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Effects of the Patient Protection and Affordable Care Act on the Federal Budget and the Balance in the Hospital Insurance Trust Fund

CBO has been asked for additional information about the projected effects of the Patient Protection and Affordable Care Act (PPACA), incorporating the manager's amendment, on the federal budget and on the balance in the Hospital Insurance (HI) trust fund, from which Medicare Part A benefits are paid. Specifically, CBO has been asked whether the reductions in projected Part A outlays and increases in projected HI revenues under the legislation can provide additional resources to pay future Medicare benefits while simultaneously providing resources to pay for new programs outside of Medicare.

How the HI Trust Fund Works

The HI trust fund, like other federal trust funds, is essentially an accounting mechanism. In a given year, the sum of specified HI receipts and the interest that is credited on the previous trust fund balance, less spending for Medicare Part A benefits, represents the surplus (or deficit, if the latter is greater) in the trust fund for that year. Any cash generated when there is an excess of receipts over spending is not retained by the trust fund; rather, it is turned over to the Treasury, which provides government bonds to the trust fund in exchange and uses the cash to finance the government's ongoing activities. This same description applies to the Social Security trust funds; those funds have run cash surpluses for many years, and those surpluses have reduced the government's need to borrow to fund other federal activities. The HI trust fund is not currently running an annual surplus.

The HI trust fund is part of the federal government, so transactions between the trust fund and the Treasury are intragovernmental and leave no imprint on the unified budget. From a unified budget perspective, any increase in revenues or decrease in outlays in the HI trust fund represents cash that can be used to finance other government activities without requiring new government borrowing from the public. Similarly, any increase in outlays or decrease in revenues in the HI trust fund in some future year represents a draw on the government's cash in that year. Thus, the resources to redeem government bonds in the HI trust fund and thereby pay for Medicare benefits in some future year will have to be generated from taxes, other government income, or government borrowing in that year.

Reports on HI trust fund balances from the Medicare trustees and others show the extent of prefunding of benefits that theoretically is occurring in the trust fund. However, because the government has used the cash from the trust fund surpluses to finance other current activities rather than saving the cash by running unified budget surpluses, the government as a whole has not been truly prefunding Medicare benefits. The nature of trust fund accounting within a unified budget framework implies that trust fund balances convey little information about the extent to which the federal government has prepared for future financial burdens, and therefore that trust funds have important legal meaning but little economic meaning.

The Impact of the PPACA on the HI Trust Fund and on the Budget as a Whole
Several weeks ago CBO analyzed the effect of the PPACA as originally proposed on the HI trust fund (http://www.cbo.gov/ftpdocs/107xx/doc10731/Estimated_Effects_of_PPACA_on_HI_TF.pdf). CBO and the staff of the Joint Committee on Taxation (JCT) estimated that the act would reduce Part A outlays by $246 billion and increase HI revenues by $69 billion during the 2010-2019 period. Those changes would increase the trust fund's balances sufficiently to postpone exhaustion for several years beyond 2017, when the fund's balance would have fallen to zero under the assumptions used for CBO's March 2009 baseline projections.

The improvement in Medicare's finances would not be matched by a corresponding improvement in the federal government's overall finances. CBO and JCT estimated that the PPACA as originally proposed would add more than $300 billion ($246 billion + $69 billion + interest) to the balance of the HI trust fund by 2019, while reducing federal budget deficits by a total of $130 billion by 2019. Thus, the trust fund would be recording additional saving of more than $300 billion during the next 10 years, but the government as a whole would be doing much less additional saving.

CBO has not undertaken a comparable quantitative analysis for the PPACA incorporating the manager's amendment, but the results would be qualitatively similar. The reductions in projected Part A outlays and increases in projected HI revenues would significantly raise balances in the HI trust fund and create the appearance that significant additional resources had been set aside to pay for future Medicare benefits. However, the additional savings by the government as a whole—which represent the true increase in the ability to pay for future Medicare benefits or other programs—would be a good deal smaller.

The key point is that the savings to the HI trust fund under the PPACA would be received by the government only once, so they cannot be set aside to pay for future Medicare spending and, at the same time, pay for current spending on other parts of the legislation or on other programs. Trust fund accounting shows the magnitude of the savings within the trust fund, and those savings indeed improve the solvency of that fund; however, that accounting ignores the burden that would be faced by the rest of the government later in redeeming the bonds held by the trust fund. Unified budget accounting shows that the majority of the HI trust fund savings would be used to pay for other spending under the PPACA and would not enhance the ability of the government to redeem the bonds credited to the trust fund to pay for future Medicare benefits. To describe the full amount of HI trust fund savings as both improving the government's ability to pay future Medicare benefits and financing new spending outside of Medicare would essentially double-count a large share of those savings and thus overstate the improvement in the government's fiscal position.