

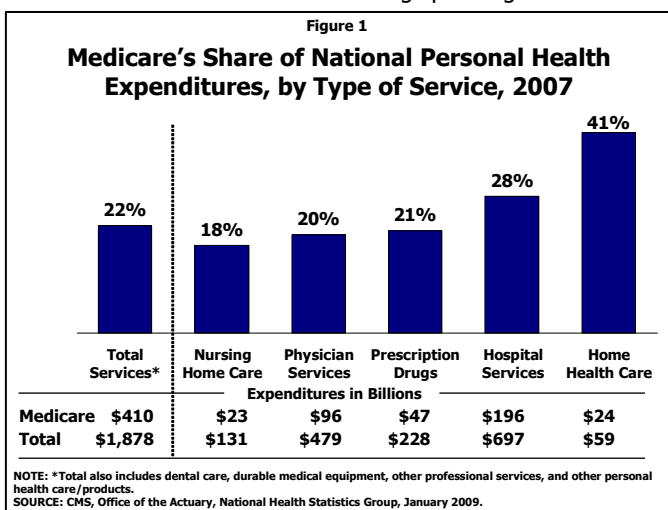
MEDICARE

MEDICARE SPENDING AND FINANCING

MAY 2009

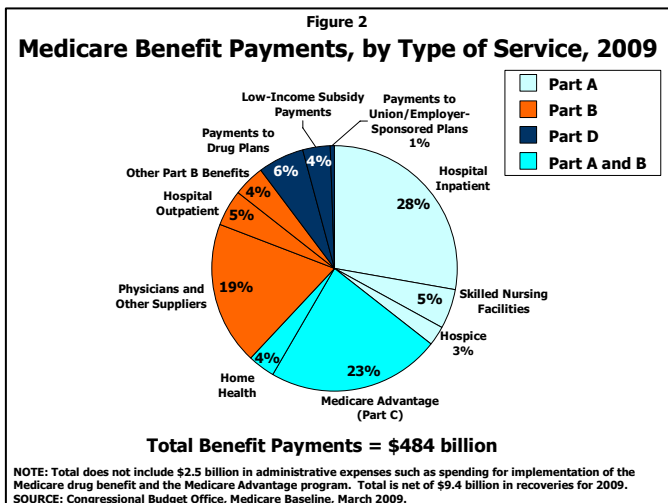
OVERVIEW OF MEDICARE SPENDING

Medicare, the federal health insurance program for 45 million elderly and disabled Americans, helps to pay for hospital and physician visits, prescription drugs, and other acute and post-acute services. Medicare spending represents 13% of the federal budget, and accounts for 22% of total national health spending, varying by type of service: 41% of home health care, 28% of hospital services, 20% of physician services, and 21% of prescription drug spending (Figure 1). Implementation of the Medicare drug benefit in 2006 sharply increased Medicare's share of total national drug spending.



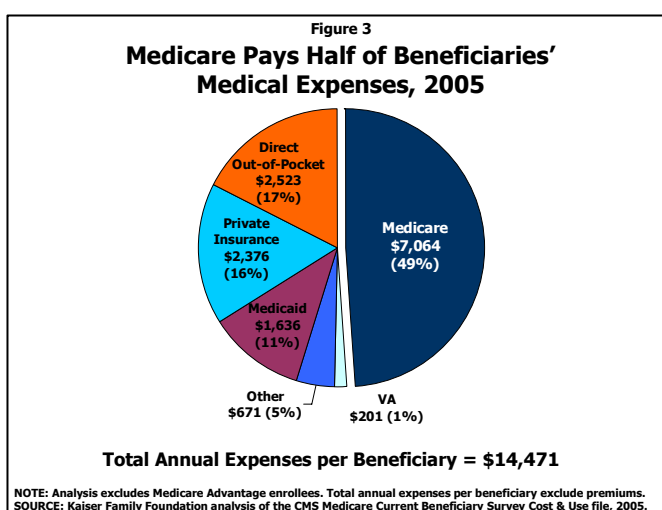
In 2009, benefit payments for the four parts of Medicare are expected to total \$484 billion (Figure 2):

- Part A – Hospital Insurance (HI) = 40% (including home health which is partially funded under Part B)
- Part B – Supplementary Medical Insurance (SMI) = 28%
- Part C – Medicare Advantage (private health plans) = 23%
- Part D – Prescription drug benefit = 11%



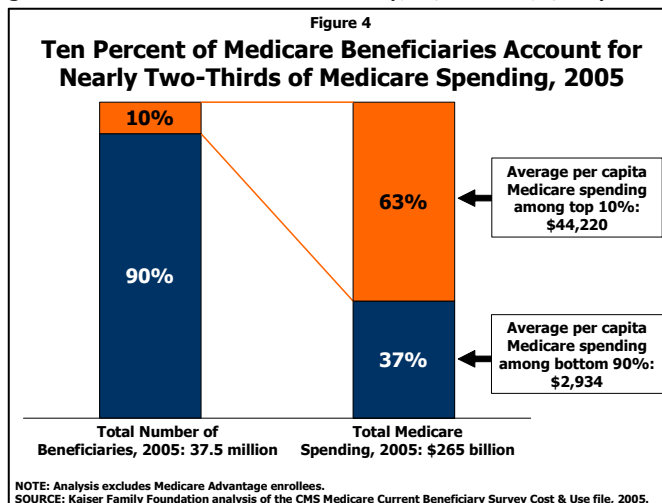
MEDICARE'S SHARE OF TOTAL MEDICAL SPENDING

In 2005, Medicare paid just under half (\$7,064) of the \$14,471 in average total medical expenses per beneficiary in fee-for-service (FFS) Medicare (excluding Medicare Advantage enrollees) (Figure 3). Beneficiaries paid just over \$2,500 (17%) out of pocket, excluding premiums. Beneficiaries' average out-of-pocket spending for medical and long-term care services in 2005 consisted primarily of long-term care (31%), prescription drugs (25%), and provider visits/medical supplies (25%). Median out-of-pocket spending as a share of income increased from 11.9% in 1997 to 16.1% in 2005.



MEDICARE SPENDING PER BENEFICIARY

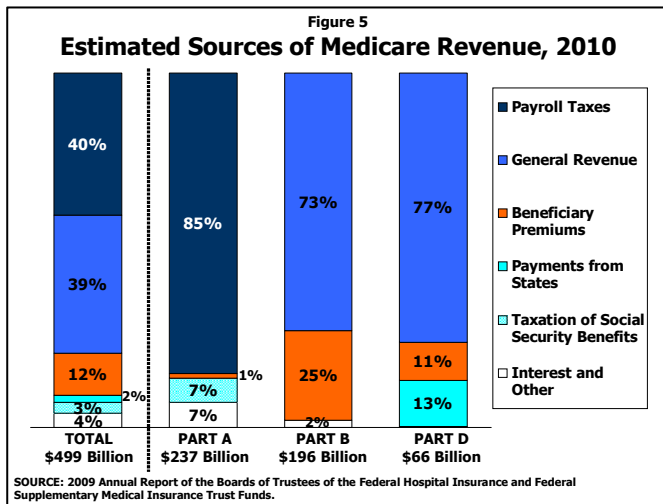
Medicare spending per beneficiary varies, with the top 10% most costly beneficiaries in FFS Medicare accounting for nearly two-thirds (63%) of total Medicare spending in 2005 (Figure 4). Average Medicare spending for the 4% of FFS beneficiaries who died during 2005 was nearly four times greater than for other beneficiaries (\$23,047 vs. \$6,351).



HOW IS MEDICARE FINANCED?

Medicare is funded primarily from three sources: payroll tax contributions (40%), general revenues (39%), and beneficiary premiums (12%) (Figure 5). Medicare Parts A, B, and D are financed separately, as follows:

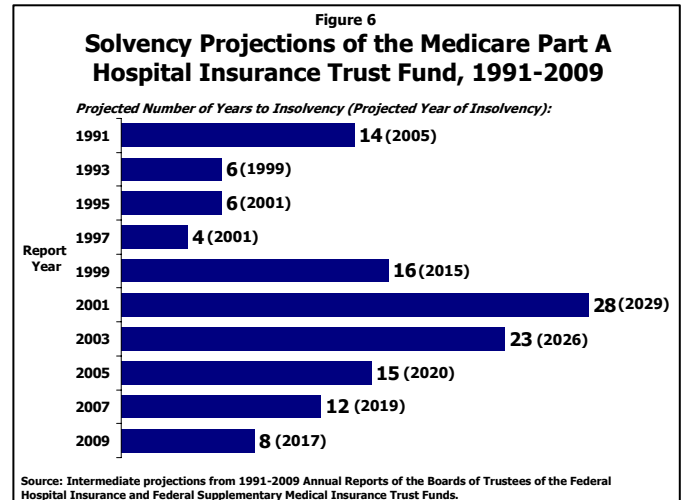
- Part A: financed largely through a 2.9% tax on earnings paid by employers and employees (1.45% each) (85%)
- Part B: financed through general revenues (73%) and beneficiary premiums (25%)
- Part D: financed through general revenues (77%), state payments for dual eligibles (13%), and beneficiary premiums (11%)



MEASURING MEDICARE'S FINANCIAL CONDITION

Medicare's financial condition is measured in a number of ways, including assessing the status of the Part A Trust Fund and comparing total Medicare spending to the gross domestic product, the federal budget, and national health expenditures. Over time, Medicare spending is projected to represent a growing share of the economy, federal spending, and the nation's total health spending.

- The 2009 Medicare Trustees report indicates that Part A spending now exceeds revenues, and that the Part A trust fund will be exhausted in 2017, at which point Medicare will not have sufficient funds to pay full benefits, unless Congress acts to make changes to improve the fiscal outlook of the trust fund, as it has in the past (Figure 6).
- Medicare is projected to grow from 3.6% of GDP in 2009 to 4.2% in 2018 and 6.4% in 2030.
- The Trustees report that general revenues will exceed 45% of total Medicare spending within a seven-year timeframe (by 2014), prompting them to issue a "Medicare funding warning", as required by law.
- SMI trust fund assets are projected to be adequate because beneficiary premiums and general revenue contributions are set to match expected outlays for Part B and Part D each year.



PART B PREMIUMS IN 2010 AND BEYOND

Beneficiary premiums, which cover 25% of Part B spending, typically increase to reflect annual growth in Part B spending, including physician payments. For 2010 and 2011, Part B premiums are expected to be affected by projections of no cost-of-living adjustment (COLA) for Social Security recipients. During these years, a majority (75%) of Medicare beneficiaries will not be required to pay any portion of the monthly Part B premium increase because a statutory "hold-harmless" provision prevents a reduction in Social Security benefit payments that would result from an increase in the Part B premium. Under current projections, premiums paid by, or on behalf of, those not protected by the hold-harmless provision (dual eligibles, higher-income beneficiaries, and new enrollees) would increase from \$96.40 per month in 2009 to \$104.20 in 2010 and \$120.20 in 2011, and then fall back to \$111.50 in 2012, when a Social Security COLA increase is projected to occur and more beneficiaries would face a premium increase.

FUTURE CHALLENGES

Sustained increases in health care costs are placing upward pressure on Medicare spending, as for other payers. Annual growth in Medicare spending is largely influenced by the same factors that affect health spending in general: increasing prices of health care services, increasing volume and utilization of services, and new technologies. Moving forward, system-wide efforts to curtail overall health care costs would help to improve Medicare's financial outlook.

Over the long term, an aging population, a decline in the number of workers per beneficiary, and increasing life expectancy will present fiscal challenges for Medicare. From 2010 to 2030, the number of people on Medicare is projected to rise from 46 million to 79 million, while the ratio of workers per beneficiary is expected to decline from 3.7 to 2.4.

Medicare provides essential coverage for its beneficiaries and enjoys broad public support. How to ensure the program's financial stability over the long term without shifting excessive costs onto beneficiaries, while meeting the health care needs of an aging population, is a pressing challenge for the nation.