and again we asked, "Can VA do its job with the budget it has?" Time and again the answer has been, "Yes."

This started last year when the Administration submitted a VA budget that was \$1.2 billion below what Secretary Principi asked for. The VSOs said that the VA needed \$3 billion more just to continue minimum service. The Administration disagreed.

In April, I joined Senators Murray and Akaka in an effort to increase the VA's budget by \$1.975 billion. That effort failed in part because VA officials wrote Members of Congress that they could finish the year with the funds it had. Turns out that, like the VA's numbers, their story did not add up.

The VA is blaming this new crisis on "unanticipated" growth. There is a lot more to this story than what the VA is admitting. Behind talk of actuarial models and complicated estimates is a history of chronic underfunding matched with unrealistic sunny forecasts. In announcing a billion-dollar shortfall, the VA is finally showing that it cannot hold the Administration's line. Quite simply, this Administration has shown it lacks credibility on the VA's budget.

When it comes to the VA, the Administration lets its own politics trump the needs of our veterans. The American Legion says it best when they say that VA spending is budget-driven, not demand-driven. Every year, the VA is given an arbitrary and meager budget to do a job that grows larger and larger. VA doctors and nurses are left alone to handle more patients with fewer resources. And Members of Congress are told tall tales of how great things are going.

MANDATORY FUNDING

During today's hearing, I hope we get some honest answers about what the VA needs to get through this year and next. We need to get honest answers about what went wrong with the VA's forecast, and why they did not tell Congress sooner. Most importantly, we must work together to develop a budgetary process that better serves our Nation's veterans.

In the short run, we need to pass a supplemental appropriation immediately. In the long run, we need to move toward mandatory funding of veterans' health care.

Our Nation's veterans should not have to hold their breath every year to find out whether or not Washington is going to do its job and fund the VA. Their well being should not be at risk because actuarial forecasts are wrong or budget directors are trying to force bad numbers to add up.

At the end of the day, we have a duty to honor the men and women who have sacrificed so much for our freedom. We can not let them down.

Thank you, Chairman Craig, Senator Akaka. I look forward to the hearing.

Chairman CRAIG. Senator Ensign.

STATEMENT OF HON. JOHN ENSIGN, U.S. SENATOR FROM NEVEDA

Senator ENSIGN. Thank you, Mr. Chairman, and thank you for holding this hearing on such short notice. I think it is very appropriate after what we have just gone through on our budget, and especially at a time of war, that we are keeping our promises to the veterans in the budget process.

We, obviously working with the Chairman and others, added \$410 million, I think it was, to the budget, thinking that that would take care of the needs. That is what the Administration had told us. Obviously, that was not adequate.

In Southern Nevada, and not to get parochial about this because I think it is critical that we take care of veterans all over our country, but we are in a situation in Southern Nevada where we are anticipating a new VA hospital. Secretary Principi was, out along with Secretary Norton, to dedicate the site. We got the land from the BLM dedicated in legislation last year for the new VA hospital. We are the largest metro area, population-wise, in the country without a VA hospital. Our veterans travel great distances to get proper care, and that is a situation obviously that Secretary Principi believed was very important to rectify.

What I would like to hear from you today is that, one, that that project will be going forward on time, on budget, and two, reassure

the veterans in Southern Nevada that this budget shortfall will not, in fact, hurt the building of the new hospital in Southern Nevada.

And then, last, I would like to hear about what kind of goals you have for squeezing out some of the inefficiencies in the Department to be able to put those monies, instead of supporting a wasteful bureaucracy, actually into health care and related services for our veterans.

Thank you, Mr. Chairman.

Chairman CRAIG. Thank you, Senator.

Senator Burr.

**STATEMENT OF HON. RICHARD BURR, U.S. SENATOR FROM
NORTH CAROLINA**

Senator BURR. Thank you, Mr. Chairman. Mr. Chairman, I may not be as kind.

Mr. Secretary, I just read your testimony and I just honed in on one paragraph. "I think the record shows the VA has been very forthcoming with information regarding both the status of the budget and responsible management decisions we have made as 2005 unfolds."

The first half of that, I would just totally disagree with. I don't question the integrity of anybody, but I don't think that the VA has been forthcoming in information. There is no way a \$1.2 billion shortfall could not have been at least—at least there should have been some indications that there was trouble, and if there weren't, then I feel very confident that you will go back and look at the system and find out how, in fact, there couldn't have been warning signs.

I have gone back and read testimony from all Members in this Committee, their questions. I don't think we missed asking the right questions. I think, in fact, we were very specific in what we asked. As I heard my colleague from Nevada ask about a hospital in Southern Nevada, I covered very thoroughly the six clinics in North Carolina, that there was no expression of concern that there would be funding for. Yet as I read here, your proposal to handle the \$1 billion, you would defer \$600 million worth of non-critical capital expenses for several months. I have to question, is that my clinics? Is that John's hospital? Where is that in the capital expenditures? I would suggest to you that the answers can't be "yes" to all of it.

I look at this, Mr. Chairman, as one more try. I am more than willing to do that with an increased commitment to you and to this Committee to make sure that we are dogged in our oversight. But I also look at the Secretary and say, this is one opportunity to redo the numbers. Make sure that they are right this time. If, in fact, you have to err, err on the side of the veterans. Err on the side of making sure that the infrastructure has the capital that it needs to meet the needs of those who need it.

I am sure that in John Ensign's case, there is a reason that there is a hospital targeted for Southern Nevada. In North Carolina's case, there is a reason there are six clinics targeted in North Carolina. We are the fastest-growing population of military retirees in

the country. If, in fact, that does not happen on time, you will not meet the health care needs of the veterans in North Carolina.

So the infrastructure is an absolutely essential piece to our ability to say, yes, we are meeting those needs. And if, in fact, that can't be met by delaying 3 months or 6 months or whatever, then we need a number that gets us there on a time line that enables you and us to answer the question, "Are we taking care of our veterans?" And that should be an affirmative answer.

Thank you, Mr. Chairman.

Chairman CRAIG. Senator, thank you.

We have been joined by the Chairman of the Appropriations Subcommittee on Military Construction and Veterans, Senator Hutchison, and it will be through her and her staff and our staff working jointly together in this Committee that we will accomplish the needs necessary here and make sure that all that is done is adequate. So I am extremely pleased that Kay has joined us today. Senator Hutchison?

**STATEMENT OF HON. KAY BAILEY HUTCHINSON, U.S.
SENATOR FROM TEXAS**

Senator HUTCHISON. Yes. Thank you very much, Mr. Chairman. I am pleased that you had this hearing scheduled and were able to do it on a very timely basis because our Subcommittee was going to markup this week for our ability to get on the floor in July. That will not occur. We are going to delay the markup because we very much want to work on a bipartisan basis with the Veterans Administration to do the right thing and do it at the right time.

Rather than waiting until we have a crisis, we would like to have the input from the Veterans' Affairs Department and add to the budget. We assume that the President's OMB is going to add to the Veterans' Affairs budget for 2006. I think we need to also address 2005.

I think from the testimony that you have already made on the House side that many of us are tentative about taking from capital accounts in 2005 to try to cover the needs. I would rather address this, and I would like to have the input from the Administration to address it fully now while we are still in the 2006 budget cycle and can also dip back.

We still have budget authority from 2005 left that we could use if we can get the input from the Administration on what it would really cost to fully fund your capital needs, as well as not deplete your rainy-day fund or your surplus ongoing fund. We want to keep the VA in a good financial situation.

Mr. Secretary, you have not been on the job very long. You have been there for a few months, and I think we have to—while we are all very disappointed and we are all certainly looking to you for guidance—we do have to acknowledge that you stepped up to the plate and took it like a guy. I mean, you did step up and say, I am not going to let this go on. We have just had our mid-year numbers and our projections which we have relied on for all these years, and they have been accurate, are not accurate. You did that and we appreciate it. Now, let us finish the job.

You are a decorated veteran. You care about these people. So let us work together to do what is right for 2005, as well as 2006. Thank you. Thank you, Mr. Chairman.

Chairman CRAIG. Senator, thank you very much. We have been joined by Senator Obama. Senator.

**STATEMENT OF HON. BARACK OBAMA, U.S. SENATOR
FROM ILLINOIS**

Senator OBAMA. Thank you very much, Mr. Chairman. I confess, this is a frustrating hearing for me, and I know that may be true for the Chairman and Ranking Member, as well.

I think a basic precept of this Committee, one that is shared by the American people, is that when we send our troops to war, we make a decision to care for them and support them when they return. I can't imagine that there is anybody in this room who wants to look a soldier in the eye who has returned and risked life and limb for this country and say, "Sorry, when it comes to health care, you are on your own." But somehow, it seems that we are willing to trot in front of flags and take photographs with soldiers, but when it comes to the appropriations process, we are not there.

Back in April, I joined with Ranking Member Akaka and Senator Murray in offering an amendment to the emergency war supplemental appropriations bill that would have added \$1.9 billion in funding. This amendment failed, I think in large part, at least that was the argument that was made on the floor, because the VA said that the money was not necessary. Now, Mr. Secretary, you assured Senator Hutchison, chairman of the Appropriations Subcommittee, that the additional funds were not needed. There was no dire emergency.

Now we discover, somewhat by happenstance, that we are potentially a billion dollars short. I mean, even in Washington, a billion dollars, that is real money. So as I understand it, at least, because of the shortfall, the VA has now been forced to turn to its emergency accounts, capital improvement funds, to try to make ends meet.

Think about that. We recently passed a budget where we had no problem finding billions and billions of dollars to give away in tax cuts, but when it comes to the priorities of providing health care to veterans, we have got to dip into a rainy day fund, and it is not even clear how solid that rainy day fund is.

So clearly, the Department, the Office of Management and Budget, and the Administration have to be more forthcoming and transparent in the budgetary calculations and they have got to be more realistic about their cost predictions. It really benefits no one, I think, to fudge the numbers on this.

We have a bipartisan consensus that veterans should be cared for. I have no doubt, Secretary Nicholson, that you and your staff want to care for veterans properly. But if we are starting to play budgetary games, then it is hard for us to make the difficult choices that are involved.

I think this current budgetary shortfall is an emergency. That is why, once again, I am going to be joining my colleagues in an effort to provide VA with the funding it needs to fully meet the health needs of our veterans.

Senator Murray's emergency supplemental funding bill, is necessary to avoid what is an oncoming crisis in the VA health system. Giving our veterans substandard treatment isn't acceptable. Our veterans deserve better.

Let me just say that I appreciate, Mr. Chairman, your calling this hearing. I thank the witnesses for joining us. I hope we improve the budgetary planning process as a whole, and I hope that this Administration recognizes that this is not an area where we should be playing politics. The Democrats are happy to work with the administration and Republicans to make sure that our veterans are cared for, but we can't do that if we are not getting the proper information, and I think that is what the American people deserve. That is what the Members of this Committee deserve. I think, most importantly, that is what the veterans deserve.

Thank you, Mr. Chairman.

Chairman CRAIG. Senator, thank you.

I only caution that we need to get the Secretary into the substance as quickly as we can, but, of course, let me recognize Senator Rockefeller for any opening statement he would like to make.

**STATEMENT OF HON. JOHN ROCKEFELLER IV, U.S. SENATOR
FROM WEST VIRGINIA**

Senator ROCKEFELLER. Thank you, Mr. Chairman, and thank you, as I always do, for your constant fairness, evenhandedness, and pursuit of the facts in all of this, as obviously the Ranking Member, Danny Akaka.

Secretary Nicholson, we have talked and I have pointed out from time to time in these meetings that in some ways, you are not your own person on this. OMB decides, and after them, the White House decides. You have got to take whatever that is, and I fully understand that, as I do you. I really do.

But this can't be left to stand. You know, the President is going to go down to North Carolina this afternoon. He is going to give a speech in front of a lot of soldiers, people on their way over to Iraq and some to Afghanistan. It would be an awfully nice time for him to correct this, because those folks are going to be hurting, and I will say something about that in a moment.

But I hope that if he does correct it, he doesn't correct it at the expense of what I am sure that Senator Murray, who has just been a champion throughout this whole thing, of the construction money that is needed for this year. Because construction money isn't sort of like putting up air traffic control towers around VA hospitals, I mean, it is basic. As you know, it is the basic way that you carry on health care and the capacity for health care in an ever-enlarged group of people.

I spent 3 hours with WV veterans and—I do this as many times as I can when I go home. I was with 12 young men and women who had just come back from, in one case Afghanistan, everybody else, Iraq. With the exception of two—in my judgment, with the exception of two—all of them either admitted to forcefully having real trauma, psychological trauma, PTSD. They are just back and they need to be taken care of. Some of them were regular, some were in the National Guard or Reservists. It doesn't make any difference to me. They were over there. They fought for us. They come back.

One of them was sitting actually next to a woman staff member of mine, said that he can't—his first reaction to everything is violent and he can't help it and he can't understand it. And once you get them talking, they feed off each other and it is a story that gets sadder and sadder.

Well, we now know that goes all the way back to World War I, PTSD, but that is not for today. For today is correcting a shortfall in a way which really does bring health care to veterans that need it. It is not about the sophisticated accounting between 2005 and 2006. But it is about what is needed for 2005, as well as 2006, and a correction that does it now.

It is incomprehensible to me, and frankly, sort of morally amazing to me, even hurtful, that we do shortchange funding. We go to war and then these people come back with more tension on them than ever. They don't want to talk about anything. No veteran ever does. They never want to talk about what they were in. They will talk about their symptoms, but they won't talk about what they did to get those symptoms. And then, all of a sudden, we are cutting the budget for their care.

I mean, I agree with Senator Obama. It is a matter of choice. There is this fascinating process of making moral choices in America, about whether you want to do tax cuts or whether you want to take care of people.

The people I represent don't get much in the way of tax cuts. Maybe about three or four of the population gets a little bit. The rest of it, no. But we have a huge proportion of people that go into the regular military, Reserves and Guard. I am going down to North Carolina this afternoon to try and protect what is being taken out of West Virginia. The Air National Guard has been ranked No. 1 for 8 consecutive years in the country, but it is not deemed necessary. That is different.

I just hope that the President will say something. I hope that you can cause him to say something. It is in his interest to say something that gives closure to what is a gaping wound in the hearts of all of us, both sides of the aisle, around this problem. Again, I admire Chairman Craig because he knows there is a problem. It is a little tricky for him, but you know he wants the right thing done, and we all do.

I don't know how we do this. We read about people, sophisticated IEDs being set off. They pay some little boy \$4 or \$5 and he goes and punches a cell phone button and new armor-piercing IEDs go off, people get killed. Maybe they are Iraqis, maybe they are Americans. It is still a horrible situation. But when these folks come home, ours, we have to take care of them.

Thank you, sir. Thank you, Mr. Chairman.

Chairman CRAIG. Thank you.

Senator Thune.

**STATEMENT OF HON. JOHN THUNE, U.S. SENATOR FROM
SOUTH DAKOTA**

Senator THUNE. Thank you, Mr. Chairman. I also want to thank you and Senator Akaka for acting quickly to address this very important matter, and Secretary Nicholson, Dr. Perlin, Mr. McClain, it is good to have you before us today.

This announcement obviously is about the billion dollar budget shortfall. It is very untimely and very unfortunate and I don't think that we are here today to belabor the obvious. We are here today to understand, one, how that shortfall happened, and two, what we can do to fix it. I look forward to working with this Committee and with the VA to make that happen.

I attended the VFW convention the weekend before last and the American Legion convention this last weekend. Obviously, this is a matter of enormous concern to the service organizations around the country. I also had an opportunity to visit with the administrator at the VA hospital in my State of South Dakota, from Sioux Falls. I think that it is clear that we need to identify what is not working here in terms of the procedures that are used to come up with assessments about what the needs are going to be. And I think as we do have more folks coming home from Iraq and Afghanistan, it is going to put a lot more pressure, and we all know that.

But somehow, further being able to, in a more definitive way, quantify what our needs are going to be is—I am very interested, I guess, in hearing your thoughts about that, because clearly the policy or the procedures we have to do that right now are not working and we don't want to see this happen again. This affects not only—this is a 2005 budget issue, but it is also, clearly, this is a 2006 budget issue and the ripple throughout subsequent years, and so it is important that we get this fixed and that we get it right. I hope that you can shed some light on how we go about doing that today. This is a situation that is unacceptable and we need to make sure that we get it fixed.

I thank you, Mr. Chairman, for calling the hearing and look forward to, Mr. Secretary, what you have to say in that regard.

Chairman CRAIG. Let me thank my colleagues for all of their comments.

Mr. Secretary, we will now turn to you. You are the panel. The Honorable James Nicholson, Secretary of Veterans' Affairs. He is accompanied by Jonathon Perlin, Under Secretary for Health, and the Honorable Tim McClain, General Counsel and Chief Management Officer of the VA.

Mr. Secretary, the floor is yours. Please proceed.

STATEMENT OF HON. R. JAMES NICHOLSON, SECRETARY, U.S. DEPARTMENT OF VETERANS' AFFAIRS, ACCOMPANIED BY JONATHAN PERLIN, UNDER SECRETARY FOR HEALTH, U.S. DEPARTMENT OF VETERANS' AFFAIRS; AND TIM S. McCLAIN, GENERAL COUNSEL AND CHIEF MANAGEMENT OFFICER, U.S. DEPARTMENT OF VETERANS' AFFAIRS

Secretary NICHOLSON. Mr. Chairman, Members of the Committee, thank you for the opportunity to come here and discuss budget forecasting and the finances of the Veterans Health Administration.

Mr. Chairman, in the past, VHA budgets were based on historical expenditures, adjusted for inflation, and then increased based on proposed new initiatives. Today, eligibility reform, increases in ambulatory care, shifting veteran population trends, rising demand for services, and escalating costs of health care call for complex,

complicated actuarial modeling to dynamically adjust our projections. Actuarial modeling is a well-tested private sector tool that the VHA applies to our 21st century health care system.

Over the past 6 years, we have successfully integrated the VHA enrollee health care demand model projections into our health care financial and management processes. In March 2005, the demand trend line moved upward. My letter of April 5 to the Chairman of the Senate Subcommittee on Military Construction and Veterans' Affairs, Senator Hutchison, said whenever trends indicate the need for reinforcing priorities, VA's leaders ensure prudent use of reserve funding for these purposes. That is simply part of good management.

At his Senate confirmation hearing on April 7, then-Acting Under Secretary Dr. Perlin testified that reserve funds were being used to meet operational needs in 2005. That was on April 7.

On April 12, Dr. Perlin wrote that the projected carryover might be diminished to address operational demands on our system and noted that we do feel confident that DHA has sufficient resources for the remainder of 2005.

On April 19, VA staff met with the Ranking Member and Members of the minority and majority staff of the House Appropriations Subcommittee to discuss the Veterans Equitable Resource Allocation, or often termed VERA, model. During this meeting, there were protracted discussions of the health system's financial status for 2005, including the reallocation of capital funds for direct patient care.

During that same week, I met with the Director of the OMB to update him on the current status and to alert him to potential issues for fiscal year 2006.

The model on which the 2005 budget was formulated relied on data from 2002, before the beginning of Operation Iraqi Freedom, and much has happened in those 3 years. In May of this year, we performed an actuarial model update for fiscal year 2006 with more current and accurate data from 2004, further indicating the significant increase in patient demand for fiscal year 2006.

In the first week of June, VA staff met with VA and DOD branch staff of OMB for a mid-year management review and to discuss the implications of fiscal year 2005 management decisions on the 2006 budget. Similarly, VA staff met on June 3 with majority staff members of the House and Senate Veterans' Affairs Committees to discuss the implications of the reallocation and use of funds projected for carryover into the base for fiscal year 2006 budget.

On June 23, the Under Secretary for Health offered testimony on the actuarial model and its limitations and the 2005 workload growth rate of 5.2 percent, compared with the 2005 forecast, which was a growth rate of 2.3 percent.

We have been very forthcoming, we believe, with information regarding both the status of our budget and the responsible management decisions we have made as 2005 unfolds. For 2006, we are working with OMB to reach a satisfactory resolution to assure for all eligible veterans that VA services will continue unabated.

The additional resources relative to the President's budget that are necessary to provide timely, high-quality care to the veterans in 2006 amount to approximately \$1.5 billion. The Administration

will soon present the Congress with a proposal to address this additional workload.

Mr. Chairman, in closing, the VHA enrollee health care demand model is a valuable budgeting and planning tool for projecting VA health care utilization. However, projecting health care trends and utilization for a huge health care system such as VA is inherently complex. It is significantly more challenging in the context of the Federal budgeting time line, which requires projections not for the next year or even for the next open season, as in private sector, but 2.5 to 3.5 years ahead.

We appreciate this opportunity for continuing dialog about management decisions to assure resources for direct patient care in 2005 and to provide recommendations for an augmented budget in 2006, all to fulfill our mission of providing world class health care to our Nation's veterans.

Thank you, Mr. Chairman.

Chairman CRAIG. Secretary, thank you.

[The prepared statement of Secretary Nicholson follows:]

PREPARED STATEMENT OF HON. R. JAMES NICHOLSON, SECRETARY, U.S. DEPARTMENT OF VETERANS' AFFAIRS

Mr. Chairman and Members of the Committee: Thank you for the opportunity to discuss the budget forecasting and finances of the Veterans Health Administration. Accompanying me this morning is our General Counsel and Chief Management Officer, Mr. Tim McClain and our Under Secretary for Health, Dr. Jon Perlin.

Background Mr. Chairman, in considering our budget planning and execution, I'd like to address three topics. First, how does VA rationally project resource requirements for the health care needs of Veterans? Second, why is there discrepancy from projections and what is the current status of resources? And, finally, what can we do to improve the budget formulation process and the current budget status?

PROJECTING RESOURCE REQUIREMENTS

The Veteran's Health Care Eligibility Reform Act of 1996 established a uniform package of health care services for enrollees. The legislation also established a priority-based enrollment system and required the VA Secretary to annually assess veteran demand for VA health care to determine which priority levels of veterans will be eligible to enroll for care based on the resources available to provide timely, quality care to all enrollees.

Eligibility reform contributed to the transformation of the Veterans Health Administration (VHA) from a health care system that provided episodic, inpatient care to a health care system that provides a full range of comprehensive health care services to enrollees. The focus on health promotion, disease prevention and chronic disease management has resulted in more effective and more efficient health care. As a result, the range of health care services utilized by VHA patients began to mirror that of other large health care plans. Therefore, VHA decided to follow private sector practice and use a health care actuary to predict future demand for VA health care services. Mr. Chairman, transforming from a hospital system to a health care system has facilitated VA's ability to take a leadership position in health care quality in the United States. A recent Washington Monthly article stated the Veterans Health Administration gives the "best care anywhere." Additionally, the results of a recent study conducted by the independent RAND Corporation revealed that based on 348 measures of performance, VA provides systematically better care in disease prevention and treatment.

In the past, VHA budgets (and most Federal budgets) were based on historical expenditures that were adjusted for inflation and then increased based on proposed new initiatives. However, rather than an arbitrary increase over prior budgets, with the implementation of eligibility reform and the shift to ambulatory care, VHA needed to more rationally budget for veteran requirements in a transformed health care system. It also needed to be able to continually adjust its budgetary projections for effects of shifting trends in the veteran population, increasing demand for services, and the escalating cost of health care, e.g., pharmaceuticals.

As a result, VA engaged Milliman, Inc., to produce actuarial projections of veteran enrollment, health care service utilization, and expenditures. Milliman consults to health insurers and as such, is the largest and most respected actuarial firm in the country in the area of providing actuarial health care modeling.

VHA Enrollee Health Care Demand Model The VHA Enrollee Health Care Demand Model (model) develops estimates of future veteran enrollment, enrollees' expected utilization for 55 health care services, and the costs associated with that utilization. These projections are available by fiscal year, enrollment priority, age, VISN, market, and facility and are provided for a 20-year period.

The model provides risk-adjustment and reflects enrollees' morbidity, mortality, and their changing health care needs as they age. Because many enrollees have other health care options, the model reflects how much care enrollees receive from the VA health care system versus other health care providers. This is known as VA reliance. Enrollee reliance on VA is assessed using VA and Medicare data and a survey of VA enrollees. The VA/Medicare data match provides VA with enrollees' actual use of VA and Medicare services, and the survey provides detailed responses from enrollees regarding any private health insurance and their use of VA and non-VA health care.

The model projects future utilization of numerous health care services based on private sector utilization benchmarks that are adjusted for the unique demographic and health characteristics of the veteran population and the VA health care system. The actuarial data on which the benchmarks are based represent the health care utilization of millions of Americans and include data from both commercial plans and Medicare, and are used extensively by other health plans to project future service utilization and cost.

The model produces projections for future years using health care utilization, cost, and intensity trends. These trends reflect the historical experience and expected changes in the entire health care industry and are adjusted to reflect the unique nature of the VA health care system. These trends account for changes in unit costs of supplies and services, wages, medical care practice patterns, regulatory changes, and medical technology.

Each year, the model is updated with the latest data on enrollment, health care service utilization, and service costs. The methodology and assumptions used in the model are also reviewed to ensure that the model is projecting veteran demand as accurately as possible. VHA and Milliman develop annual plans to improve the data inputs to the model and the modeling methodology. Notably, Mr. Chairman, perhaps going to a focus of the Committee today, on average for the past 3 years, patient projections have been within -0.6 percent of actual patients and enrollee projections have been within +1.9 percent of actual enrollees.

As required by eligibility reform legislation, VA annually reviews the actuarial projections and determines whether or not resources are available to meet the expected demand for VA health care and develops policies accordingly. For example, the model's projection of continued significant growth in enrollment in Priority 8 formed the basis of VA's decision to suspend Priority 8 enrollment in January of 2003, to ensure that resources were available to provide timely, quality health care to enrolled veterans.

Over the past 6 years, VHA has integrated the model projections into our financial and management processes. The VA health care budget is now formulated based on the model projections, as are the impact of most policies proposed in the budget.

Some services VA provides are not modeled by Milliman. These include readjustment counseling, dental services, the foreign medical program, CHAMPVA, spina bifida, and non-veteran medical care. Demand estimates and budgets for these programs are developed by their respective program managers.

Enrollee demand for long-term care services is modeled by VHA. The VHA long-term care model uses utilization rates from nationally recognized surveys adjusted for the unique characteristics of the enrollee population and known reliance factors to account for distance (access to VA facilities), multiple eligibilities, and case management to project demand for both nursing home care and community-based care.

DISCREPANCY FROM PROJECTIONS AND STATUS OF HEALTH CARE RESOURCES

Actuarial modeling is the most rational way to project the resource needs of a health care system like the Veterans Health Administration. As noted, this is the approach utilized private sector. Unlike private sector, however, where projections are used to formulate budgets for the next year or even the next "open season," the Federal budget cycle requires budget formulation using data 2½ to 3½ years ahead of budget execution.

For example, the data used to formulate the budget for 2005 derive from health care utilization in 2002, in this case, the last full year of data before the Department's 2005 budget formulation began. While it is remarkable that the budget has been as accurate as it has, a lot can change in 3 years.

The actuarial projection model forecast numbers of enrollees. The number of patients from the enrollee pool is a derivative calculation based on what has been, to date, a fairly constant relationship. One factor that has compounded the projections is the increased utilization of health care services by enrolled Veterans in all priority levels and from all combat eras.

The actuarial model forecasted 2.3 percent annual growth in healthcare demand in FY 2005. We discovered that growth has accelerated through April, 2005 to 5.2 percent above FY 2004, which is almost 3 percent above our annual projection. This constitutes a substantial increase in workload and resource requirements.

In 2002, we were not yet a Nation with large numbers of service members deployed to combat zones. Appropriately, VA continued to use separation data from the Department of Defense to project potential rates of utilization separating service members. Our FY2005 budget assumed that 23,553 VA patients (at a cost of \$81 million) would be veterans of the Global War on Terrorism. The number of these patients in 2005 is now estimated to be 103,000, so we are \$273 million short. This additional cost is a substantial but not a predominant (or even the majority) component of the increased medical care cost in 2005.

Fortunately, many are seeking routine services. Some require dental care that was deferred as they deployed for combat. Others require more intensive care for both the physical and psychological consequences of combat. About 60 percent of the combat veterans who have come to VA are reservists or members of the National Guard. Veterans deployed to combat zones are entitled to 2 years of eligibility for VA health care services following their separation from active duty even if they are not immediately otherwise eligible to enroll at VA. Because of this, these combat veterans then come to VA in numbers much higher than if they were to separate from DoD without a combat history. The general DoD separation trends data available from the routine 2001 separation planning report could not anticipate the numbers of reserve service members who were subsequently activated and then separated from service.

In summary, the increased medical care cost in 2005 is nearly \$1.0 billion of which \$273 million (28 percent) is associated with veterans returning from the current combat theatres.

Questions have been raised about the timing of the information disclosed about VA's 2005 budget situation. I want to be clear that we continue to feel that we can meet the needs of timely, high-quality health care for veterans. In fact, I indicated this in my letter of April 5 to Chairman Hutchison of the Senate Subcommittee on Military Construction and Veterans Affairs, in which I stated that, "whenever trends indicate the need for refocusing priorities, VA's leaders ensure prudent use of reserve funding for these purposes. That is just simply part of good management."

In a similar fashion, at his confirmation hearing on April 7, 2005, then Acting Under Secretary for Health Perlin, testified to the Senate Veterans Affairs Committee that reserve funds were being used to meet operational needs in 2005. This generated some subsequent questions from the Committee, and in a letter on April 12, Dr. Perlin wrote that the projected carryover might be diminished to address operational demands on our system, including the care of returning combat veterans of Operation Iraqi Freedom and Operation Enduring Freedom, noting that "we do feel confident that VHA has sufficient resources for the remainder of 2005."

The following week, on April 19, VA staff met with Ranking Member and Members of the minority and majority staff of the House Appropriations Subcommittee to discuss the Veterans Equitable Resource Allocation (VERA) model. During this meeting there was protracted discussion of the health system's financial status in 2005, including the management decision to reallocate capital funds for direct patient care. During that same week, I met with the OMB Director to update him on the current status and to alert him to potential issues for Fiscal Year 2006 suggested by preliminary and incomplete data. We agreed to monitor the situation as more complete and actual data emerged.

In May, we performed our periodic actuarial model update for FY 2006 with more current and accurate data. This further validated the emerging phenomenon of increasing workload. This was discussed internally as part of the Department's mid-year financial review. In the first week of June, VA staff met with OMB staff for its annual mid-year management review where we discussed in general terms the implications of FY 2005 management decisions on the FY06 budget. Similarly, VA staff met on June 3 with majority staff members of the House and Senate Veterans Affairs Committee, where they had very candid dialog about the implications of the

reallocation and use of funds projected for carryover into the base for the FY 2006 budget.

On June 23, the Under Secretary for Health offered testimony on the actuarial model and its limitations. Actuarial modeling for 2005 forecast a growth rate of 2.3 percent, and as of April 2005, VA was experiencing workload growth at the rate of 5.2 percent annually, explaining the need to reallocate funds and devote carryover funds for patient care. As discussed in the hearing, VA's 2005 increased medical care cost is nearly \$1.0 billion, which VA will manage by reducing the 2006 carry-over balance by \$375 million and deferring \$600 million of non-critical capital expenses for a few months.

I think that the record shows that VA has been very forthcoming with information regarding both the status of our budget and the responsible management decisions we have made as 2005 unfolds. It is our first responsibility to provide the highest quality care to veterans. It is our next responsibility to be good stewards of the substantial resources entrusted to us for that care. While resources have been adequate to make reallocation decisions to meet the most essential needs in 2005, it is now clear that the budget picture for 2006 needs to be revisited. We are working with OMB to reach a satisfactory resolution for 2006 that assures VA is there for all eligible veterans.

After looking at what additional efficiencies may be possible in what is arguably the nation's most efficient health system, I believe that the additional resources relative to the President's Budget that are necessary to provide timely, high quality care to the Veterans in 2006 amount to approximately \$1.5 billion. This includes \$375 million to repay the carryover, nearly \$700 million for increased workload, and \$446 million for an error in estimating long-term care costs. The Administration will come forward to the Congress shortly with a proposal to provide VA the additional resources. This amount assumes enactment of the policies in the President's Budget. If Congress does not accept any of the policies in the President's Budget, additional resources will be needed.

PLANNED IMPROVEMENTS

In a sense, VA and other Federal agencies like DoD who use actuarial modeling to project resource requirements 2½ to 3 years hence push the performance envelope compared to private sector, which uses these data at 1 year. In fact, the 2.9 percent margin of error we experienced is far better than the 11 percent error that occurred when budgets were projected by inflating an historical base. Mathematically, at 3 years, a 2.9 percent margin of error is pretty good. Still, we recognize that the consequences are not.

In order to improve the model and budget process going forward, additional model inputs are required. We must figure out how to better approximate changes needed to compensate for the lag in data in our estimates. In addition, we need to do a better job of linking DoD experience with our input.

The development of the actuarial model has been an evolutionary process. It is a prerequisite for the data necessary for the Secretary's annual enrollment decision which matches enrollment levels to resource availability. Enhancements to the model include more detailed and robust adjustments for enrollee reliance, morbidity, and mortality, adding new data sources, and expanding the number of services modeled. Future planned improvements include access to data on enrollee's use of Medicaid, Tricare, and military treatment facilities, the integration of the VHA long-term-care model into the actuarial model, and modeling additional services such as dental care.

CONCLUSION

Mr. Chairman, in closing, I believe that the VHA Enrollee Health Care Demand Model is a valuable budgeting and planning tool for projecting VA health care utilization. We look forward to working with you to ensure that we continue to provide timely and high-quality health care to our Nation's Veterans.

Chairman CRAIG. Let me start the questions. We will go to 5 minute rounds and move through our colleagues as often as we need to to complete this, with the clear intent of being able to understand exactly where you are now and what we must do with you to correct this problem, Mr. Secretary.

I am confused as to know how this problem—how a problem of this magnitude can catch everyone, even a cabinet Secretary, off guard. Now, I can understand all of the dynamics that you just

spoke to. As I understand it, VA discovered the need to cover the present-year shortfall during a mid-year review. Yet, Dr. Perlin wrote to me in April during debate on the supplemental that operating requirements are addressed on a daily basis throughout VA.

When exactly did this mid-year review occur? That is my first question. Wouldn't data captured in this review be collected as a routine matter by senior VA managers? And if so, wouldn't that suggest that VA should have known about this resource shortfall well before it occurred?

Secretary NICHOLSON. Well, Mr. Chairman, review of the spending is an ongoing process, and I had meetings with the chairman and other members of the VISN finance committee, the VISN being our network directors who have a committee of themselves, sat down with them months ago and discussed the fact that there may not be enough in the budget allocations for the rest of this fiscal year. So this has been an evolving process. It has not been a bolt of lightning or a bolt of blue to me or our Department.

But, and this is probably where we disagree, in a sense, with most of you here, in that we looked at this and made a decision that it was going to take about a billion dollars more to get through the end of this fiscal year—that is about 3 percent of our overall budget—and for management to make some legally permissible transfers to cover themselves to the end of the year seemed to me to be prudent judgment and not an extraordinary thing to do. I have that authority as the Secretary. I am tasked to inform the Congress. I did that with letters to both bodies, and that is the way we have proceeded.

So in the semantical realm, to those who say this is a crisis, I do not agree. The defining job that we have at the VA is to take care of our veterans and provide them with the world-class health care service that they expect, that they are getting, and that they deserve. So that is our mantra and we made a decision to use the reserve that we had for that plus to use part of the money that was allocated for maintenance and some capital acquisitions.

Chairman CRAIG. I understand reserve, the value of using that. We will talk about that as we jump into 2006 and the move through of that money. The capital issue, obviously, some have discussed that in their opening statements and I will let others pursue that.

Dr. Perlin testified before the Committee in March of this year that as of December 2004, 244,054 OIF and OEF veterans had separated from active duty. Approximately 20 percent of these veterans, 48,733, have sought health care from VA.

According to your testimony this morning, Mr. Secretary, the 2005 budget assumed only 23,553 veterans from the global war on terrorism would use VA health care. It would seem, then, that you knew very early on that your demand projections for returning OIF and OEF veterans would be wrong. Why wasn't that alarm sounded sooner?

Secretary NICHOLSON. Well, we did not get the hard data, the confirming data for our model until after the first 6 months of the fiscal year, and we have been tracking it on actual usage and we were on plan. Then it began to spike since then, the 7th and 8th and now in the 9th month. So we have gone back and looked at

what that is versus what it was projected and it is a 126 percent increase over what was projected.

The Operation Enduring Freedom and Iraqi Freedom portion of that looks like 103,000 veterans. Many of those are returnees who have been part of the Reserve component force who are eligible now for VA services, and they are coming in in numbers far in advance of anticipation. In fact, because of the budget cycle, the data used to project 2005 is 2002 and there was no Operation Iraq Freedom.

But as we tracked this, we realized, and have, we think, been transparent about the fact that there was going to be a need for transfer of a billion dollars.

Chairman CRAIG. Let me clarify and then turn to my colleague. Of the number you just gave us, the 103,000, you are saying 103,000 servicemen and women who are eligible for or who are in the system now?

Secretary NICHOLSON. That number that I referred to there was just those eligible who are returnees from Operation Iraqi Freedom and Enduring Freedom.

Chairman CRAIG. Eligible for services, but have not applied for?

Secretary NICHOLSON. No, those who have come in. They are all eligible.

Chairman CRAIG. Come into the VA system?

Secretary NICHOLSON. Yes, sir.

Chairman CRAIG. OK.

Secretary NICHOLSON. They are all eligible under the law—

Chairman CRAIG. Yes.

Secretary NICHOLSON [continuing]. For a 2-year period. And then, of course, if they have any service-connected—

Chairman CRAIG. Sure.

Secretary NICHOLSON [continuing]. Or actually, if they come in and enroll, they are eligible, really, indefinitely. But I think I should add for clarity that that is a large number, but that is not the majority of our growth.

Chairman CRAIG. No, but you are saying that is new growth that was not anticipated in the model?

Secretary NICHOLSON. Yes, sir.

Chairman CRAIG. OK. Thank you.

Senator Akaka?

Senator AKAKA. Thank you very much, Mr. Chairman.

Mr. Secretary, before Senator Murray and I offered our amendment to the supplemental, I want you to know that it was based on our reaching out to providers in the field. They plainly told us at that time about shortfalls and the raiding of capital accounts. Some truly desperate providers shared spreadsheets with us, detailing the shortfall and what mechanisms they were using to stay afloat.

At that time, the Senate was debating the supplemental bill, and as you know, Senator Murray and I did offer amendments on increasing the funding for Veterans' Affairs. In my case, I had recommended a \$2.9 billion increase based on the information that we had from the field. In your testimony this morning, you indicated that you were aware that VA was facing financial problems back in April.

Mr. Secretary, my question to you, was it possible that VA managers here in D.C. were aware of that crisis?

Secretary NICHOLSON. Senator, it is the fact, I think, that VA managers were aware of—or became aware after we got the first 6 months' look and then we started seeing it spike, that because of that, there was not sufficient funds in the health delivery budget to care for that increased demand on our health services. That is where we made the management decision. It was about a 3 percent transfer, which was to take the reserve funds and some of the maintenance funds to get us through the end of the year.

I would also point out to you, because I think you mentioned it, as did, I know, Senator Burr, that the money in this maintenance account is not money for capital construction. It wouldn't affect that, does not affect that.

Senator AKAKA. Mr. Secretary, I am curious, curious as to how exactly the supplemental funds are being distributed to the networks. Are they being allocated evenly through VERA, or through some other mechanism driven by the central office? And does each network need to submit a request to the central office?

Secretary NICHOLSON. I will answer that in a general way, Senator, and then ask Dr. Perlin to give you specifics. But we used the VERA model, which is the Veterans Equitable Resource Allocation model. It is based on the veteran population within the VISNs. So we take the pie and see where the veterans are and it is allocated to VISNs on that equitable model. I would ask Dr. Perlin if he would like to respond in more detail to the second part of your question.

Dr. PERLIN. Thank you, Mr. Secretary, Ranking Member Akaka. As the Secretary stated, the Veterans Equitable Resource Allocation model distributes funds each year based on workload, based on the complexity of patients. In this past year, there have been a number of requests for additional resources in and above. That is not unusual in any given year, that there are requests. I think Senator Murray knows that VISN 20 was exploring their requirements. We had a particular facility in the mid-South that suggested additional requirements. Our finance committee of the network directors actually reviews the resources and determines what sort of resource requirements might be additionally needed.

Senator AKAKA. Mr. Nicholson, this whole situation really makes the case for assured or mandatory funding. Please share with us why you believe the current system of VA's projections into the future is better than setting spending on a more guaranteed path.

Secretary NICHOLSON. I anticipated that you or that someone who has expressed themselves on that might ask me that question, Senator, and I have thought about that in a different way. As you know, I think, our position has been pretty clear about that.

I think we all need to keep in mind what we are talking about here. We are delivering this health care to the individual veteran. There is no intermediary between us, the Federal Government and that patient. There is no HMO. There is no third party provider. It is us. So whatever comes in, we have to be able to administer. We have to be able to take care of that patient.

I see this differently than I have, quite honestly, in the past. If you had some mechanical formula of spending for the number of

veterans that came in and you multiplied that times those increases that we have just talked about, let us say the 103,000 from the combat area, you couldn't deliver. You would get the money under your formula, but you wouldn't have the facilities to take care of them if you hadn't gone through and tried to project what it is going to be and anticipated it. You would have to do that.

You know, benefits, and we spend more money in the VA in benefits than we do in health care, and benefits are mandatory. Whatever it is, it is. But that is writing a check. Here, it is bringing them into a facility and putting them in a bed and tending to them with resources. So I don't see how that would work.

Senator AKAKA. Thank you very much, Mr. Chairman.

Chairman CRAIG. Senator Murray.

Senator MURRAY. Mr. Secretary, when we offered the amendment to the emergency supplemental, we were basing that very clearly on what we were seeing from our VISNs, what we were being told, our preliminary looks at the mid-term budget review that you are now going off of. Yet you wrote a letter to Secretary Hutchison saying that there was not a problem. We had the information. We knew there was a problem. The VA was saying there wasn't. OK. We are here now. Do you think there is a problem?

Secretary NICHOLSON. I think that is a matter of definition. When I wrote that letter to Senator Hutchison, we thought we had a situation that we could handle, and I think that we were right and—

Senator MURRAY. But do we have a problem now?

Secretary NICHOLSON. For 2005?

Senator MURRAY. Correct.

Secretary NICHOLSON. We certainly don't have a crisis, no.

Senator MURRAY. Do we have a problem?

Secretary NICHOLSON. Well, I suppose—

Senator MURRAY. How much is it?

Secretary NICHOLSON. Well, we are talking about a billion dollars, but we have, as I have just said, Senator, we have the way to take care of that within our 2005 resources.

Senator MURRAY. But we do have—we will get to that. We do have a problem. It is one billion. I have heard 1.6, I have heard 1.4, I have heard 1. What is it?

Secretary NICHOLSON. For 2005, because this gets confusing—

Senator MURRAY. Well, we—

Secretary NICHOLSON [continuing]. 2005 and 2006. For 2005, we are making transfers of approximately \$1 billion.

Senator MURRAY. Approximately \$1 billion for 2005. That doesn't even get to the 2006 problems.

Secretary NICHOLSON. That is correct.

Senator MURRAY. We are making transfers out of the construction account and of a—

Secretary NICHOLSON. Maintenance.

Senator MURRAY. Well—

Secretary NICHOLSON. Not capital construction.

Senator MURRAY. Mr. Secretary, we passed the 2005 budget. I have it here in front of me. You are talking about taking \$600 million out of a \$770 million, I think, \$780 million account. I think Congress and several Senators—

Chairman CRAIG. There is an operation and maintenance and a capital account, two separate accounts—

Senator MURRAY. Correct. Mr. Secretary, how much is in the maintenance account?

Chairman CRAIG. It is capital and—

Senator MURRAY. It is under construction, I believe is what you have been saying in all your public statements, is the construction account.

Chairman CRAIG. Let us make sure we clarify that. What are the two accounts you are taking money from?

Secretary NICHOLSON. From medical facilities and from—

Senator MURRAY. Construction of medical facilities, I assume?

Secretary NICHOLSON. I think it is—excuse me—go ahead.

Dr. PERLIN. I think in the restructuring of the appropriations, it came to three separate accounts, medical administration, medical facilities, and operational dollars. It is not absolutely construction. It includes some operational maintenance activities—

Senator MURRAY. But I have also heard, Secretary, you have said—

Dr. PERLIN. There is a separate capital construction—

Senator MURRAY [continuing]. It will not affect the health care of veterans. It will come from construction. I think the Senators here have a right to know, since we are spending about \$780 million out of the 2005 appropriations bill that we passed, if you are not going to take it out of health care, you are going to have to take it out of somebody's facilities, whether it is Senator Ensign's Nevada facility or whether it is the VA facility in Puget Sound or whether it is the Texas CBOX. Whatever it is, it is going to not happen.

These are funds that this Congress debated, we approved, we put into our appropriations bill. You are going to go back and take that money out and say we are not going to spend it. That is \$600 million of your \$1 billion problem, correct?

Secretary NICHOLSON. May I respond?

Chairman CRAIG. Please.

Secretary NICHOLSON. First of all, I respect—I know you are totally concerned about this. The fund from which we are taking that \$600 million was approved by the Congress—

Senator MURRAY. That is correct, in our appropriations.

Secretary NICHOLSON [continuing]. In an amount of \$1.3 billion. But that is not—

Senator MURRAY. Well, I will take your figure. Half of the projects that we worked through, agreed in the Senate, agreed in the House, went to conference, and approved—

Chairman CRAIG. Let us—I don't want to interfere here or interrupt, but let us clarify. There is a capital account over here to build new projects.

Senator MURRAY. That would be construction.

Chairman CRAIG. Then there is an O&M account that is both O&M and maintenance, which includes construction within old projects to modify them and modernize them.

Senator MURRAY. Correct, including asbestos—

Chairman CRAIG. Which of those two accounts are you borrowing from?

Senator MURRAY. Including asbestos abatement and—
Secretary NICHOLSON. The latter.

Chairman CRAIG. The latter. So, in other words, if a new hospital is planned and part of that is in the budget, that is not the account you are borrowing from.

Secretary NICHOLSON. That is correct.

Chairman CRAIG. OK.

Senator MURRAY. So asbestos abatement that is happening in some of our facilities. It will be projects where we have severe damage that needs to be replaced. Those kinds of accounts will not be done? I know that you are not going to be able to hand this back today, but I think we need to understand that is what we are talking about not funding this year, and those, I believe, are all critical to the care of our veterans.

The other part of it you are talking about is this \$400,000 surplus that I asked Dr. Perlin about that he said doesn't exist, that would actually, if it did exist, would be robbing from 2006, which would compound the appropriations bill that Senator Hutchison is currently putting in place.

I guess, Mr. Secretary, we have to be real about this. Every step of the way, we have been told there is not a problem. There is not a problem. If we paper this over today and are not real about what our needs are, we are going to do a disservice to our veterans. We need to know what the problem is for this year, \$1.0 billion, \$1.5 billion, and we need to take care of that, because Mr. Chairman, if we don't, that will defer all of these maintenance projects to 2006. We have already found out that the funding formula is incorrect at 2.3 percent. It is going to be more than that. Health care costs have increased. We are going to have a problem.

If we defer all these maintenance problems until next year, we are going to be sitting here 6 months from now, 1 year from now, 2 years from now, and we are going to have not just a \$1 billion crisis, we are going to have a \$5 billion crisis. We need to make sure that we put forward an accurate figure and we need from you, Mr. Secretary, for the record, a list of the projects from that account, whatever you are calling it, as exactly what will not be done if we don't provide emergency supplemental funds this year.

Secretary NICHOLSON. We will—we can put together a list of those kinds of things that you are talking about that are intended—

Senator MURRAY. And what is the timing on that?

Secretary NICHOLSON [continuing]. That were intended for that fund, yes, ma'am.

Senator MURRAY. What is the timing on that, because my guess is with the \$1.5 billion, whatever it is—and I have heard \$1 to \$1.6 billion is what I am now hearing—if it is that much, we can't wait until the last week of July or September to begin to address that. We need to do it immediately, so when can we see this list of projects that you, if we don't come up with an emergency supplemental, will be deferred or not done?

Secretary NICHOLSON. I would say within a matter of days. We will turn to it right away to develop that for you.

Senator MURRAY. I think that is critical for this Committee, and I apologize for being rather angry, but I am rather angry.

Chairman CRAIG. Senator Salazar.

Senator SALAZAR. Secretary Nicholson, I would like you to speak a little bit as to the actuarial modeling and the problems with respect to the modeling. As you explained what the shortfall is here that we are facing and the adjustments that you are making, you talked about how the budget that we are currently operating on was based on the assumptions from the year 2002, prior to the engagements in Iraq and Afghanistan.

Secretary NICHOLSON. In Iraq.

Senator SALAZAR. In Iraq, OK. And then you later on said that we have 103,000 returning veterans that are seeking assistance, are eligible for assistance from that operation.

You are a businessman and a very successful businessman. It just strikes me that for our Veterans Administration to somehow not include into the actuarial model this reality that we are going to have a significant surge in the number of veterans to take care of coming out of both OEF and OIF is something that should not have happened at all. So I was wondering whether you could comment on that.

Why did that, in fact, not happen, or why did the actuarial model, and ultimately, it seems to me, that is a tool that basically provides you with information on the kind of budgetary request that you make. How did the Veterans Health Administration fail to take into account this surge that we were going to have from both of these operations that have involved so many of our men and women?

Secretary NICHOLSON. Senator Salazar, they didn't take it into account because they didn't know it. We are working right now on the 2007 budget because we have to. We are sitting here in mid-2005 and we only have preliminary data for 2005, so what we have actual data is 2004. So the 2007 budget right now is being formulated based on 2004 numbers.

So if we back up to the 2005, which is what we have been talking about now, that was based on 2002 for force. The timing of that—

Senator SALAZAR. I understand that, that in 2002, obviously, we did not know the level of engagement in either Iraq or Afghanistan and the effect that that would have on our veterans. I understand how the actuarial model is looking at what has happened in the past and make projections into the future. But there is a sense of reality that also hits the manager, and that is that we know and have known since these two engagements that we are going to have an increased demand on veterans' health services for our country. So why is it that the Veterans Administration from a management point of view, as you were projecting your budgets, couldn't make those adjustments and only that that was a reality you were facing?

Secretary NICHOLSON. Well, I think those are—

Senator SALAZAR. And that is probably not—

Secretary NICHOLSON [continuing]. Good, logical questions, but let me tell you, we monitor this all the time. For the first 6 months of this fiscal year, we were right on plan even with Operations Enduring Freedom and Iraqi Freedom going on at the intensity that they had been going.

Senator SALAZAR. So then is there a fundamental—you monitor all the time, so we are not just looking at a number that was given to us based on 2002. This is an ongoing monitoring of the needs for veterans' health care. So as you were monitoring, as this year came along and now we have the \$1 billion surprise, tell us how we can avoid this problem in the future so that we don't—and let me not go back. We know we have a problem and you are correcting the problem with adjustments. There is an emergency supplemental that is going to be considered and we are going to try to move forward.

But looking ahead, looking ahead, how do we change the actuarial model in such a way so that we don't have this kind of problem in the future?

Secretary NICHOLSON. I think that is a very good question and I was asked the same question this morning in the House. Given these givens that we have of this long budget cycle, and we are going to have to see if there is a better way to do that. This actuarial model—it is owned by Milliman and they have a very good track record in the private sector with HMOs and other private insurers—it doesn't model everything, by the way. It doesn't model long-term care, it doesn't model prosthetics, and it doesn't model dentistry. And, in fact, dentistry is one of the material items that has come up with these young folks returning from combat areas.

So we will have to, I think, take a look at what the—what somebody's judgment is going to be about what it is going to be like. Now, we are sitting here in June of 2005 and I am making commitments on the request side today, and we have a group working on this right now, on 2007. Well, do you know what it is going to be like in 2007 and what our demand is going to be vis-a-vis any combat going on and other increased propensity to use the VA, which is really the majority of our phenomenon of growth? Is it that more and more eligible veterans are coming in and using our facilities?

That is the challenge, is to see—and if we miss it, if we miss it now because we are talking about 2007, we are going to have conditions like this where, in this case in 2005, we are about 3 percent off. In 2006, because of what we now know that is happening, we have not requested enough, and that is why we are talking with OMB and you all about asking for more money for 2006.

Senator SALAZAR. My time is up, but let me just make this comment and this suggestion, Chairman Craig and Members of the Committee. It seems to me that that is a very fundamental question that we need to work together on to address when we are looking ahead and wanting to make sure that we don't miss the mark next time. What is the soundness of this actuarial model? How is Milliman going to help us make sure that we don't have this problem in the future? What are the assumptions that are being made in this actuarial model? How are those assumptions taking into account the numbers of veterans that we are getting back from Iraq and Afghanistan that need the help of the veterans' health system?

There are a whole host of questions around that very important issue that I think it would help this Committee and it would help the VA and certainly ultimately our veterans if we had a much better handle in understanding how we are making these projections.

Thank you, Mr. Secretary.

Chairman CRAIG. Thank you, Senator.
Senator Obama.

Senator OBAMA. Thank you, Mr. Chairman.

I would just say that Senator Murray and Senator Salazar summed up, I think, a lot of the frustrations that I feel in this process. I thought that Senator Salazar's comment at the end was constructive. How can we improve the system?

I have to say just a quick observation. It is surprising to me that long-term care, prosthesis, and dentistry would not be included in the modeling. Why we wouldn't expect that there would be significant costs associated with those items is something that I am just curious about, and maybe just very briefly, Secretary or Mr. Perlin, can you just give me a sense of why wouldn't we include such basic items?

Secretary NICHOLSON. I would like to ask Dr. Perlin to respond, Senator.

Senator OBAMA. Particularly something like prosthesis, where we know that what is happening in Iraq is resulting in record numbers of amputees.

Dr. PERLIN. Thank you, Senator, for that question. Because they are not actually in the actuarial model doesn't mean they are not budgeted for. Prosthetics is so very important that it is actually a line item and the line item usage has gone up actually faster than projected beforehand.

Your comments about long-term care are absolutely on target, as well. Long-term care is something that should be projected, but to date, there has been very little in the way of modeling for that. In fact, now, we are beginning to contract with Duke University to develop long-term care actuarial projections and they will become part of the models going forward.

As to dental, as well, dental is not a part of the standard benefits package. It is very complex in terms of the eligibility for that. It is so idiosyncratic that it would be impossible to model in the standard actuarial projections.

But these things are, I assure you, accounted for in the budget, because as you have rightly indicated, they are a critical part of care.

Senator OBAMA. OK, well, let me say this, just to follow up on Senator Salazar's point. I think that there should be some time certain for some process or procedure whereby your office is reporting back to this Committee very specifically in terms of how improvements are going to be made in this budget process.

I understand that budgeting is inevitably imprecise when you have 2- or 3-year lag times in terms of your budgets and given the magnitude of the Federal budget. But my sense is we know we can do better than what we are doing right now.

And let me just add one other point on this, and that is a sense of transparency in how this budget process works. Mr. Secretary, this is not entirely directed at you, because as Senator Rockefeller indicated, your hands are tied to some degree. But I will go ahead and make the comment that this Administration seems to have a chronic habit of understating costs during budget negotiations and then suddenly we have, in the case of Iraq, \$80, \$90 billion emergency supplementals.

I don't think the VA should get in that habit of emergency supplementals. We should have a process where we are honestly assessing the cost because I don't think this is subject to politics and I don't think we should be trying to squeeze the budget just to make the numbers look better and then have to scramble to make sure that we have the resources.

One final question that I have specific to some of the issues that I am hearing back in Illinois. I have heard some constituents complaining that veterans' clinics have been reducing hours. Is there any association to—if that is the case, is that one strategy to handle this shortfall? Are we reducing hours as a way of handling the shortfall?

Secretary NICHOLSON. I will ask the Health Administrator to respond to that.

Dr. PERLIN. I will look into specific concerns in Illinois.

Senator OBAMA. OK. I would appreciate it, and this goes to Senator Murray's important point. The bottom line is, are veterans being impacted in terms of their health care? I would be deeply disturbed if it turns out that as a consequence of this, what you say is managing this budget shortfall turns out to be simply scrimping on the care that we are providing our veterans, so I would like a specific answer to that.

Chairman CRAIG. Yes. Any additional questions that we don't have time for today will be handed in writing and we will get a response forthcoming. Thank you very much.

[The submitted questions follow:]

RESPONSE TO WRITTEN QUESTIONS FOR HON. R. JAMES NICHOLSON, SECRETARY, U.S. DEPARTMENT OF VETERANS AFFAIRS, FROM SENATOR DANIEL K. AKAKA

Question: I would like a list of planned "non-critical capital expenses" that would no longer be funded if the transferred \$600 million is not replaced.

Response: The President submitted a supplemental request for fiscal year (FY) 2005 and a budget amendment for fiscal year 2006. With the resources provided from the above, all needs, including those for non-critical equipment and non-recurring maintenance projects, known by VA will be met.

Chairman CRAIG. Senator Thune.

Senator THUNE. Thank you, Mr. Chairman.

Mr. Secretary, it seems like a lot of the—I am more concerned with where we go from here and how do we fix this and how do we make sure this doesn't happen in the future, because this kind of unpredictability and uncertainty and surprise obviously isn't well received up here, nor, I would think, is it received well by you and your many facilities throughout the VA.

It seems like it comes down to having accurate data. I realize the somewhat ambiguous nature of trying to make projections based upon data that is dated, but doing a 2005 budget on 2002 data, or a 2007 budget on 2004 data doesn't seem to make much sense. I know that the budgeting process around here, you are working out there a ways. We are now working on the 2006 budget. But why can't we have more current data, and are you getting current data from DOD, for example?

The question that was raised about amputees, we know, for example, that the number of amputees has gone from 3 percent to 6 percent as a result of this most recent conflict. Are you getting that kind of information from DOD about the nature of the injuries that

are out there and what the anticipated needs are going to be at the VA as some of those folks start coming into the system? I just find it hard to believe that we are going to be making decisions based upon data that is 3 years old. That makes no sense. There has to be a more—we ought to be able to capture more recent data on which to base some of these decisions.

Secretary NICHOLSON. Senator, there is in most things, including health care, there is a discipline and there is a system of metrics with the people who develop these software programs, and this company that we have been using now for 5 years, Milliman, has a really solid track record. It is sort of uncanny how well they have been able to predict what the growth is going to be on these big systems, including the VA, up until 2005. They really were within, I think, 1 percent of deviation either way, a little over 1 percent 1 year. So you have to have some basis from which to start to project what your business demand is going to be out.

But we are in a unique business, and I think you raise a very good point about DOD. We have been working with DOD and trying to get the best available release from active duty forecast that they can provide us, because we are beginning to get a sense of the percentage of these folks that are released that come back from the combat theater that come in our doors. So that would be another tool, and the sooner that we have it, as long as that ratio holds, then we have another way to predict more closely what our needs are going to be.

But it is complex and it is not an exact science, and it is something that we are just going to have to keep working on. But again, as I said before, we are working right now on 2007 and trying to develop the best data points that we can to make a good projection.

But I will have to say, because it is me. I mean, we are sitting here and we are going to be sitting here in 2007 and I am off by a billion dollars, I am—to me, that is not real unreasonable or, depending on how you respond to it, a crisis. In the 2005 context, that is a 3 percent variation in a world that has changed quite a bit.

Senator THUNE. Well, I guess the only thing I would say about that is that I understand—and especially in 3 years, I mean, the world can change dramatically in a 3-year period. And if you are using information that is 3 years old when you are trying to make projections—we have a hard time making projections around here, obviously, from 1 year to the next.

But I just think that currency of information and data is going to be critical in terms of trying to get a higher level of accuracy going forward. So to the degree that we can be helpful in ensuring that you all have—if the problem is getting information, good information—if there is some way we can compel that from DOD or whatever, I just think that, Mr. Chairman, that is a big part of this problem.

Is the shortfall distributed across all VA services? Is it medical care? There are a whole range of things, of course, benefits, memorial and other services that are covered by the VA. Or is this just specific to the health—

Secretary NICHOLSON. It is just health.

Senator THUNE. OK. Well, I see my time has expired. I would like to at some point pursue a question with respect to ideas that you might have about alternative models of funding going forward, too, because it seems to me maybe that there is some combination of mandatory-discretionary funding that might help address some of these issues so we don't have this kind of uncertainty going forward. But I will explore that at another time. Thank you.

Thank you, Mr. Chairman.

Chairman CRAIG. Senator Jeffords, welcome.

STATEMENT OF HON. JAMES JEFFORDS, U.S. SENATOR FROM VERMONT

Senator. JEFFORDS. Mr. Chairman, I greatly appreciate your holding this hearing this morning, and I share your concern over the situation. This news of a \$1 billion shortfall in the veterans' budget confirms what many of us have suspected for some time. I don't know why the Veterans Administration operated on such low assumptions of patient growth in the face of clear evidence that veterans from the conflicts in Iraq and Afghanistan were streaming into the VA. We were hearing from the VISNs that they were going to have trouble meeting projected needs.

I am also very disappointed that the Administration opposed our efforts 2 months ago to add money to the Iraq supplemental for care of our veterans. That was the time to fix this problem.

I am pleased that Senator Akaka and Senator Murray are moving to offer an amendment on the floor to provide additional emergency funding for the VA. I plan to cosponsor this amendment and urge you to support it, also, as I expect you will.

I thank the Chairman for helping us to try to find answers to this problem. We owe it to the veterans.

Mr. Secretary, I share my colleagues' concern that we are not meeting one of the Nation's most sacred obligations, to care for the wounds of those who have been borne in battle. I am also concerned that efforts to shift resources to treatment of Iraq and Afghanistan veterans will leave the system short of capacity to care for the veterans already in the system. What about Priority 7 veterans? Does the VA need even more than the \$1 billion so that they can be covered, as well?

Secretary NICHOLSON. To get through the rest of this fiscal year, Senator Jeffords, we are estimating a need for \$1 billion because of that surge in demand, both from returnees from the combat theaters and even more from other era veterans who have decided to take advantage of their eligibility to use our services. The delivery of health care is the No. 1 priority of the organization and continues to be. This transfer is coming, about 40 percent of it from a reserve account and 60 percent of it from an operation and maintenance account to go into the health care account to ensure that high-quality care continues.

Senator. JEFFORDS. Thank you. I am sure we will all be following this very closely to make sure that our veterans get the care that they need.

Thank you, Mr. Chairman.

Chairman CRAIG. Jim, thank you very much.

Mr. Secretary, we are going to jointly solve this problem. We are a bit unique in that—and you have heard two Senators refer to it—we are in the midst of an appropriation bill on the floor and there is angst and concern and there will be action taken during this moment in time, in the next day or day and a half, to resolve the current situation and possibly move us into a 2006 overview.

And so numbers are going to be tremendously important here, to be as accurate as we can be so that we can put those numbers together. We are dealing with OMB. You have engaged OMB at this moment and we expect some language to be forthcoming.

Here is my concern, because what you have basically said to us is that the model didn't work based on the standard and the input and the dynamics of the environment in which you are currently addressing needs. What I am sitting here thinking about, so that we can stay current to the situation, because we have a dynamic that is not modelable at this moment, and you are right to ask for exit numbers and all of that as to how we make it more accurate, dealing with a 2006 budget.

Therefore, maybe we are at a time when you and we need to do a mid-year review collectively, concurrently, and to come back and look at those numbers, anticipating, not fending off or fighting or raiding other accounts, that there will be differences because we think we are good, but we are not as good as we think we are in relation to these models and the dynamics of health care, not the other areas. Those are stageable. They are predictable. They are controllable. But this is a new dynamic we are into.

So I would like you to think in that context as we address this issue. I think that the question as to if we don't address and resupply, I guess is a word I can use, the current accounts that you are using, especially the O&M capital, what happens out there? Are you canceling contracts? Are there a series of things that will happen as you pull money out of those accounts that would be forthcoming, if there is any construction within these that are contracted out that you would be pulling? Do you know if that would occur if this money is not replaced?

Secretary NICHOLSON. To my knowledge, we are not canceling any contracts, Senator. Do you know, Dr. Perlin?

Dr. PERLIN. To the best of my knowledge, no, we are not. These are deferment of repairs.

Chairman CRAIG. I appreciate that, but I was led to believe, Doctor, and maybe you can answer this, that some of these repairs were quite significant and that you don't just—and here we are in the last 3 months of the budget cycle and you are pulling money out of these accounts now. Was that construction underway? Is it halted? Were there contracts canceled? How does that happen?

Dr. PERLIN. I think it is absolutely fair to say that we need to invest in the infrastructure. I don't think contracts were canceled mid-course. There are probably certain things that were simply not contracted for in terms of repairs.

Chairman CRAIG. OK. I would hope you would take a look at that, because I am assuming that if you are going to do repairs in July and August, the contracts have been let and those kinds of things. Is that not the case?

Dr. PERLIN. I don't believe so, but as you rightly indicate, we have to make the investments in the infrastructure for these repairs.

Chairman CRAIG. OK. We are going to determine here in the Senate, because of the cycle we are in at the moment, we are going to determine within the next 10 to 12 hours exactly what we are going to do. So, Mr. Secretary, it is going to be awfully important for you and your people and OMB to stay very connected with us as we move through this. There is a vehicle on the floor that will get amended. Already, there are two amendments up.

How that amendment is crafted to deal with 2005 and on into 2006 is going to be critical. Some would suggest we deal only with 2005. Others are suggesting we deal with 2005 and 2006, because, if you will, we have a delay, as the Chairman spoke of, in Military Construction-VA until the numbers are forthcoming so that we can move, and we don't want that delay to languish long, it might be forthcoming today, and so we want to thank you for that.

I think the question that Senator Salazar has asked is the question that is the most opportune at the moment. We are going to fix this problem, and there are dynamics in it that would suggest that some of it was not in your control and obviously others would suggest that some of it might have been. But more importantly, we have now recognized it. We now see it.

And there is one thing this Congress will do in a very bipartisan way, and that is fund the necessary services to the veterans who need them, period, end of statement. Whether we allow the reserve to be depleted and moved through and be replenished in 2006 or not is yet to be decided. But we will obviously serve those who are in need.

Senator Salazar, do you have any other questions?

Senator SALAZAR. Just a brief comment, Mr. Chairman. First, again, I applaud your leadership and I also have great confidence in the intentions and the abilities of the people who are in charge of the VA, including my friend, Secretary Nicholson.

I would suggest that as we get into this discussion about how we move forward in the next few days that it is important that we have accurate information on exactly what is going on. I would suggest that it might be useful for the Committee to have a letter with a set of questions that we could get back, answers that we could get back from the VA so that we are all operating off of the same set of information.

For example, I would include in those questions the following:

One, the \$1 billion budget adjustment that is underway for this year, what specifically will that mean in terms of the projects and the O&M part of the budget that will be impacted so that we will know what we are talking about?

Two, when we look forward to the 2006 projections that have come out of the actuarial modeling, what are we looking at in terms of what those projections are? Are they still accurate? Are we sure that all the assumptions are being dealt with in that actual modeling?

Three, generally, with respect to the actuarial modeling, is it something that we are comfortable with? What exactly is hap-

pening with the actuarial modeling to give us confidence that we are going to have good predictions in the future?

I would say that it would be important for us, Mr. Chairman, if you would find something that you want to undertake in this Committee, for us to try to get back together to see how we can move forward together, because this is not a Republican problem. It is not a Democratic problem. We may not call it a crisis yet, Secretary Nicholson, but it certainly is a significant problem that I think has gotten the attention of a lot of people and we have to move forward as Republicans and Democrats, as executive and legislative branch, to solve the problem onto the future.

Chairman CRAIG. I thank you for those suggestions. They are very good ones. Let me suggest that all that we find out will be very transparent and available to all the Committee Members and any recommendations that I and Chairman Hutchison come up with will be in full consultation with the Democrats on both of those committees. We will both be involved in it as authorizing and as appropriating, and I think that is tremendously important. Whether we are effectively able to bring the committee back together or not is one thing. We may huddle in a corner somewhere and share collective information prior to a decision being made. But I pledge to you obviously full knowledge and transparency as we move forward.

Senator SALAZAR. Thank you, Senator.

Chairman CRAIG. Mr. Secretary, gentlemen, Dr. Perlin, Mr. McClain, thank you very much for being here this morning, as I said early on in my opening statements, with the short notice involved, but I think you sense, as we do, the critical character of this issue and that we get it answered. These are the kinds of things that should not languish long, but when problems are understood and a clear picture of them is assessed, then for us to be able to respond as quickly as we can is important for all of the parties involved.

So again, thank you very much. The Committee will stand adjourned.

[Whereupon, at 12:50 p.m., the Committee was adjourned.]