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The 2014 Medicare Trustees Report: A Dire Future for Seniors and Taxpayers Without Reform

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The recently released annual Medicare trustees report reiterates a decades-old message: The Medicare program faces an unsustainable financial future. Unless the program is reformed, it will impose a huge financial burden on American taxpayers and jeopardize access to care for seniors.

While these facts are incontrovertible, the Obama Administration's allies and some in the media are touting the trustees report as official evidence that the "Medicare benefits are secure today"[1] or even "flush."[2] A four-year delay in Medicare trust fund insolvency and a temporary relief from annual cash deficits in the trust fund does not remotely indicate that the program is approaching financial stability. Indeed, media commentators routinely overlook the program's most fiscally significant metric: Medicare's enormous long-term debt, on the most realistic assumptions, currently ranges between $28 trillion and $35 trillion.[3]

Taxpayers and seniors should grasp the full meaning of some key facts concerning Medicare's current and future status.

Trust Fund Exhaustion Date Is 2030

The hospital insurance (HI) trust fund, which funds Medicare benefits for Part A (primarily inpatient hospital services) is financed almost entirely through the Medicare payroll deduction. The date when the trust fund balance is projected to hit zero fluctuates a bit each year, as it has for decades. This year, the trustees project that the trust fund will be depleted in 2030—four years later than last year's projection.

Since 2008, the trust fund has been running deficits, meaning that it is spending more on benefits than it takes in through payroll taxes; and it is expected to continue to do so through 2014.[4] But the trustees now project a brief period of surpluses from 2015 to 2023. In 2023, the HI cash deficits are projected to resume and continue until the trust fund is depleted in 2030.

Trust fund depletion means that Part A benefits can be paid out only to the extent that money comes in; meaning that seniors will experience a benefit reduction, workers a new tax increase, or some combination of both. In a July 2014 report, the Congressional Budget Office (CBO) estimated that the size of the gap in funding between expenditures and revenue in Part A is 0.8 percent over the next 25 years, worsening in the future[5]:

> Eliminating a gap of that size would require an immediate and permanent increase in HI payroll taxes from 2.9 percent to 3.7 percent [about a 28 percent increase] of taxable payroll as currently projected, an immediate and permanent cut in spending on Part A equal to about one-fifth of current spending, or some combination of tax increases and spending cuts with an equal present value.

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Medicare's Long-Term Financial Challenge

HI trust fund insolvency is only one marker of Medicare's fiscal health. Indeed, the entirety of Medicare's fiscal challenge is far more dramatic, making Medicare the nation's largest spending problem. The Medicare actuary estimates that, under the most realistic set of policy assumptions, Medicare has a long-term unfunded obligation ranging between $28 trillion and $35 trillion.[6] This means that the federal government has promised tens of trillions of dollars' worth of Medicare benefits that it does not currently have the money to pay for over the next 75 years.

While this issue is routinely overlooked, the sheer enormity of these obligations is America's greatest entitlement challenge. The current path is unsustainable, as many government officials and independent analysts have long argued, and it guarantees massive tax increases, benefit cuts, or some combination of both if real structural reform of the program is not implemented soon.

Obamacare Increases the Likelihood of Access and Quality-of-Care Issues for Medicare Beneficiaries

The Obama Administration's major tool to achieve "cost control" is the mandatory Medicare payment reductions enacted in Obamacare. The national health law imposes record-breaking payment reductions on Medicare providers, yielding an estimated $716 billion in savings in the initial 10 years of the law.[7]

This strategy guarantees access problems for seniors. Of those payment reductions, the CBO estimates that more than $500 billion fall on Part A providers, which include hospitals, home health agencies, skilled nursing facilities, and hospices. The Medicare trustees say that if these cuts are implemented as the law currently requires, they could cause access and quality-of-care issues for seniors as Medicare's payment falls increasingly below providers' costs:

> Simulations suggest that up to 5 percent more hospitals would experience negative total facility margins by 2019 and an additional 5–10 percent would experience negative Medicare margins by 2019....
>
> By 2040, simulations suggest that approximately half of hospitals, two-thirds of skilled nursing facilities, and 90 percent of home health agencies would have negative total facility margins, raising the possibility of access and quality of care issues for Medicare beneficiaries....
>
> Providers could not sustain continuing negative margins and would have to withdraw from serving Medicare beneficiaries or (if total facil-

1. Press release, "Statement of Secretary Lew on the Release of the Social Security and Medicare Trustees Reports," U.S. Department of the Treasury, July 28, 2014, http://www.treasury.gov/press-center/press-releases/Pages/jl2589.aspx (accessed July 31, 2014).
2. Julie Rovner, "Good News for Boomers: Medicare's Hospital Trust Fund Appears Flush Until 2030," Kaiser Health News, July 28, 2014, http://www.kaiserhealthnews.org/Stories/2014/July/28/Medicare-trustees-say-fund-will-last-until-2030.aspx (accessed July 31, 2014).
3. Suzanne Codespote, "Medicare Unfunded Obligations for 2014 Trustees Report," U.S. Department of Health and Human Services, Centers for Medicare and Medicaid Services, Office of the Actuary, letter to the Senate Budget Committee, July 28, 2014, http://themorningconsult.com/wp-content/uploads/2014/07/CMS-Actuary-memo-on-Medicare-75yr-unfunded-obligation-2014-Trustees-Report-1.pdf (accessed July 30, 2014).
4. U.S. Department of Health and Human Services, Centers for Medicare and Medicaid Services, *2014 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplemental Medical Insurance Trust Funds*, July 28, 2014, p. 25, http://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/downloads/tr2014.pdf (accessed July 30, 2014).
5. Congressional Budget Office, "The 2014 Long-Term Budget Outlook," July 15, 2014, p. 43, http://www.cbo.gov/sites/default/files/cbofiles/attachments/45471-Long-TermBudgetOutlook_7-29.pdf (accessed July 30, 2014).
6. Codespote, "Medicare Unfunded Obligations for 2014 Trustees Report."
7. Douglas W. Elmendorf, Director, Congressional Budget Office, letter to Speaker John Boehner (R–OH), U.S. House of Representatives, July 24, 2012, pp. 13–14, http://www.cbo.gov/sites/default/files/cbofiles/attachments/43471-hr6079.pdf (accessed July 29, 2014). The letter estimates the cost of repealing Obamacare, which would increase Medicare spending due to the absence of Obamacare's Medicare cuts. If Obamacare were repealed, the CBO states, "[w]ithin Medicare, net increases in spending for the services covered by Part A (Hospital Insurance) and Part B (Medical Insurance) would total $517 billion and $247 billion, respectively. Those increases would be partially offset by a $48 billion reduction in net spending for Part D."

ity margins remained positive) shift substantial portions of Medicare costs to their non-Medicare, non-Medicaid payers.[8]

The Administration's current course is a "lose-lose" proposition for seniors and taxpayers alike. If the strategy is successful, reduced access to care among seniors is virtually guaranteed. If it is unsuccessful, the Medicare financial condition simply worsens, and taxpayers face even higher costs. Both the CBO and the Medicare actuary have formally stated that the President's payment-reduction strategy is politically difficult to sustain and unrealistic.[9]

The Baby-Boomer Challenge

The baby-boomer generation (those persons born between 1946 and 1965) is retiring and, since 2011, has been flooding the Medicare program with an estimated additional 10,000 beneficiaries per day. This vast influx of new enrollees will continue to join the ranks of the Medicare beneficiaries until 2030—growing the Medicare population from about 52 million in 2013 to about 81 million.

The sheer size of the Medicare population poses a significant problem for Medicare financing. Medicare is a "pay-as-you-go" program, meaning current workers fund current beneficiaries' benefits. Today, taxpayers fund roughly 90 percent of total Medicare spending. Historically, there were four workers per Part A beneficiary from 1980 to 2008. In 2013, as the trustees point out, the ratio had declined to about 3.2 workers to pay for each beneficiary's Part A benefit and is expected to decline further to 2.3 workers per beneficiary in 2030.[10]

Limited and Unpleasant Options Without Reform

Given the magnitude of the Medicare challenge, there are only a few options available to policymakers. The first is raising general or payroll taxes to cover the rapidly rising costs of the Medicare program. This would mean levels of taxation unlike Americans have ever seen, reducing disposable income for younger families, small businesses, and private-sector capital investment.

The second option is to double down on provider payment cuts with the certain knowledge that ever-deeper cuts will make it increasingly difficult for health care providers to continue to offer the level or quality of care that seniors are getting today. It also means that the practice environment for physicians will worsen, aggravating the already dangerous physician shortage that baby boomers are facing.

A Better Medicare Future Through Market Competition

Serious public policy problems, no matter how difficult, are not unsolvable. Medicare beneficiaries need not be consigned to a frustrating future of stingy medicine delivered by a shrinking number of demoralized doctors. American taxpayers need not be sentenced to a future of enormous debt, explosive taxation, or a lower standard of living.

Though Heritage and other conservatives opposed the creation of a universal drug entitlement in the Medicare program in 2003, private competition in Medicare Part D has an outstanding record of success.[11] Congress can build upon the defined-contribution (premium support) payment structure that is already used in Part D, a competitive system

8. Centers for Medicare and Medicaid Services, *2014 Annual Report*, pp. 208–209.
9. U.S. Department of Health and Human Services, Centers for Medicare and Medicaid Services, Office of the Actuary, "Projected Medicare Expenditures under Current Law, the Projected Baseline, an Illustrative Alternative Scenario," July 28, 2014, http://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/2014TRAlternativeScenario.pdf (accessed July 30, 2014).
10. Centers for Medicare and Medicaid Services, *2014 Annual Report*, pp. 67.
11. See Robert E. Moffit, "Expanding Choice Through Defined Contributions: Overcoming a Non-Participatory Health Care Economy," *Journal of Law, Medicine and Ethics*, Vol. 40, No. 3, (Fall 2012), pp. 558–573, http://onlinelibrary.wiley.com/doi/10.1111/j.1748-720X.2012.00689.x/abstract (accessed July 31, 2014). See also Robert E. Moffit and Alyene Senger, "Real Medicare Reform: Why Seniors Will Fare Better," Heritage Foundation *Backgrounder* No. 2800, May 20, 2013, http://www.heritage.org/research/reports/2013/05/real-medicare-reform-why-seniors-will-fare-better.

of private drug plans. Part D has injected intense competition into drug coverage. The CBO, for example, has estimated that Medicare premium support could save both taxpayers and seniors money.[12] This approach, properly crafted,[13] would not only enhance the solvency of the Medicare program but also help to secure a balanced federal budget and help maintain that balance indefinitely.

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12. Congressional Budget Office, "A Premium Support System for Medicare: Analysis of Illustrative Options," September 18, 2013, http://www.cbo.gov/sites/default/files/cbofiles/attachments/09-18-PremiumSupport.pdf (accessed July 31, 2014). See also Robert E. Moffit and Rea S. Hederman, "CBO Confirms: Medicare Premium Support Means Savings for Taxpayers and Seniors," Heritage Foundation *Backgrounder* No. 2878, February 3, 2014, http://www.heritage.org/research/reports/2014/02/cbo-confirms-medicare-premium-support-means-savings-for-taxpayers-and-seniors.
13. See Stuart M. Butler, Alison Acosta Fraser, and William W. Beach, "Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity," Heritage Foundation *Special Report* No. 91, May 10, 2011, http://www.heritage.org/research/reports/2011/05/saving-the-american-dream-the-heritage-plan-to-fix-the-debt-cut-spending-and-restore-prosperity.