

Executive Memorandum

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THE MEDICARE TAX REVOLT OF 1989

Lawmakers returning to Washington for the new session of Congress have been engulfed in a torrent of angry letters from senior citizens. The reason: elderly Americans are extremely upset over the new taxes they must pay for the Medicare catastrophic legislation enacted last June. To fund expanded Medicare benefits, many Americans aged 65 or older must now pay a surtax of \$22.50 added to every \$150 they owe in regular income taxes. As a result they are paying 15 percent higher income tax rates than non-elderly Americans, in addition to a \$4 hike for all retirees in their monthly \$27.90 Medicare premiums.

Lawmakers received plenty of warning, but Congress consistently ignored critics who predicted that the new taxes would trigger a backlash among senior citizens. Instead, Congress and Reagan Administration Secretary of Health and Human Services Otis Bowen stubbornly persisted in enacting a bill that most of America's elderly neither needed nor wanted. Now lawmakers who authored and expanded the legislation, assuming they would win praise from senior citizens, find themselves the targets of angry retirees. Meanwhile, the handful of congressmen who voted against the bill are winning applause. And the American Association of Retired Persons (AARP), which strongly supported the legislation, is on the defensive. The organization's Washington office recently dispatched 150 speakers across the country in a desperate attempt to "sell" the catastrophic legislation to the elderly and calm a massive revolt within its own ranks.

Higher Taxes for 11 Million Seniors. The original sponsors of the legislation continue to insist that it benefits the elderly, claiming that the opposition is coming from a small number of wealthy retirees. But 35 percent of all retirees, or more than 11 million senior citizens, will be forced to pay the new Medicare surtax this year. Furthermore, both the tax rates and the percentage of elderly paying the tax will continue to grow in future years. The Congressional Budget Office (CBO), reports that 42 percent of the elderly, or 14 million retirees, will be paying the new tax by 1993 — and by that time the surtax rate will have climbed from today's 15 percent to 28 percent.

Congress should admit its mistake and correct the deficiencies and inequities of the 1988 catastrophic health legislation. Some members already have urged congressional leaders to reconsider the measure. For instance, a bipartisan group of 58 Congressmen, 24 of whom originally voted for the legislation, has sent a letter to Fortney "Pete" Stark and Henry Waxman, the California Democrats, who chair the health subcommittees of the House Ways and Means Committee and the Energy and Commerce Committee, asking for hearings on revising the legislation. The author of the letter, Harris Fawell, the Illinois Republican, also has introduced legislation to repeal the law and establish a commission to consider alternatives. A similar bill, introduced by William Archer, the Texas Republican and Ways and

Means Committee ranking minority member, would delay implementation of the law by one year while a commission studies its impact.

Freezing at 1989 Levels. One problem with such "time out" bills is that because the law has already gone into effect, on January 1 of this year, some Medicare patients have been receiving the new benefits. As a result, if Congress were simply to repeal the entire law, it would have to cancel benefits already being received.

A better alternative would be for the new benefits to be frozen at 1989 levels, while retaining the flat \$4 increase in the monthly premium (rising to \$7 in 1993) needed to fund them. Congress could then repeal the income surtax and buy time to consider further changes in the catastrophic legislation without reducing benefits currently being received by patients. As the law now stands, this could be done without undermining Medicare finances because the whole package of new benefits is to be phased in over several years. The most desirable but least expensive benefits, which expand hospital and skilled nursing coverage, take effect this year, and could be funded by the monthly premium increases alone, according to projections by the Congressional Budget Office. The less important, but much more expensive benefits, such as the cap on total physician expenses and the new prescription drug coverage, do not take effect for at least another year.

Better Proposals. After freezing the new benefits at 1989 levels and repealing the surtax, Congress could take a serious look at restructuring the Medicare program to provide the elderly with more appropriate health care protection. Numerous proposals for doing just that were advanced during the two years in which Congress and the Reagan Administration developed the catastrophic legislation. Among these:

- ◆ ◆ Restructure the deductibles and coinsurance in Medicare so that middle - and upper-class retirees pay a greater share of their routine medical expenses out-of-pocket. Medicare could then use the resulting savings to increase coverage for the poor elderly and finance catastrophic hospital care for all retirees needing it — without resorting to increased premiums or new taxes.

- ◆ ◆ Change the minimum standards for Medicare supplemental (Medigap) policies, as set forth in the 1980 Baucus Amendment, to require coverage for catastrophic hospital stays of more than 60 days. To cover the cost of this new benefit, insurers should be allowed to charge higher deductibles for such non-catastrophic services as out-patient physician care.

In their haste to buy the votes of elderly Americans with an expansion of Medicare, Congress and former Health and Human Services Secretary Bowen repeatedly rejected such sound ideas. This failure to consider alternatives produced legislation that was not only bad policy but bad politics. The Bush Administration and the new Congress should learn from the debacle and calm the anger of America's elderly by giving the nation real Medicare reform.

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For further information:

Edmund F. Haislmaier, "Catastrophic Health Legislation: Congress's Case of Medicare Malpractice," Heritage Foundation *Issue Bulletin* No. 139, April 18, 1988.

Sandra Christensen and Rick Kasten, "The Medicare Catastrophic Coverage Act of 1988," Congressional Budget Office Staff Working Paper, October 1988.