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New Research From EBRI:

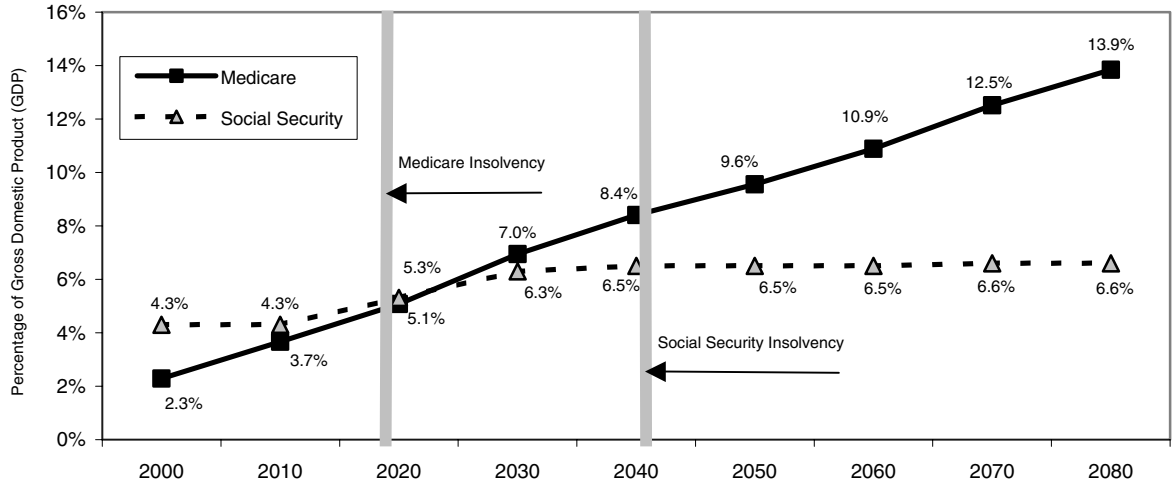
Medicare Will Reach A Cliff Years Before Social Security

WASHINGTON—Medicare faces far larger long-term financial problems than Social Security and will soon account for a greater and rapidly growing share of the nation's gross domestic product, a new report by the Employee Benefit Research Institute shows, and those problems will send Medicare into insolvency 23 years before Social Security.

Given the size of Medicare—the largest single entitlement program in the nation—any changes adopted by Congress that attempt to control the program's costs or affect the program's health care quality will be likely to affect the entire U.S. health care system, the EBRI report also notes.

Over the next 75 years, Medicare's unfunded liability is more than seven times greater than Social Security's—nearly $28 trillion compared $3.7 trillion, according to the report (see Fig. 1).

Figure 1
Medicare and Social Security Spending as a Share of Gross Domestic Product (GDP), 2000–2080



Source: 2004 Medicare Trustees' Report and 2004 Social Security Trustees' Report.

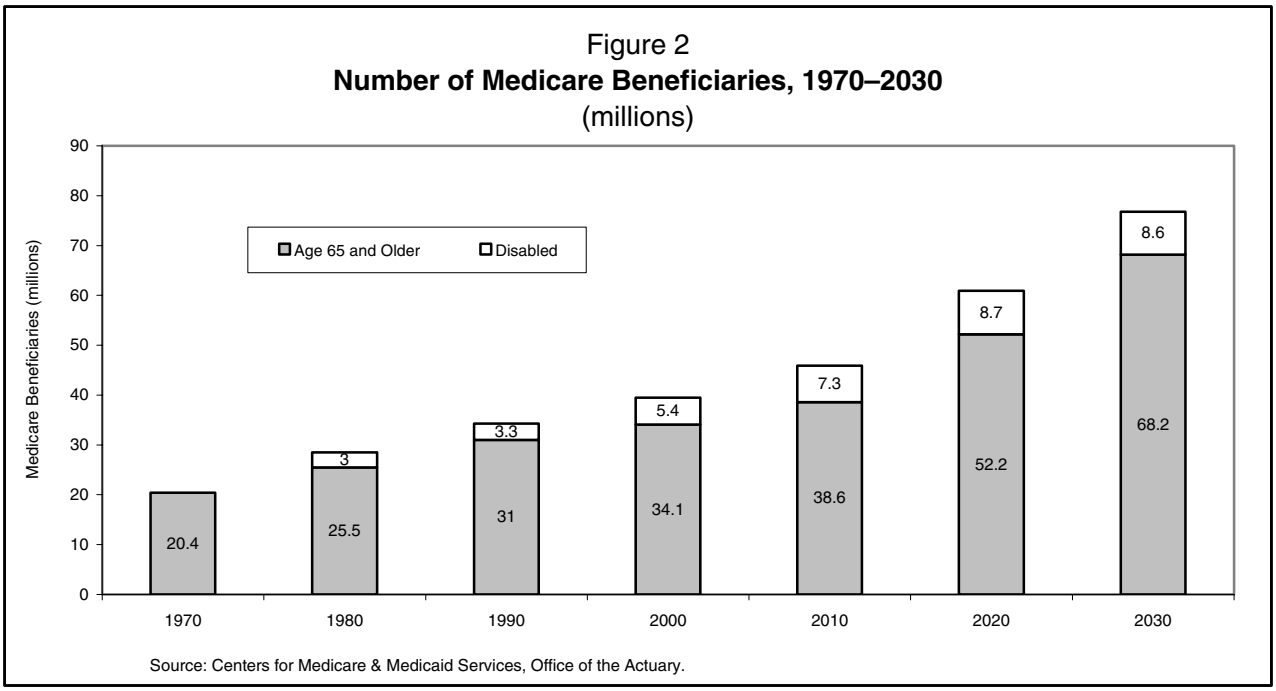
"Medicare's financial problems are much more immediate—and more difficult to solve—than what the Social Security program will face in several decades," said Dallas Salisbury, EBRI president.

The EBRI report, "Controlling Health Costs and Improving Health Care Quality for Retirees," appears in EBRI's February *Issue Brief,* and is available on the Internet at www.ebri.org. The analysis was released as President Bush and Congress are starting to debate proposals to change Social Security in hopes of improving its long-term solvency, and at the same time that Medicare officials are preparing to implement a new Medicare prescription drug benefit that will add at least $720 billion to the program's costs over the next decade.

Rising health care costs—and what to do about them—was the overall theme of the report, which was based on a policy forum sponsored by EBRI's Education and Research Fund. In addition to analyzing the financial condition of the U.S. health system, and of Medicare in particular, the report includes perspectives of several health system experts.

Overall, the report found that the problem of increasingly costly medical bills is a rapidly rising national priority for policymakers and the general public alike. Turning specifically to the federal health program for the nation's elderly and disabled, the report says: "Medicare, which insures nearly all retirees over age 65, casts an enormous shadow over the entire American health care system." The report makes these points, among others:

- Assets in the Medicare trust fund will begin declining in 2010 and will be exhausted within a decade, according to the program's trustees.
- The number of Medicare beneficiaries has doubled, to 40 million, since 1970 and is projected to nearly double again by 2030, to 77 million (see Fig. 2).
- Medicare will claim a growing share of the federal budget in the years ahead, increasing from about 3 percent now to 5 percent in 2020, 7 percent in 2030 and 14 percent in 2080. According to analysts, Medicare spending will surpass Social Security in 2024.



"Basically, Medicare is providing expanded coverage for a growing population even as the cost of care for each individual relentlessly increases—while the program's already inadequate revenue structure is left unchanged," said Paul Fronstin, director of EBRI's health research and education program.

The report notes that without major changes Medicare trustees last year predicted the program will become insolvent in 2019, seven years sooner than projected in 2003. By comparison, Social Security trustees last year projected the federal retirement program will become insolvent in 2042. The funding problem of both programs takes place at time when the ratio of workers to beneficiaries is declining.

But Medicare faces an additional problem. Health costs have been rising significantly faster than overall inflation for several years. While the Center for Studying Health System Change reported the growth rate slowed in 2003, Paul B. Ginsburg, center president, says in the report that he does not anticipate large changes from current trends. During the first half of 2004, the center said, health care costs rose 7.5 percent while the nation's gross domestic product increased 5.9 percent.

In the report, Fronstin predicts that policymakers are likely to take an increasing interest in trimming Medicare reimbursement rates in high-cost localities around the country to conform to the norms in other areas. For example, Medicare spends about $3,500 per beneficiary in Santa Fe, NM, but nearly triple that amount ($9,200) in Miami.

The EBRI report also notes that despite the growth of health care costs, the *percentage* of total spending paid out-of-pocket by individuals has been declining for years, even as the total amount spent on health care is growing (meaning everyone is paying more). In the first half of 2004, health care costs were driven up, by an 8.8 percent in the costs of prescription drugs and an 8.6 percent rise in hospital spending, among other factors, the report says.

Information technology could reduce some cost pressures for both Medicare and private insurance, the report says, but it adds there is no "silver bullet" to controlling health care costs. Jim Bentley, senior vice president for strategic planning at the American Hospital Association, notes that trying to fix separate parts of the U.S. health care system—rather than approaching it as a whole—appears destined to failure.

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