

## **Digging the Medicare Hole Deeper**

By Leonard Burman \*

Will Rogers once said, "If you find yourself in a hole, the first thing to do is stop digging." Medicare is in a deep hole. The small surpluses accruing right now will turn to deficits starting in about a decade when the baby boomers start to retire. By 2026, government actuaries estimate that the Medicare trust fund will be exhausted.<sup>1</sup>

The proposed prescription drug benefit under Medicare and associated tax subsidies for health savings accounts may not directly dig the Medicare hole deeper, but they represent a major expansion of the Medicare program, which will only partially be financed by premiums.<sup>2</sup> The Congressional Budget Office estimated that the new program will cost \$394 billion over the next decade—more than four times the projected Medicare surpluses over the same period (\$88 billion).<sup>3</sup> The costs in the first decade, however, understate the long run costs because prescription drug coverage under Medicare does not begin until 2006. Assuming that costs will grow at the rate of overall Medicare outlays, the second ten years would cost nearly \$1 trillion. In fact, if recent trends continue, prescription drug costs are likely to grow faster than overall health spending, so this is likely to be an underestimate.

Money spent on the controversial drug benefit could actually help to mitigate Medicare's long run imbalances. As an illustration, if projected expenditures for the new benefit were instead deposited in the Medicare Health Insurance trust fund, the life of the trust fund would be extended until 2047, or 21 years past the current projection. (See Figure 1.) That is, the solvency period could be nearly doubled.

To see this point in a different light, suppose Medicare's new unfunded obligations had to be paid out of the trust fund. Medicare would become insolvent by the end of 2014—the trust fund's life would be halved.

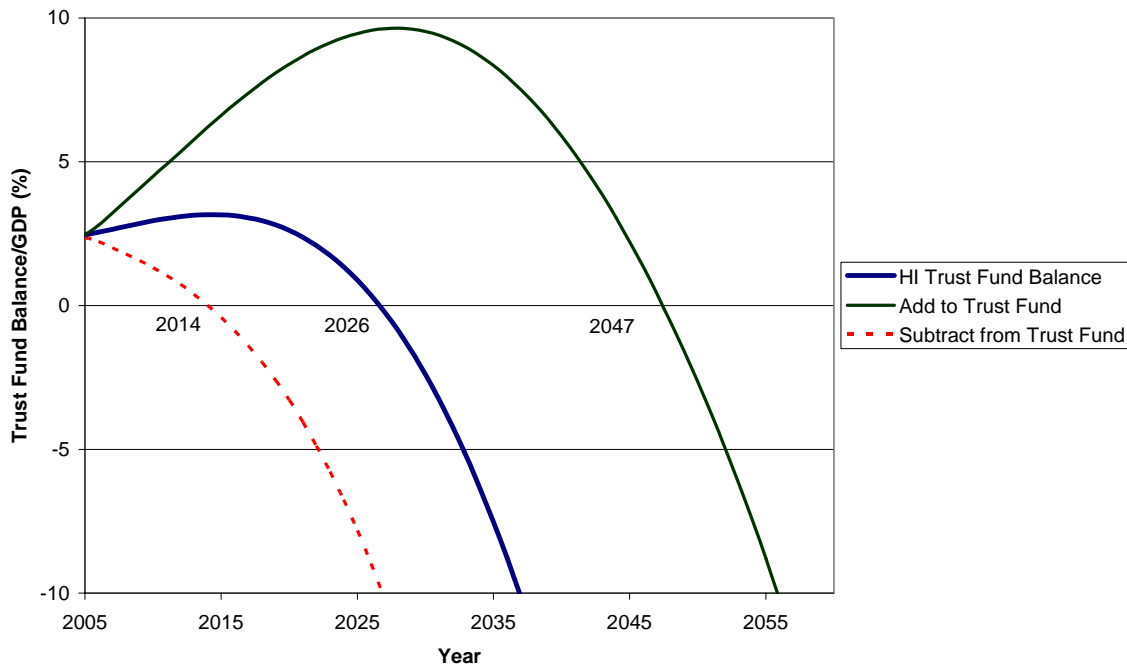
Nobody is proposing either of these alternatives. But the fact remains that, even before passage of a prescription drug benefit, Medicare represents a huge potential burden on our children and grandchildren. Maybe it is time to stop digging.

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\* Leonard Burman is a Senior Fellow at the Urban Institute, Codirector of the Tax Policy Center, and Visiting Professor at Georgetown Public Policy Institute. Views expressed are his own.

Figure 1. Proposed Prescription Drug Benefit and Medicare Trust Fund



<sup>1</sup> All estimates refer to the Hospital Insurance portion of Medicare, so-called Part A, which is financed by payroll taxes. (Supplementary Medical Insurance—Part B—is financed by an optional premium and general revenues.) The source for short-run projections is Centers for Medicare and Medicaid Services, *2003 Annual Report of the Board of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, <http://cms.hhs.gov/publications/trusteesreport/2003/tr.pdf>. Long-run estimates are based on the “tables by single year,” a supplement to the *2003 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds*, published on the Social Security Administration website. See Table VI.F5, at <http://www.ssa.gov/OACT/TR/TR03/tr6F5-2.html>. All calculations are based on intermediate assumptions.

<sup>2</sup> Some experts believe that the design of the new benefit actually does threaten the long-run viability of traditional Medicare, because private insurers will seek to attract the healthiest individuals for subsidized private coverage leaving Medicare with a sicker than average participant pool. This could lead to higher costs for Medicare, curtailed benefits for participants in traditional Medicare, or some combination. See Edwin Park, Melanie Nathanson, Robert Greenstein, and John Springer, “The Troubling Medicare Drug Agreement,” Center on Budget and Policy Priorities, November 19, 2003. <http://www.cbpp.org/11-18-03health2.htm>.

<sup>3</sup> Congressional Budget Office, “Cost Estimate for H.R. 1, Medicare Prescription Drug, Improvement, and Modernization Act of 2003,” November 20, 2003. <ftp://ftp.cbo.gov/48xx/doc4808/11-20-MedicareLetter.pdf>.