American Academy of Actuaries

Issue Brief

Medicare's Financial Condition: Beyond Actuarial Balance

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Key Points

- The Medicare Program faces serious financing challenges:
  - Income to the Hospital Insurance (HI) trust fund is not adequate to fund HI benefits after 2027;
  - Increases in costs to the Supplementary Medical Insurance (SMI) trust fund increases pressure on beneficiary household budgets and the federal budget; and
  - Increases in total Medicare spending threatens the program's long-term sustainability.
- As calculated in the 2025 Medicare Trustees Report, the projected HI trust fund depletion date of 2033 is three years earlier than projected last year and the 75-year HI deficit is higher. It remains critical to address the HI shortfall sooner rather than later.
- Changes continue to be needed to improve Medicare's long-term solvency and sustainability. Delaying corrective measures increases the likelihood of financial burdens being imposed on beneficiaries and taxpayers. As changes to improve Medicare's financial condition are considered, they should be evaluated in terms of the program's ability to meet beneficiaries' health care needs.

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Each year, the Boards of Trustees of the Federal Hospital Insurance (HI) and Supplementary Medical Insurance (SMI) Trust Funds submit the statutorily required report, frequently referred to as the Medicare Trustees Report, on the Medicare program's financial condition to Congress.[1]

The federal Medicare program is operated through two trust funds. The first, the HI trust fund (Medicare Part A), pays primarily for inpatient hospital services and post-acute care. The second, the SMI trust fund, includes the Medicare Part B program, which covers physician and outpatient hospital services, and the Medicare Part D program, which covers prescription drug costs. Medicare Advantage (MA) plans, which cover Part A and Part B services, receive capitated payments funded through both the HI and the SMI trust funds.

The annual Medicare Trustees Report is the primary source of information on the financial status of the Medicare program, reflecting the valued expertise and contributions of federal actuaries who prepare and provide additional analyses.

The 2025 Medicare Trustees Report finds that the HI trust fund is projected to be depleted in 2033, three years earlier than in last year's report. The program faces three fundamental long-range financing challenges:

- Income to the HI trust fund is not adequate to fund the HI portion of Medicare benefits after 2027;
- Increases in SMI costs increase pressure on beneficiary household budgets and the federal budget; and
- Increases in total Medicare spending threaten the program's sustainability.

1 2025 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds; The Boards of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds; June 2025.

The trustees conclude: “The projections in this year’s report continue to demonstrate the need for timely and effective action to address Medicare’s remaining financial challenges—including the projected depletion of the HI trust fund, this fund’s long-range financial imbalance, and the rapid growth in Medicare expenditures.”[2]

In this issue brief, the American Academy of Actuaries’ Medicare Committee examines the findings of the Medicare Trustees Report with respect to program solvency and sustainability. The Medicare program continues to face serious financing problems. Due to Medicare’s critically important role in ensuring that Americans age 65 and older and certain younger adults with permanent disabilities have access to health care, it is important for policymakers to address the challenges that threaten the program’s long-term solvency and financial sustainability. The longer that corrective measures are delayed, the worse the financial challenges will become and, in turn, the greater the burden that is likely to be imposed on beneficiaries, providers, and taxpayers.

Medicare HI Trust Fund Income Falls Short of the Amount Needed to Fund HI Benefits

Medicare’s trust funds account for all income and expenditures. The HI and SMI programs operate separate trust funds with different financing mechanisms. General revenues, payroll taxes, premiums, and other income are credited to the trust funds, which are used to pay benefits and administrative costs. Any unused income is required by law to be invested in U.S. government securities for use in future years. In effect, the trust fund assets represent loans to the U.S. Treasury’s general fund. The HI trust fund, which pays for inpatient hospital services and post-acute care, is funded primarily through earmarked payroll taxes.

2 Ibid., p. 43-44.

This paper was drafted by the Medicare Committee, whose members include: Derek Skoog, MAAA, FSA – *Chairperson*; Emily Bartel, MAAA, ASA; Andrew Bourg, MAAA, ASA; Bradley Budnick, MAAA, ASA; Eric Buzby, MAAA, FSA; Veronika Chervenska, MAAA, FSA; Peter Davidson, MAAA, FSA; Glynn Davis, MAAA, ASA; Marshall Forest, MAAA, FSA; Tyler Grossi; MAAA, ASA; William Olaprath, MAAA, ASA; David O’Shaughnessy, MAAA, FSA; Bradley Paulis, MAAA, ASA; Ryan Pestka, MAAA, ASA; Bruce Pyenson, MAAA, FSA; Neela Ranade, MAAA, FSA; Brian Regan, MAAA, FSA; David Scholl, MAAA, ASA; Annoria Shah, MAAA, ASA; Paul Spitalnic, MAAA, ASA; Cori Uccello, MAAA, FCA, FSA; and Todd Wanta, MAAA, FSA.

The projections of Medicare's financial outlook in the report are based on current law. The projected HI trust fund exhaustion date is 2033, three years earlier than projected in last year's Medicare Trustees Report. In addition, the 75-year HI deficit increased—from 0.35% of taxable payroll in the 2024 report[3] to 0.42% in this year's report. This is mainly due to higher-than-anticipated 2024 expenditures and higher projected spending for inpatient hospital and hospice services. These impacts are partially offset by lower payment updates.

- **HI expenditures are projected to exceed HI revenues.** HI revenues exceeded expenditures in 2024, and fund surpluses are expected to continue through 2027. Deficits are projected to return beginning in 2028 and to persist for the remainder of the projection period. As a result, the HI trust fund assets will need to be redeemed. When the federal government is experiencing unified budget deficits, funding the redemptions requires that additional money will need to be borrowed from the public, thereby increasing the federal deficit and debt.

- **The HI trust fund is projected to be depleted in 2033.** At that time, revenues are projected to cover only 89% of program costs, with the share declining to 86% in 2049 and then increasing to about 100% in 2099. Current law bars general-fund transfers for HI deficits.

- **The projected HI deficit over the next 75 years is 0.42% of taxable payroll.** Eliminating this deficit would require an immediate increase in the standard payroll tax (2.90%) to the amount of the actuarial deficit (3.32%), resulting in a 14% increase in the standard payroll tax, an immediate 9% reduction in expenditures, or some combination of payroll tax increases and expenditure reductions. Delaying action would require more significant changes in the future.

The trustees acknowledge that the estimates based on current-law projections could understate the seriousness of Medicare's financial condition, because actual Medicare expenses might exceed current-law estimates. In particular, the trustees and the chief actuary of the Center for Medicare and Medicaid Services' (CMS) Office of the Actuary (OACT) point to scheduled reductions in provider payments that may not occur. Current law requires downward adjustments in payment updates for most non-physician providers to reflect productivity improvements; however, these adjustments might not be sustainable in the long term. There is a more immediate concern related to physician services, as payment rate updates have been low or even negative for a number of years and are projected to be below the rate of inflation in all future years. In the Statement of Actuarial Opinion that accompanies the Medicare Trustees' Report, the CMS chief

3 2024 Annual Report of the Boards of Trustes of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds; The Boards of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds; May 2024.

actuary specifically states, "[s]hould payment rates prove to be inadequate for any service, beneficiaries' access to and the quality of Medicare benefits would deteriorate over time, or future legislation would need to be enacted that would likely increase program costs beyond those projected under current law in this report."[4]

At the request of the trustees, the CMS Office of the Actuary developed an alternative analysis, providing an illustration of the potential understatement of current-law Medicare cost projections should the productivity adjustments be phased down gradually beginning in 2028 and physician updates were more consistent with cost growth.

Although the illustrative alternative projections are not intended to be interpreted as the official best estimates of future Medicare costs, they do, as noted in the trustees' report, "…help illustrate and quantify the potential magnitude of the cost understatement."[5]

Under the alternative scenario, the HI trust fund would still be depleted in 2033. However, the projected deficit over the next 75 years would be 1.28% of taxable payroll, compared to 0.42% under current law. Eliminating this deficit requires an immediate 44% increase in standard payroll taxes or a 24% reduction in expenditures or some combination of the two.

Increases in SMI Costs Increase Pressure on Beneficiary Household Budgets and the Federal Budget

The SMI trust fund includes accounts for the Medicare Part B program, which covers physician and outpatient hospital services, and the Medicare Part D program, which covers prescription drug costs. Approximately one-quarter of SMI spending is financed through beneficiary premiums, with federal general tax revenues covering the remaining three-quarters.[6]

The SMI trust fund is expected to remain solvent because its financing resets annually to meet projected future costs. As a result, increases in SMI costs require increases in beneficiary premiums and general revenue contributions. Increases in general revenue contributions will put more pressure on the federal budget. SMI general revenue funding is scheduled to double from 1.7% of gross domestic product (GDP) in 2024 to 3.5% in 2099.

4 2025 report, *op. cit.*, p. 261.

5 Ibid., p. 197.

6 Premiums for Medicare Parts B and D are income-related. Standard premiums are set to cover approximately 25% of program costs. Higher-income beneficiaries pay higher premiums, ranging from 35% of program costs to 85% of program costs. Many Part D beneficiaries will receive low-income premium subsidies, lowering their premiums below 25% of program costs. In the aggregate, beneficiary premiums covered only about 13% of total Part D costs in 2024. State payments on behalf of certain beneficiaries covered about 12% of costs and general revenues will cover the remaining 75% of costs.

Premium increases will similarly increase the burden 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 are projected to increase from 25% of the average Social Security benefit in 2025 to 39% of the average Social Security benefit by 2099. These expenses do not include cost-sharing under Part A.

The 2025 Medicare Trustees Report projects that total SMI spending will continue to grow faster than GDP, with total spending expected to increase from 2.4% of GDP in 2024 to 4.8% of GDP in 2099.

Spending under the illustrative alternative analysis would be higher, especially in the long term, reflecting the phase-down of productivity adjustments for non-physician provider payments and higher physician updates in the long range. SMI spending projected in the alternative analysis would increase from 2.4% of GDP in 2024 to 5.9% of GDP in 2099.

Increases in Total Medicare Spending Threaten the Program's Sustainability

A broader issue related to Medicare's financial condition is whether the economy can sustain Medicare spending over time. To help gauge the future sustainability of the Medicare program, the trustees consider the share of GDP that will be consumed by Medicare. With Medicare spending expected to continue growing faster than GDP, greater shares of the economic growth will be devoted to Medicare over time, meaning smaller shares of the economy will be available for other priorities.

Under current law, Medicare expenditures as a percentage of GDP will grow from 3.8% of GDP in 2024 to 6.7% of GDP in 2099. Under the CMS Office of the Actuary alternative scenario, total Medicare expenditures would increase to 8.8% of GDP in 2099 (see Table 1 below).

Table 1: Total Medicare Expenditures as a Percent of GDP

Calendar Year	2025 Report	2025 Alternative Projection
2024	3.8	3.8
2030	4.8	4.8
2040	5.9	6.1
2050	6.2	6.7
2060	6.4	7.2
2070	6.7	7.8
2080	6.8	8.3
2090	6.8	8.6
2099	6.7	8.8

Sources: 2025 Medicare Trustees Report, CMS Office of the Actuary.[7]

7 2025 report, *op. cit.*

Future Policy Considerations

As noted by the trustees, Medicare's financial challenges could be more severe than projected under current-law assumptions. The report's Medicare spending projections are considered understated, as the future impacts of novel health care delivery payment reforms' on reducing costs in the U.S. health care system is uncertain. The trustees recommend that "… policymakers [continue] to monitor the adequacy of Medicare payment rates over time to ensure beneficiary access to high-quality care."[8]

The trustees note the urgency of addressing Medicare's financial challenges, stating:

> The Board of Trustees believes that solutions can and must be found to ensure the financial integrity of HI and reduce the rate of growth in Medicare costs. The sooner solutions are enacted, the more flexible and gradual they can be. The early introduction of reforms also increases the time available for affected individuals and organizations—including health care providers, beneficiaries, and taxpayers—to adjust their expectations and behavior. The Board recommends that Congress and the executive branch work together to quickly address these challenges.[9]

Medicare's challenges are not solely financial. Medicare beneficiaries reflect a segment of the broader population with diverse health care needs. Certain beneficiary populations, such as those with a disability or multiple chronic conditions, may experience a greater impact due to these higher health care needs. Many beneficiaries have limited resources, which creates increasing financial challenges and difficult choices when faced with high out-of-pocket health costs. Aside from the addition of the prescription drug program (Medicare Part D) in 2006, Medicare's fee-for-service benefit package has remained mostly unchanged, with some services not covered and beneficiary out-of-pocket costs not capped. Therefore, any policy changes to improve Medicare's financial condition should consider how the proposed changes impact the program's ability to meet the health care needs of beneficiaries as well as whether the changes would encourage beneficiaries to seek cost-effective care.

8 Ibid., p. 197.
9 Ibid., p. 44.

Conclusion

Consistent with prior trustees' reports, the 2025 Medicare Trustees Report stresses the serious financial challenges facing the Medicare program. It remains critical to address the HI shortfall sooner rather than later. In addition, Medicare spending will continue to grow faster than the economy, increasing the pressure on beneficiary household budgets as well as the federal budget, threatening the program's sustainability.

Medicare's financial challenges could be more severe than projected, which leaves policymakers with the challenge to address the short- and longer-term challenges of program solvency while understanding the potential implications on beneficiary's ability to afford and receive appropriate health care. Understanding the implicit and explicit consequences of any potential change or lack thereof requires continued collaboration between actuaries, program and agency staff, consumer advocates, and Congress.