2016 MAKING ISSUES COUNT

MEDICARE'S LONG-TERM SUSTAINABILITY CHALLENGE

MEDICARE SPENDING WILL INCREASE DRAMATICALLY over the next few decades as the baby boomer population ages into the program and health spending per beneficiary grows. At the same time, number of workers per enrollee will shrink. As a result, benefit payments are expected to exceed payroll taxes, threatening solvency of one of its major trust funds. And Medicare will make up increasing shares of federal government and household spending, meaning decreasing shares will be available for other needs.

Medicare's Hospital Insurance (HI) Trust Fund Income Falls Short of the Amount Needed to Pay HI Benefits

Medicare's HI trust fund receives revenues from payroll taxes and pays for beneficiaries' inpatient hospital and post-acute care services. It had built up a surplus of $197 billion at the end of 2014 but is projected to be depleted in 2030. At that time, tax revenues are projected to cover only 86 percent of program costs, with the share declining to 79 percent in 2039.

No current provision exists for general fund transfers to cover HI expenditures in excess of dedicated revenues, so additional revenues would need to be raised, benefits cut, or some combination of the two. Eliminating the looming deficit over the next 75 years would require an immediate 23 percent increase in payroll taxes, or an immediate 15 percent reduction in expenditures, or some combination of both.

Higher Supplementary Medical Insurance (SMI) Costs Increase Pressure on Beneficiary Household Budgets and the Federal Budget

Medicare's SMI trust fund—which covers physician services, hospital outpatient care, and prescription drugs—receives about three-qarters of its funding from federal general tax revenues and one-quarter from beneficiary premiums. The SMI trust fund is expected to remain solvent because its financing is reset each year to meet projected future costs. But increases in SMI costs will require increases in beneficiary premiums and federal tax dollars, which will add pressure to the federal budget. SMI general revenue funding is scheduled to increase from 1.4 percent of GDP in 2015 to 2.8 percent in 2089.

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SMI premium increases similarly will place pressure on beneficiaries, especially when considered in conjunction with increasing beneficiary cost-sharing expenses. The average beneficiary expenses (premiums and cost sharing) for Parts B and D combined currently equal 23 percent of the average Social Security benefit. These expenses will increase to 36 percent of the average Social Security benefit by 2089.

Increases in Total Medicare Spending Threaten the Program's Sustainability

Because Medicare spending is expected to continue growing faster than GDP, greater shares of the economy will be devoted to Medicare over time, meaning smaller shares of the economy will be available for other priorities. Medicare expenditures as a percentage of GDP are projected to grow from 3.5 percent of GDP in 2014 to 6.0 percent of GDP in 2085.

Tough Medicare Choices

The Affordable Care Act enacted in 2010 contains provisions designed to reduce Medicare costs, increase Medicare revenues, and develop new health care delivery systems and payment models that improve health care quality and cost efficiency. But these do not go far enough to solve Medicare's financial challenges, which will require tough choices by policymakers on changes to benefit coverage, provider and plan payments, and taxpayer funding.

Additional Resources From the Academy

Medicare at 50: Is It Sustainable for 50 More Years? READ MORE...

Medicare Subcommittee Issue Brief on Trustees' Report READ MORE...

Addressing Health Care Cost Growth in Medicare: A Framework READ MORE...