

# ISSUE BRIEF

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## CBO Report Echoes Trustees on Medicare, Social Security

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The 2012 Congressional Budget Office (CBO) long-term budget outlook illustrates a grim picture for the nation's fiscal future unless entitlements are reformed. In particular, spending on Medicare and Social Security is the largest driver of federal spending and debt. In combination with the 2012 trustees report, the projections in this latest CBO report present a compelling case to reform these entitlements now—before a European-style fiscal crisis forces needlessly painful policy changes on Americans.

**Unsustainable Growth in Federal Spending, Debt.** CBO predicts that spending on entitlements—Medicare, Medicaid, and Social Security—will grow from 10 percent of gross domestic product (GDP) today to a staggering 18.5 percent of GDP by mid-century.

By that time, U.S. publicly held debt would soar well beyond 250 percent of GDP. Many economists agree that economic growth is materially slowed when debt approaches the size of the economy. With debt at two-and-a-half times the size of the economy, the economic consequences would be devastating.

This unsustainable growth in spending and debt would also cause net interest costs on the U.S. federal debt to spiral to unbearable levels. CBO predicts that net interest costs will increase nearly sevenfold, surging from 1.4 percent of GDP today to 9.5 percent in 2037. This is particularly troubling as net interest costs already exceed spending for many government programs. By 2037, net interest costs—just the interest on the publicly held debt—would nearly equal spending on all discretionary programs, including national defense and education.

**Medicare at Risk.** The central fiscal challenge facing Medicare is the dramatic growth in its spending and debt. Demographic changes and rising health care costs have put Medicare on a path to crisis. Reform should be imminent if the federal health care program is to be affordable and fiscally sustainable in the future.

According to the 2012 trustees report,<sup>1</sup> Medicare Part A—the Hospital Insurance, or HI program, financed almost entirely by payroll taxes—will be insolvent starting in 2024. This insolvency date would have moved forward by one year to 2023 had it not been for Medicare cuts put in place in 2011 through the Budget Control Act sequestration that totaled almost \$100 billion over the next 10 years.<sup>2</sup> Part A has spent more than it has taken in through payroll taxes since 2008, and these cash deficits will continue well into the future.

Under current-law projections, Medicare's unfunded obligation (net present value)<sup>3</sup> to pay promised benefits over the 75-year period is approximately \$26.9 trillion. The more realistic assessment by the Medicare actuary, however, has projected the unfunded obligation to be about \$10 trillion higher at approximately \$36.9 trillion.

The vast gap between the two estimates of Medicare's long-term fiscal challenge result from a difference in policy scenarios. The Medicare actuaries take into account that some policies included in the trustees' estimate are unlikely to occur. For example, the Sustainable Growth Rate (SGR) is scheduled to cut Medicare

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This paper, in its entirety, can be found at <http://report.heritage.org/ib3638>

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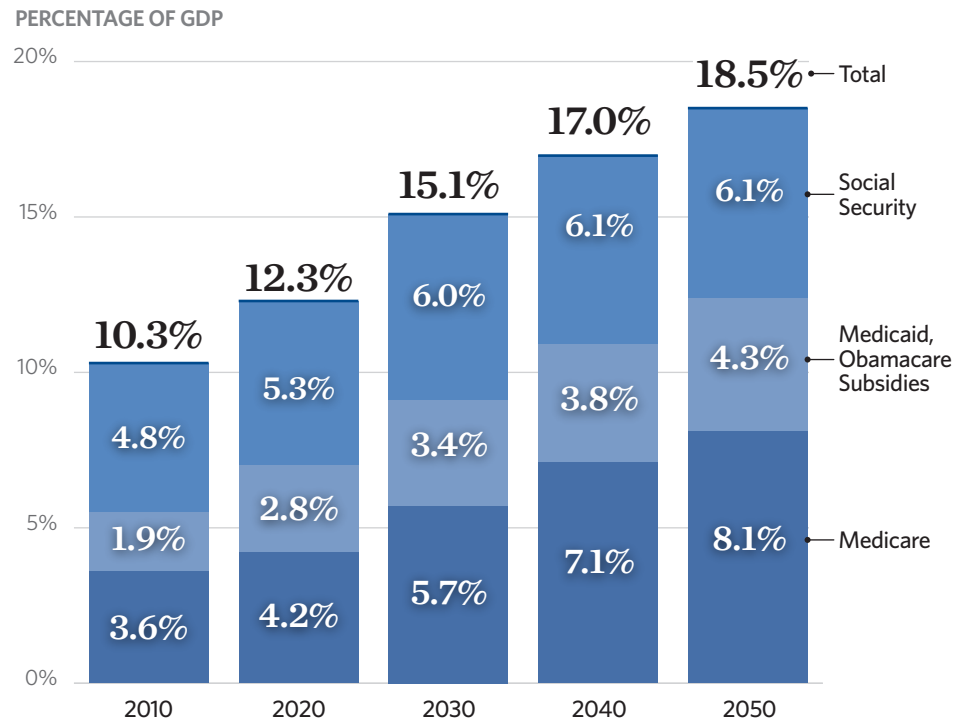
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CHART 1

## Entitlement Spending Will Nearly Double by 2050

*Spending on Medicare, Medicaid, Social Security, and the Obamacare subsidies will soar as 78 million baby boomers retire and health care costs climb. Total spending on federal health care programs will nearly double. Future generations will be left with an untenable debt burden.*

**Source:** Congressional Budget Office, 2012 *Long-Term Budget Outlook, Alternative Fiscal Scenario*, June 5, 2012, <http://www.cbo.gov/publication/43288> (accessed June 5, 2012).



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physician payments by 30 percent in 2013. However, Congress has over-ridden the implementation of the SGR every year since 2002. Similarly, the actuaries' alternative report assumes that cuts from Obamacare are unattainable and will not be fully implemented. It therefore projects that Medicare spending will surpass 10 percent of GDP, at which point it will devour more than half of all federal tax revenue. The status quo is unsustainable and, if maintained,

guarantees a Medicare crisis in the not-so-distant future.<sup>4</sup>

**Social Security Benefit Cuts on the Horizon.** Social Security's deficits are permanent and growing. Unless the program is reformed, everyone receiving Social Security benefits faces a benefit cut of about 25 percent as soon as 2033.

Social Security began running deficits in 2010. That year, the program spent \$49 billion more in benefits than it took in from its payroll

tax. In 2011, Social Security incurred a \$45 billion deficit. According to the 2012 trustees report,<sup>5</sup> the expected average annual gap between Social Security spending and the program's payroll tax revenue is \$66 billion between 2012 and 2018.

The amount of money Congress would have to invest today to pay for Social Security's promised benefits over the 75-year long-term horizon is \$11.3 trillion (net present value). This figure is the difference between what

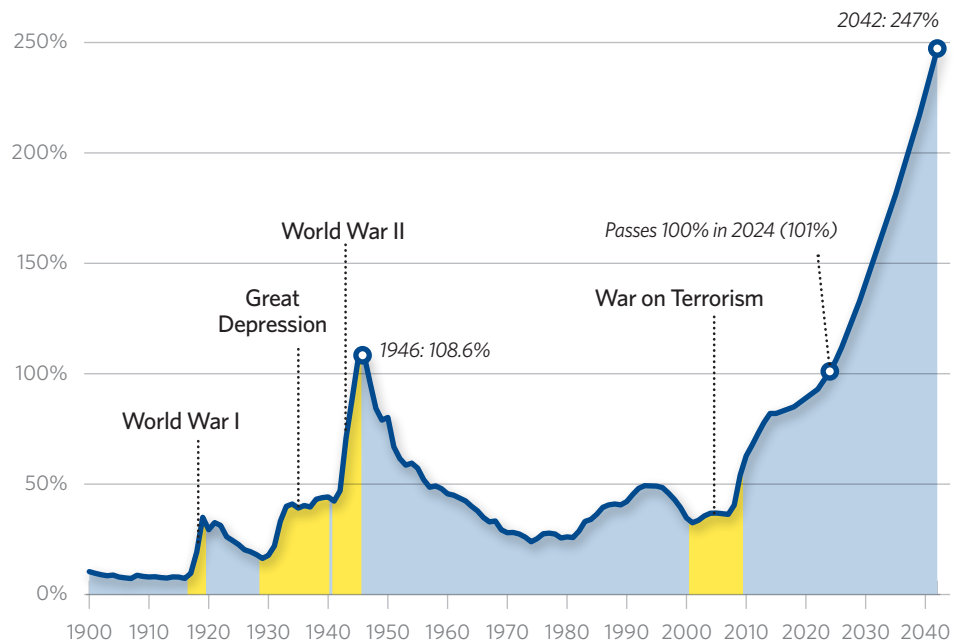
1. *2012 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and the Federal Supplemental Medical Insurance Trust Funds*, April 23, 2012, <http://cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/TR2012.pdf> (accessed June 13, 2012).
2. Richard Foster, Chief Actuary of Medicare, comments at the American Enterprise Institute, April 24, 2012.
3. Net present value is the amount of money that would have to be invested today in order to have enough money on hand to pay deficits in the future. This money would be *in addition to* what the program receives during those years from its payroll taxes.
4. Robert E. Moffit and Rea S. Hederman, Jr., "Medicare Trustees to America: A Bleak Future Without Real Reform," Heritage Foundation *Issue Brief* No. 3581, April 26, 2012, <http://www.heritage.org/research/reports/2012/04/medicare-trustees-2012-report-bleak-future-without-real-reform>.
5. *The 2012 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, U.S. Social Security Administration, April 23, 2012, <http://www.socialsecurity.gov/OACT/TR/2012/index.html> (accessed June 13, 2012).

CHART 2

## U.S. Federal Debt Will Explode to Economically Damaging Levels

*U.S. federal debt will explode to 100 percent of GDP—an economically damaging level—within only one decade. Publicly held debt is the part of U.S. federal debt most relevant to credit markets. It excludes intragovernmental debt, the amount that the government owes to specific programs or agencies, such as the Social Security Trust Fund.*

**Source:** U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2013* (Washington, D.C.: U.S. Government Printing Office, 2012), Historical Tables, <http://www.whitehouse.gov/omb/budget/Historicals> (accessed May 9, 2011); and Congressional Budget Office, *2012 Long-Term Budget Outlook, Alternative Fiscal Scenario*, June 5, 2012, <http://www.cbo.gov/publication/43288> (accessed June 5, 2012).



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Social Security owes in benefits and what it will receive in taxes.<sup>6</sup>

**Saving the American Dream with Entitlement Reform.** By all measures, Medicare and Social Security are on a path of perpetual deficits and debt. Successful reform would make these major federal entitlements more effective, efficient, affordable, and fiscally sustainable in the long run. As these are the major drivers of overall federal

spending and debt, Medicare and Social Security reform would further improve the prospects for robust economic growth.

Scaling back benefits for the most affluent seniors and focusing help on those who truly need it first would strengthen and preserve Medicare and Social Security. This is already a tried and true bipartisan solution for Medicare.<sup>7</sup> The Heritage Foundation's *Saving the*

*American Dream* plan lays out how to implement these entitlement reforms, along with other budget and tax reforms, to ensure long-term prosperity for current and future generations.<sup>8</sup>

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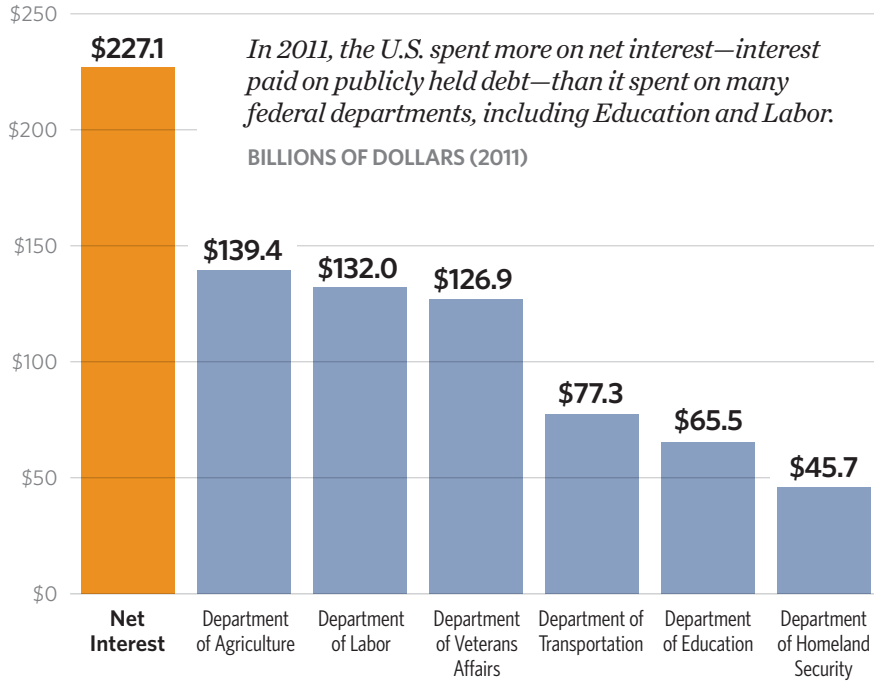
6. David C. John, "Social Security Finances Significantly Worse, Says 2012 Trustees Report," Heritage Foundation *Issue Brief* No. 3577, April 23, 2012, <http://www.heritage.org/research/reports/2012/04/social-security-finances-significantly-worse-says-2012-trustees-report>.

7. J.D. Foster, "The Good News in the Medicare Trustees Report," Heritage Foundation *Issue Brief* No. 3602, May 14, 2012, <http://www.heritage.org/research/reports/2012/05/medicare-trustees-report-reform-imminent>.

8. Stuart M. Butler, Alison Acosta Fraser, and William W. Beach, eds., *Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity*, The Heritage Foundation, 2011, <http://www.heritage.org/research/reports/2011/05/sang-the-american-dream-the-heritage-plan-to-fix-the-debt-cut-spending-and-restore-prosperity>.

CHART 3

### Interest on the Debt Exceeds Spending for Many Programs



**Source:** U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2013* (Washington, D.C.: U.S. Government Printing Office, 2012), <http://www.whitehouse.gov/omb/budget> (accessed May 9, 2011).

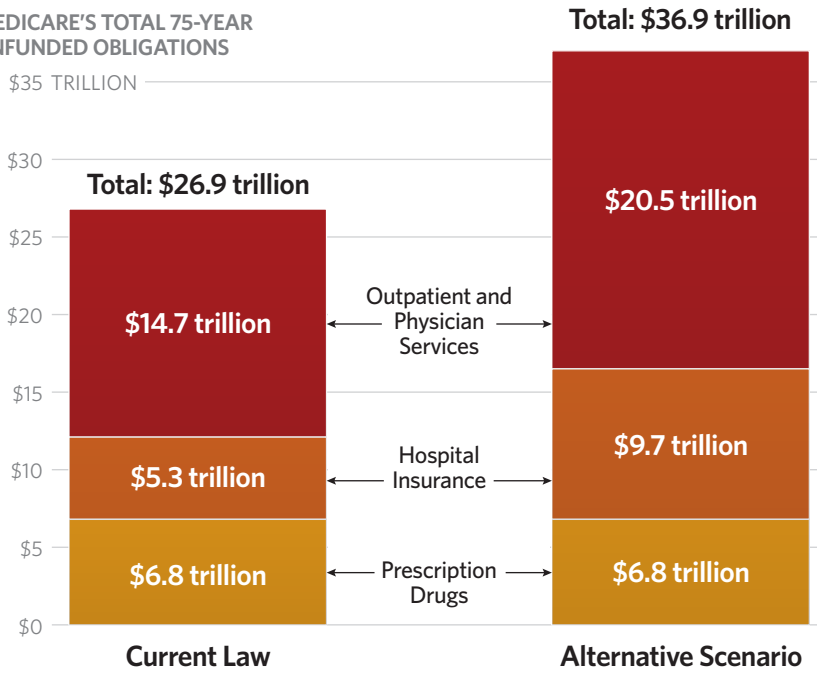
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CHART 4

## In Projecting Medicare's Cost, More Realistic Assumptions Show an Even Worse Outlook

*The Medicare trustees are required to base their projections on current law as it is written. These projections rely on unrealistic assumptions, such as Congress allowing staggering provider payment cuts that will harm seniors' access to care. The alternative scenario paints a more likely picture of the program's cost. Either way, the future is bleak.*

MEDICARE'S TOTAL 75-YEAR UNFUNDED OBLIGATIONS



**Source:** Suzanne Codespote, "Medicare Unfunded Obligations for 2012 Trustees Report," Centers for Medicare and Medicaid Services, Office of the Actuary, Letter to the Senate Budget Committee, April 23, 2012.

CHART 5

## Social Security Deficits Are Permanent and Growing

*Social Security began running deficits in 2010, paying out \$48.9 billion more in benefits than it received through payroll taxes. These deficits will never end without reforms. Social Security will exhaust its trust fund and add billions to the deficit and debt each year.*

**Source:** U.S. Social Security Administration, *The 2011 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, May 13, 2011, <http://www.ssa.gov/oact/tr/2011/index.html> (accessed February 9, 2012).

