

Updated July 3, 2018

Medicare Is Not “Bankrupt”

By Paul N. Van de Water

Claims by some policymakers that the Medicare program is nearing “bankruptcy” are highly misleading. Although Medicare faces financing challenges, the program is not on the verge of bankruptcy or ceasing to operate. Such charges represent misunderstanding (or misrepresentation) of Medicare’s finances.

The 2018 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 2026. Even in 2026, when the HI trust fund is projected to be depleted, incoming payroll taxes and other revenue will still be sufficient to pay 91 percent of Medicare hospital insurance costs.¹ The share of costs covered by dedicated revenues will decline slowly to 78 percent in 2042 and then rise gradually to 85 percent in 2092. This shortfall will need to be closed through raising revenues, slowing 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 2026, as the “bankruptcy” term may suggest.

The 2026 date does not apply to Medicare coverage for physician and outpatient costs or to the Medicare prescription drug benefit; these parts of Medicare do not face insolvency and cannot run short of funds. These parts of Medicare are financed through the program’s Supplementary Medical Insurance (SMI) trust fund, which consists of two separate accounts — one for Medicare Part B, which pays for physician and other outpatient health services, and one for Part D, which pays for outpatient prescription drugs. Premiums for Part B and Part D are set each year at levels that cover about 25 percent of costs; general revenues pay the remaining 75 percent of costs.² The trustees’ report does not project that these parts of Medicare will become insolvent at any point — because they can’t. The SMI trust fund always has sufficient financing to cover Part B and Part D costs, because the beneficiary premiums and general revenue contributions are specifically set at levels to assure this is the case. SMI cannot go “bankrupt.”

The outlook for the HI trust fund has worsened somewhat since last year, largely as a result of actions by the Trump Administration and Congress. The 2017 tax law reduces

¹ Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds, *2017 Annual Report*, June 5, 2018, p. 28, <https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/TR2018.pdf>.

² Upper-income beneficiaries pay higher, income-related premiums. Low-income beneficiaries receive premium subsidies.

income taxes on Social Security benefits, part of which go to the HI trust fund. Repealing the tax penalty for failing to get health insurance (also part of the tax law) will increase the number of uninsured and increase Medicare payments for uncompensated care. Policymakers also repealed the Independent Payment Advisory Board, which was projected to help slow Medicare's cost growth. And the Administration has failed to address excessive Medicare Advantage payments due to insurance company assessments of their beneficiaries that make them appear less healthy than they are.

The trustees' latest projections are broadly in line with those that the trustees have issued for some time. Since 1970, changes in the law, the economy, and other factors have brought the projected year of Medicare HI insolvency as close as two years away or pushed it as far as 28 years into the future.³ The latest projection falls within that spectrum. Trustees' reports have been projecting impending insolvency for over four decades, but Medicare has always paid the benefits owed because Presidents and Congresses have taken steps to keep spending and resources in balance in the near term. In contrast to Social Security, which has had no major changes in law since 1983, the rapid evolution of the health care system has required frequent adjustments to Medicare, a pattern that is certain to continue.

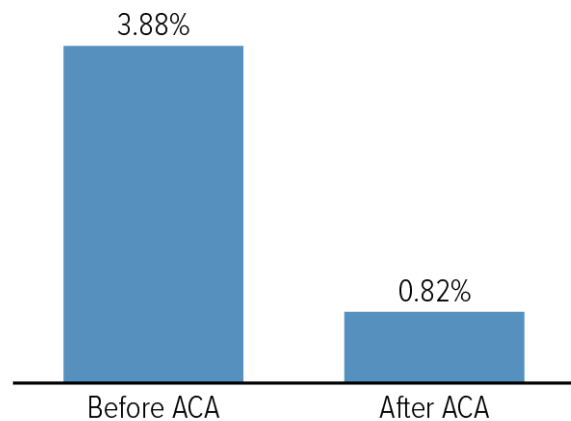
The Affordable Care Act (ACA), along with other factors, has significantly improved Medicare's financial outlook, boosting revenues and making the program more efficient. The HI trust fund is now projected to remain solvent eight years longer than before the ACA was enacted. And the HI program's projected 75-year shortfall of 0.82 percent of taxable payroll is much less than the 3.88 percent of payroll that the trustees estimated before health reform. (See Figure 1.) This means that Congress could close the projected funding gap by raising the Medicare payroll tax — now 1.45 percent each for employers and employees — to about 1.85 percent, or by enacting an equivalent mix of program cuts and tax increases.

Despite the improvements the ACA has made, Medicare continues to pose long-term budgetary challenges, stemming from the aging of the population and the continued rise in costs throughout the U.S. health care system. Total Medicare spending is projected to grow from 3.7 percent of gross domestic product (GDP) today to 5.9 percent in 2040.

FIGURE 1

Affordable Care Act (ACA) Significantly Improved Medicare's Finances

75-year shortfall in Hospital Insurance trust fund as a percent of taxable payroll



Note: Taxable payroll = payroll subject to the Medicare tax.

Source: 2009 and 2018 annual reports of the boards of trustees of the Medicare trust funds

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³ Patricia A. Davis, *Medicare: Insolvency Projections*, Congressional Research Service, June 18, 2018, <https://www.fas.org/sgp/crs/misc/RS20946.pdf>.

Medicare has been the leader in reforming the health care payment system to improve efficiency and has outperformed private health insurance in holding down the growth of health costs. Since 1987, Medicare spending per enrollee has grown by 5.4 percent a year, on average, compared with 6.8 percent for private health insurance.⁴ (See Figure 2.)

The ACA envisions that Medicare will continue to lead the way in efforts to slow health care costs while improving the quality of care. The research and pilot projects that the ACA establishes should yield important lessons. Until these efforts bear fruit, it will be difficult to achieve big additional reductions in Medicare expenditures.

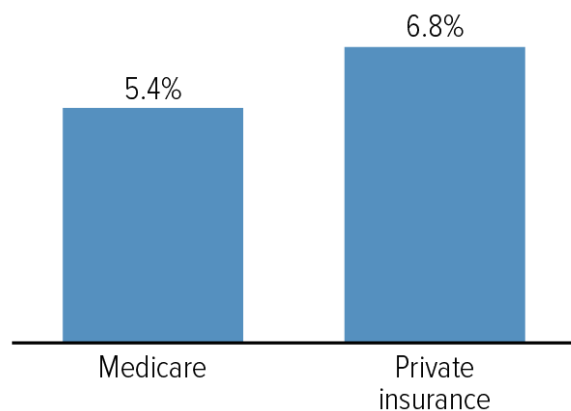
Some additional savings can be achieved over the next ten years, however, while preserving Medicare’s guarantee of health coverage and without raising the eligibility age or otherwise shifting costs to vulnerable beneficiaries. Possible measures include ending Medicare’s overpayments to pharmaceutical companies for drugs prescribed to low-income beneficiaries, increasing funding for actions to prevent and detect fraudulent and wasteful Medicare spending, further reducing overpayments to Medicare Advantage plans, and ensuring efficient payments to other health care providers.

A key fiscal policy goal is to stabilize the federal debt relative to the size of the economy. But it is neither necessary nor desirable to accomplish this by radically restructuring Medicare — such as through “premium support” proposals that would convert it to vouchers whose purchasing power fails to keep pace with the cost of health care — or by shifting more health care costs to Medicare beneficiaries, as the House Republican budget plan would do.⁵ Policymakers and the American public should not be driven into adopting such proposals by misleading claims that Medicare is on the verge of “bankruptcy” or is “unsustainable.” Instead, we should pursue a balanced deficit-reduction approach that puts all parts of the budget on the table, including revenues.

FIGURE 2

Medicare Spending per Beneficiary Has Grown More Slowly Than Private Insurance

Average annual growth rate per enrollee, 1987-2016



Source: Centers for Medicare & Medicaid Services, National Health Expenditure Tables, December 2017, Table 21

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⁴ Centers for Medicare & Medicaid Services, *National Health Expenditure Tables*, December 2017, Table 21, <https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/NationalHealthExpendData/NationalHealthAccountsHistorical.html>.

⁵ Joel Friedman and Richard Kogan, *House GOP Budget Retains Tax Cuts for the Wealthy, Proposes Deep Program Cuts for Millions of Americans*, Center on Budget and Policy Priorities, June 28, 2018, <https://www.cbpp.org/research/federal-budget/house-gop-budget-retains-tax-cuts-for-the-wealthy-proposes-deep-program-cuts>.