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The President's Medicare Budget: A First Step Toward Entitlement Reform

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The President's Medicare Budget proposal should spark a major debate on entitlement reform. Under the Bush proposal, growth in Medicare spending would be marginally slowed, from an annual projected growth rate of 7.2 percent to 5 percent. The Bush proposal would save $178 billion over five years and $556 billion over ten years. If enacted, its long-term impact would be a $10 trillion reduction in Medicare spending,[1] almost a third of the total unfunded liability of the program. House and Senate leaders have made it clear that they will ignore the President's Medicare proposals,[2] but neither they nor taxpayers can avoid the consequences of failure to address the rising costs of Medicare and other unreformed entitlement programs: massive debt, crushing taxation, and a lower standard of living for tomorrow's working families.

Congress must start to consider long-term reform. The best option is to transform Medicare from the defined benefits program it is today into a defined contribution program for the next generation of seniors. Such a program could incorporate the best features of the Federal Employees Health Benefits Program (FEHBP), thus maximizing patient choice and health plan competition while providing predictable financing for taxpayers.

A Legal Requirement. This year's presidential budget submission acknowledges the need for budgetary action on Medicare that is required by law. Under the Medicare Modernization Act of 2003 (MMA), Congress established a Medicare funding warning. In doing so, Congress also established a procedure for presidential and congressional action, triggered by the findings of the Medicare trustees for two consecutive years that general revenue funding for Medicare exceeds 45 percent within a seven-year period. In 2007, the Medicare Trustees made such a finding.[3] The President, in accordance with the "Medicare funding warning" provisions of the MMA, may submit a more detailed legislative proposal by February 19, 2008.

An Incentive for Broader Reform. The President's budget proposal would put in place an automatic 0.4 percent reduction in Medicare payments to doctors, hospitals, and other Medicare "providers" in any year in which the 45-percent threshold for general revenues is exceeded. An additional 0.4 percent reduction would continue to apply as long as the dedicated revenues for Medicare—the payroll taxes and premiums—cover 55 percent or less of the program's total costs.[4] The Administration has made it clear that the provision is an incentive for Congress to get serious on broader Medicare reform: "The provision is intended to encourage Congress and the Administration to reach agreement on reforms needed to slow the growth in program costs."[5]

Caution on "Provider" Payments. The President also proposes to adjust payment annually for Medi-

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care providers in such a way as to promote "best practices." Medicare payment, in other words, would reflect "value-based purchasing" to ensure efficient and high-quality delivery of care. This approach is doubtless attractive to many in Congress, precisely because the current Medicare payment system, which is a system of administrative pricing, does not account either for value or benefit to the patient in the delivery of care. It is a system of price controls imposed on a nominally "fee for service" system of reimbursement. Of course, the problem of value to the patient, and regard for quality and benefit to the patient, could easily be achieved through the introduction of market-based pricing into Medicare program, a radical departure from current practice. Markets reward the provision of quality and benefit very efficiently.

Without further detail about "best practices," caution is, for now, appropriate. The devil is in the details. Many prominent health policy analysts favor a "pay for performance" system, a recent fashion in health care policy, over the introduction of free-market pricing into the program. But such a system would, in effect, require the government to establish medical practice guidelines for purposes of physician reimbursement. In the enactment of the original Medicare law, Congress specifically drew a bright line, though breached in practice, against federal officials directing or guiding the practice of medicine in the program. Naturally, many members of the medical profession are properly concerned that such an arrangement would increase the already heavy level of bureaucracy that governs Medicare physician payment, as well as encourage gaming in the provision of medical services at the expense of the sickest patients.[6] Budget proposals to secure savings should not become a vehicle for policies that entrench or increase the power of the existing Medicare bureaucracy.

Income-Related Subsidies. Taxpayers subsidize roughly 90 percent of beneficiary costs. In the MMA, Congress provided for differential premium payments for wealthy seniors, requiring them to pay higher premiums for Part B services, while also providing generous subsidies for low-income seniors in the Medicare Part D drug program. In its budget submission, the Bush Administration proposes to increase the financial responsibility of wealthier seniors for the costs of their care. High-income seniors would be expected to pay more than low-income seniors, and the Administration would formalize this distinction in other parts of the program. According to the Administration, "This will be facilitated by a number of steps the Administration has taken already that increase the transparency of health care costs and quality, and support greater health care value for Medicare beneficiaries."[7]

Conclusion. The President's Medicare budget proposals should start a major national debate on Medicare, in particular, and the future of entitlements in general. Given the enormity of the challenge, the President has offered several major proposals that would significantly reduce future Medicare spending and thus the massive unfunded liability of the program. This, in turn, would lighten the burden on current and future taxpayers.

The President has addressed the need to provide for long-term sustainability of Medicare and has also suggested some desirable policy changes that

1. Office of Management and Budget, *Fiscal Year 2009 Budget of the U.S. Government* (Washington D.C.: U.S. Government printing Office, 2008), p. 22.
2. Senator Max Baucus (D–MT), Chairman of the Senate Finance Committee, has declared the President's Medicare reductions "dead on arrival." See Drew Armstrong, *CQ Today*, February 4, 2008.
3. For an excellent description of this process, see Hinda Chaikind and Christopher M. Davis, "Medicare Trigger," Congressional Research Service, *CRS Report for Congress*, February 1, 2008.
4. *Fiscal Year 2009 Budget of the U.S. Government*, p. 22.
5. *Ibid.*
6. For a description of the Medicare "pay for performance" proposal, see Richard Dolinar, M.D., and S. Luke Leininger, "Pay for Performance or Compliance? A Second Opinion on Medicare reimbursement," Heritage Foundation *Backgrounder,* No. 1882, October 5, 2005, at: *www.heritage.org/research/healthcare/bg1882.cfm.*
7. *Fiscal Year 2009 Budget of the U.S. Government*, p. 23.

would improve the functioning of the program. His proposal for linking the Medicare subsidy to beneficiaries' income is a reasonable alternative to current law, as are his proposals to make pricing and quality more transparent. It is not necessary that Members of Congress agree in detail with the President's specific proposals; but if not, it is necessary for them to engage the entitlement issue and develop reasonable alternatives of their own.

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