WebMemo
Published by The Heritage Foundation

No. 1796
February 4, 2008

Washington Must Pull the Trigger to Contain Medicare Spending

Robert E. Moffit, Ph.D., and Alison Acosta Fraser

For years, official Washington has studiously ignored the warnings of prominent liberal and conservative analysts, as well as the Government Accountability Office, about the entitlement crisis, particularly the exploding costs of the Medicare program. As a result, the crisis has deepened, piling up future debt and threatening huge tax increases on younger workers. The law requires that the President and Congress begin to address the issue in 2008. Even though there is no requirement that legislation be enacted, the debate is unavoidable.

A Fiscal Alarm. Today, payroll taxes, beneficiary premiums, and general revenues finance Medicare. The long-term impact of the increasing draw-downs on general revenue funds to cover Medicare benefits will mean huge tax increases, especially after the baby boomers begin to retire in 2011. Medicare already has unfunded costs of $34 trillion over the next 75 years (in net present value terms).

When Congress created a universal prescription drug benefit with the Medicare Modernization Act of 2003 (MMA)—adding an estimated $8 trillion to the program's long-term unfunded liability—it enacted a "cost containment" mechanism designed to control excessive general revenue funding for Medicare. That amount becomes "excessive" when it funds more than 45 percent of total Medicare outlays. The "trigger" for presidential and congressional action is when two consecutive Medicare trustees' reports project that the "excessive" threshold will be met within seven years.

The alarm was triggered by the 2007 Medicare Trustees Report, in which the trustees concluded for the second year in a row that total Medicare outlays will reach 45 percent of total outlays in fiscal year 2013—the seventh year of the projection.

Required Presidential Action. Under Title VIII of the MMA, the President and Congress are required to take specific steps to control an excessive growth in Medicare spending.[1]

Under Sec. 802, the President is required to submit legislation to respond to the Medicare funding warning. The legislation must be submitted within 15 days of the President's budget request in the year following the trustees' report. The President would not be required to submit a legislative proposal if, in the meantime, Congress were to take remedial action to eliminate the excessive general revenue funding of Medicare within the seven-year period. The President has already submitted a Medicare budget proposal that would, if enacted, reduce spending by $178.2 billion over five years and $556 billion over ten years.[2]

For its part, Congress has done nothing significant since the enactment of the MMA. In fact, the House leadership went in the opposite direction with the failed Children's Health and Medicare Protection Act (H.R. 3162), legislation to reauthorize

This paper, in its entirety, can be found at:
www.heritage.org/Research/Budget/wm1796.cfm

Produced by the Center for Health Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 • heritage.org

The Heritage Foundation
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the State Children's Health Insurance Program (SCHIP). They supported a provision that would have repealed the early-warning mechanism, breaking the fiscal alarm clock. Left-wing health policy analysts generally want to get rid of the trigger because it would encourage what they consider to be undesirable structural changes in the Medicare program—changes that would move the program toward a market-based system driven by real consumer choice and genuine competition. Such reforms would also preclude general tax increases to finance the rapidly rising Medicare costs.[3]

Required Congressional Action. Under Sec. 803 of the MMA, the House Majority Leader must introduce the President's proposal for remedial action within three days of receiving it. The legislation is then referred to the appropriate House committees, which must report remedial legislation no later than June 30, 2008. The Chairman of the House Budget Committee must certify whether the legislation would eliminate "excessive" general revenue funding for Medicare within the seven-year period. The legislation can be the President's proposal or any other measure that would address the "Medicare funding warning." If the House fails to vote on the legislation by July 30, the law provides for an expedited discharge process to bring the legislation to the floor of the House of Representatives.

Under Sec. 804 of the MMA, the Senate Majority Leader and Minority Leader are required to introduce the President's legislation, which is to be referred to the Senate Finance Committee. This remedial legislation and any companion legislation enacted by the House of Representatives would be subject to special procedures prescribed for expedited Senate floor consideration. If the Senate Finance Committee does not report the "Medicare funding legislation" by June 30, any Senator may move to discharge the legislation from committee consideration and bring it to the floor for full Senate consideration.

The motion to discharge the remedial legislation is no longer available to Senators if the Chairman of the Senate Budget Committee certifies that legislation eliminating the "excessive" general revenue funding of Medicare has already been enacted. Otherwise, the discharge motion takes priority over other measures or motions; it cannot be amended, and debate on the motion is to be limited to two hours.

What Washington Should Do. The law provides a rare opportunity for the President and Congress to deal directly with the entitlement crisis in a responsible bipartisan fashion.

A single package of remedial legislation should include both short- and long-term changes in the Medicare program. The short-term budgetary changes could bring the program into compliance with the requirement that Medicare's reliance on general funds remain within the 45 percent range, while long-term changes (enacted with a date certain for implementation) should address the graver problem—the enormous unfunded liability of the program that threatens the future standard of living of working families. A crucial test of the proposals would be their logical compatibility; that is, any short-term changes should be logically compatible with efforts to secure the long-term reform of the Medicare program. There are ample reform options to accomplish both objectives.

Short-Term Changes. Congress should make specific changes in Medicare policy that would be compatible with a broader Medicare reform. President Bush has already offered several proposals that would better target Medicare funding to those who need the most help. For example, Congress could

1. The President has indicated, however, that he is not constitutionally bound by this legislative directive. Nonetheless, if the President decided to submit such legislation, he would do so before February 19, 2008, since he submitted his budget on February 4, 2008.
2. The White House, Office of Management and Budget, *Fiscal Year 2009 Budget of the U.S. Government*, (Washington, D.C.: United States Government Printing Office, 2008), p. 22.
3. It should be noted that the specific funding issue could also be addressed directly by raising the Medicare payroll tax, since higher dedicated revenues would decrease the draw-downs on the Treasury. This option, however, would leave unresolved the problem of the growth in Medicare spending.

start by limiting taxpayer subsidies to wealthy beneficiaries in Medicare Part B through an elimination of the annual indexing of income-related Part B premiums. This would mean that the income threshold would not be adjusted upwards each year, resulting in billions of dollars in savings. Congress could also apply the Medicare Part B income-related premium rules to Medicare Part D, the prescription drug program.[4] Congress could also explore a more rational cost-sharing structure for traditional Medicare, including the hospital program, that would vary co-payments on the basis of income.

Long-Term Comprehensive Reform. Medicare should remain as it is today for all current Medicare beneficiaries; but for future Medicare beneficiaries, at a certain date, the program should be transformed into a defined-contribution system. This would guarantee seniors and disabled citizens a wide choice of health plans while making Medicare funding predictable to taxpayers. The government contribution should reflect the real conditions of supply and demand for medical services, and the contribution for beneficiaries should also be adjusted for significant factors such as age, income, or health status. Medicare enrollees would be able to bring their private health insurance coverage with them into retirement if they wished to do so, or they could pick any other licensed health plan of their choice.

As in the Federal Employees Health Benefits Program (FEHBP),[5] the government contribution should be capped annually for enrollees at a specific dollar amount. If they wanted to buy an expensive health plan at a price greater than the government contribution, they would be free to do so—just as federal employees and retirees do today. If they wanted to buy a health care plan at an amount less than the government contribution, they would be able to keep 100 percent of the difference in the savings. For enrollees, this would be an improvement over both the FEHBP, which does not provide rebates, and Medicare Advantage,[6] which limits savings to enrollees to 75 percent of the total amount of savings.

In the design of a new Medicare program for the next generation, the President and Congress can draw upon a treasure trove of policy work that has already been completed in this area. They should borrow from the best features of the FEHBP, Medicare Advantage, and Medicare Part D and should consider the majority recommendations of the National Bipartisan Commission on the Future of Medicare, reported in 1999.

Change the Legislative Dynamics. The trigger included in the MMA requires actions by Congress and the Administration to ensure a more fiscally sustainable future for Medicare. In a sense, it is a tacit admission that the current legislative system for ensuring sound financial health for Medicare is flawed. The same is true for Social Security.

Though they currently comprise about one-third of the entire federal budget, Congress is not required to pass an annual budget for either program. Rather, they each operate on auto-pilot under formulas contained in their governing laws. Moreover, the tendency of politicians to make promises to expand or enact new benefits is greatly enhanced by the lack of any measure of long-term costs of these programs in the budget. Two changes should be made in the budget process to ensure better stewardship for the nation's long-term solvency.

First, Congress should ensure that the long-term costs for entitlement programs are built into the budget process and considered along with other priorities during the annual budget process so that spending on Medicare would be considered in the same context as defense, education, or tax policy. Any changes in entitlement programs should also

4. Robert E. Moffit, "The President's Medicare Budget Proposal: A Step Forward on Entitlement Spending," Heritage Foundation *WebMemo* No. 1344, February 6, 2007.
5. Stuart Butler, "The FEHBP as a Model for Reforming Medicare," Testimony, March 20, 2002, at *www.heritage.org/Research/HealthCare/Test032002.cfm.*
6. Medicare Advantage is an optional system of private Medicare plans which offers more generous benefits and lower cost-sharing. It is especially valued by seniors who live in rural areas or those with lower incomes who cannot afford supplemental coverage. For more information, see "The Facts: Medicare Advantage," at *www.heritage.org/Research/HealthCare/factsonmedicareadvantage.cfm.*

be measured over the long term. When the Medicare drug benefit was enacted, there was no debate over the costs it would impose on younger generations. It was only after the law was passed that Congress and the public learned that this burden was as large as the entire federal debt. Bringing long-term costs into the legislative debate will mean that, unlike today, Congress must consider whether children and grandchildren can really afford to pay for new benefits for their parents and grandparents.

Second, Congress should put all programs on a more level playing field—from "discretionary" programs like defense and education to "mandatory" programs like Medicare and Social Security (also referred to as "entitlements"). Because entitlement programs grow on auto-pilot, they are putting more budgetary pressure on other priorities, so there is not a fair or honest consideration of budgetary trade-offs. At the same time, retirement programs require longer time horizons and planning. Thus, Congress should create a framework for a budget that would be periodically evaluated to ensure that entitlement programs are sustainable over the long term.

This could be done by creating a long-term budget window—for example, 30 years. All spending on entitlements would have to be reviewed and reauthorized every five years. This is similar to how other countries manage their long-term commitments. Congress should include "triggers" that would make automatic adjustments should spending grow above budgeted levels. One way to keep spending within budgeted levels would be to *automatically* raise premiums, deductibles, and out-of-pocket expenses for Medicare Part B and Part D for middle- and upper-income retirees.

Conclusion. Since the enactment of the MMA, Congress has repeatedly been warned about the explosive growth of entitlement spending on the horizon. Congress has steadfastly refused to address the gravity of the situation. Now the cost-containment provisions embodied in the MMA are forcing Washington to begin taking action.

Congress has an opportunity to forge a sound policy that will address the immediate need to bring the program into the funding balance required by law—while also setting in motion changes that will result in long-term savings to the taxpayer. Instead of simply re-adjusting Medicare payment formulas, tightening price controls on doctors and hospitals, or imposing research-killing price regulations on prescription drugs, Congress should go back to the drawing board and craft a rational and responsible Medicare policy that integrates short-term and long-term reform objectives and aligns incentives for doctors, patients, and health plans. At the same time, Congress should change the budget process to account for a longer time horizon. This would tilt the political dynamics toward sound fiscal management and better stewardship for future generations.

Current Medicare law provides Congress and the taxpayers an early warning. It gives Congress the opportunity to put the long-term good of the country, taxpayers, and seniors ahead of short-term partisan politics. It can be done. Congress has no excuse for "blowing it."

—Robert E. Moffit, Ph.D., is Director of the Center for Health Policy Studies and Alison Acosta Fraser is Director of the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.