Pension Section News

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2004 Status of the Social Security and Medicare Programs

Editor's Note: The following excerpt is taken from STATUS OF THE SOCIAL SECURITY AND MEDICARE PROGRAMS, A SUMMARY OF THE 2004 ANNUAL REPORTS, A MESSAGE TO THE PUBLIC from the Social Security and Medicare Boards of Trustees. The complete report can be found at http://www.ssa.gov/OACT/TRSUM/trsummary.html

Each year the Trustees of the Social Security and Medicare trust funds report on the current status and projected condition of the funds over the next 75 years. This message summarizes the 2004 Annual Reports.

The fundamentals of the financial status of Social Security and Medicare remain problematic under the intermediate economic and demographic assumptions. Social Security's current annual cash surpluses will soon begin to decline and then turn into rapidly growing cash deficits toward the end of the next decade as the baby-boom generation retires. The financial outlook for the Medicare Hospital Insurance (HI) Trust Fund that pays hospital benefits has deteriorated significantly from last year, with annual cash flow deficits beginning this year and expected to grow rapidly after 2010 as baby boomers begin to retire. The growing annual cash deficits in both programs will lead to exhaustion in trust fund reserves for HI in 2019 and for Social Security in 2042. In addition, the Medicare Supplementary Medical Insurance (SMI) Trust Fund that pays for physician services and the new prescription drug benefit will require substantial increases over time in both general revenue transfers and premium charges. As the reserves in Social Security and HI are drawn down and SMI general revenue financing requirements continue to grow, the pressure on the federal budget will intensify. We do not believe the currently projected long run growth rates of Social Security and Medicare are sustainable under current financing arrangements.

Social Security

The annual cost of Social Security benefits represents 4.3 percent of gross domestic product (GDP) today and is projected to rise to 6.6 percent of GDP in 2078. The projected 75-year actuarial deficit in the combined Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI) Trust Funds is 1.89 percent of taxable payroll, down slightly from 1.92 percent in last year's report. The program continues to fail our long-range test of close actuarial balance by a wide margin. Projected OASDI tax income will begin to fall short of outlays in 2018 and will be sufficient to finance only 73 percent of scheduled annual benefits by 2042, when the combined OASDI trust fund is projected to be exhausted.

Social Security could be brought into actuarial balance over the next 75 years in various ways, including an immediate increase in payroll taxes of 15 percent or an immediate reduction in benefits of 13 percent (or some combination of the two). To the extent that changes are delayed or phased in gradually, greater adjustments in scheduled benefits and revenues would be required. Ensuring the sustainability of the system beyond 2078 would require even larger changes.

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Medicare

As we reported last year, Medicare's financial difficulties come sooner—and are much more severe—than those confronting Social Security. While both programs face essentially the same demographic challenge, health care costs per enrollee are projected to rise faster than the wages per worker on which the payroll tax is paid and on which Social Security benefits are based. As a result, while Medicare's annual costs are currently 2.7 percent of GDP, or about 60 percent of Social Security's, they are now projected to surpass Social Security expenditures in 2024 and reach almost 14 percent of GDP in 2078, more than twice the percent for Social Security in that year.

The projected 75-year actuarial deficit in the Hospital Insurance (HI) Trust Fund is now 3.12 percent of taxable payroll, up significantly from 2.40 percent in last year's report mainly due to higher actual and projected hospital expenditures, as well as lower actual and projected taxable payroll, and new Medicare legislation. The fund now fails our test of short-range financial adequacy, as assets drop below the level of the next year's projected expenditures within 10 years—in 2012. The fund also continues to fail our long-range test of close actuarial balance by a wide margin. The projected date of HI Trust Fund exhaustion has moved forward significantly to 2019, from 2026 in last year's report, and projected HI tax income falls short of outlays beginning this year, as compared to 2013 in last year's report. HI could be brought into actuarial balance over the next 75 years by an immediate 108 percent increase in program income or an immediate 48 percent reduction in program outlays (or some combination of the two). However, as with Social Security, adjustments of far greater magnitude would be necessary to the extent changes are delayed or phased in gradually, and continuation of the program after 2078 would require substantial changes.

Part B of the Supplementary Medical Insurance (SMI) Trust Fund, which pays doctors' bills and other outpatient expenses, and the new Part D, which pays for access to prescription drug coverage, are both projected to remain adequately financed into the indefinite future because current law automatically sets financing each year to meet next year's expected costs. However, this automatic provision will result in a rapidly growing amount of general revenue financing—projected to rise from 0.9 percent of GDP today to 6.2 percent in 2078—as well as substantial increases over time in beneficiary premium charges.

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Conclusion

Though highly challenging, the financial difficulties facing Social Security and Medicare are not insurmountable. But we must take action to address them in a timely manner. The sooner they are addressed the more varied and less disruptive can be their solutions. The problem of finding ways to allow older Americans access to high quality medical care is daunting and likely to demand frequent legislative adjustments in the future, as it has since Medicare was first enacted. With informed public discussion and creative thinking that relates the principles underlying these programs to the economic and demographic realities, as well as to the changing needs and preferences of working and retired households, Social Security and Medicare can continue to play a critical role in the lives of all Americans. ◆