

A Guide to Medicare's Financial Challenges and Options for Improvement

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Understanding Medicare's current challenges: three things you need to know

- How Medicare is financed
- The facts about Medicare's financial condition (findings from the 2012 Medicare Trustees Report)
- Some current proposals for improving Medicare's financial condition



Structure of the Medicare trust funds

	Hospital Insurance trust fund (HI)	Supplementary Medical Insurance trust fund (SMI)
Benefits	Part A inpatient hospital care	Part B physician and outpatient care; Part D prescription drug benefit
Financing	Payroll taxes	Beneficiary premiums and general tax revenues

Note: Medicare Advantage (MA) plans, also known as Medicare Part C, cover inpatient hospital care as well as physician and outpatient care. They can also cover prescription drugs. MA plans are funded through both the HI and SMI trust funds.



What is Medicare's financial condition?

- Income to the HI trust fund is not enough to cover the HI portion of Medicare benefits
- Increases in SMI spending will increase both beneficiary premiums and the cost to the federal government
- Increases in overall Medicare spending threaten the program's sustainability



Medicare HI Trust Fund income falls short of the amount needed to fund HI benefits

From the 2012 Medicare Trustees Report:

- In all future years, more money is going out than coming in
- Assets currently in the HI trust fund will have to be drawn down in order to finance the shortfall
 - The HI trust fund is projected to be depleted by 2024
 - HI revenues projected to cover only 87% of benefits in 2024
- Eliminating the shortfall over the next 75 years would require:
 - Immediate 47% increase in payroll taxes, or
 - Immediate 26% reduction in benefits, or
 - Some combination of the two



Increases in SMI costs increase pressure on beneficiary budgets and the federal budget

- The SMI trust fund will remain solvent, but only because premiums and government contributions are adjusted each year to meet projected future costs
- Increase in SMI spending will mean:
 - Higher beneficiary premiums
 - More federal funds will be necessary to support the program



Increases in total Medicare spending threaten the program's sustainability

- Medicare spending is expected to grow faster than the Gross Domestic Product (GDP), which means that more of the U.S. economy will be devoted to Medicare over time
 - According to the Medicare trustees, Medicare spending is projected to increase from 3.7% of GDP in 2011 to 5.3% in 2030, and to 6.7% in 2085
- A smaller part of the economy will be available for other priorities



Effect of health care reform on Medicare

- The Affordable Care Act (ACA) includes a number of Medicare-related provisions that will improve Medicare's financial condition by reducing spending and increasing revenues
- This represents an important first step, but it is *NOT* enough to solve Medicare's long-term financial problems



We need action now

- Medicare continues to face serious long-term financial challenges
- Improving Medicare's financial condition will require:
 - Increasing revenues,
 - Reducing spending, or
 - Some combination of both

“The sooner solutions are enacted, the more flexible and gradual they can be.”

--2012 Medicare Trustees Report



What are some of the specific options?

- Limit the growth in health spending
- Transition to a premium support or voucher program
- Expand the authority of the Independent Payment Advisory Board (IPAB) established by the ACA
- Reform the Sustainable Growth Rate system
- Reduce spending for prescription drugs
- Revise the “traditional Medicare” fee-for-service (FFS) benefit design and cost-sharing requirements
- Raise the Medicare eligibility age
- Increase Medicare Part B premiums



Choosing among the options

- How can we evaluate a proposal for improving Medicare's financial condition? Some criteria include:
 - How it affects the cost of the program
 - How it affects beneficiaries' access to care
 - How it affects the quality of care
 - Whether it slows the growth in health spending, rather than just shifting costs from one payer to another
 - Whether it gives health care providers, and their patients, incentives that encourage the kind of integrated and coordinated care that could help both control costs and improve quality



Option: Limit the growth in health spending

- Set spending targets for Medicare or for all health spending that trigger automatic cuts to benefits or provider payments if exceeded
- Cost:
 - Medicare savings would depend on how aggressively (i.e., low) spending targets are set
 - Savings would be offset to the extent that costs are shifted to other payers
- Access/Quality: Depends on the specific recommendation



Option: Transition to a premium support or voucher program

- Federal government would limit amount it contributes toward Medicare coverage (or private plans)
- Beneficiaries would pay the difference between plan premiums and the government contribution
- Cost: Depending on how contribution is set, federal Medicare spending could be lower than currently projected
 - Beneficiaries could face higher premiums and cost sharing
 - Could lower spending growth by reducing utilization
- Access/Quality:
 - Access to coverage may decline if beneficiaries have to pay higher premiums
 - To bring costs down, care quality might be compromised



Option: Expand the authority of the Independent Payment Advisory Board (IPAB)

- IPAB is charged with making recommendations to reduce growth in Medicare spending if spending exceeds a targeted growth rate
- This option would remove some restrictions on IPAB's recommendations and/or give it authority over all federal health spending
- Cost: To the extent that spending growth targets are lowered, more cost savings could be achieved
- Access/Quality: Depends on specific recommendations



Option: Reform the Sustainable Growth Rate (SGR) system

- SGR formula reduces physician fees if cumulative spending exceeds a specified target
- Physician fee cuts of 31% estimated for 2013
 - Scheduled fee cuts are usually overridden, but overrides are becoming more expensive
 - Large fee cuts could threaten access to care
- Option would eliminate SGR and develop a new physician payment system



Option: Reform the Sustainable Growth Rate (SGR) system (cont.)

- Cost: Eliminating SGR would increase Medicare spending projections unless offset by other spending reductions
- Access/Quality:
 - Could help maintain access to care
 - New payment system could better align payments with provision of high-value care



Option: Reduce spending for prescription drugs

- Options include:
 - Require Medicare to negotiate drug prices under Part D
 - Expand drug rebates
 - Establish a government-run Part D drug plan option
- Cost: By reducing prescription drug prices, would lower Part D spending and beneficiary premiums
- Access/Quality:
 - Could reduce pharmaceutical research and development
 - Government-run Part D option could lead to private plans leaving the market, reducing enrollee choice



Option: Revise fee-for-service (FFS) benefit design and cost-sharing requirements

- Concerns regarding current FFS plan design:
 - Deductibles are higher for inpatient care
 - Most beneficiaries have supplemental policies, reducing the financial incentive to seek cost-effective care
 - No limit on what a beneficiary may have to pay in a year
- Options include:
 - Combine Parts A and B cost-sharing and add a limit on beneficiaries' annual "out-of-pocket" spending
 - Eliminate first-dollar coverage in Medigap plans or levy excise tax on plans with first-dollar coverage



Option: Revise FFS benefit design and cost-sharing requirements (cont.)

- Cost:
 - Increasing cost-sharing requirements could reduce Medicare spending, but shift costs to beneficiaries
 - Savings also from reduced utilization
- Access/Quality:
 - Could better align beneficiary incentives for high-quality, cost-effective care
 - Low-income and chronically ill more sensitive to cost-sharing increases



Option: Raise the Medicare eligibility age

- Options include increasing Medicare eligibility age from 65 to 67 or higher and/or index it for increased longevity
- Cost:
 - Would reduce Medicare costs, but savings would be offset by increased federal spending in other areas (e.g., premium subsidies through health insurance exchanges, Medicaid)
- Access/Quality:
 - People between age 65 and new eligibility age would have to find new source of coverage
 - ACA provisions would increase the availability of other coverage sources



Option: Increase Part B premiums

- Current premiums set at 25% of costs
 - Beginning in 2007, higher-income beneficiaries pay between 35% and 80% of costs, depending on income
- Part B premiums could be increased for everyone, or raised even more for higher-income beneficiaries
- Cost: Would increase Medicare revenues by shifting costs to beneficiaries; would not affect Medicare spending
- Access/Quality: Beneficiaries unwilling or unable to pay higher Part B premiums might face reduced access to care



The bottom line

- Sooner is better than later
- Improving Medicare's long-term solvency and sustainability will ultimately require slowing the growth in health spending rather than just shifting costs from one payer to another
- Slowing the growth in health spending, while maintaining quality, will require provider payment and health care delivery systems that encourage integrated and coordinated care



What can you do?

- Understand that **there is no silver bullet**
 - There is no one, simple solution for shoring up Medicare
 - Ensuring that Medicare benefits are payable in the future will almost certainly require shared responsibility from Medicare beneficiaries, taxpayers, and health care providers
- **Learn as much as you can** about the Medicare program and its financial challenges
- **Urge your elected officials to act now** to put Medicare on a sound financial footing



Selected resources from the American Academy of Actuaries

- Medicare's financial condition
 - [Medicare's Financial Condition: Beyond Actuarial Balance](#) (Issue brief, May 2012)
 - [Revising Medicare's Fee-For-Service Benefit Structure](#) (Issue brief, March 2012)
 - [An Actuarial Perspective on Proposals to Improve Medicare's Financial Condition](#) (Issue brief, May 2011)
- Other related publications
 - [An Actuarial Perspective on Accountable Care Organizations](#) (Issue brief, June 2011)
 - [Health Insurance Coverage and Reimbursement Decisions: Implications for Increased Comparative Effectiveness Research](#) (Issue brief, Sept 2008)
 - [Value-based Insurance Design](#) (Issue brief, June 2009)



Resources from the American Academy of Actuaries (cont.)

- All publications from the American Academy of Actuaries are available at www.actuary.org

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