

CRS Insights

Medicare: Insolvency Postponed

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On July 28, 2014, the Medicare Board of Trustees released their [annual report](#) on the current and projected financial status of the Medicare trust funds. Due to lower than expected Medicare Part A spending in 2013 (the base projection year) and lower expected future utilization of hospital inpatient services, the Trustees have postponed the [expected insolvency date](#) of the Medicare Hospital Insurance trust fund to 2030, four years later than projected in last year's report.

What Are the Medicare Trust Funds?

The [Medicare program](#) is funded through two separate [trust funds](#)—the Hospital Insurance (HI) trust fund, which finances Part A, and the Supplementary Medical Insurance (SMI) trust fund, which finances Parts B and D. (Part C is funded by a blend of HI and SMI monies.) Similar to [Social Security](#), the HI portion of Medicare was designed to be self-supporting and is funded through dedicated sources of income, primarily [payroll taxes](#) levied on current workers and employers and taxes on Social Security benefits. Parts B and D were not designed to be self-supporting. Those parts of Medicare are funded mainly through general revenue, beneficiary premiums, and state transfer payments, and the level of SMI funding is automatically updated each year to cover expenditures. Both funds are maintained by the Department of the Treasury and are overseen by a [Board of Trustees](#) that [reports annually to Congress](#) concerning the funds' financial status.

Solvency of the Hospital Insurance Trust Fund

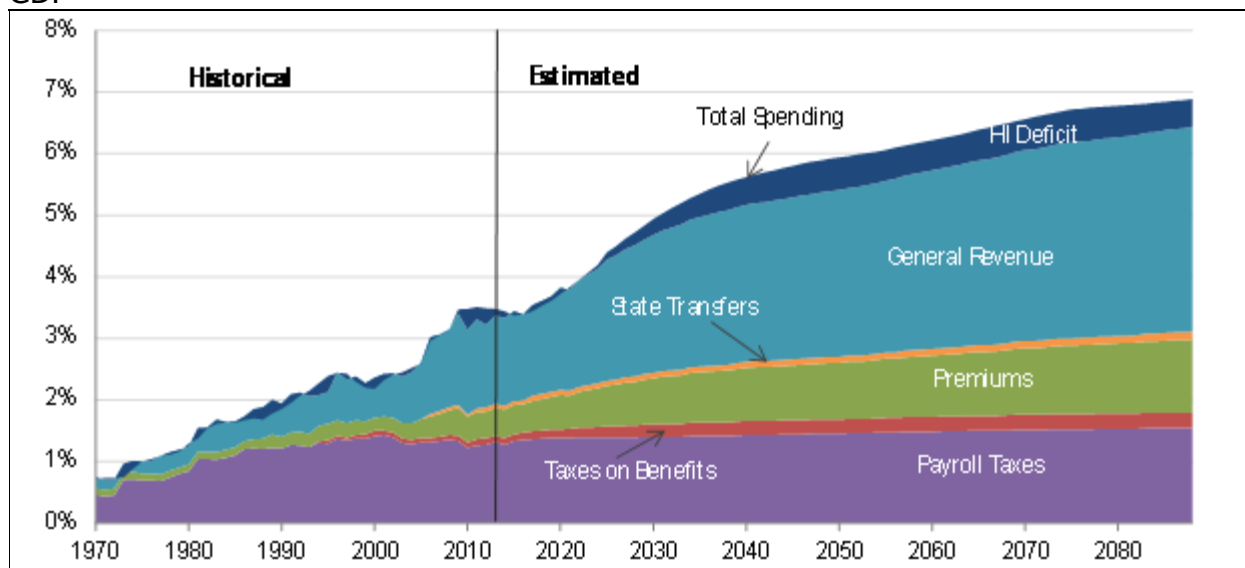
HI operates on a "pay-as-you-go" basis; the Medicare payroll taxes paid by current workers are used to pay Part A benefits for today's Medicare beneficiaries. When the government receives Medicare payroll taxes, the income is credited by the Treasury to the HI trust fund in the form of special issue interest-bearing government securities. When payments for Medicare Part A services are made, the payments are paid out of the general treasury and a corresponding amount of securities is deleted from the HI trust fund. In some years, annual income to the HI trust fund has exceeded amounts needed to pay for Part A benefits, and the accumulated extra funds have been credited to the HI trust fund. These trust fund surpluses are not reserved for future Medicare benefits but are simply bookkeeping entries that indicate how much Medicare has lent to the Treasury. At the end of 2013, the [balance of the HI trust fund](#) was approximately \$205 billion.

When a trust fund is not able to pay all of current expenses out of current income and accumulated trust fund assets, it is considered to be *insolvent*. Beginning in 2008, annual [income to the HI trust fund](#) has not been sufficient to fully cover annual Part A expenditures and Medicare has needed to redeem trust fund assets (securities) accumulated in previous years. With the exception of [certain years](#), future annual Part A expenditures are expected to continue to exceed dedicated income, with the asset balance of the HI trust fund becoming depleted in 2030 (at which time the fund would be insolvent).

What Would Happen if the HI Trust Fund Became Insolvent?

Insolvency of the HI trust fund does not mean that the Medicare program will run out of money. After depletion, the HI trust fund would continue to receive tax income from which some benefits could be paid; however, [funds would only be sufficient](#) to pay for 85% of Part A expenses in 2030 and subsequently drop to 77% by 2088. Because the level of SMI funding is automatically updated each year, the SMI trust fund cannot become insolvent. Therefore, Parts B and D benefits would continue to be paid in full regardless of the status of the HI trust fund. (See [Figure 1](#) for an illustration of estimated Medicare spending and the HI deficit as a percentage of GDP through time.)

Figure 1. Medicare Spending and Non-interest Income, by Source as a Percentage of GDP

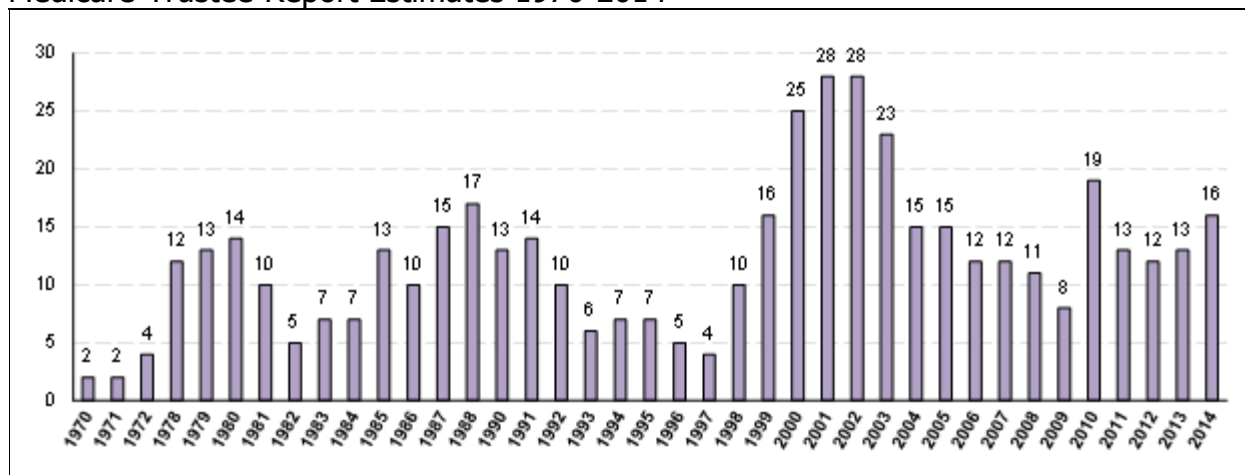


Source: Summary of the 2014 Annual Reports of the Social Security and Medicare Boards of Trustees, Chart C, <http://www.ssa.gov/oact/TRSUM/index.html>.

Medicare has faced insolvency since the inception of the program (see [Figure 2](#)); however, the HI trust fund has never become insolvent primarily due to [actions taken by Congress](#) to increase dedicated revenues and/or reduce program spending. There are no provisions in the Social Security Act that govern what would happen should the HI trust fund become insolvent. For example, there is no authority in law for the program to use general revenue to fund Part A services in the event of such a shortfall.

Figure 2. Projected Number of Years Until HI Insolvency

Medicare Trustee Report Estimates 1970-2014



Source: Intermediate projections of various Medicare Trustees reports, 1970-2014.

Medicare Program Financial Outlook

Although the 2014 Medicare Trustees Report projects a slowing in expected Medicare spending and an improved outlook for the solvency of the HI trust fund, the [Trustees express concern](#) that the program still faces substantial financial challenges. For example, total Medicare spending is expected to increase from \$583 billion in 2013 to \$1.1 trillion in 2023, due primarily to the large baby-boom population aging into Medicare. In 2013, nearly 52 million people were enrolled in Medicare; by 2023, this number is expected to increase to almost 70 million. The Trustees also expect per beneficiary spending to continue growing at a slightly faster rate than per capita GDP, increasing from an average of \$12,210

per person in 2013 to \$17,364 in 2023.

Additionally, the [Trustees caution](#) that "[p]rojections of Medicare costs are highly uncertain" due to the difficulty in predicting future health care costs. As such, the Trustees included an [illustrative Medicare alternative projection](#) in their 2014 report based on the possibility that certain [provider payment adjustments](#) required by the Patient Protection and Affordable Care Act ([P.L. 111-148](#)) would be phased out beginning in 2020. This alternative projection suggests higher total Medicare spending levels than the report's baseline figures and a [slightly earlier HI trust fund depletion](#) date of 2029.

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