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CBPP STATEMENT

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Social Security and Medicare Face Manageable Financial Challenges, 2018 Trustees' Reports Confirm

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The financial outlook for Social Security is much the same as last year, with the program as a whole able to pay full benefits until 2034, while the outlook for Medicare's Hospital Insurance (HI) trust fund has worsened somewhat, according to new reports from the programs' trustees.

The trustees project that the HI trust fund will be depleted three years earlier than previously thought — in 2026. The 75-year HI shortfall has increased from 0.64 percent to 0.82 percent of taxable payroll, or 0.18 percentage points less favorable than estimated last year. Much of this deterioration is due to policy actions by the Administration and the Republican Congress, including the tax law enacted in 2017.

Social Security's Disability Insurance (DI) trust fund is now projected to be depleted in 2032 — four years later than projected last year and eight years later than projected two years ago — because of lower-than-expected applications for, and awards of, DI benefits. Social Security's retirement fund is now projected to be depleted one year earlier, in 2034. The size of Social Security's long-run shortfall is virtually unchanged.

Although both Social Security and Medicare face long-run financing challenges that must be addressed, the challenges are manageable. The programs are not "running out of money" or "going bankrupt," as critics sometimes suggest. Even if their trust funds were depleted, Social Security could still pay about three-fourths of scheduled benefits using its tax income and Medicare HI could pay about 80 percent or more, though such an outcome should not be acceptable.

The aging of the population is the major driver of the projected growth in Social Security and Medicare costs. The share of Americans 65 or older will grow by more than a third between now and 2040 as the baby boomers retire. That alone will raise Social Security spending from nearly 5 percent of gross domestic product (GDP) today to about 6 percent of GDP in 20 years, where it is expected to remain for the remainder of the 75-year projection period. Together with rising health care costs, the demographic shift will raise Medicare spending from 3.7 percent to 5.8 percent of GDP over the same period.

Social Security and Medicare benefits are not overly generous. The average Social Security retired worker benefit is $16,950 a year, and aged widows and disabled workers typically receive less. Medicare has significant cost-sharing requirements and gaps in coverage; as a result, Medicare households, on average, spend a much larger share of their budgets on health care costs than other households.

There is some room to trim Social Security benefits for high earners (particularly to use much or all of the proceeds to strengthen benefits for particularly vulnerable groups), and policymakers must take further steps to curb the growth of health care costs both in public programs — particularly Medicare — and in the private sector. But even with reasonable efforts to limit their growth, Social Security and Medicare will necessarily require a larger share of our nation's resources in the coming decades as the population ages. Social Security and Medicare are highly popular programs, and polls show a widespread willingness to support them through higher tax contributions.

Medicare

Much of the deterioration in the Medicare HI trust fund's outlook is due to actions by the Administration and the Congress over the past year. These include:

- Enacting the 2017 tax law, which reduces 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), which will increase the number of uninsured and increase Medicare payments for uncompensated care;
- Repealing the Independent Payment Advisory Board, which was projected to help slow Medicare's cost growth; and
- Failing to address higher Medicare Advantage (MA) payments due to insurance company assessments of their beneficiaries that make them appear less healthy than they are.

In fact, legislative changes and higher MA payments account for the entire increase in HI's 75-year shortfall, along with a major part of the change in the HI depletion date.

The change in the HI projections, however, should be kept in perspective. Since 1970, changes in the law, the economy, and other factors have brought the projected year of HI depletion as close as two years away or pushed it as far as 28 years into the future. 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.

Moreover, the Affordable Care Act (ACA), along with other factors, has significantly improved Medicare's financial outlook compared to what it was just a few years ago. 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. This means that policymakers could close the entire 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 a mix of program cuts and tax increases.

Social Security

The trustees' 2034 depletion date is for the combined Old-Age and Survivors Insurance (OASI) and DI trust funds, the traditional focus of their report. The two funds are legally separate, however. The trustees expect the OASI fund to remain solvent until 2034, and the DI fund through 2032. The significant improvement in the DI fund's outlook gives policymakers more time before they must revisit DI solvency and reduces any pressure for hasty action. This improvement is welcome news, though these are projections and could change, especially if there is a recession.

The number of DI applicants and beneficiaries has declined over the past several years, as demographic and economic pressures on the program have eased. Analysts largely anticipated this trend, since most of the recent growth in DI enrollment was due to demographic factors like the aging of the baby-boom generation, but the slowdown in enrollment has proved even greater than expected. As the boomers reach retirement, the number of workers receiving DI benefits has declined for four straight years. Likewise, DI applications, which spiked during the aftermath of the Great Recession, have fallen every year since 2010. The trustees project that the share of insured Americans receiving DI will remain relatively stable in coming decades, and costs will stay steady at about 0.75 percent of GDP.

Social Security's overall shortfall over the next 75 years — 2.84 percent of taxable payroll (which is the total wages and self-employment income subject to Social Security taxes), or 1 percent of GDP — is virtually identical to last year's estimate of 2.83 percent of taxable payroll.

The trustees caution that their projections are uncertain. For example, they estimate a 95 percent chance that Social Security's trust fund reserves will be depleted between 2030 and 2043. The Congressional Budget Office has estimated that exhaustion would occur in 2030. In no scenario would improved economic growth eliminate the shortfall, as Treasury Secretary Steven Mnuchin has implied.

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