Joint Economic Committee Democrats

Senator Jack Reed (D-RI) – Ranking Democrat

Economic Fact Sheet **May 2006**

Highlights of the 2006 Medicare Trustees' Report

In its 2006 annual report, the Board of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds projects that the Hospital Insurance (HI or Part A) Trust Fund will be able to pay full benefits until 2018. Although this is two years earlier than the projection in last year's report, 12 years is about the typical length of solvency in past Medicare projections. In the past, Congress has been able to maintain Medicare's short-run fiscal stability without adversely affecting benefits.

The Medicare HI Trust Fund is projected to grow in the near term.

- Medicare HI is funded primarily by a payroll tax of 2.9 percent of earnings (1.45 percent each paid by employers and employees). Unlike Social Security, there is no cap on the amount of earnings subject to the HI payroll tax.
- In 2006, total HI income, including interest on trust fund assets and a portion of income taxes paid on Social Security benefits, is projected to reach $210.2 billion, while expenses are expected to total $200.5 billion.
- The HI Trust Fund is expected to increase by approximately $9.7 billion to a total of $295.5 billion by the end of 2006. The Trust Fund is projected to grow through 2009, reaching $311.3 billion by the end of that year.

In the future Medicare HI expenses are projected to exceed revenues.

- Starting in 2010, the HI Trust Fund will begin to pay out more in benefits ($259.2 billion) than it will receive in income from all sources ($257.4 billion).
- Without changes, the HI Trust Fund will not be able to cover all costs starting in 2018. At that point, the Trust Fund's assets will be depleted and tax revenue will finance 80 percent of estimated costs. That percentage will decrease over time.
- The Medicare HI deficit will equal 3.4 percent of taxable payroll over the next 75 years. That means, for example, that the actuarial deficit could be closed by an immediate increase in payroll taxes of 3.4 percentage points.
- Another way to measure the long-term deficit is as percentage of gross domestic product (GDP). The report estimates that the long-term shortfall is equal to1.6 percent of cumulative GDP.
- The Report also estimates that the present value of the 75-year deficit is $11.0 trillion. (Present value is the amount today that, with interest, could make up the difference between future cost and revenue.)

The addition of Medicare Part D has increased both income and expenditures in Medicare Supplementary Medical Insurance (SMI or Parts B & D).

- Medicare SMI is funded differently from HI, with approximately 75 percent coming from general revenue and approximately 25 percent from beneficiary premiums.
- Medicare SMI income, including general revenue transfers and interest income, is expected to be $236.5 billion in 2006, while expenditures are projected to be $232.4 billion. Those amounts are a substantial increase over 2005 levels because of the implementation of the Medicare Part D prescription drug benefit and changes in physician payment arrangements.
- Part D spending is expected to rise from $1.1 billion in 2005 to $59.1 billion in 2006, accounting for most of the increase in SMI spending from $158.1 billion in 2005.
- Estimated Part D spending in 2006, while raising total SMI spending, is lower than what was estimated in last year's report, largely due to lower enrollment and slower growth in prescription drug prices.

The "45-percent threshold" for general revenue financing is projected to be reached in 2012.

- The 2003 Medicare Modernization Act stipulated that each year the Trustees must report whether Medicare general revenue funding is projected to exceed 45 percent of total Medicare spending from all revenue sources at any time over the next six years. If that condition is met in two consecutive Trustees' reports, the President is required to submit legislation to bring general revenue financing below 45 percent, and Congress is required to take action subsquently (which may include accepting, modifying, or rejecting the President's proposal.)
- The 2006 Trustees' report projects that the 45 percent threshold will be met in 2012. If next year's report also projects that general revenue will exceed 45 percent of Medicare spending within the next six years, the President will need to propose legislation no more than 15 days after the release of the FY 2009 budget .
- Critics argue that the 45 percent threshold is a subjective target. General revenues were always expected to finance the majority of SMI spending and there is no special significance to the 45 percent criterion. Limiting the use of general revenue transfers is likely to force either an increase in premiums or a reduction in benefits.

Table

Comparison of Projections in the 2005 and 2006 Medicare Trustees' Reports

	2005 Report	2006 Report
Year in which annual HI spending exceeds income from all sources	2012	2010
Year in which HI Trust Fund can no longer pay full benefits	2020	2018
Percentage of scheduled benefits payable when HI Trust Fund can no longer pay full benefits	79% in 2020	80% in 2018
HI Trust Fund 75-year deficit as a percent of taxable payroll [a]	3.00%	3.40%
HI Trust Fund 75-year deficit as a percent of gross domestic product	1.40%	1.60%
HI Trust Fund 75-year deficit (present value) [b]	$8.6 trillion	$11.0 trillion

[a] Differs from the actuarial deficit, which is 3.51 percent of taxable payroll in 2006. The actuarial deficit includes the cost of accumulating a target trust fund balance equal to 100 percent of annual cost by the end of the period.

[b] The difference in the present value between 2005 and 2006 is primarily the result of a lower assumed real interest rate, a later valuation date starting in 2006 instead of 2005, and the addition of a larger deficit year at the end of the 75-year period.

JOINT ECONOMIC COMMITTEE – DEMOCRATS
SENATOR JACK REED (D-RI) – RANKING DEMOCRAT

804 HART SENATE OFFICE BUILDING
PHONE: (202) 224-0372 FAX: (202) 224-5568
INTERNET: JEC.SENATE.GOV/DEMOCRATS