

Paying for the Looming Medicare Expenditures: Options for the New Administration

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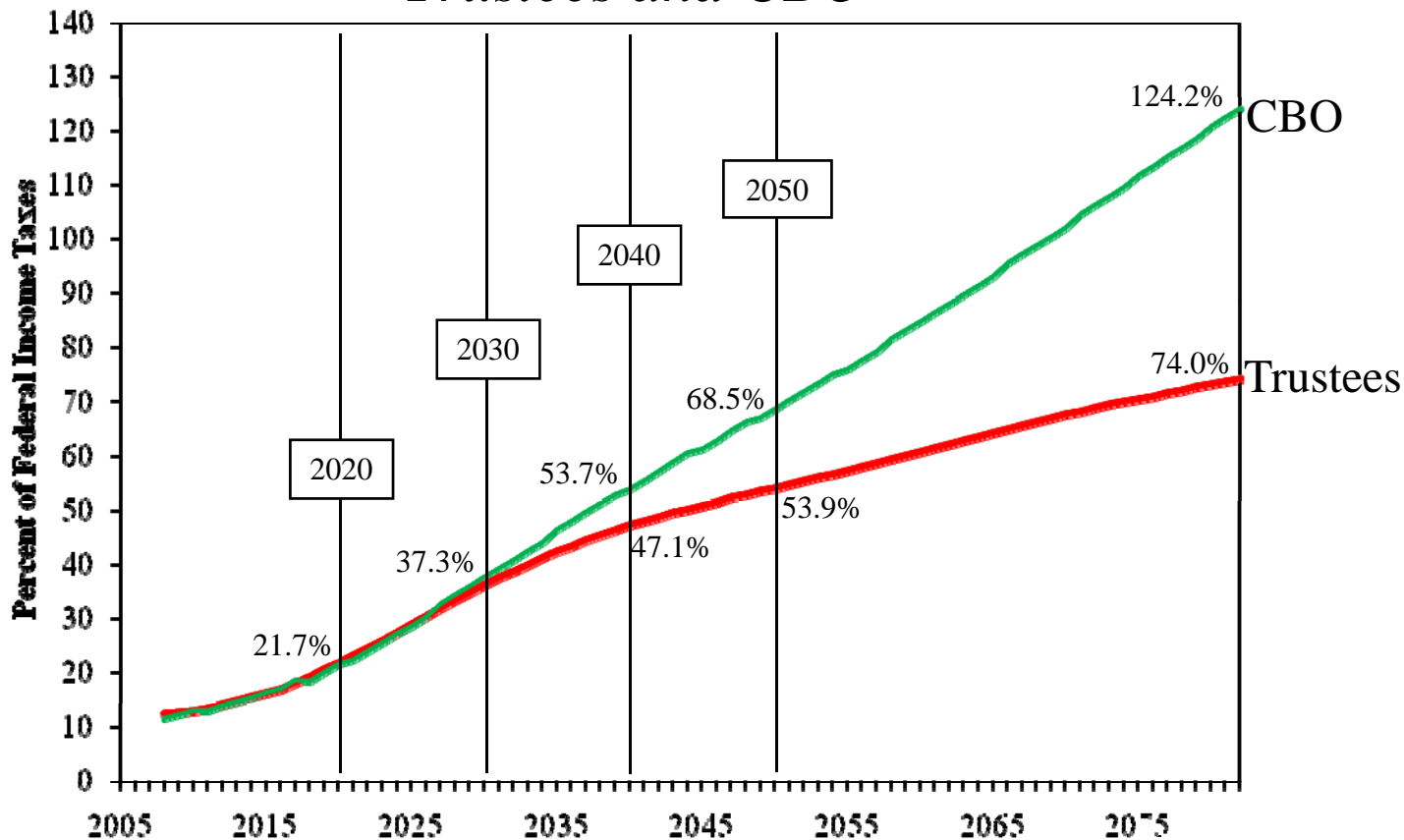
Some Startling Forecasts



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Medicare Funding Shortfalls as a Percent of Federal Income Taxes

Trustees and CBO

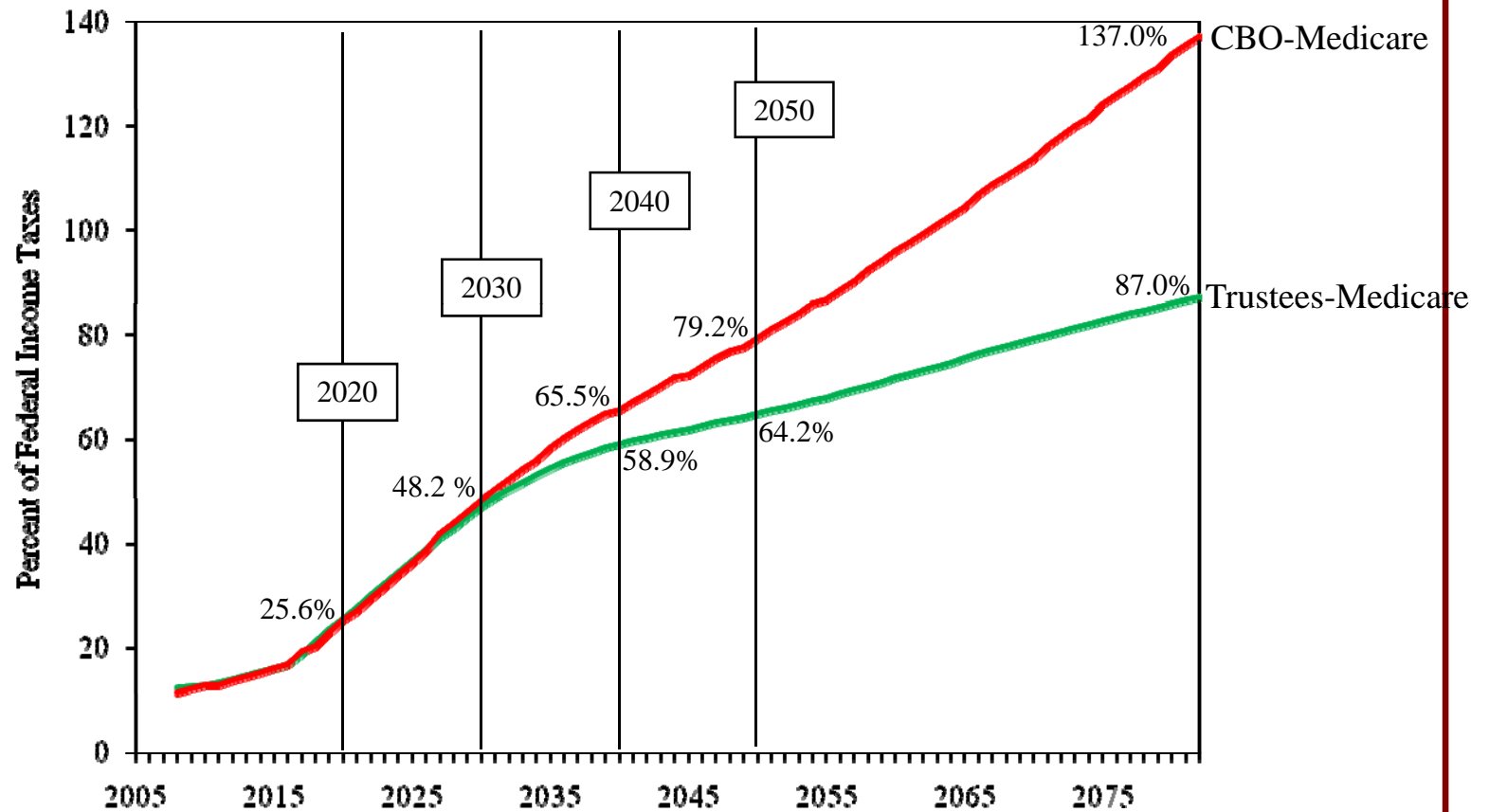


Source: 2008 Medicare Trustees Report, CBO “The Long-Term Outlook for Health Care Spending,” Nov. 2007 and author’s estimates. Federal Income Taxes are estimated to be 10.7% of GDP, the 50-year average.



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Social Security and Medicare Funding Shortfalls as a Percent of Federal Income Taxes



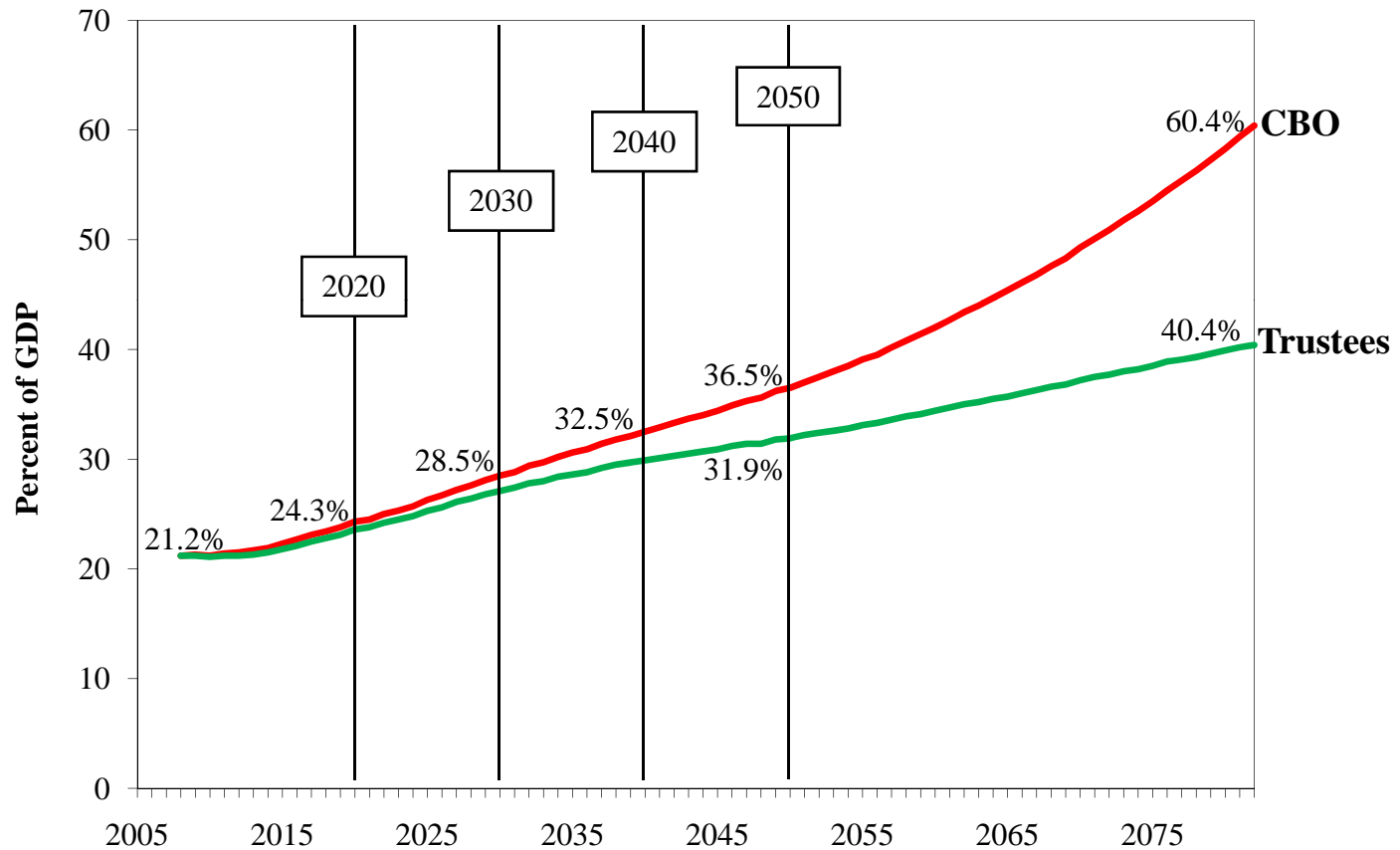
Source: 2008 Social Security and Medicare Trustees Reports, "The Long-Term Outlook for Health Care Spending," Congressional Budget Office, Nov. 2007 and author's estimates. Federal Income Taxes are estimated to be 10.7% of GDP, the 50-year average.



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Federal Government Share of GDP

Non-Entitlement Expenditures Remain at Current GDP Share

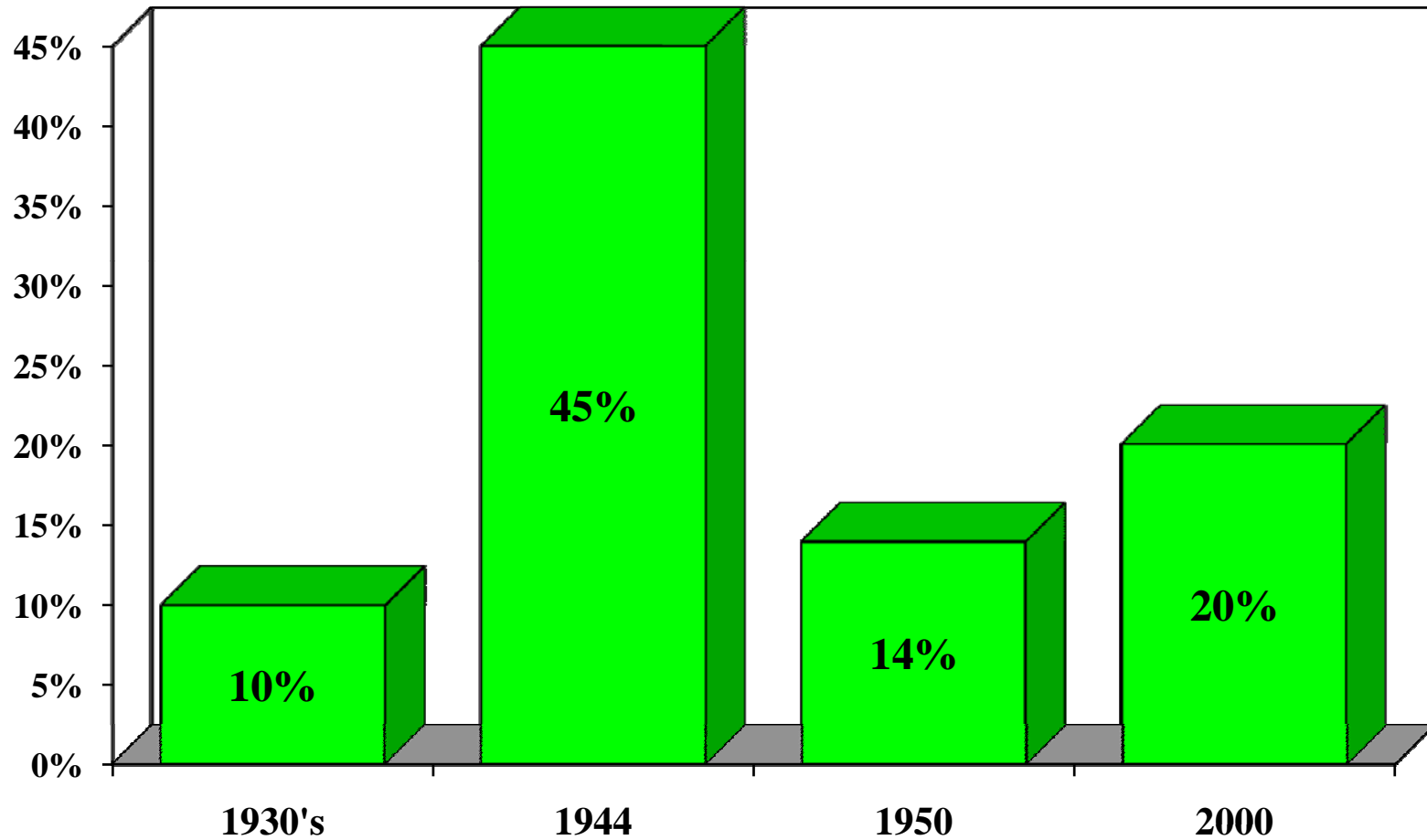


Source: 2008 Social Security and Medicare Trustees Reports, "The Long-Term Outlook for Health Care Spending," Congressional Budget Office, Nov. 2007, "The Long-Term Budget Outlook," Congressional Budget Office, December 2007 and author's estimates.



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Past Federal Government GDP Share



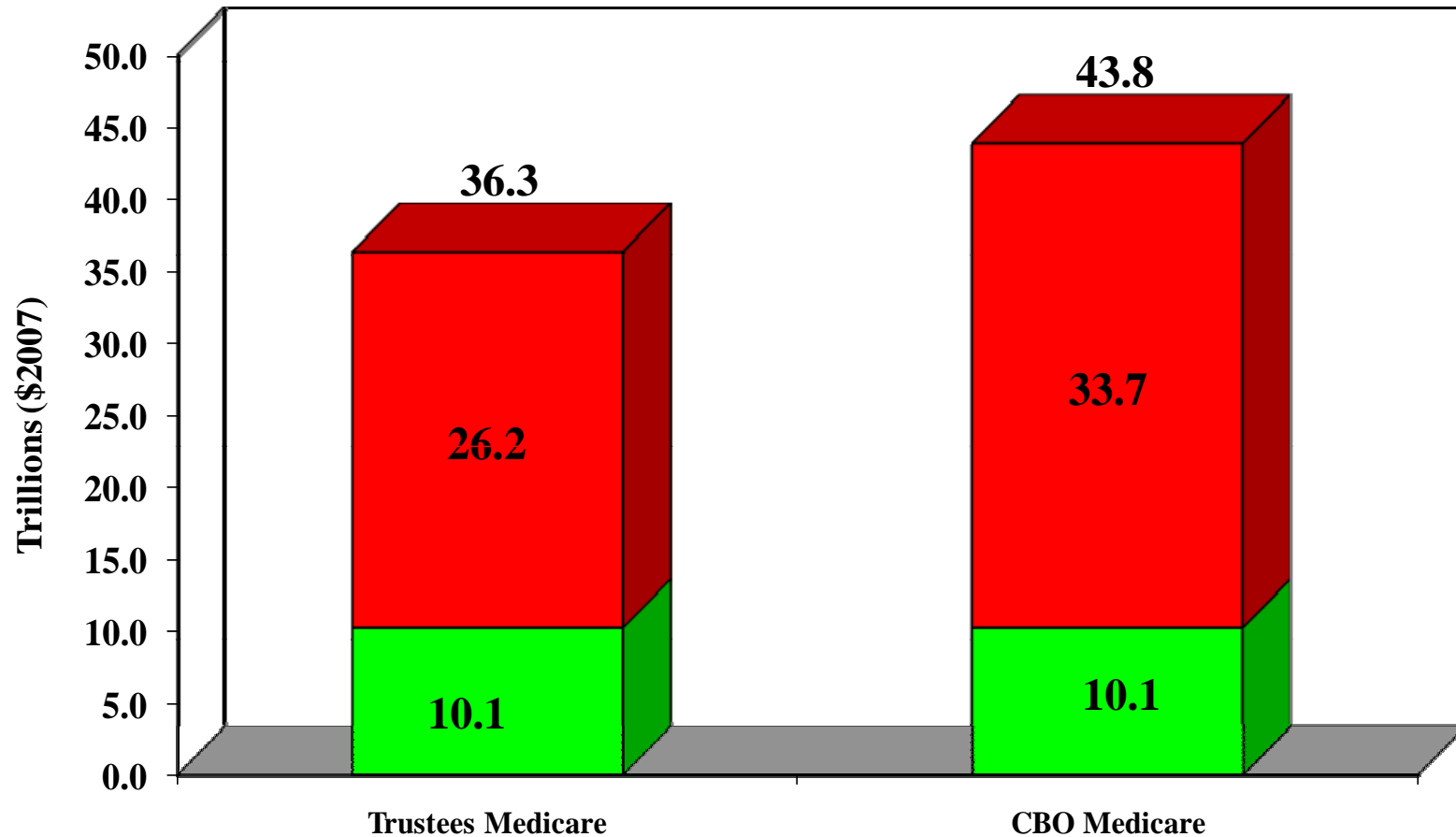
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The Medicare Debt



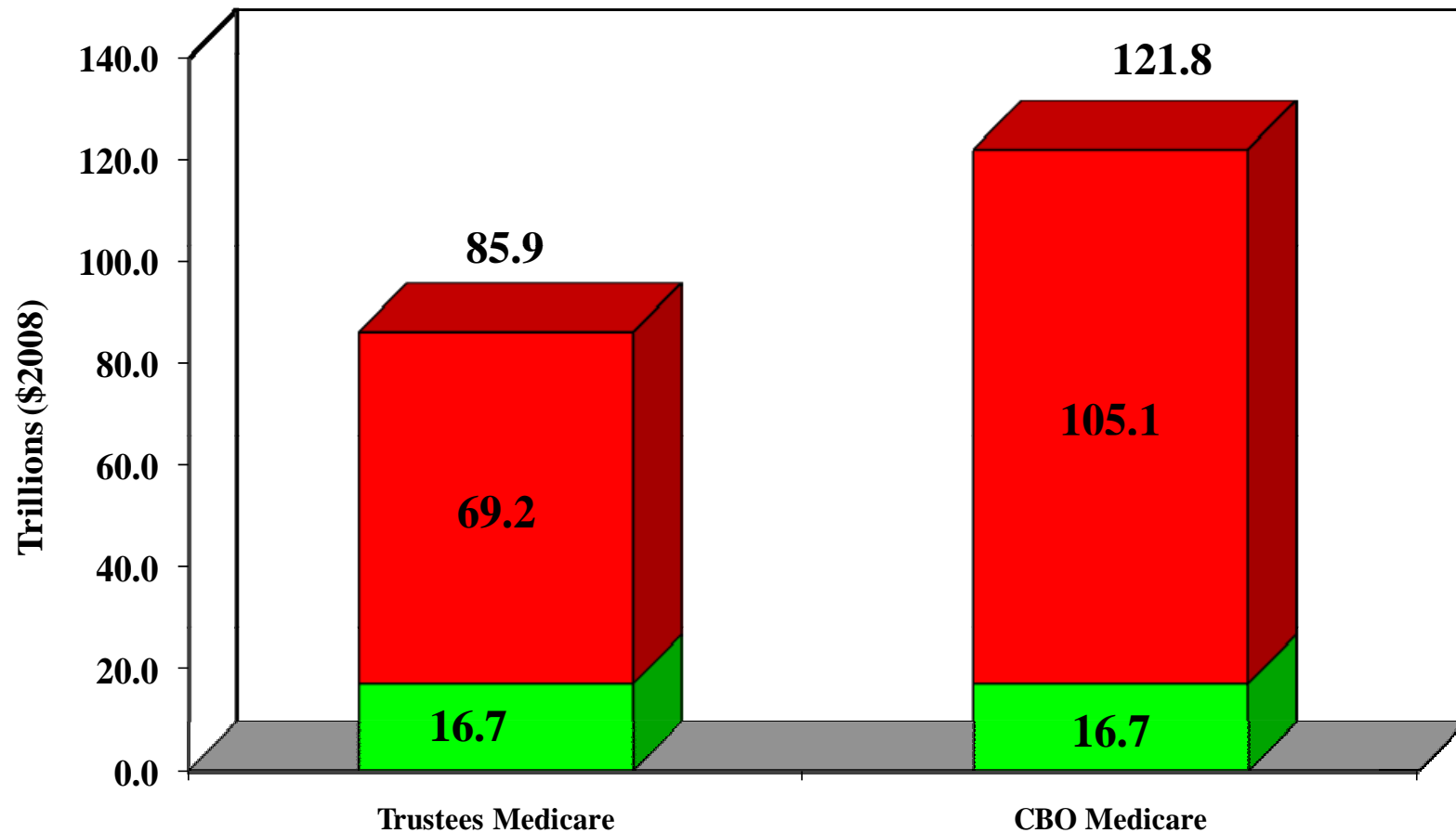
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Medicare's 75-Year Obligations in Excess of Current Transfer Share of GDP



Medicare's Long-Run Obligations in Excess of Current Transfer Share of GDP

Congressional Budget Office Projections Extended by Assuming Medicare Growth rate Equals GDP
Growth Rate After 2082



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The Cost of Doing Nothing



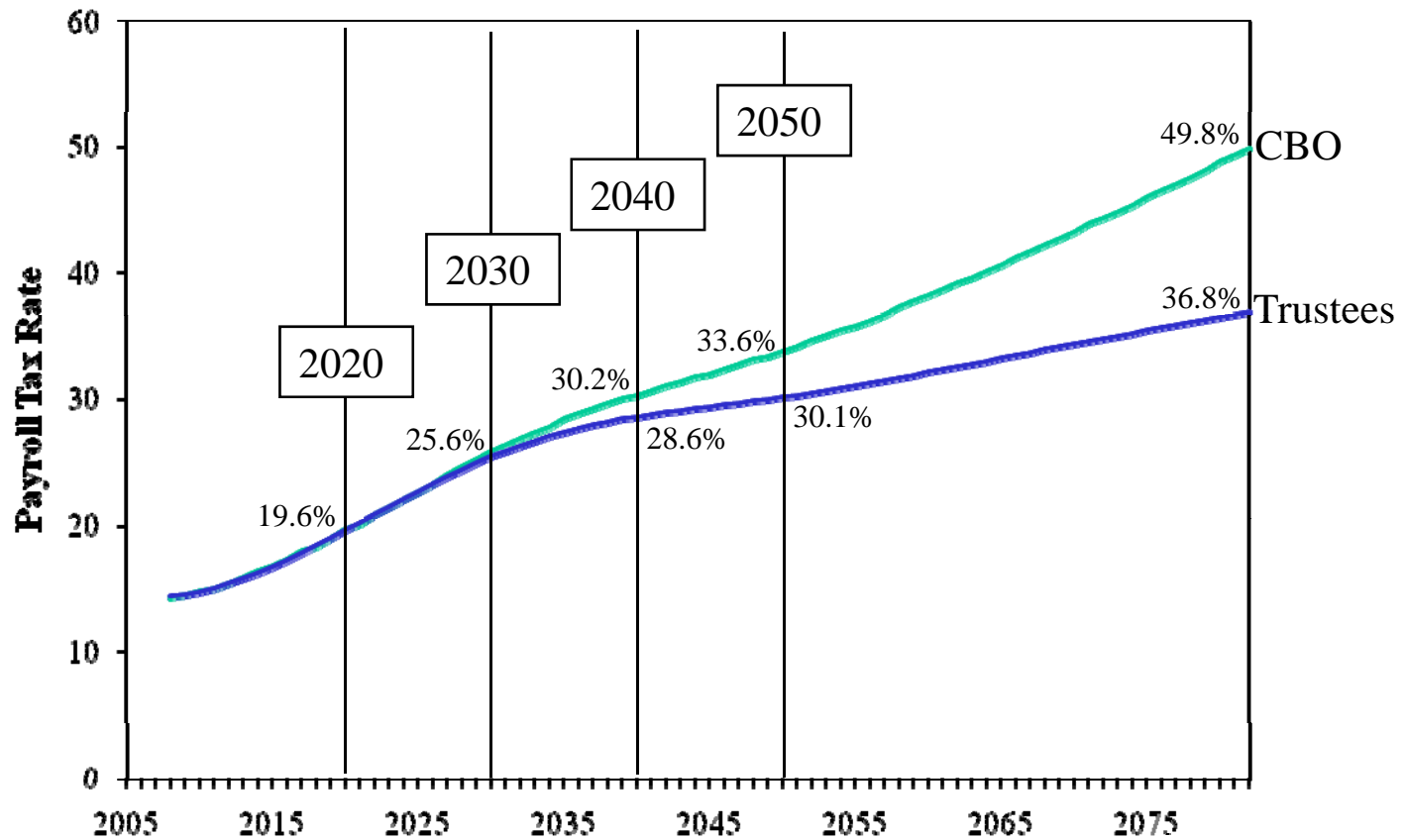
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Let The Workers Pay



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**The Payroll Tax Required to Pay for Projected Medicare
and Social Security Deficits While Maintaining Non-Entitlement Expenditure Share of GDP**
2008 Trustees Report Base



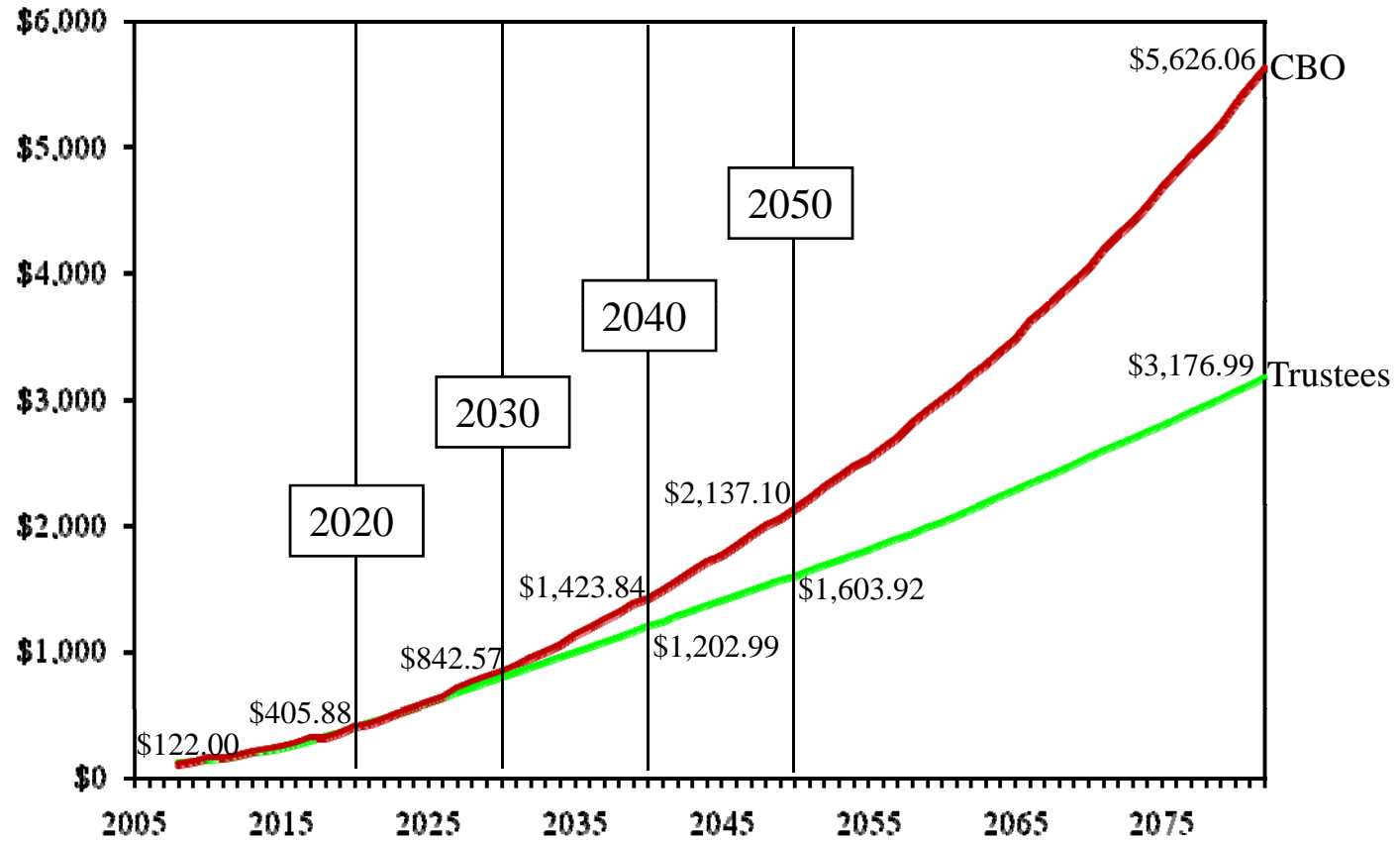
Let the Elderly Pay



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Medicare Premiums if Premiums Cover Medicare Deficits Monthly \$2008

*Constant Transfer Share From Non-Entitlement Federal Revenues
2008 Trustees Report Base*



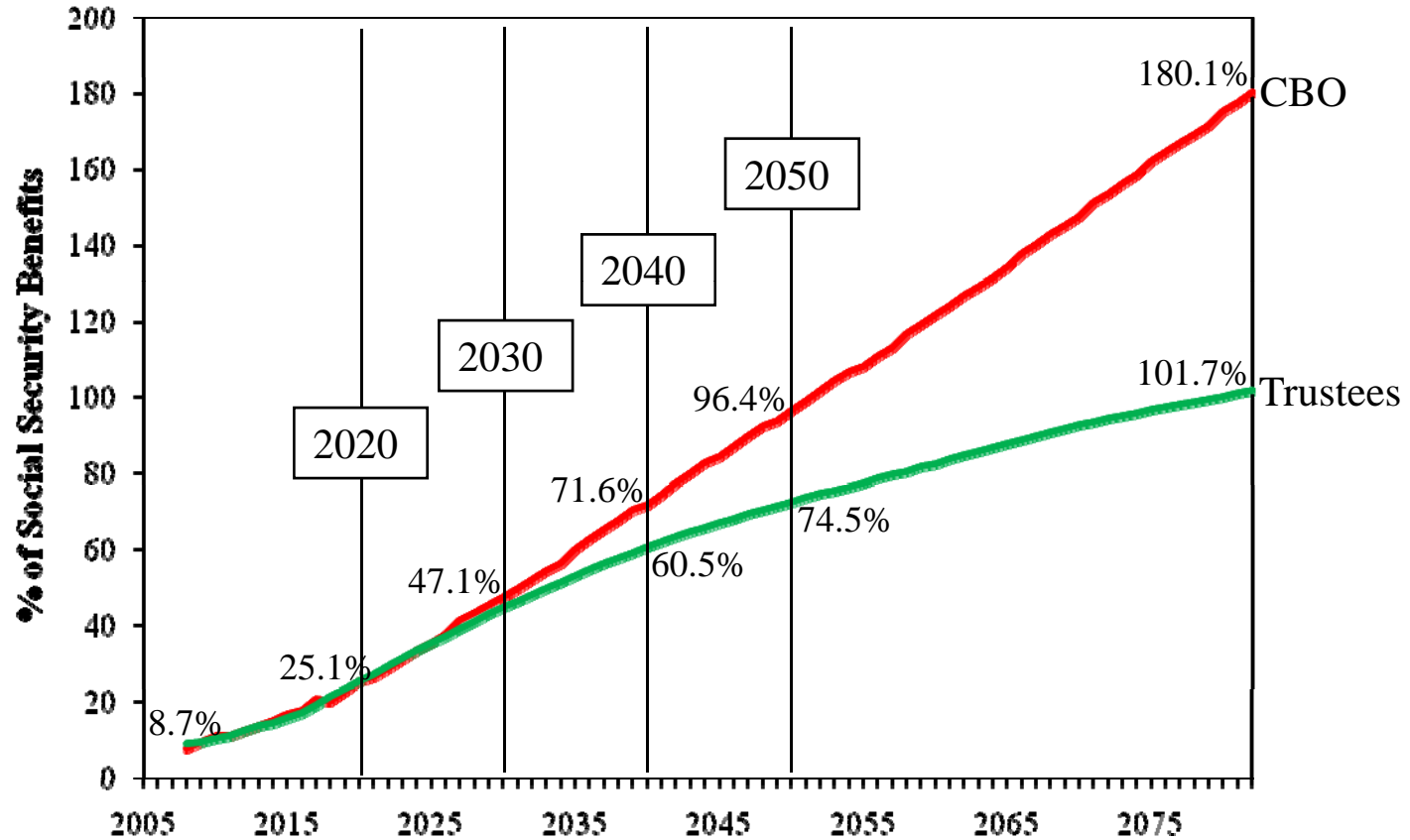
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Medicare Premiums as a Share of Projected Medium Earner Social Security Benefits

Medicare Transfer is a Constant Share of Federal Non-Entitlement Revenues

Part A Payroll Taxes Remain at Current Level

2008 Trustees Report Base



Transfer fixed 2008 share of GDP from Table III.A2 2008 Medicare Trustees Report.



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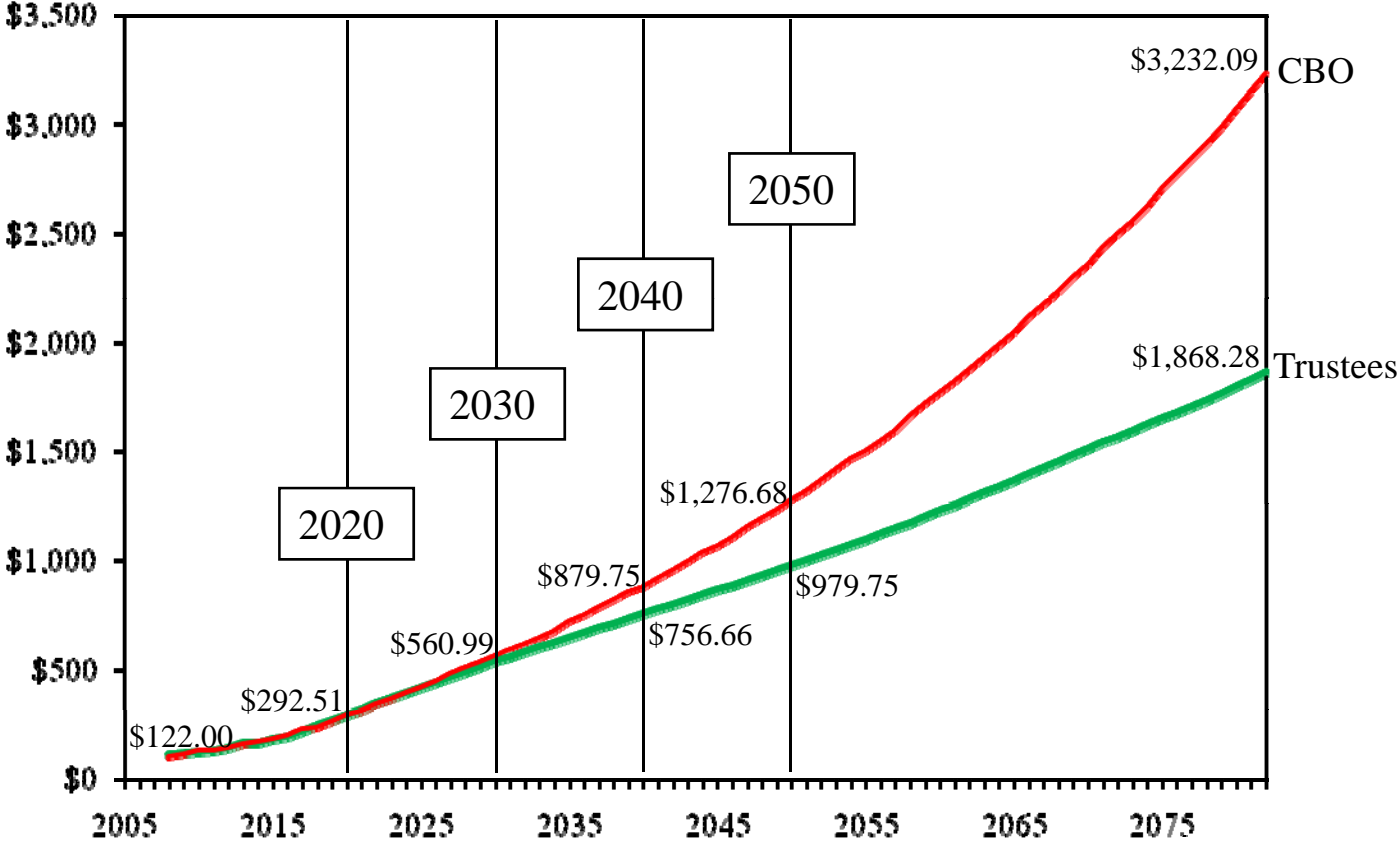
Let Workers and the Elderly Share the Burden



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Medicare Premiums if Payroll Taxation Balances the Medicare Part A Budget Monthly \$2008

*Constant Transfer Share From Non-Entitlement Federal Revenues
2008 Trustees Report Base*



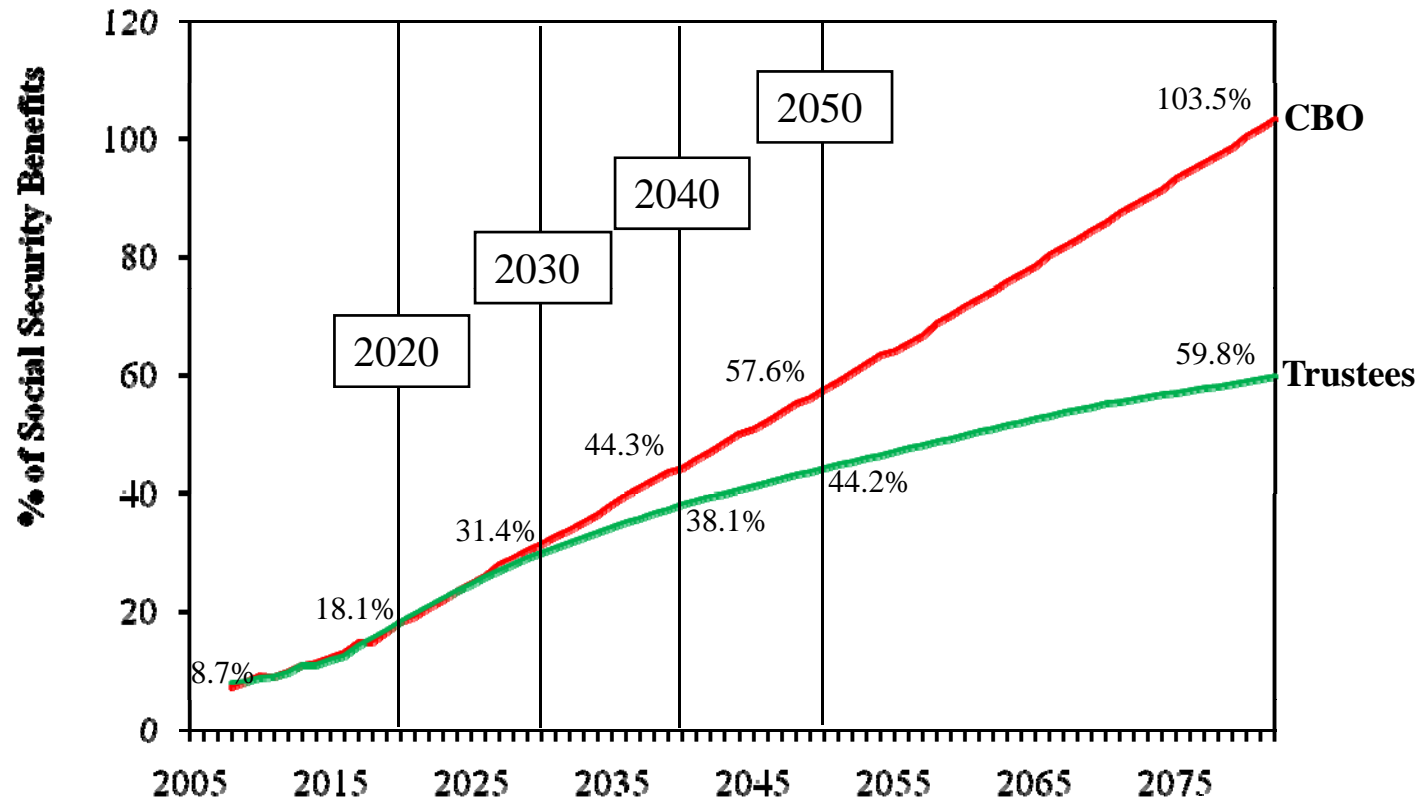
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Premiums as a Share of Projected Medium Earner Social Security Benefits

Constant Transfer Share of Federal Non-Entitlement Revenues to Parts B and D

Part A Payroll Taxes Balance the Medicare Part A Budget

2008 Trustees Report Base



Transfer fixed at 2008 share of GDP from Table III.A2 2008 Medicare Trustees Report.



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What Can Reform Accomplish?



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Benefit Cut Reforms



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The Usual Reforms

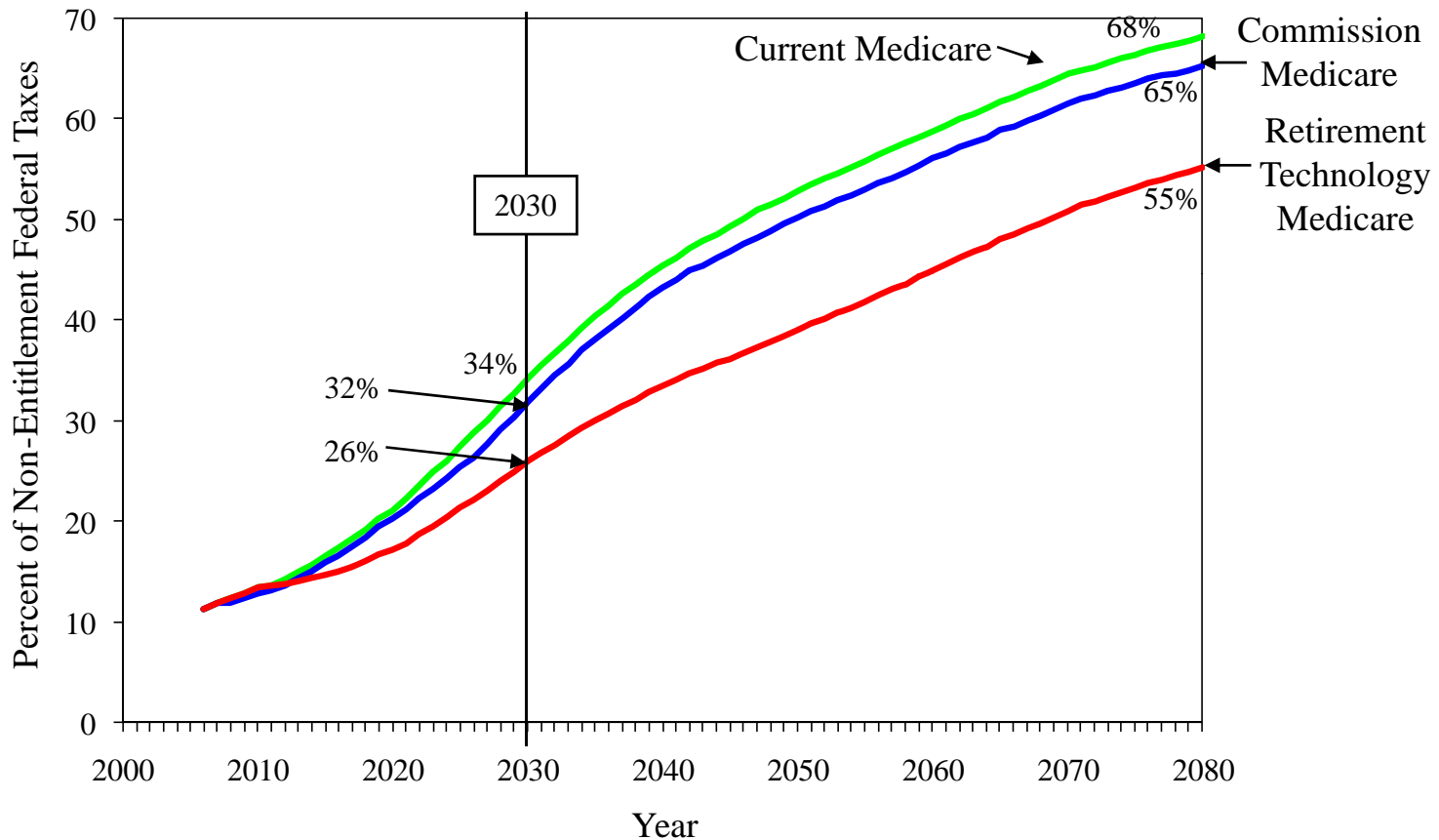
- The Bipartisan Commission on Medicare
 - Raise Age of Eligibility to match Social Security
- Fixing Benefits at Retirement
 - As of the date of your retirement
- No First Dollar Coverage
 - \$5,000 deductible
 - No Medi-gap
- Means Testing
 - Those below or near poverty pay nothing
 - Above the minimum threshold, benefits fall until they reach only 20% of current levels



Required Transfers with Three Reforms:

Commission, Retirement Technology, and 2011 Technology Medicare

% Non-Entitlement Federal Revenues

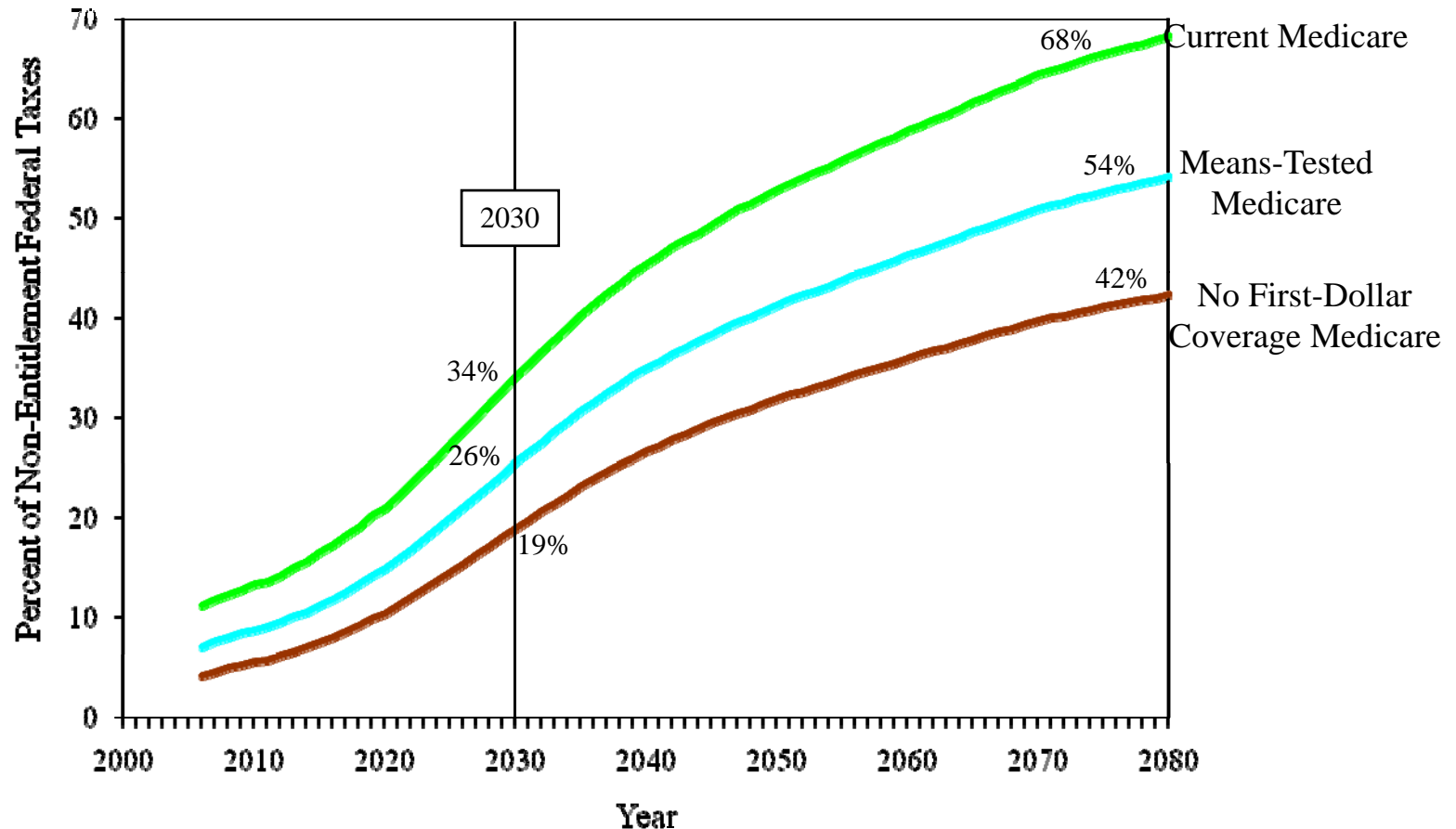


Non-entitlement Federal Taxes are estimated to be 11.80% of GDP, the 25-year average. Assumes no change in projected total spending.



Required Transfers with Two Reforms: Means-Tested and No First-Dollar Coverage Medicare

% Non-Entitlement Federal Revenues

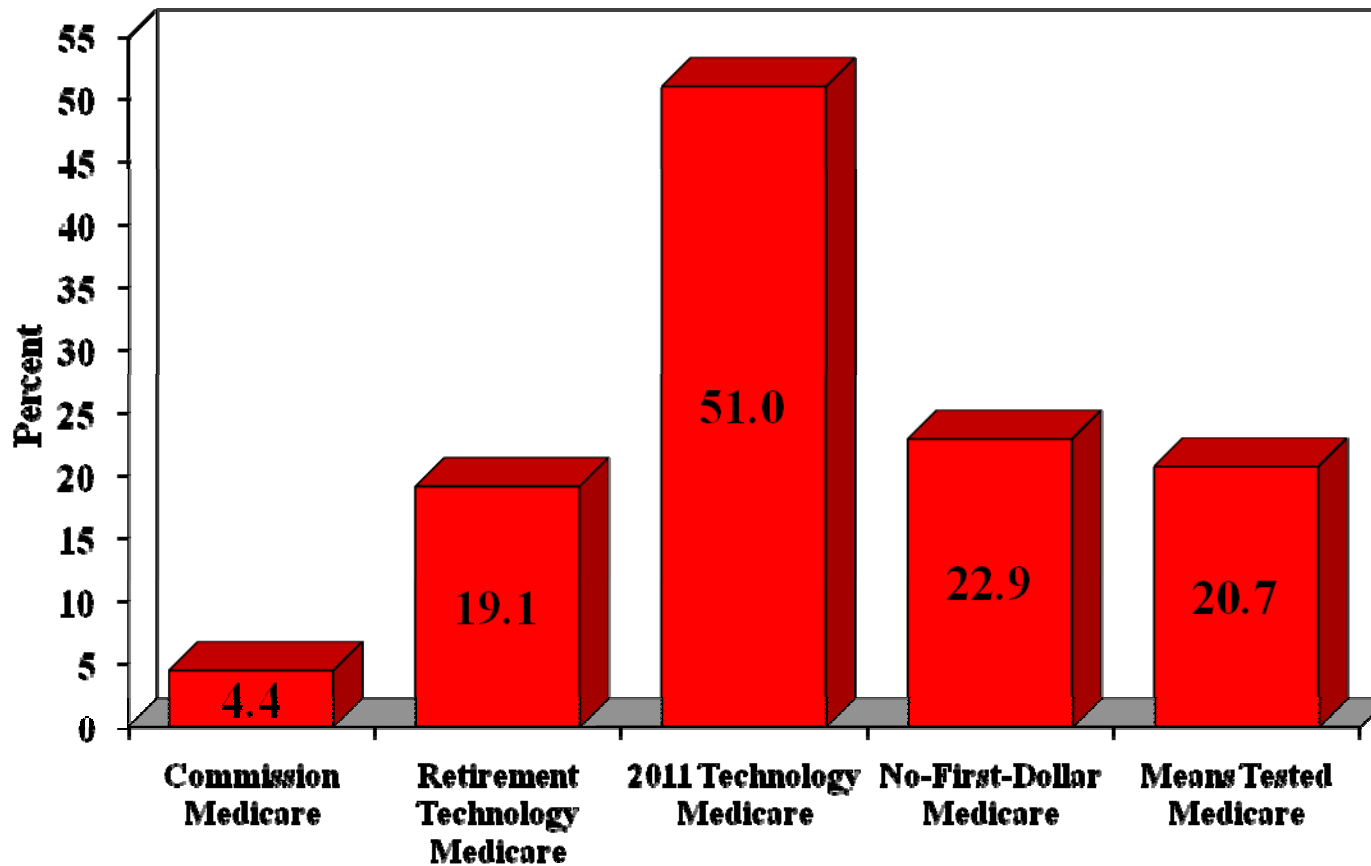


Non-entitlement Federal Taxes are estimated to be 11.80% of GDP, the 25-year average. Assumes no change in projected total spending.



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Percent Reduction in Projected Medicare Expenditures After 75 Years



Note: Restricted to beneficiaries 65 and older.



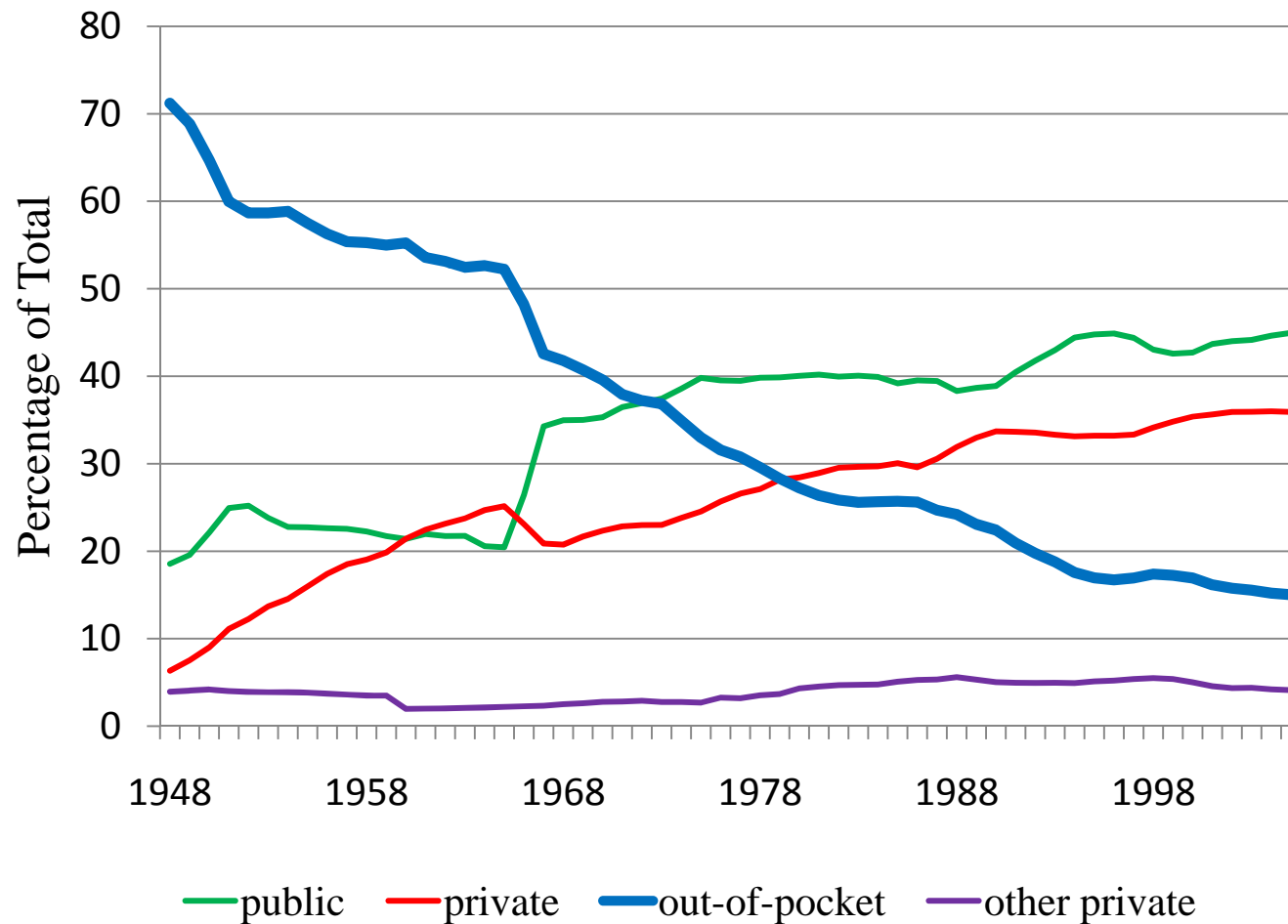
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The Source of the Problem?



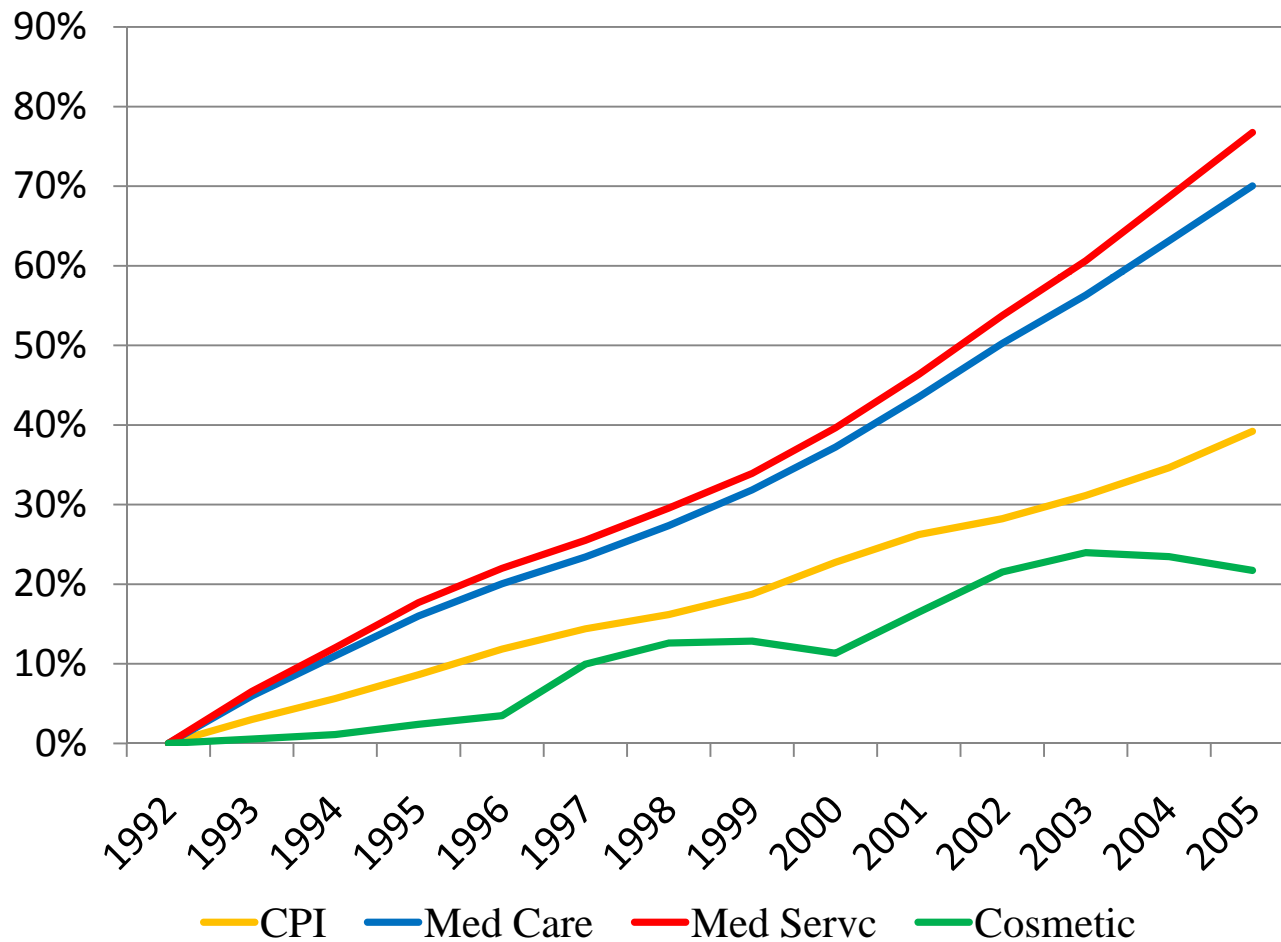
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Personal Health Care Spending by Source of Funds



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Cosmetic Surgery and General Health Care Inflation



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The Real Answer

Prepaying Retirement Consumption
of Both Goods and Health Care
Through Private Accounts



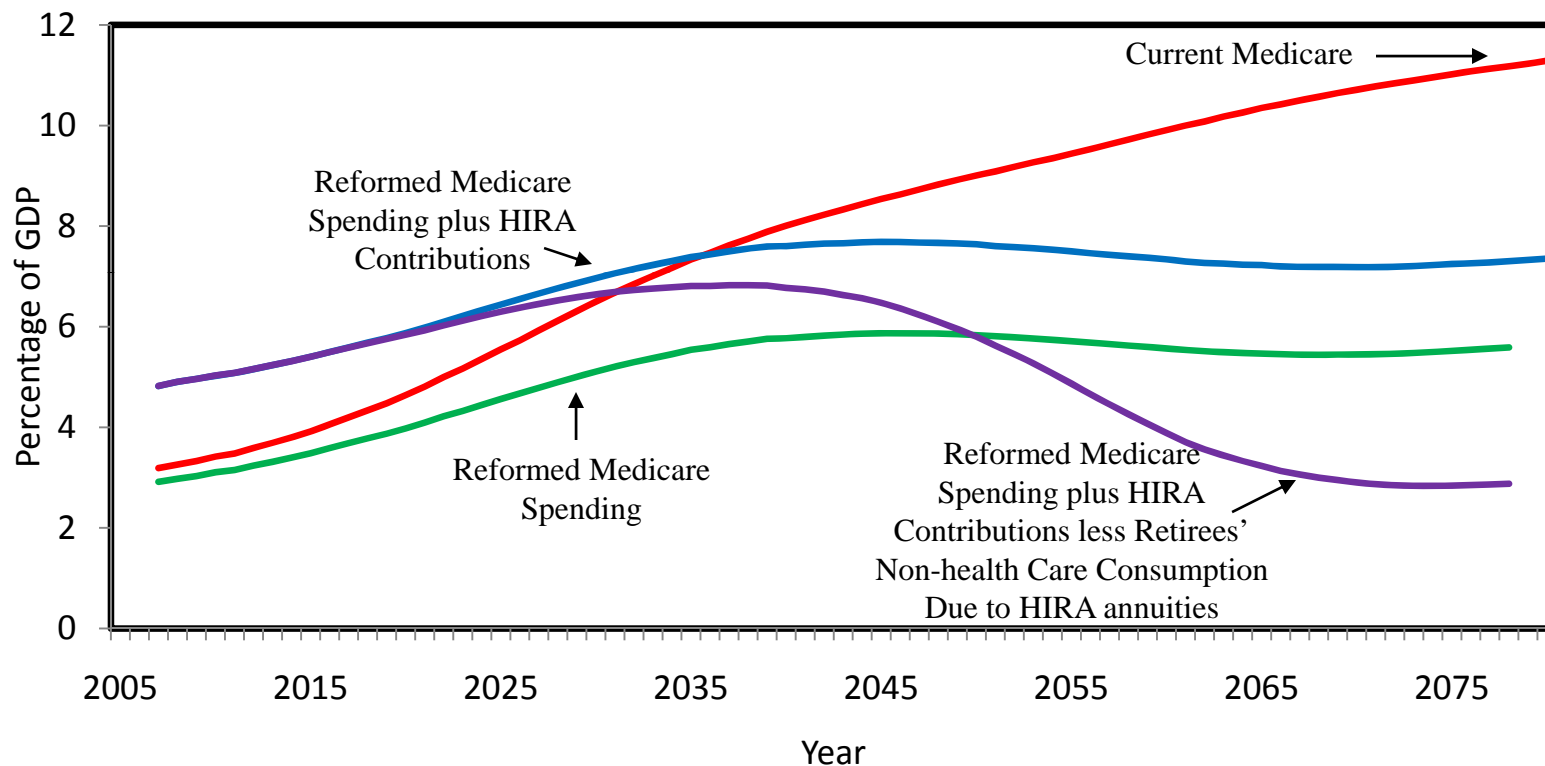
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Details

- Workers contribute a fixed percentage of their total wage income to a Health Insurance Retirement Account (HIRA) during their working lives.
- When they enroll in Medicare at age 65, beneficiaries will use their HIRA balances to purchase an annuity paying an annual fixed sum to a spending account, such as a Roth Health Savings Account (HSA).
- Accounts are not heritable.
- Beneficiaries will use their HIRA annuities to pay for a share of their Medicare costs and any funds remaining at the end of the year can be withdrawn tax free and spent on nonmedical goods and services.



Current and Reformed Medicare Spending as a Percentage of GDP, Including Capacity Supply Side Responses



Estimation parameters: Contribution rate 4%, accumulation and decumulation real return 5.2% and 2.9%, respectively, base deductible in 2007 \$2,500.



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The Bottom Line

- Fundamental reform with prepayment can revitalize Medicare while reducing government debt.
- Over the short term, reform is not free.
- Over the long term, reform can reduce taxes and restore Medicare to a sound fiscal position.
- Reform will eventually benefit recipients and workers alike by bestowing real ownership of retirement benefits.



The Diagnosis and Treatment of Medicare

"A must read, Rettenmaier and Saving cut through the heated rhetoric and inscrutable figures that plague Medicare discussions, providing a clear, readable explanation of what's wrong with the program and what's to be done. They haven't simply written a great book; they've performed a crucial public service."

—David Grutzer, senior fellow, Manhattan Institute

"This is by far the most comprehensive and compelling analysis produced to date of the long-term fiscal challenge posed by Medicare. The authors render with great clarity and precision just how and why the economic burden of financing the health care of America's senior citizens will mushroom in the decades ahead, as well as the nature and consequences for future generations of taxpayers and beneficiaries of the various generic remedies—bitter medicine all—available to federal policymakers. The book makes a strong case for fundamental reform of Medicare and aptly demonstrates that the sooner such reform is undertaken, the less onerous will be the consequences."

—John L. Palmer, university professor and dean-emeritus,
The Maxwell School of Syracuse University, and public trustee
of the Social Security and Medicare Trust Funds (2000–07)

"This book forces us to confront the unpleasant and unavoidable facts about the heavy financial burden Medicare will impose on future generations. The authors clearly demonstrate the shortfalls of current proposals and the painful tradeoffs among them. This book will have a significant, sobering, and positive impact on the Medicare reform debate, and will certainly be read carefully by policymakers and researchers around the country involved in Medicare reform."

—John F. Cogan, Leonard and Shirley Ely senior fellow, Hoover
Institution, and professor of public policy, Stanford University

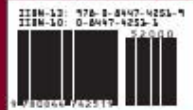
"This book is a tour de force in its description of Medicare's financial crisis. It examines several reform options and its carefully calibrated analysis shows that piecemeal reforms would not successfully avert a future fiscal crisis—even those involving seemingly draconian benefit cuts. The authors present some real approaches to soften Medicare's future financial crunch—such as prepaid health insurance that would effectively increase our national saving, productivity, and output."

—Jagadeesh Gokhale, senior fellow, Cato Institute

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The Diagnosis and Treatment of Medicare

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THE DIAGNOSIS & TREATMENT of MEDICARE

Andrew J. Rettenmaier
Thomas R. Saving



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