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WHAT YOU NEED TO KNOW ABOUT PREMIUM SUPPORT
By Paul N. Van de Water

The budget resolution that House Budget Committee Chairman Paul Ryan (R-WI) will unveil this week is expected to include a Medicare premium support proposal fashioned by Ryan and Senator Ron Wyden (D-OR). Although billed as a kinder, gentler form of premium support, the Ryan-Wyden plan has the same basic features as earlier premium support proposals.1

The Ryan-Wyden plan would shift substantial costs to Medicare beneficiaries rather than protect them from cost increases, in part because the payment that beneficiaries would receive to help them buy coverage would likely fail to keep pace with health care costs. The plan also would likely lead to the gradual demise of traditional Medicare by making the pool of Medicare beneficiaries smaller, older, and sicker — and increasingly costly to cover. Finally, the plan would produce few budgetary savings beyond those that the health reform law calls for, since both plans have the same target growth rate for Medicare costs. The Ryan-Wyden plan is similar to Newt Gingrich’s 1995 proposal that, according to Gingrich, would have caused traditional Medicare to “wither on the vine.”

Premium Support Shifts Significant Costs to Medicare Beneficiaries

The Ryan-Wyden plan would replace Medicare’s guarantee of health coverage with a flat payment, or voucher, that beneficiaries would use to purchase either private health insurance or traditional Medicare.2 The value of the voucher would initially equal the cost of the second-lowest-cost private plan in an area or traditional Medicare, whichever is less. As a result, the impact of the proposal on individual beneficiaries would differ significantly depending on whether traditional Medicare or private plans provided less costly coverage in their particular area of the country. In areas where Medicare incurs relatively high costs, the amount of the voucher would equal the cost of an inexpensive private plan, and beneficiaries would have to pay higher premiums to participate in traditional Medicare. In areas with relatively low Medicare spending, beneficiaries who wanted to

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1 For a detailed examination of the main issues that premium support raises, see Paul N. Van de Water, Converting Medicare to Premium Support Would Likely Lead to Two-Tier Health Care System, Center on Budget and Policy Priorities, September 26, 2011, [http://www.cbpp.org/cms/?fa=view&id=3589](http://www.cbpp.org/cms/?fa=view&id=3589).

enroll in a private plan would face higher premiums or fewer benefits, or might find that no private plan was available.

The Ryan-Wyden plan would limit the rate of growth of the voucher from year to year to the rate of growth of gross domestic product (GDP) per capita plus one percentage point — an amount that is likely to fall short of the actual rate of growth of health care costs. Although the plan would give Congress a period of time in which it could cut provider payment rates or make other changes to limit the growth of Medicare spending, the plan includes no mechanism that would reduce the cost of the Medicare benefit package to fit within the shrinking premium support payment. As a result, seniors would have to pay more to keep the health plans and the doctors that they like, or they would get fewer benefits.

Most Medicare beneficiaries live on modest incomes and are not in a position to pay much more for their health care. The median income of Medicare households is about $25,000 a year, and only about 15 percent of Medicare households have total household incomes over $50,000. Medicare households also spend three times as large a percentage of their budgets on out-of-pocket health expenses — 15 percent compared to 5 percent — as non-Medicare households do. The Ryan budget thus would significantly raise the out-of-pocket health costs that Medicare beneficiaries with modest incomes face, even as it proposes tax cuts for the wealthiest Americans.

Premium Support Slowly but Surely Undermines Traditional Medicare

Ryan and Wyden claim that their proposal guarantees that traditional Medicare “will always be offered as a viable and robust choice.” Unfortunately, that’s not the case. Under premium support, traditional Medicare would tend to attract a less healthy pool of enrollees, while private plans would attract healthier enrollees (as occurs today with Medicare and private Medicare Advantage plans). Although the proposal calls for “risk adjusting” payments to health plans — that is, adjusting them to reflect the average health status of their enrollees — the risk adjustment process is highly imperfect and captures only part of the differences in costs across plans that stem from differences in the health of enrollees.

Inadequate risk adjustment would mean that traditional Medicare would be only partially compensated for its higher-cost enrollees, which would force Medicare to raise beneficiary premiums to make up the difference. The higher premiums would lead more of Medicare’s healthier enrollees to abandon it for private plans, very possibly setting off a spiral of rising premium costs and falling enrollment for traditional Medicare. Over time, traditional Medicare would become less financially viable and could unravel — not because it was less efficient than the private plans, but because it was competing on an unlevel playing field in which private plans captured the healthier beneficiaries and incurred lower costs as a consequence. Ryan-Wyden also would allow private plans to tailor their benefit packages to attract healthier beneficiaries and deter sicker ones, which only makes this outcome more likely.

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Ryan and Wyden say that their proposal would not affect people age 55 and older, but this claim is unlikely to be true. As fewer new beneficiaries enrolled in traditional Medicare at age 65, the population in traditional Medicare would gradually get older, sicker, fewer in number, and much more expensive per person to cover. Moreover, as the size of the Medicare population shrunk, administrative costs would rise relative to benefit payments, traditional Medicare’s power to demand lower payment rates from providers would erode, and providers would have less incentive to participate in the program. As a result, people now age 55 and older might well face higher premiums and cost sharing for traditional Medicare, a more limited choice of providers, or both.

Ryan-Wyden Plan Produces Little Additional Budgetary Savings

Health reform (the Affordable Care Act) takes steps to slow the growth of health care costs through delivery system reforms, such as accountable care organizations, bundled payments, and comparative effectiveness research. As a backstop, it creates an Independent Payment Advisory Board (IPAB) that is required to produce proposals to hold Medicare cost growth per beneficiary to the rate of growth of GDP per capita plus one percentage point, and those proposals will take effect automatically unless the President and Congress enact legislation to overturn them. This is the same growth rate that Ryan-Wyden promises, so Ryan-Wyden likely would produce few additional budgetary savings. Rather, it would produce the savings in a different manner.

There are two key differences. First, Ryan-Wyden would deny Medicare much of its ability to serve as a leader in controlling costs by depriving it of the considerable market power it secures from its large enrollment. Ryan-Wyden would rely instead on multiple private insurance plans, which have proven much less effective than Medicare in driving cost control on their own. Traditional Medicare also has much lower administrative costs, amounting to roughly 2 percent of spending compared to about 11 percent of spending for private Medicare Advantage plans. For these reasons, the Congressional Budget Office’s analysis of Ryan’s previous premium support

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Large Majority of Americans Oppose Premium Support

A recent Kaiser Family Foundation health tracking poll finds that 70 percent of Americans would prefer to keep Medicare as it is today, with the government guaranteeing seniors health insurance and making sure everyone is eligible for the same set of benefits. Only 25 percent want the program changed to a premium-support system in which the government would guarantee each senior a fixed amount of money toward health care.

According to Kaiser, “There is remarkable agreement on this issue by age, with at least two thirds in each age group supporting keeping Medicare as it is.” Eighty-three percent of Democrats, 71 percent of independents, and 53 percent of Republicans say that they would prefer to keep Medicare as it is currently structured, rather than adopt premium support.

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proposal found that replacing traditional Medicare with private health plans would drive up total health care spending attributable to Medicare beneficiaries (the beneficiaries’ share plus the government’s share).  

Second, under current law, if the cost-growth target is missed, IPAB is charged with developing proposals to produce the requisite savings while shielding beneficiaries. Health reform specifically prohibits the board from rationing health care, raising Medicare’s premiums or cost sharing, cutting benefits, or restricting eligibility. It must focus exclusively on proposals that achieve savings in the payment and delivery of health care services. Under Ryan-Wyden, in contrast, beneficiaries would bear the brunt of offsetting the added costs, unless Congress chose to intervene.

Claim That Medicare Will Go Bankrupt Is False

Some advocates of premium support attempt to scare people into supporting such a dramatic change by falsely claiming that it is necessary to keep Medicare from going bankrupt. In fact, the program is not on the verge of bankruptcy or ceasing to operate.  

The 2011 report of Medicare’s trustees finds that Medicare’s Hospital Insurance (HI) trust fund will remain solvent — that is, able to pay 100 percent of the costs of the hospital insurance coverage that Medicare provides — through 2024; at that point, the payroll taxes and other revenue deposited in the trust fund will be sufficient to pay 90 percent of Medicare hospital insurance costs. Over the next 75 years, revenue will cover an average of 83 percent of Medicare’s hospital insurance costs. This shortfall will need to be closed through the provision of additional revenues, program changes that slow the growth in costs, or most likely both. But the Medicare Hospital Insurance program will not run out of all financial resources and cease to operate after 2024.

Health reform has significantly improved Medicare’s long-term financial outlook. Under the trustees’ main projection, the HI program faces a shortfall over the next 75 years equal to 0.79 percent of taxable payroll — that is, 0.79 percent of the total amount of earnings that will be subject to the Medicare payroll tax over this period. The Medicare actuary estimates that if health reform were repealed, HI’s long-term shortfall would increase from 0.79 percent to 3.89 percent of taxable payroll. Under that analysis, health reform has reduced the size of HI’s shortfall by four-fifths. Without health reform, the Medicare Hospital Insurance program would become insolvent eight years earlier, in 2016. Even under the Medicare actuary’s alternative scenario, in which only about 60 percent of health reform’s Medicare savings are achieved, the projected insolvency date of the HI trust fund remains at 2024, and the program’s long-run shortfall is reduced by nearly one-half.  

7 Douglas W. Elmendorf, Director, Congressional Budget Office, Letter to the Honorable Paul Ryan, April 5, 2011.
9 Office of the Actuary, Centers for Medicare & Medicaid Services, Memorandum to the Subcommittee on Health, House Committee on Ways and Means, June 21, 2011.
Although Medicare continues to face substantial long-term financial challenges stemming from the aging of the population and the continued rise in costs throughout the U.S. health care system, adopting a premium support system would represent a big step in the wrong direction. Traditional Medicare — rather than private health insurance — has been the leader in instituting reforms in the health care payment system to improve efficiency and constrain costs. Because of its large buying power, Medicare can secure the implementation of payment and delivery system reforms that private insurance companies lack the market clout themselves to extract from health care providers. Historically, Medicare has instituted reforms, such as prospective payment systems for hospitals and other health care providers, and private insurance companies have followed Medicare’s lead. Indeed, partly because of its record of innovation, Medicare has outperformed private insurance in holding down the growth of health costs. Between 1970 and 2009, Medicare spending per enrollee grew by an average of one percentage point less each year than comparable private health insurance premiums.

Health reform envisions that Medicare will continue to lead the way in efforts to slow health care costs while improving the quality of care. In contrast, premium support would weaken Medicare’s ability to promote cost reduction throughout the health care system, likely resulting in higher total health costs. This makes it all the more important that policymakers and the American public not be driven into adopting such a radical proposal by misleading claims that Medicare is on the verge of “bankruptcy” or that our budgetary problems require us to adopt premium support.