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MEMORANDUM

To: American Society of Transplant Surgeons

From: Peter Thomas and Adam Chrisney

Date: February 17, 2011

Re: The President's FY 2012 Budget Request

On February 14, President Obama released his \$3.7 trillion FY 2012 federal budget. The budget would narrow deficits by \$1.1 trillion over the next 10 years, mainly by freezing domestic discretionary spending for the next five years and imposing an inflation-adjusted cap on defense spending over the same period. However, the President's budget does increase funding on several programs focused on research, innovation and education. Federal spending, a sluggish economy, and last year's bipartisan tax deal is now expected to push this year's deficit to a record \$1.6 trillion. The administration's goal of reaching "primary balance"—revenues matching spending, except for interest payments on the debt—would slip from 2015 to 2017. Gross government debt would continue to rise until reaching 77 percent of gross domestic product (GDP) in 2021.

The President's budget did not include major changes to entitlement programs such as Social Security and Medicare but did include some proposals to reduce expenditures for Medicaid and more modest proposals to curb some Medicare expenditures. Reactions to the President's budget from Republican leaders were expectedly negative, with leaders announcing that they would include entitlement reforms in their version of the budget when the House Budget Committee acts in the next several weeks. President Obama has suggested that he is open to entitlement reform and many agree that if it is accomplished, it will have to be bipartisan. The reason offered by the Administration for not reducing spending further than it proposed was that fragile economic growth could be imperiled by more significant budget cuts.

Under its budget, the White House envisions a reduction of approximately \$500 billion from the deficit next year, and by 2015, the annual deficit would be well below \$1 trillion, bottoming out at about \$600 billion in future years. At that point, the costs of Medicare and Social Security as

“baby boomers” enter the program would overtake the spending reductions and the deficit would start to rise again.

Having accepted the necessity of budget cuts, President Obama’s budget includes spending reductions for programs that are strongly supported by many in his own political party. For instance, home heating oil subsidies would be pared back significantly, as would funding for the U.S. Forest Service, the Army Corps of Engineers, some housing programs, and community development block grants.

In contrast, House Republicans have proposed \$100 billion in discretionary spending cuts for the *current* fiscal year, FY 2011, compared to President Obama’s proposed budget for that same year. In real terms, the amount of the reduction would be approximately \$60 billion less than FY 2010. This proposal is in the form of a Continuing Resolution (CR) and is currently being debated on the House floor. President Obama has already stated that he would veto this bill if it remains in its current form. The House Republican’s proposal for FY 2012, which will be unveiled over the next several weeks, is expected to be even more austere and will include entitlement reform proposals as well. Given the divided partisan control of Congress, the outlook for compromise on these immediate and long term budget and appropriations items is very unclear.

One complicating factor in this developing budget debate is that neither the Administration nor House Republicans have revealed their strategies for following through with entitlement reforms (Social Security, Medicare and Medicaid) to date. In the wake of two major reports from bipartisan commissions on the national debt, there are expectations that entitlements need to be meaningfully addressed, but both sides would prefer the other side to make their proposals first.

Impact of the Unresolved FY 2011 Budget

The government has been operating throughout fiscal year 2011—which began on October 1, 2010—on a CR, which amounts to a discretionary spending freeze at FY 2010 levels. Congress did not adopt a budget resolution last year and has not yet passed any of the 12 regular appropriations bills. Instead, lawmakers passed a series of Continuing Resolutions that have financed the federal agencies to date. The most recent CR expires on March 4th and if Congress cannot agree to either an Omnibus Spending bill or a CR through the end of the current fiscal year, another short-term CR will be necessary. The alternative is a shut-down of the federal government, much like occurred in 1995.

President’s Budget Request for the Department of Health & Human Services (HHS)

Under the President’s FY 2012 budget request, the Department of Health and Human Services would receive \$79.9 billion. This amount is \$400 million lower than last year’s request and \$1.4 billion less than estimated 2011 expenditures.

Funding for several major agencies within HHS is increased, including a \$740 million increase for the National Institutes of Health to bring that budget up to a total of \$32 billion. NIH is proposing to establish a new national Center for Advancing Translational Sciences (NCATS) on October 1, 2011, in order to place the agency in a pivotal position to re-engineer the pipeline for

diagnostics and therapeutics discovery and development. NCATS will align and bring together in one organization a number of trans-NIH programs that are inherently cross-cutting, including the Cures Acceleration Network (CAN), the Clinical and Translational Science Awards (CTSA), and the Therapeutics for Rare and neglected Diseases (TND) program. At this time, NIH also plans to abolish the existing National Center for Research Resources (NCRR); its programs will be transferred to the new Center or to other parts of NIH. One of the reasons this center would be abolished is the cap of 27 NIH institutes and centers that is currently written into federal law. The FY 2012 budget request for the National Center for Medical Rehabilitation Research is \$70.8 million, an increase of \$1.2 million, or 1.7 percent over the FY 2010 comparable level.

The Food and Drug Administration would be funded at \$2.7 billion, an increase of \$147 million over FY 2010 actual spending, largely because the administration would like to support full implementation of food-safety legislation which contains broad new FDA authorities to recall tainted food and the ability to require food producers to implement preventive controls. In addition, there is \$1.4 billion (\$124 million increase) for medical product safety and \$15 million to establish a new regulatory pathway for approving generic biologic products.

However, coming with these increases for NIH and FDA are significant cuts to programs with wide support among Democrats, including a \$2.5 billion reduction to the Low Income Home Energy Assistance Program (Li-HEAP). Community Services Block Grants are cut by 50 percent to \$350 million because recipients are not held accountable for program outcomes. The budget also eliminates funding for a historically bipartisan program that funds medical residency programs at children's hospitals.

The Centers for Disease Control and Prevention (CDC) also would receive a budget cut, bringing their budget down to \$5.9 billion, with some of those reductions coming from a consolidation of several individual disease prevention centers within CDC, including heart disease, stroke, diabetes, and cancer, into one coordinated program called the Comprehensive Chronic Disease Prevention and Health Promotion Program. The Budget includes \$1.2 billion, an increase of \$236 million above FY 2010 for this new competitive grant program that refocuses activities from disease specific programs into a program that is more comprehensive in its approach. The new program will improve health outcomes by coordinating the interventions that can reduce the burden of chronic disease across common diagnoses. The budget includes \$144 million for Birth Defects, Developmental Disabilities, Disability, and Health, the same as FY 2010.

The Health Resources & Services Administration (HRSA) receives a net increase of \$975 million for a total of approximately \$9 billion under the President's budget. This includes \$1.3 billion to support a health workforce strategy that expands the capacity and improves the distribution of the primary care workforce; encourages inter-professional training; focuses on elder care; reduces disparities in the health workforce; and develops the capacity to track and analyze health workforce-related data. The HRSA budget also includes \$26 million to support a national system to develop policies to ensure the fair allocation and distribution of organs for purposes of transplantation, consistent with the FY 2010 funding level.

Centers for Medicare & Medicaid Services (CMS)

The Centers for Medicare and Medicaid Services (CMS) would receive \$4.4 billion for FY 2012 under President Obama's budget request, an increase of \$700 million over the \$3.7 billion spent in FY 2010. President Obama's fiscal 2012 budget request proposes a \$54 billion temporary fix to the Medicare physician fee schedule problem, the cost of which is offset by lowering a Medicare provider tax threshold in 2015 (saving \$18 billion) and increasing the number of generic drugs used in government health programs. Specifically, the President's budget calls for two sets of payment adjustments to the Medicare physician payment system. The first is a 2-year fix costing \$54 billion and the second would provide relief from 2014 onward costing \$315 billion. Notably, no funding for the second proposal is included in the budget request.

However, the budget proposes a number of other payment reductions including anti-fraud initiatives, a controversial change to biosimilars policy, and limits on so-called "pay for delay" settlements. The administration aims to increase generic drug use by reducing the number of years that brand-name pharmaceutical companies have "exclusivity" over complex biologic drugs (saving nearly \$5 billion) and prohibiting agreements between brand-name and generic pharmaceutical companies that postpone generic drugs' entry to the market (saving \$8 billion).

The budget proposal would also shift \$495 million to extend a program that covers Medicare Part B premiums for qualified low-income seniors. Other offsets include recovering improper Medicare Advantage payments (saving 46.2 billion), rebasing payments to Medicaid disproportionate share hospitals (DSH) as of 2021 (saving \$4.2 billion), and tracking the highest users of prescription drugs in Medicaid (saving \$3.4 billion).

The budget also increases the agency's funds to fight fraud and abuse to \$581 million, up from the \$311 million from FY 2010. The Administration had earlier indicated that fraud in the Medicare program alone costs about \$60 billion. The budget request describes the investment as "part of a multiyear fraud-and-abuse proposal."

In addition, the budget expands CMS' program integrity authority, including strengthening third-party liability under Medicaid and dedicates a portion of funds recovered by Recovery Audit Contractors (RACs) to efforts to prevent improper payments and fraud (saving \$70 million). Another proposal alters the Quality Improvement Organization (QIO) program to improve efficiency, such as expanding the pool of eligible contractors, lengthening the QIO contract period, and examining the geographic scope of QIO contracts (saving \$3.26 billion).

Other new program integrity proposals include a new Medicare Claims Ordering System (effective CY 2014) which would Create a Medicare claims ordering system and require electronic submission of orders for certain high risk services, such as durable medical equipment (DME) and home health, prior to payment of a claim in order to validate that a physician or other eligible professional ordered the service (saving (\$1.76 billion). Also, effective FY 2012, CMS would start requiring prepayment review for all power wheelchair claims to ensure they meet criteria before payment (saving \$240 million).

On the Medicaid front, the President's budget includes program integrity proposals that would eliminate the use of "provider taxes" to augment the state share of Medicaid expenses, thereby allowing states to draw down additional federal matching funds (saving \$18.370 billion). The budget would also require drug manufacturers to repay States for improperly reporting Medicaid-

covered prescription drugs, and would impose penalties for fraudulent noncompliance on rebate agreements (no savings).

The Departments of Education and Labor

In an era of budget cutting, one of the few places that the White House is pushing for significantly more funding is in education. President Obama's request for fiscal 2012 seeks almost \$28 billion more than last year—from \$49.7 billion for education to \$77.4 billion.

Areas for new investment run the spectrum and for people with disabilities they include a \$200 million increase for the Individuals with Disabilities Education Act (IDEA) State Grants to provide a high quality education and help offset State and local education costs for children with disabilities. The Budget also provides a \$50 million (11 percent) increase for the IDEA Infants and Families Program to provide the youngest children a good start. In addition, a new \$30 million joint pilot, Promoting Readiness of Minors in SSI (PROMISE), will develop and evaluate innovative approaches to improving outcomes of children receiving Supplemental Security Income and their families.

The budget provides \$120 million for the National Institute on Disability and Rehabilitation Research (NIDRR), nearly \$11 million over FY 2010 levels and including \$10 million to support a new cloud computing initiative that uses the internet infrastructure to improve technology access through the development, implementation, and delivery of mechanisms that will provide on-demand accessibility for everyone who faces technology accessibility barriers.