

Medicare and Social Security: Weighing Solvency

Cori E. Uccello, MAAA, FSA, FCA, MPP

Senior Health Fellow, American Academy of Actuaries

Ron Gebhardtsbauer, MAAA, FSA, FCA, EA

Senior Pension Fellow, American Academy of Actuaries

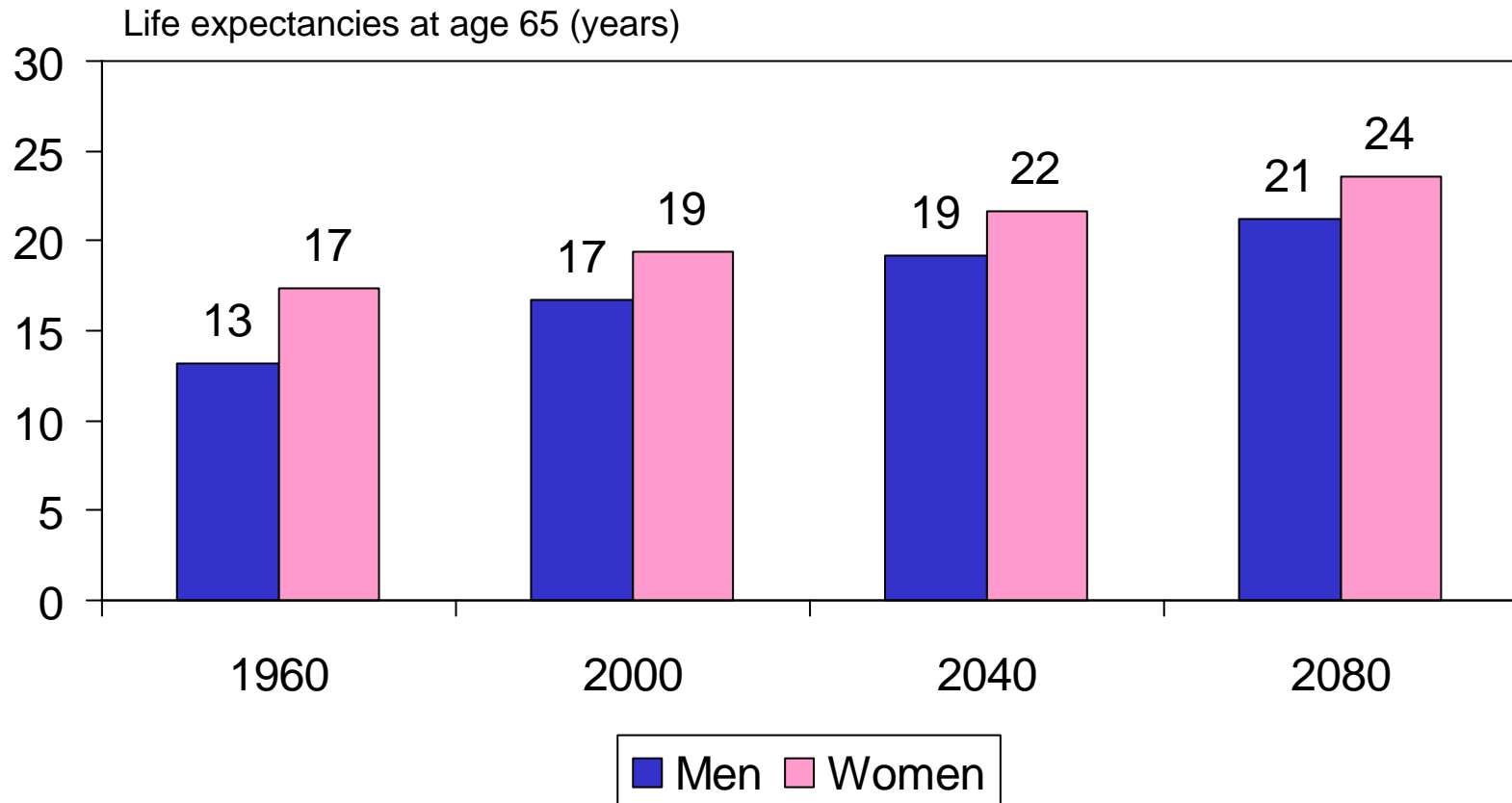
May 12, 2006

Noon – 1:00 pm

2261 Rayburn House Office Building



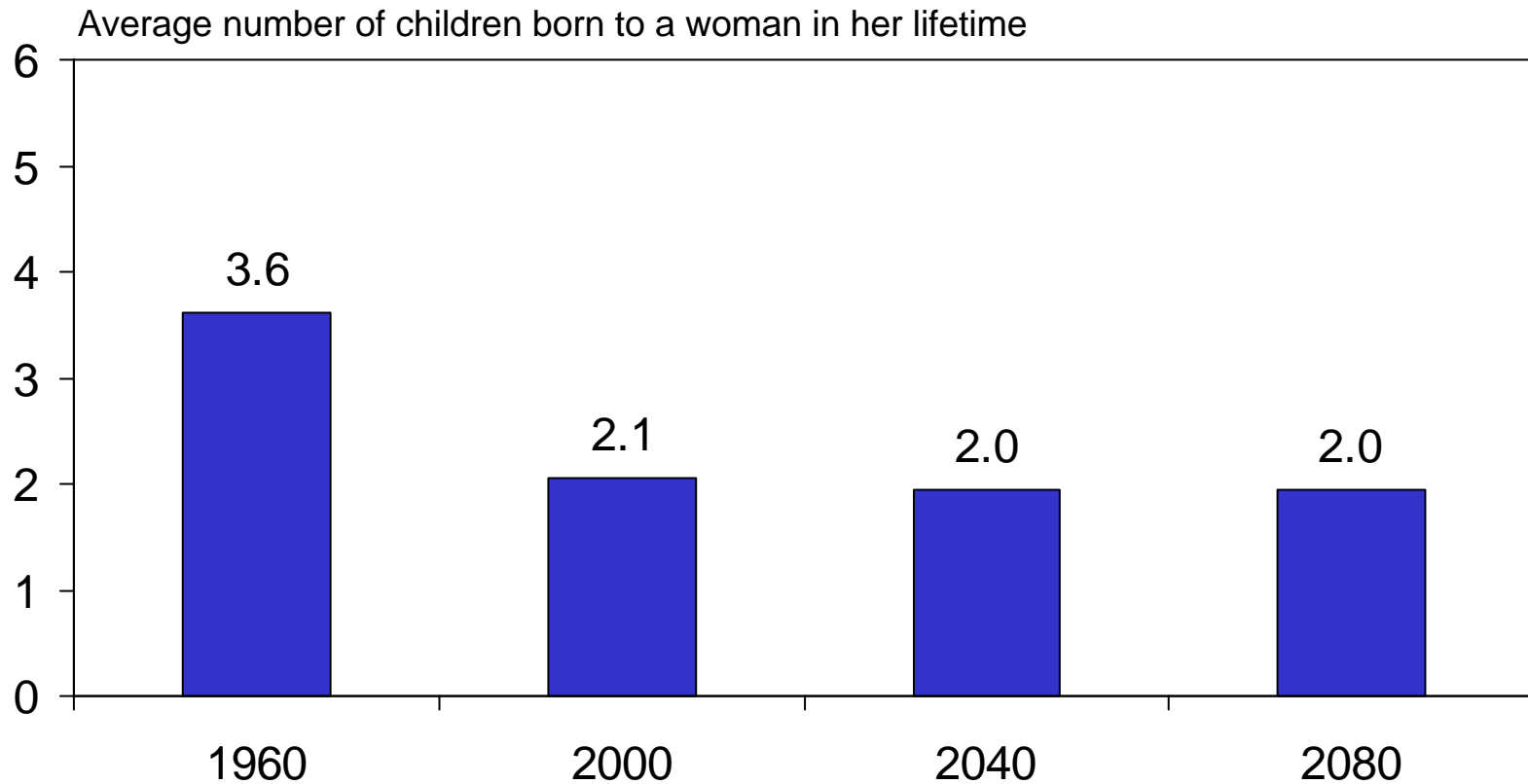
Seniors Are Living Longer



Source: Cohort life expectancies from the 2006 Social Security Trustees' Report, Intermediate Assumptions



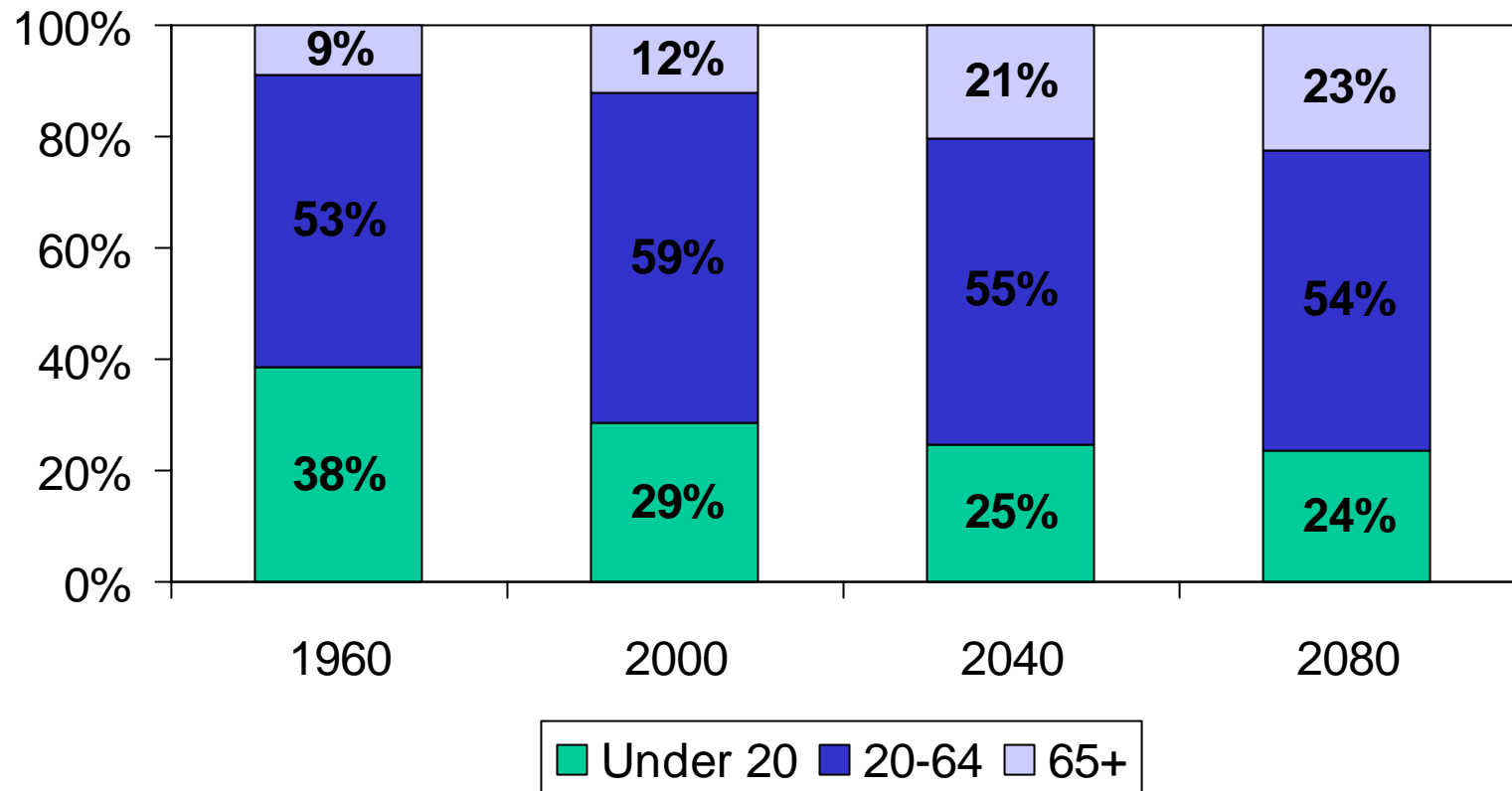
Birth Rates Have Declined



Source: 2006 Social Security Trustees' Report, Intermediate Assumptions



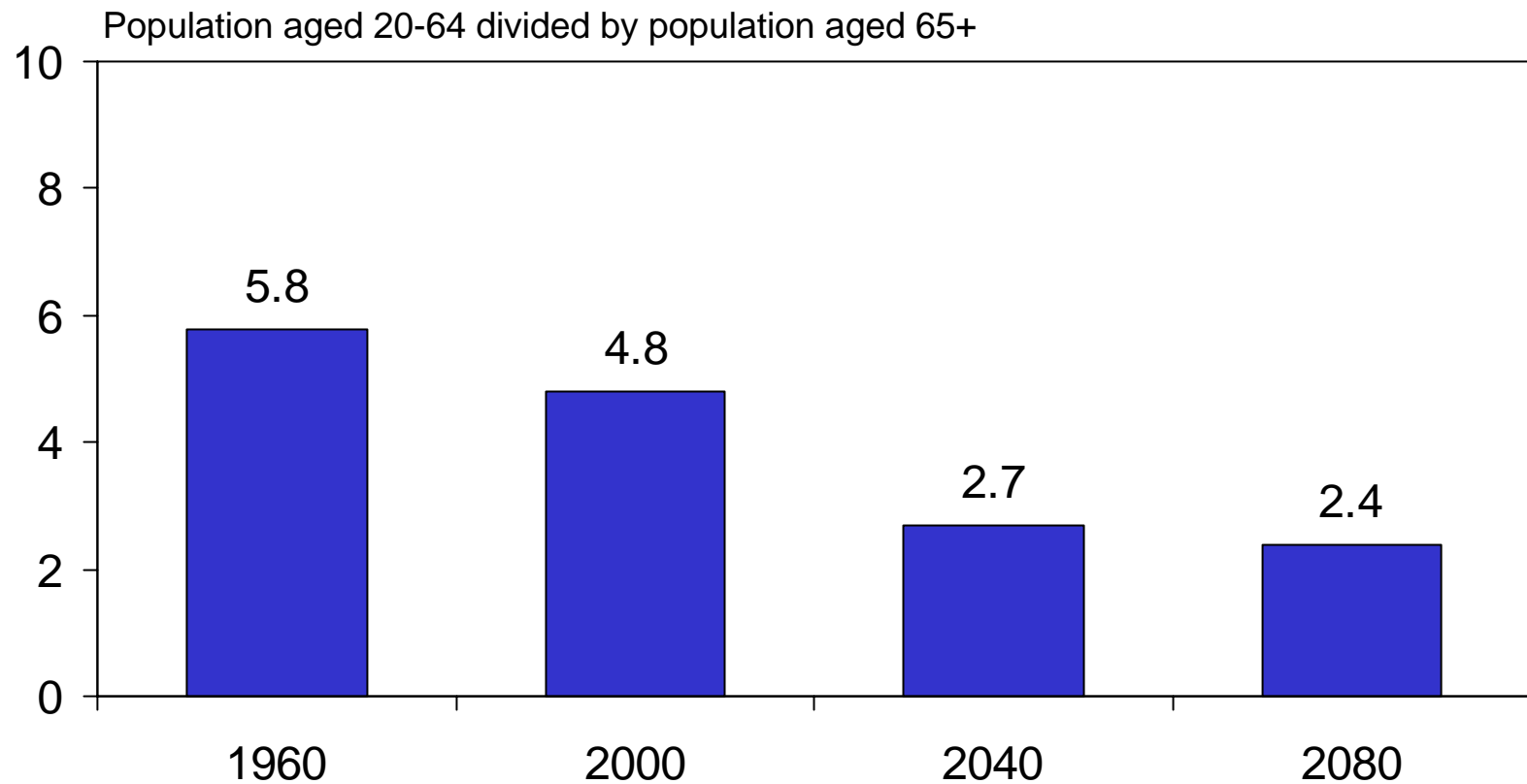
Seniors Are a Growing Share of the Population



Source: 2006 Social Security Trustees' Report, Intermediate Assumptions



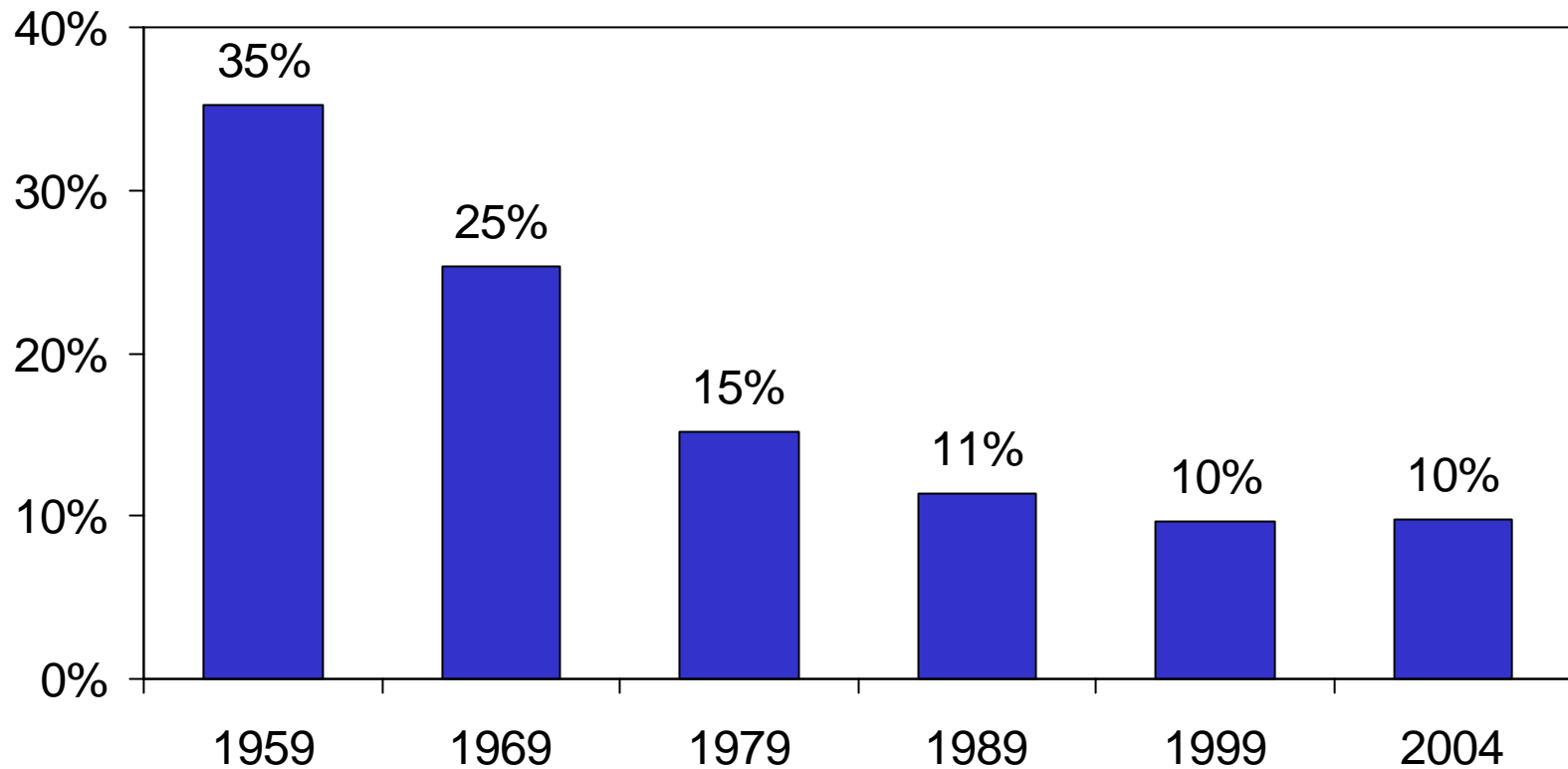
Fewer Workers To Support Each Retiree



Source: 2006 Social Security Trustees' Report, Intermediate Assumptions



Poverty Rates Among Seniors Have Declined Dramatically



Source: US Census Bureau's Current Population Survey.



Medicare

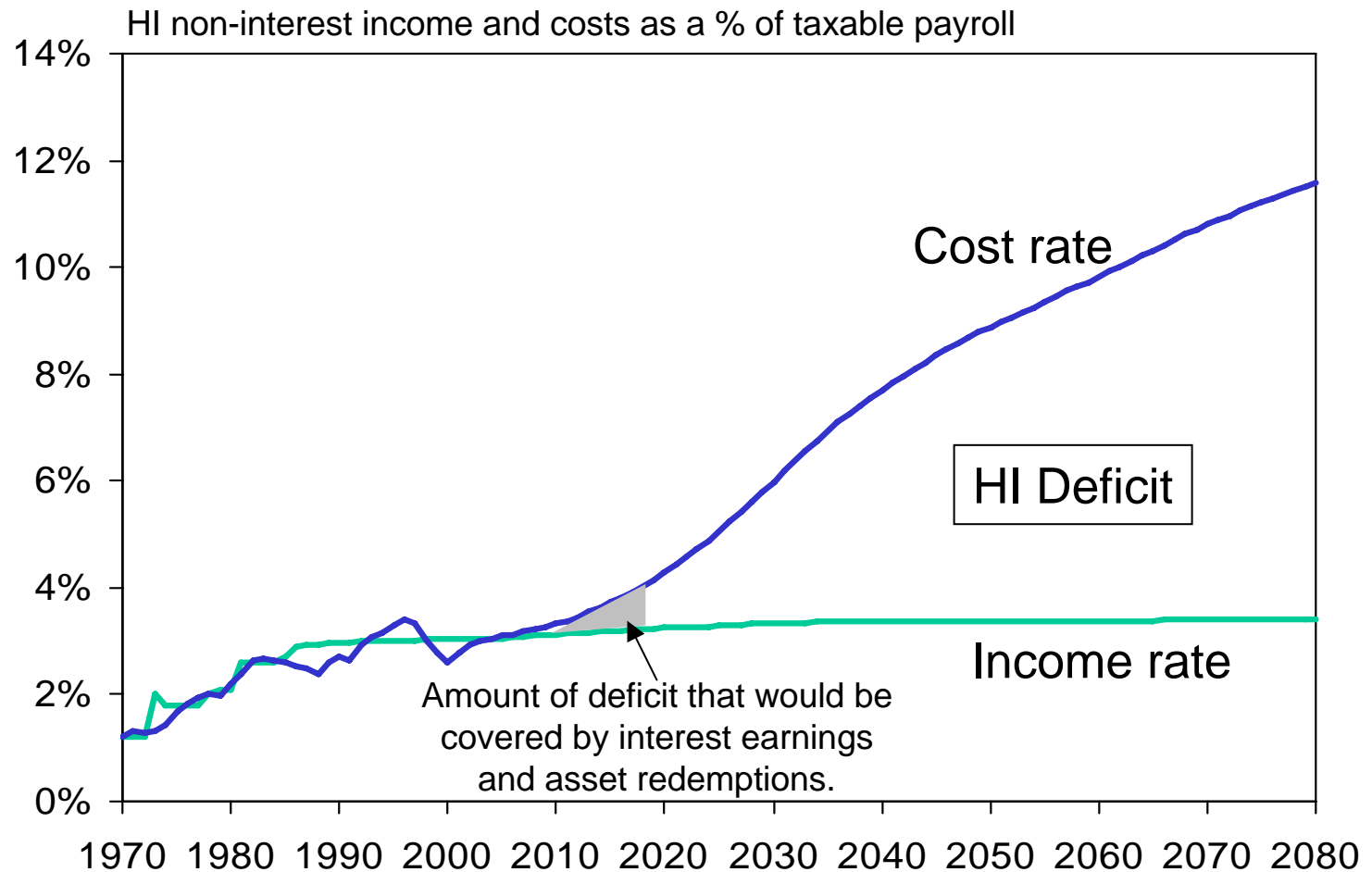


Medicare Trust Fund Basics

	Hospital Insurance (HI)	Supplementary Medical Insurance (SMI)
Benefits	Inpatient hospital care	Physician and outpatient care; Part D benefit
Financing	Payroll taxes	Beneficiary premiums (~25%) and general tax revenues (~75%)



HI Costs Will Exceed Non-Interest Income This Year



Source: 2006 Medicare Trustees' Report



Key Dates For HI Trust Fund

- First year outgo exceeds income
 - Excluding interest income – 2006
 - Including interest income – 2010
- Year trust fund assets are depleted=2018
- Trust fund depletion date (2018) is two years earlier than projected last year, due to:
 - Slightly higher hospital expenditures
 - Upward revisions in short-range assumptions about utilization of HI services



Bottom Line for HI Trust Fund

- HI tax revenues will cover 80% of benefits in 2018, when trust fund assets are depleted
- HI deficit over the next 75 years = \$11 trillion (3.4% of taxable payroll)
- Eliminating 75-year deficit would require:
 - Immediate 121% increase in payroll taxes, or
 - Immediate 51% reduction in benefits, or
 - Some combination

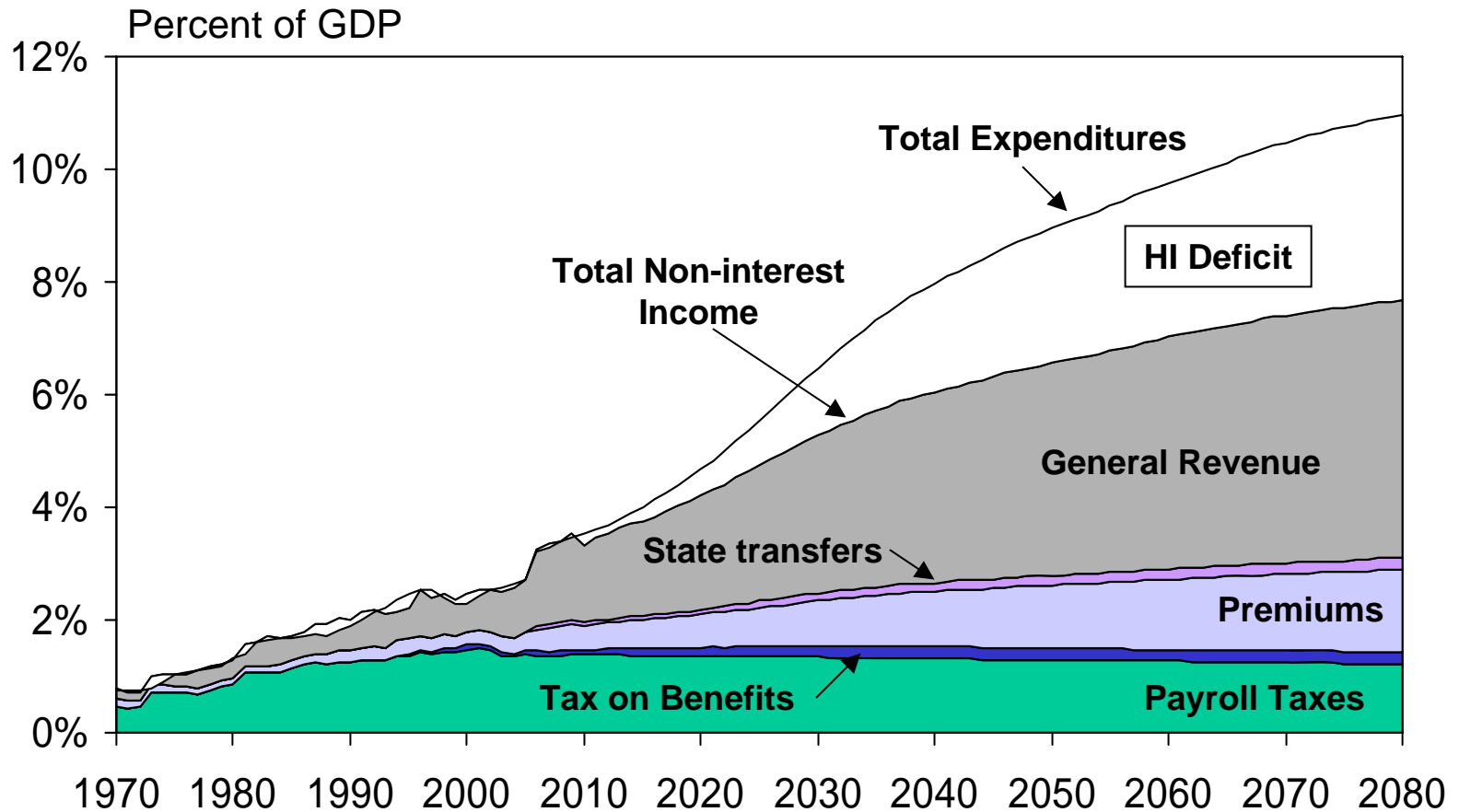


SMI Trust Fund

- The SMI Trust Fund, which includes new Rx benefit, is expected to remain solvent, but only because its financing is reset each year to meet projected future costs.
 - Projected increases in SMI expenditures will require increases in beneficiary premiums and general revenue contributions over time.
 - 2005 Part B monthly premium: \$78.20
 - 2006 Part B monthly premium: \$88.50
 - 2007 Part B monthly premium (projected): \$98.20
- SMI expenditures are projected to increase faster than HI expenditures. Therefore, general revenues will finance increasing share of overall Medicare expenditures.



Total Medicare Expenditures and Income



Source: 2006 Medicare Trustees' Report

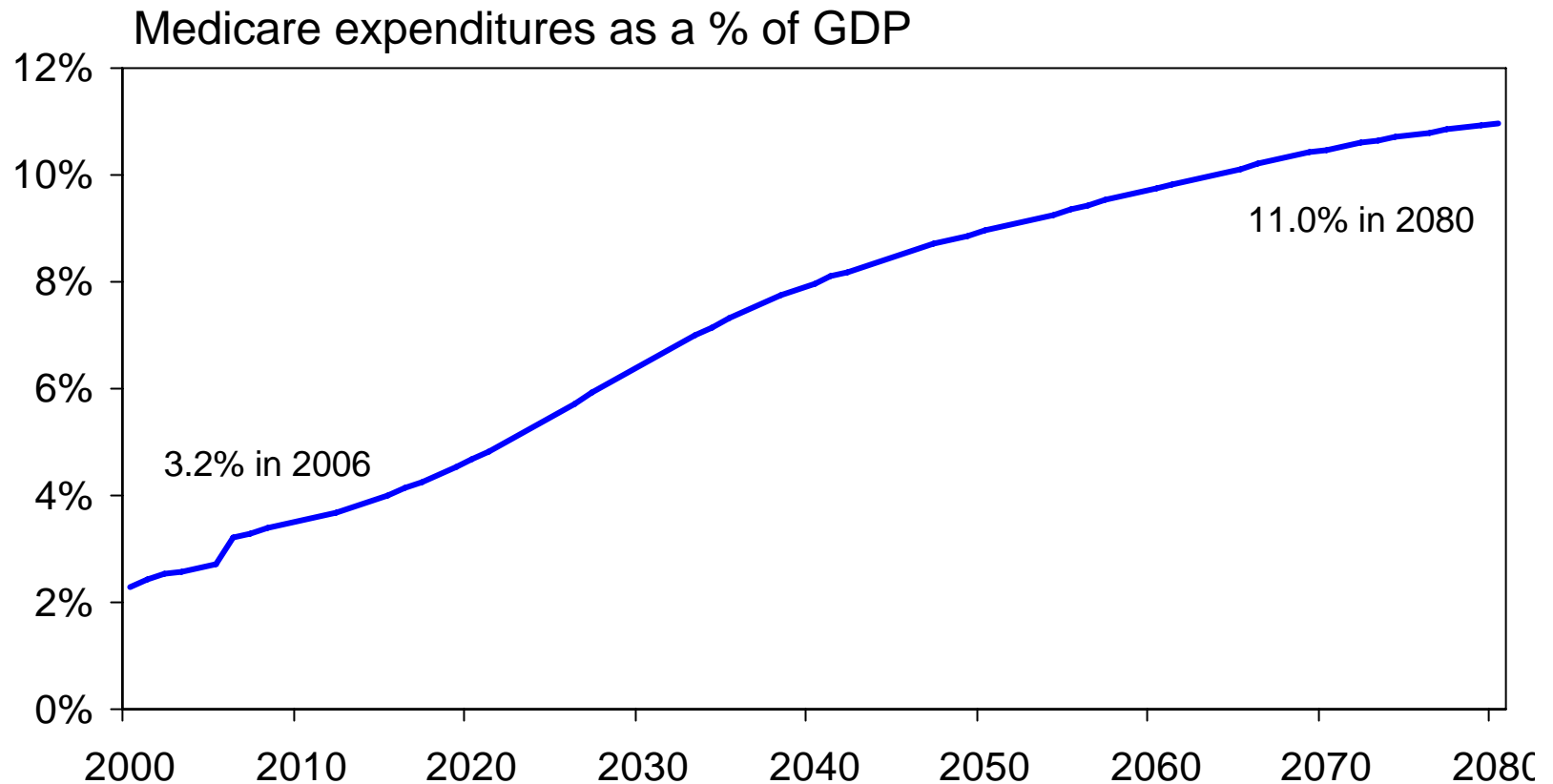


Limit on General Revenue Financing

- If for 2 consecutive Trustees' Reports, general funding sources account for more than 45% of Medicare spending within the next 7 years, the President is required to recommend ways to reduce this share.
 - President's legislative proposal must come within 15 days of next budget submission.
- Congress required to *consider* the legislation on an expedited basis.
- Medicare Trustees' Report estimates that the 45% threshold will be reached in 2012, thereby triggering the provision in 2007.
 - President's legislative proposal would be required in 2008.



Rising Costs Are Key Challenge to Medicare's Long-Term Sustainability



Source: 2006 Medicare Trustees' Report



Social Security

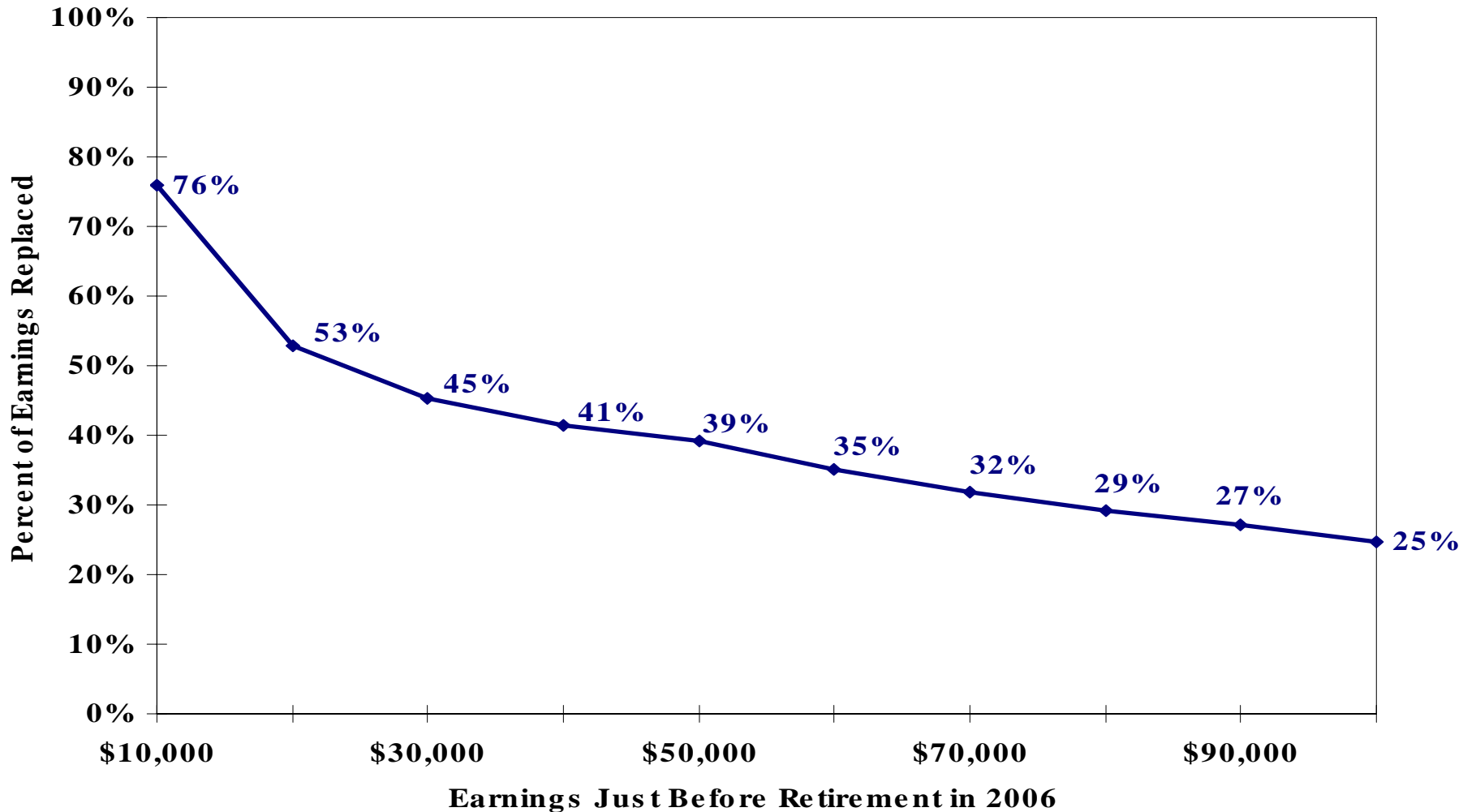


Social Security Benefits

- Replacement rates maintained
 - Initial benefits increase by average wages each year
- Benefits being paid increase by CPI each year
- Payable for life
 - No matter how long you live
 - No matter how bad the markets
- Disability and Survivor benefits (1/3rd of total benefits)
- Spousal benefits
 - At least 50% of worker's benefit
 - Survivor: at least 100% of worker's benefit
 - Valuable for non-working spouses



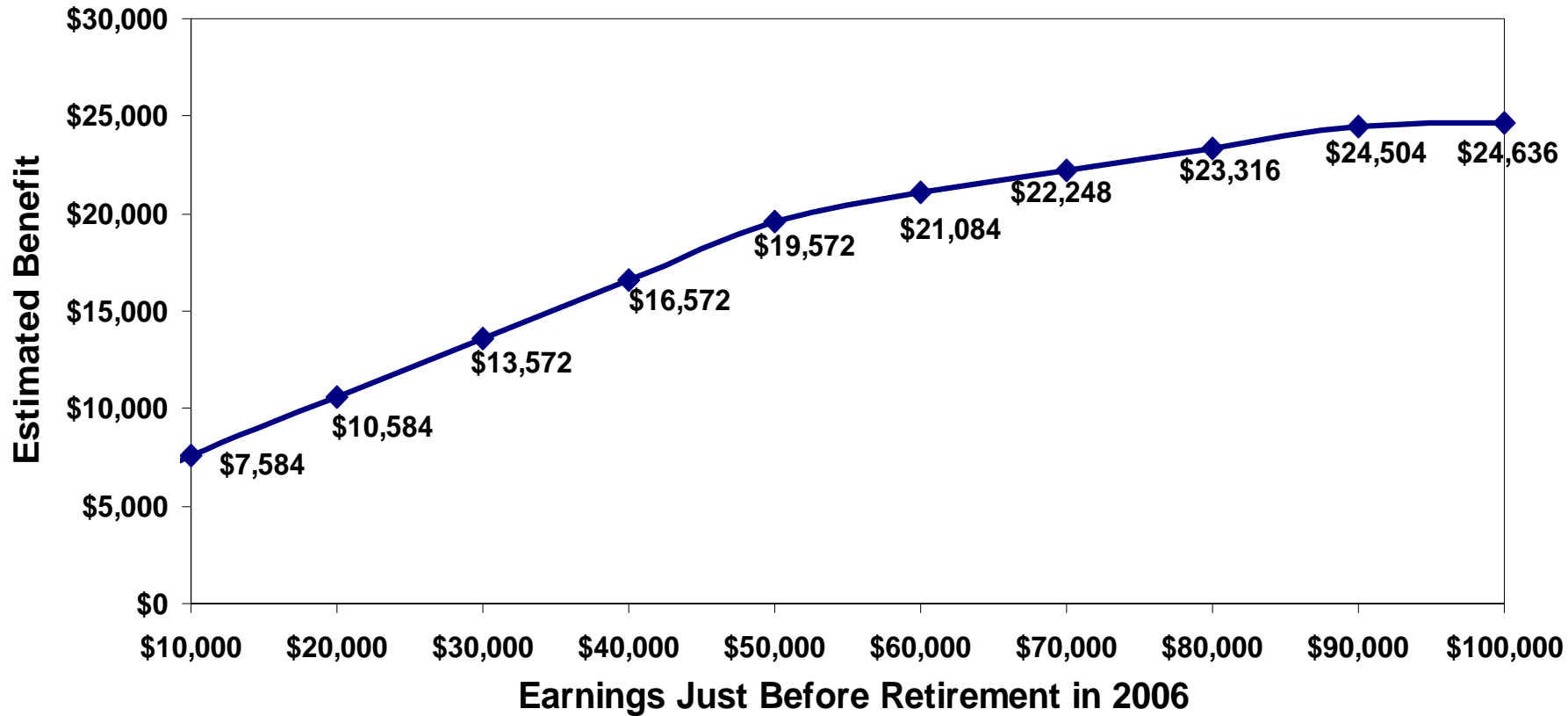
Social Security Replacement Ratios at Normal Retirement Age (and at Disability)



See History of Provisions at www.ssa.gov/OACT/HOP. Past wages based on National Average Wage Index
These percentages decrease by about 5 percentage points over the next 20 years, per Table VI.F10 in 2006 rpt.



Social Security Benefits at Normal Retirement Age (and at Disability)



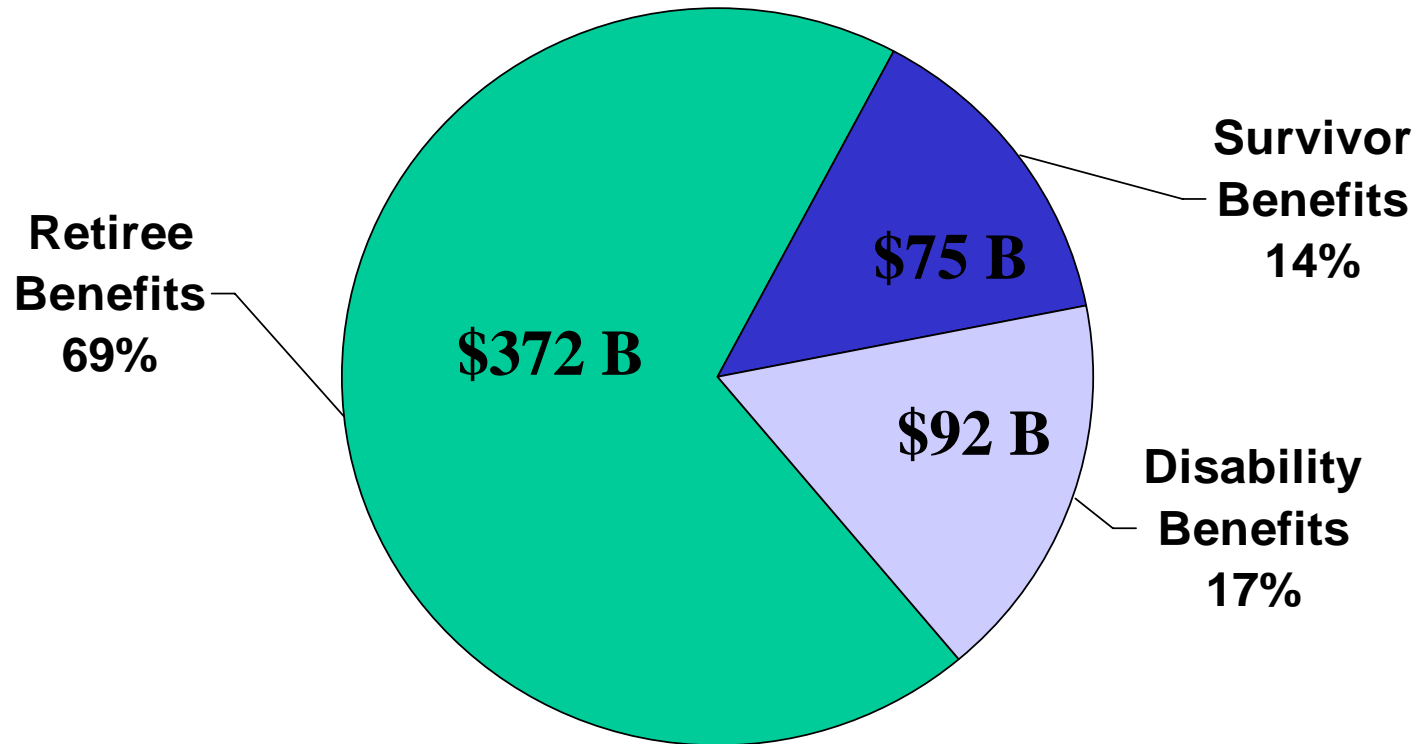
This and following graph show the primary goals of Social Security:

- (1) **Individually equitable** benefits (important to higher wage earners - the more contributed, the more received).
- (2) **Socially adequate** benefits (progressive benefits that are more important to lower wage earners)

Source: Calculations by Ron Gebhardt/bauer



Estimated Social Security Benefits For Calendar Year 2006



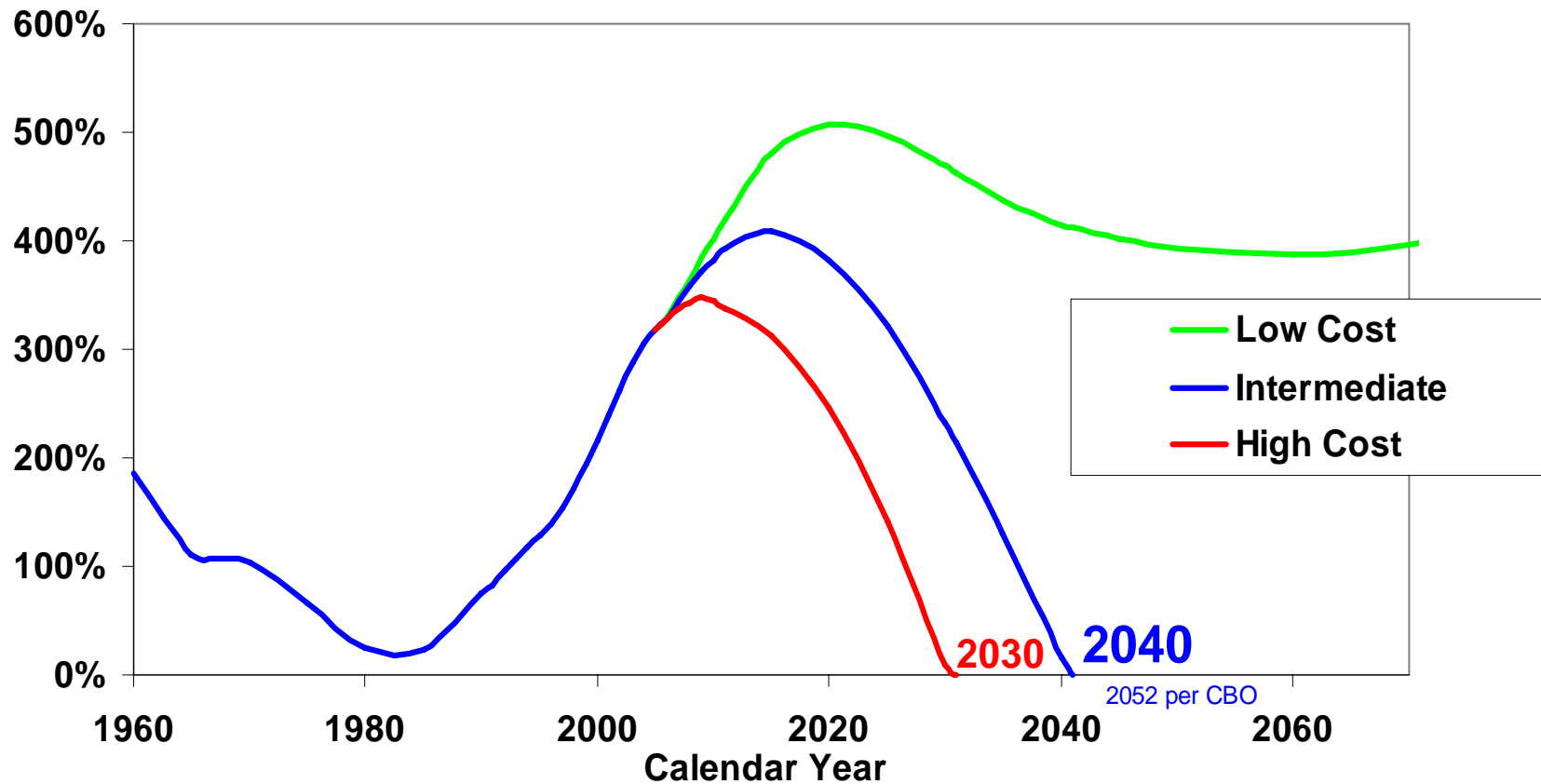
Total Estimated Benefits = \$539 Billion

Source: Social Security Administration: <http://www.ssa.gov/pressoffice/basicfact.htm>



Social Security Trust Fund Ratios

(Beginning of Year Assets as a Percentage of Expenditures)



The Social Security Trust Funds are projected to be exhausted in 2040 using the Intermediate Assumptions. In 2040, tax income can pay 74% of benefits, per Figure II.D2 (70% in 2080). The assumptions are reasonable in the aggregate per GAO/PWC report & individually reasonable per SS Chief Actuary. Social Security solvent but may not meet the Sustainability Test (trust fund ratios stable or increasing around 75th year) on low cost figures. 2006 Trustees Report Table IV.B3. Historical ratios from VI.A4.



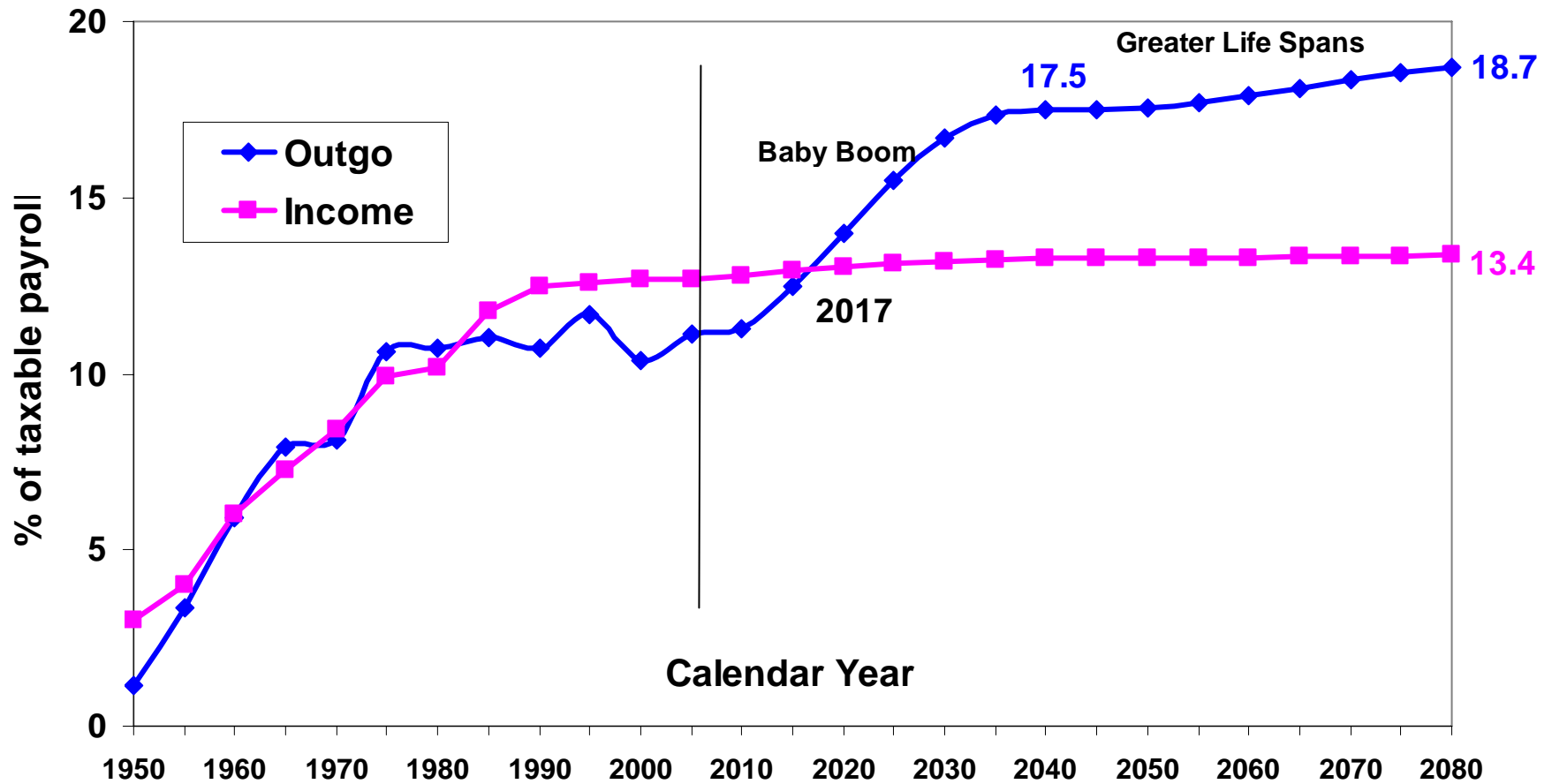
Assumptions

- Demographic
 - Fertility
 - Mortality
 - Immigration
- Economic
 - Interest Rates on Treasury Bonds
 - Productivity
 - Wage Increases
 - Price Inflation
 - Labor Force Participation and Unemployment Rates



Social Security Income & Outgo

Intermediate Assumptions



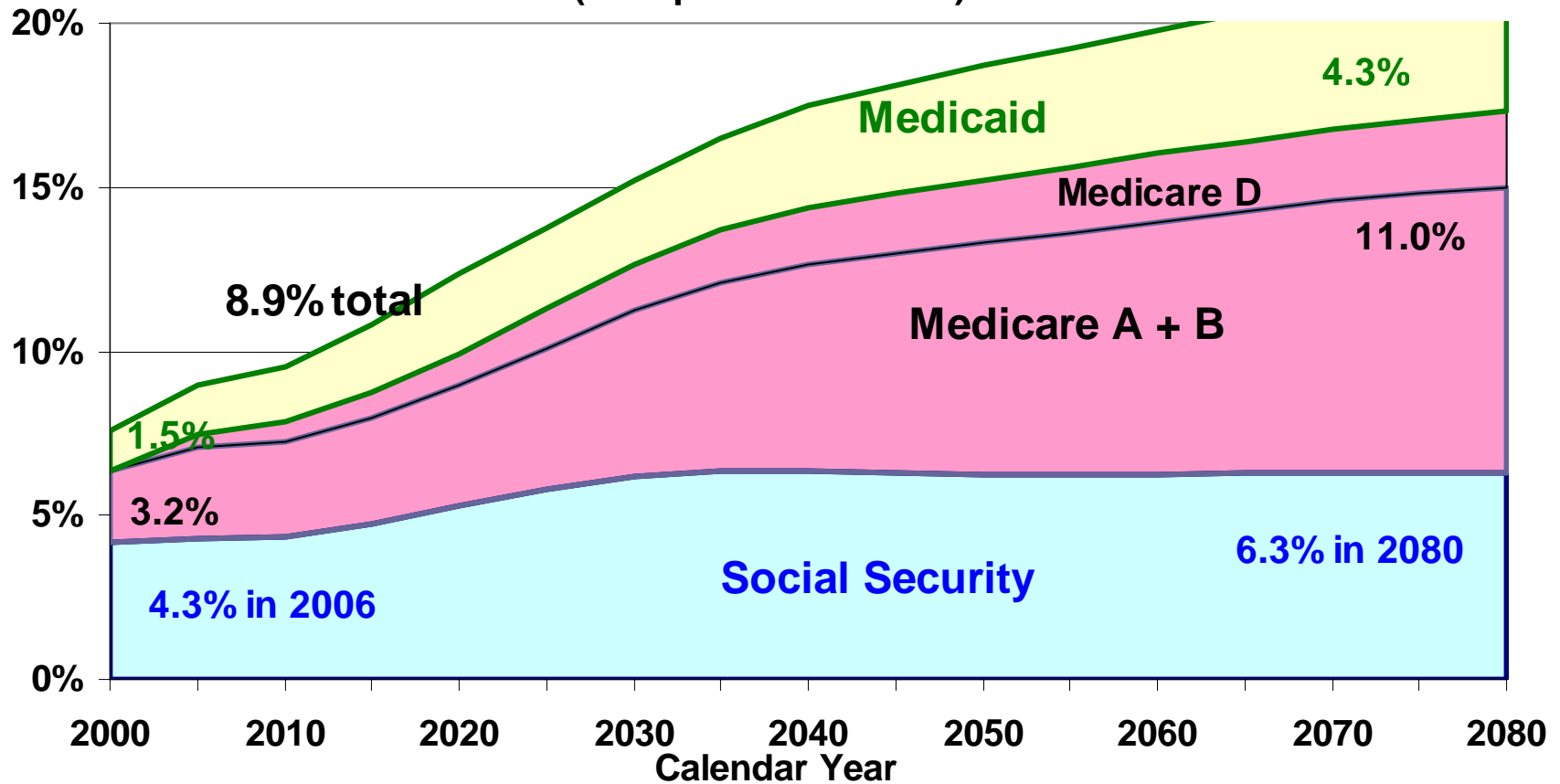
2006 Report Table IV.B1. Using low (high) cost assumptions, the 2080 outgo is 13.5% (27%), & the 2017 date is 2022 (2013); 2020 per CBO. The unfunded obligations over the next 75 years = \$4.6 trillion = -2.02%, -5.17 & 0.35% of taxable payroll for the intermediate, high, & low cost assumptions, per Table IV.B4 (1% per CBO). Table IV.B6&7 show it is \$13.4 trillion or -3.7% of payroll (1.3% of future GDP) over the infinite future (although we could increase SSNRA in the future). Future workers pay for themselves.



Conclusion



Total Costs of Social Security, Medicare, & Medicaid (as a percent of GDP)



Sources: 2006 OASDHI Table VI.F4; SMI (Parts B & D) from Medicare report Tables III.C14 & 20; & Medicaid projected from CBO 12/2005 Long Term Budget Outlook. Today, these programs are half of non-interest government expenses. Total costs more than double to 21.6% by 2080 (Medicare more than triple, surpassing SS by 2028 per Conclusion on p. 27) and eventually exceed 20% of the economy, which would require taxes to increase or government programs shrink.



Reasons to Reform Medicare and Social Security Sooner Rather Than Later

- More options available to policy-makers
- More people included in reform
- Benefit cuts & tax increases for future cohorts can be less
- Reforms can be phased-in
- Plans for the changes can be made in advance
- Faith can be restored in the two programs and government



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