STATEMENT OF EDWARD L. SHAPOFF,

VICE PRESIDENT, GOLDMAN, SACHS & CO.,

ON BEHALF OF THE HEALTHCARE FINANCING STUDY GROUP

BEFORE

THE HOUSE COMMITTEE ON FINANCIAL SERVICES,

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

April 24, 2002

Good afternoon Madam Chairwoman and distinguished Members of the Subcommittee; I thank you for the opportunity to testify today in support of H.R. 3995.

I am Edward Shapoff, a Vice President of Goldman, Sachs & Co., and the President of Goldman Sachs Housing and Health Care Funding Company, a Federal Housing Administration ("FHA") approved mortgage lender. I am appearing today on behalf of the Healthcare Financing Study Group ("Study Group"), an association of national and regional investment bankers and municipal bond insurers (Exhibit A) actively engaged in financing the construction and modernization of needed health care and assisted living facilities throughout the United States under the mortgage insurance provisions of the National Housing Act ("Act"). Madam Chairwoman, I have previously had the opportunity to testify before the Senate Subcommittee on Housing and

Transportation on legislation introduced by Senator Rick Santorum (R. PA), which paralleled legislation that had been introduced in the House by Congressman Rick Lazio (R. NY), the former chair of this Subcommittee, to enable present programs to meet the needs of elderly, sick, injured and disabled persons. I was pleased to join Congressman Lazio in speaking in support of those legislative changes before the Senate Subcommittee. We welcome and appreciate your support Chairwoman Roukema, and thank you for including in H.R. 3995 legislative provisions which are so important to America's aging and ill populations.

My remarks today will focus on Sections 203 through 206 of H.R. 3995 that would amend the FHA health care and assisted living programs of the Act to modernize and make them more consistent with today's methods of delivering health care services of the highest quality and most affordable price. These amendments would help to assure that quality, affordable health care is more accessible to rural and urban American communities which have been unable to enjoy the benefits of the Act in its present form, and where conventional financing may not be readily available. I will refer to those four sections of H.R. 3995 collectively as the "Amendments."

The Study Group, whose members have worked with the FHA programs for decades, strongly supports the Amendments to make the health care and assisted living programs more useful in meeting the growing health and housing needs of elderly, sick and disabled Americans in all areas of our country.

As you know, the basic health care sections of the Act (Section 232 for nursing home, intermediate care, board and care, and assisted living facilities, and Section 242 for hospitals and associated facilities) providing mortgage insurance for health care projects were enacted more than thirty years ago, and since their inception have assisted in or enabled the development of more than one hundred thousand nursing home and assisted living units, and three hundred hospital projects in over forty states and Puerto Rico. Thanks to the credit enhancement provided through FHA mortgage insurance, many worthy projects, which might have been unable to obtain affordable construction or modernization financing through conventional private sources, have been successfully completed. In addition, these two sections of the Act have netted hundreds of millions of dollars to the Treasury and the FHA insurance funds from FHA fees and mortgage insurance premiums.

Furthermore, these FHA programs do not compete with private sector financing. Rather, they have tended to foster a sound working relationship between government and private industry. This fact is well illustrated by the active participation of private bond insurance companies (one of which is a member of the Study Group) in bond financed FHA hospital and nursing home projects. Their involvement has materially reduced the cost of financing, thereby helping to assure the repayment of the insured loan and reducing FHA's insurance risk. Debt service savings realized under these programs have also resulted in lower federal and state Medicare and Medicaid reimbursements. At the same time, FHA insurance is available to fill a void left by the conventional private sector which, traditionally, has preferred to lend at reasonable rates only to the very best

investment grade credits. That is not to say, however, that all health care projects should or do have free entitlement to FHA credit enhancement. Indeed, few high-risk mortgage insurance applications would survive FHA's rigorous underwriting processes.

The great majority of providers that have enjoyed the benefits of the FHA programs has established a successful history of operations thereafter. When a pattern of successful project operation emerges and is recognized in the financial community, borrowers have often been able to refinance at affordable rates in the private market, and thus leave behind the additional mortgage insurance premiums and programmatic restrictions which FHA has reasonably established for the protection of its insurance funds.

Since their enactment over thirty years ago, Sections 232 and 242 have undergone only a limited number of modifications, with the result that the Act does not entirely reflect or accommodate the changing methodology and regulation of health care and assisted living delivery in the United States today. Two examples are found in the definitions of the types of facilities eligible for mortgage insurance, and in the Certificate of Need ("CON") requirements, and alternative procedures, for the hospital and nursing home programs.

With respect to the former, the narrow definitions of eligible facilities fail to reflect the "continuum of care" now commonly provided, within an individual facility or

in a campus environment, for purposes of operational and cost efficiency, and continuity of care. This is a shortcoming that would be corrected by the Amendments of H.R. 3995.

As to the Certificate of Need problem, mortgage insurance under the hospital and nursing home programs of Sections 242 and 232 of the Act is conditioned upon the receipt of state issued CONs. In fact, many states over the last twenty years have eliminated all or part of their CON programs, or the agencies that would normally have issued the certificates. Examples are Arizona, California, Colorado, Iowa, Kansas, New Mexico, Oregon, Texas and Wyoming among others. Because of this and other anachronisms in the FHA programs, otherwise needed projects would be ineligible for low interest rate FHA financing. While the Act contains alternative requirements for states in which CONs are no longer available, the alternative requirements, though well intended, have proven unworkable or difficult to implement, particularly with respect to hospital financing, with the result that FHA loan insurance may be unavailable to assist in meeting healthcare needs in those states. This impediment has made it difficult for FHA to diversify its loan portfolio geographically, and has also made it difficult, if not impossible, for "critical access hospitals," particularly in more sparsely populated rural and western states, to obtain needed financing to modernize facilities which may date back to the mid 1900's. The Amendments would solve this problem as well.

Without in any way intending to slight or diminish the stature of any portion of the Amendments (all of which we support), I would like now to examine in greater detail, and comment further upon, some of the more important areas of the Amendments which I

feel are of particular significance to the Subcommittee and to the continued success of the FHA programs:

Sec. 203, Insurance for Integrated Service Facilities Mortgages

Integrated Service Facility. The definition of Integrated Service Facility appears in this section of H.R. 3995. This is a technical amendment to existing law, and recognizes the changes to health care delivery methodology that have occurred over the years. Directed, as it is, toward the needs of our aging population, as well as to the sick, injured, disabled, or infirm, and for the prevention of illness, this new definition provides an FHA insurance authorization for new types of facilities for the same Americans intended to be covered originally by the National Housing Act, and recognizes the need to provide services on the most cost efficient and affordable basis. In addition, the definition includes facilities designed to provide a continuum of care, as determined by FHA, which affords FHA a greater ability to approve worthy, needed projects more suited to today's delivery environment, if the other definitional requirements of Section 203 are met.

Licensure. Another important element of Section 203 is the amendment to the assisted living facility licensure requirement of the Act. Unless a facility is licensed by the state or other political subdivision where the facility is located, the facility will be ineligible for FHA mortgage insurance under current law. In those states or subdivisions where no licensing is required or obtainable, otherwise worthy assisted living projects are precluded from the benefits of FHA mortgage insurance. Section 203 solves this problem

by permitting FHA to establish underwriting standards in lieu of licensure under those circumstances.

Sec. 204. Insurance for Mortgages for Integrated Service Facilities Owned in Connection with Hospitals

Definitions. This section updates the thirty-year old Section 242 definition of an eligible "Hospital" to permit recognition of current health care delivery methodology and advances in medical science and technology since the enactment of Section 242 so long ago. The archaic test that denies eligibility to some hospitals treating such illnesses as drug and alcoholic, epileptic, mental and tubercular would be eliminated. Today, some of these afflictions are recognized as acute in nature, and may be reimbursed on that basis in an acute care hospital. Furthermore, since acute care services (operating and emergency rooms, for example) are not permitted under the FHA nursing home program, the Section 242 rules, particularly in a "continuum of care" environment, created a financing void for hospitals providing significant services of the type proscribed in the existing definitions of the Act.

Hospital-Based Integrated Service Facilities. The definition of Integrated Service Facility introduced in Section 203 of H.R. 3995 is incorporated into Section 204 by reference. Such a facility, when owned by a hospital sponsor, will become eligible for FHA insurance under Section 242 of the Act. As hospitals continue to add low cost, non-acute outpatient and ambulatory services, the Act's acute care site oriented provisions

artificially limit FHA's ability to provide affordable capital to finance less costly, more efficient hospital-sponsored services. For example, the Act does not currently permit the separate financing of a hospital's non-acute care community health clinics for the care and prevention of illness, or laboratories and offices on sites separate and apart from the primary hospital site. This restriction would be eliminated by the Amendments.

Sec. 205. Insurance for Mortgages for Refinancing Debt of Existing Integrated Service Facilities.

Section 205 adds existing integrated service facilities to the list of projects which may be refinanced under Section 223(f) of the Act, and authorizes the insured loan to include additional costs such as repairs, maintenance, minor improvements, or additional equipment as may be approved by FHA, all of which is consistent with conventional refinancings and considered standard in the lending community. In addition to authorizing the refinancing of high rate long term debt, this section would permit an institution to escape from a cycle of expensive roll-overs of short or intermediate term conventional debt. The ability of existing facilities to refinance high rate uninsured mortgage loans will become even more important in those states which will benefit from the modification of the CON protocols as set forth in Section 206.

Sec. 206. Standards and Need for Health Care Facility Mortgage Insurance.

As I stated earlier, the Certificate of Need requirement of both the nursing home and hospital programs has been an impediment to health care delivery and capital formation in a number of states. Recognizing the evolving nature of regulation in many

areas of the country, an earlier amendment to the Act established, for states in which CONs were no longer obtainable, an alternative to the issuance of a CON; the alternate procedure has proven cumbersome, time consuming and difficult to implement.

While the basic CON requirement concept would not be altered, the Amendments would modify the alternate procedure to help assure that states without CON laws or implementing agencies would not be excluded from the FHA programs. The effect of this amendment will be to speed up and modernize the overall application process, relieve the state of unwanted burdens, and reduce costs. In addition, it will more effectively enable FHA to achieve geographic diversification in its insurance portfolio, a goal which has long been sought by FHA.

Conclusion.

In conclusion, Madam Chairwoman and distinguished Members of the Subcommittee, I would like to say that the Study Group supports H.R. 3995, and views it as a singularly important and timely measure for the benefit of the health care delivery system, FHA, and the American people for the following reasons:

1. It will help to assure the availability of **affordable**, low rate capital for projects for the sick, disabled and elderly in all areas of our country, rural as well as urban.
2. It will assist in reducing debt service costs as well as related expenses of state/federal cost based reimbursement.

3. Where reimbursement is based upon services rather than cost, lower debt service overhead will free additional project revenues for maintenance, modernization and the improvement of services.

4. H.R. 3995 will also help to maintain strong community job bases. Health care providers are often the largest neighborhood employers, enjoying strong philanthropic and community support. They may also become magnets for non-health care neighborhood and community improvement and preservation, as well as economic development.

5. The Amendments will assure the availability of low cost financing for new forms of integrated health care facilities (the continuum of care approach) which, to deal with changes in traditional revenue sources, are emerging as a means of providing the highest level of service at the lowest cost.

6. Sections 232 and 242 of the Act will continue to produce substantial revenues to the Treasury through FHA mortgage insurance premiums and fees.

Madam Chairwoman, this concludes my testimony. I thank the Chairwoman and the distinguished Members of the Subcommittee for the opportunity to appear before you today.