The Impact of Medicare Premiums on Social Security Beneficiaries

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Summary

Most Social Security beneficiaries pay Medicare premiums. Unless they qualify for low-income assistance, beneficiaries who participate in Medicare Part B (Supplementary Medical Insurance) or Part D (prescription drugs) must pay monthly premiums. Part B participants have premiums automatically deducted from their Social Security benefit checks. Part D participants may choose to have their premiums deducted from their Social Security checks.

Medicare premiums are absorbing a growing share of Social Security benefits. To see the effect of growing premiums, consider a Social Security beneficiary who earned the average wage throughout his or her career (called a medium earner). If this retiree chose to participate in Part B—as the vast majority of Social Security beneficiaries do—the standard Part B premium would have absorbed about 5% of the retiree’s benefits in 2000 and about 8% in 2009. The proportion of benefits needed to pay the Part B premium rose by about two-thirds over the past decade.

The introduction of Medicare Part D adds to the premium expenses of beneficiaries who choose to participate; it also substantially reduces their out-of-pocket prescription drug costs. Part D premiums vary widely among plans; this report focuses on average premiums for standard coverage plans. The Medicare Trustees calculate that combined premiums for both Part B and Part D absorb about 12% of the average initial Social Security benefit check in 2009.

Medicare’s trustees project that premiums for Parts B and D will grow at a faster rate than average Social Security benefits in the future, thus consuming a greater proportion of benefits over time. By 2078, the Medicare trustees project that as a proportion of the average Social Security benefit amount, premiums will more than double. In 2078, a retired worker receiving the average initial Social Security benefit amount is projected to need 22% of benefits to pay the Part B premium and 31% of initial benefits to pay combined Parts B and D premiums.

The deduction of Medicare premiums affects beneficiaries differently, depending on their incomes and Social Security benefit amounts. Medicare premiums absorb a greater fraction of lower earners’ Social Security benefits than of higher earners’ benefits, because although benefit amounts are progressive, low earners tend to have lower dollar amounts of benefits. However, some low-income beneficiaries are eligible for subsidies that cover their Medicare premiums and other out-of-pocket costs. Other beneficiaries with low benefits may be protected by a hold harmless provision that prevents a beneficiary’s Social Security check from declining because of increases in the standard Part B premium.

The Social Security Administration (SSA) has announced that there will be no Social Security cost-of-living adjustment (COLA) in 2010, and both SSA and the Congressional Budget Office predict that there will be no COLA in 2011. Over the same period, total Medicare Part B program costs are expected to increase. In a typical year, the hold harmless provision affects a small fraction of beneficiaries and has a limited impact on program finances. However, in a scenario where Medicare Part B premiums increase but Social Security benefits do not, the effects of the hold harmless provision are larger and more complex. For more information on this issue, please see CRS Report R40561, How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?, by Jim Hahn and Alison Shelton.

Finally, it is important to note that although Social Security beneficiaries are affected by rising health-care costs, the benefits of participating in Medicare are substantially greater than the costs.
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Introduction

Social Security and Medicare are large and important parts of America’s safety net. About 45
million older and disabled individuals—1 in 7 Americans—are beneficiaries of both Social
Security and Medicare.1 Social Security and Medicare account for a large amount of federal
spending. For 2009, spending on the two programs was estimated at about $1.2 trillion, about
33% of the federal budget and about 8% of gross domestic product (GDP), one measure of the
size of the U.S. economy.2

Although Social Security and Medicare both play important roles in the well-being of older and
disabled Americans, the interactions between the two programs are rarely examined. These
interactions will become increasingly important as policymakers look for ways to slow the
growth in spending on Social Security and Medicare. This report focuses on how Medicare
premiums affect Social Security beneficiaries. Medicare premiums are rising faster than Social
Security benefits, consequently consuming an increasing share of benefits over time.

Rising Medicare premiums could have a large effect on Social Security beneficiaries, particularly
on those with low incomes and those who rely on Social Security as their primary source of
income. Some beneficiaries may have more difficulty paying for rising health-care costs than
others. For example, among Americans aged 65 and older, about two-thirds receive more than
half of their income from Social Security, and more than one-third receive more than 90% of their
income from Social Security. Some of these beneficiaries may see a decline in their standard of
living as their Medicare premiums rise.

This report shows how the deduction of Medicare Part B and Part D premiums affects Social
Security beneficiaries.3 It describes how increases in Social Security benefits and Medicare
premiums are calculated under current law and explains the circumstances under which many
Social Security beneficiaries are held harmless for increases in the standard Part B premium, as
well as the premium assistance available to low-income beneficiaries. It shows the growth in
Social Security benefits and Part B premiums in recent years and describes how rising Part B
premiums have affected Social Security beneficiaries, comparing the effects of premium
deductions on people with different levels of earnings. It also provides estimates of Social
Security benefits and Medicare Parts B and D premiums to 2078, using the Social Security and
Medicare trustees’ intermediate projections, and describes how beneficiaries would be affected by
projected Medicare premium increases. Finally, it outlines current legislation that would affect the
relationship between Social Security benefits and Medicare premiums.

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1 Social Security Administration, 2009 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors
(Hereafter cited as 2009 Social Security Trustees Report.) Centers for Medicare and Medicaid Services, 2009 Annual
Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust
as 2009 Medicare Trustees Report.)


3 Medicare Part B, Supplementary Medical Insurance (SMI), covers physician services and other outpatient expenses.
Medicare Part D covers prescription drugs through private plans.
Background

Social Security Benefits

Social Security provides retirement, disability, and survivors benefits to workers and their families. People become insured for benefits by working in Social Security-covered employment (i.e., by paying Social Security payroll taxes). Generally, people who qualify for retirement benefits may receive reduced Social Security benefits as early as age 62 or full benefits at the full retirement age. Those who qualify for disability or certain survivors benefits may receive them at any age. The amount of a worker’s Social Security benefit is calculated by applying a progressive benefit formula to his or her lifetime earnings, adjusted for wage growth. Historically, the average Social Security benefit paid to new beneficiaries has increased at about the same rate as average earnings.

Annual Cost-of-Living Adjustment (COLA)

After a person becomes eligible to receive Social Security benefits, his or her monthly benefit amount is increased annually to maintain purchasing power over time. Near the end of each year, the Social Security Administration (SSA) announces the cost-of-living adjustment (COLA) payable in January of the following year. The amount of the COLA is based on inflation as measured by the Consumer Price Index—Urban Wage Earners and Clerical Workers (CPI-W).

COLA for 2009

In January 2009, Social Security benefits increased by 5.8% for current beneficiaries. This benefit increase was based on the change in the CPI-W between October 2007 and September 2008. SSA estimated that the COLA increased the average retired worker’s monthly benefit by $63.

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4 The amount of time a person must work in Social Security-covered employment to be insured for benefits depends on the type of benefit, among other factors. For more details, see CRS Report 94-27, Social Security: Brief Facts and Statistics, by Gary Sidor.
5 The age at which workers may receive full retirement benefits is rising from 65 (for those born before 1938) to 67 (for those born after 1959).
6 Social Security benefits provided to a worker’s family, such as spouse benefits and survivor benefits, are based on the lifetime earnings of the worker. For more information, see CRS Report 94-27, Social Security: Brief Facts and Statistics, by Gary Sidor.
7 The CPI-W tracks the prices of a fixed market basket of goods and services over time. Social Security’s COLA is calculated as the change in the CPI-W from the third quarter of the prior calendar year to the third quarter of the current calendar year. If the CPI-W increases during this period, Social Security benefits for the next year increase proportionately. If the CPI-W decreases, Social Security benefits stay the same—benefits are not reduced during periods of deflation. See CRS Report 94-803, Social Security: Cost-of-Living Adjustments, by Gary Sidor and CRS Report RL30074, The Consumer Price Index: A Brief Overview, by Brian W. Cashell.
COLAs for 2010 and 2011

SSA has announced that there will be no Social Security COLA in 2010, and both SSA and the Congressional Budget Office predict that there will be no COLA in 2011. For more on this subject and how this could affect Medicare Part B premiums, see CRS Report R40561, How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?, by Jim Hahn and Alison M. Shelton.

Medicare Premiums

Medicare is the federal health insurance program for people aged 65 and older and for certain disabled people. Medicare is composed of four parts:

- Part A: Hospital Insurance (HI);
- Part B: Supplementary Medical Insurance (SMI), which covers physician services and other outpatient expenses;
- Part C: Medicare Advantage (MA), which covers the same services as Parts A and B through private health insurance plans; and
- Part D: covers prescription drugs through private plans.

Participation in Part A is required for Social Security beneficiaries aged 65 and older and for those who have received disability benefits for more than 24 months.9 Part A beneficiaries may choose to participate in Parts B, C, and D.10

Medicare is funded through a combination of payroll taxes, general revenues, and beneficiary premiums. Medicare Part A is funded primarily through the payroll taxes of current workers and their employers, which are credited to the HI trust fund.11 Parts B and D are financed through a combination of beneficiary premiums and federal general revenues, which are credited to the SMI trust fund. Part C is financed through the HI and SMI trust funds; Part C participants must pay the Part B premium.12 Because this report focuses on the payment of Medicare premiums, the analysis herein primarily relates to Parts B and D.

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9 People who receive Social Security benefits that confer eligibility for Part A (i.e., retirement benefits for those aged 65 and older and disability benefits after 24 months) may not waive Part A entitlement. (Social Security Administration, Program Operations Manual System, HI 00801.002, at https://s044a90.ssa.gov/apps10/poms.nsf/lnx/0600801002/opendocument.)

10 Of Part A beneficiaries, roughly 94% are enrolled in Part B, and about 22% are enrolled in Part C. In 2008, about 90% of Medicare beneficiaries had prescription drug coverage of some kind. About 25 million were enrolled in stand-alone Part D plans or had prescription drug coverage through their Part C plans, and an additional 14 million were enrolled in other health insurance plans that were subsidized by Part D. (CRS Report RL34280, Medicare Part D Prescription Drug Benefit: A Primer, by Jennifer O'Sullivan.)

11 About 99% of Medicare beneficiaries qualify for premium-free Part A coverage, which they earn if they (or their spouses) have worked at least 10 years in Medicare-covered employment. Individuals without sufficient work history who are otherwise eligible for Medicare may participate in the program if they pay monthly Part A premiums.

12 The law requires that Part C participants pay the Part B premium. Some Part C plans subsidize the premium for their enrollees; others require that enrollees pay the full Part B premium plus an additional premium directly to the plan sponsor.
Part B Premiums

At the end of each year, the Centers for Medicare and Medicaid Services (CMS) announce Part B premiums for the next year. The Balanced Budget Act of 1997 permanently set the standard Part B premium to cover 25% of projected per capita Part B program costs for beneficiaries aged 65 and older. If projected Part B costs increase or decrease, the premium rises or falls proportionately. Unless they qualify for low-income assistance, Part B participants must pay monthly premiums; they must also pay other out-of-pocket costs when they use Part B services.

Starting in 2007, higher-income beneficiaries pay higher Part B premiums. An estimated 5% of Part B beneficiaries must pay income-related premiums in 2009.

Part B Premiums for 2009

In 2009, the standard Part B premium is $96.40 per month, the same as in 2008. In 2009, individuals whose modified adjusted gross income (AGI) exceeds $85,000, and couples whose modified AGI exceeds $170,000, are subject to higher premium amounts, as shown in Table 1 below. The analysis in this report focuses on the standard Part B premium, which is paid by most beneficiaries. In addition to premiums, Part B beneficiaries must also pay other out-of-pocket costs when they use services. The annual deductible for Part B services is $135 in 2009. After the annual deductible is met, beneficiaries are responsible for coinsurance costs, which are generally 20% of Medicare-approved Part B expenses.

<table>
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<th>Modified Adjusted Gross Income (AGI)</th>
<th>Single</th>
<th>Couple</th>
<th>Premium</th>
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<td>$170,000 or less</td>
<td>$96.40</td>
<td></td>
</tr>
<tr>
<td>$85,001-$107,000</td>
<td>$170,001-$214,000</td>
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<td>More than $426,000</td>
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</tr>
</tbody>
</table>


Note: For more, see CRS Report R40082, Medicare: Part B Premiums, by Jim Hahn.

13 Disabled Medicare beneficiaries under age 65 pay the same premium amount as those aged 65 or older, though their per capita Part B costs are higher.


16 For more information, see CRS Report R40082, Medicare: Part B Premiums, by Jim Hahn.
Part D Premiums

Medicare Part D was established in the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA, P.L. 108-173) and began covering beneficiaries’ prescription drugs through private plans in January 2006.\(^{17}\) To participate in Part D, qualified individuals must enroll in a participating prescription drug plan. Unless they qualify for low-income assistance, Part D participants must pay monthly premiums; they must also pay other out-of-pocket costs when they use Part D services.

MMA established guidelines for *standard* Part D coverage, including specific deductible and coinsurance amounts and a formula for calculating average premiums. Individual prescription drug plans are also allowed to offer *alternative* coverage that has at least actuarially equivalent benefits. In other words, alternative coverage plans must pay, on average, equal or greater benefits per person than standard coverage plans. Alternative coverage plans may charge higher or lower premiums, deductibles, and coinsurance than standard coverage plans.\(^{18}\) This report focuses on beneficiaries’ premiums for *standard* Part D coverage, which vary by plan. On average, a beneficiary’s premium covers 25.5% of the value of a standard coverage plan and the federal government pays for the remaining 74.5%.

**Part D Premiums for 2009**

The average premium for standard Part D coverage is $28 in 2009. The annual deductible for standard coverage is $295 in 2009. After meeting the deductible, beneficiaries pay 25% coinsurance costs for drug costs up to $2,700, all of their drug costs between $2,700 and $6,145, and about 5% of drug costs above $6,154.\(^{19}\)

**Medicare Advantage (Part C)**

Beneficiaries who are entitled to Medicare Part A and enrolled in Part B may choose to enroll in a private health insurance plan through Part C, also known as Medicare Advantage (MA), which provides health-care coverage in lieu of traditional Medicare. In 2009, about 22% of Medicare beneficiaries are enrolled in Part C, mostly in managed care plans.\(^{20}\) Medicare Advantage plans are generally required to offer the same services as Medicare Parts A and B. MA managed care organizations must also offer at least one Medicare Advantage-prescription drug plan (MA-PD) that includes drug coverage at least equivalent to standard coverage in Part D plans. (Beneficiaries enrolled in MA managed care plans may not enroll in a stand-alone Part D plan.\(^{21}\))


\[^{19}\] The majority of plans offered to beneficiaries in 2009 were alternative coverage plans. Many of these plans include tiered cost-sharing, under which costs are lower for generic drugs and higher for brand-name drugs (Kaiser, *Part D Fact Sheet*).


\[^{21}\] MA providers of nonmanaged care plans (i.e., private fee-for-service [PFFS] plans and medical savings accounts [MSAs]) are *not* required to offer prescription drug coverage. Drug coverage is optional for PFFS providers; PFFS plan (continued...
The Impact of Medicare Premiums on Social Security Beneficiaries

Part C Premiums

Medicare Advantage participants’ total premium amounts may be higher or lower than the Part B premium. Although the law requires that MA participants pay the Part B premium, some plans subsidize the premium for their enrollees. Other plans require that enrollees pay the full Part B premium plus an additional premium directly to the plan sponsor.22

Premium Subsidies for Low-Income Beneficiaries

The analysis in this report focuses on Social Security beneficiaries who pay Medicare premiums. However, low-income individuals (including MA participants) may qualify for low-income subsidies, which cover all or part of their Part B and Part D premiums.23 As of 2009, about 8.8 million low-income Medicare beneficiaries receive full Part B subsidies, and 9.6 million receive Part D subsidies.24 Some beneficiaries who qualify for premium subsidies do not apply for them.

To qualify for subsidies, beneficiaries must have limited income and assets. Beneficiaries may qualify for full Part B premium subsidies if they have incomes of less than 135% of poverty and assets of less than $4,000 for an individual or $6,000 for a couple. Beneficiaries may qualify for full or partial Part D premium subsidies if they have incomes of less than 150% of poverty and assets of less than $12,510 for an individual and $25,010 for a couple in 2009.

Relationship Between Social Security Benefits and Medicare Premiums

Ultimately, everyone who is eligible for Social Security retirement or disability benefits qualifies for Medicare.25 Most people who elect to participate in the Part B or Part D programs pay premiums.26 By law, the Medicare Part B premium is automatically deducted from the Social Security benefits of those enrolled in Part B (including MA and MA-PD participants).27 Medicare enrollees without drug coverage are permitted to enroll in a stand-alone Part D plan. MSAs may not offer drug coverage.

22 As of 2009, about half (49%) of MA participants’ total premiums were equal to the Part B premium amount, and about half (49%) paid higher premiums. About 2% paid lower premiums. (AARP Public Policy Institute, A First Look at How Medicare Advantage Benefits and Premiums in Individual Enrollment Plans Are Changing from 2008 to 2009, by Marsha Gold and Maria Cupples Hudson, March 2009, at http://assets.aarp.org/rgcenter/health/25_medicare.pdf.)
25 Generally, people aged 65 and older who qualify for Social Security benefits and people of any age who receive disability benefits (after a two-year waiting period) are entitled to Part A, with some exceptions. Part A beneficiaries are also eligible to enroll in Part B, in a private health insurance plan through Part C, and/or in a private prescription drug plan through Part D.
26 Some beneficiaries do not pay Medicare premiums, either because they receive low-income assistance or because they choose not to enroll in Medicare Part B or Part D.
27 42 U.S.C. § 1840(a)(1). Part B premiums are also deducted from Railroad Retirement benefits (42 U.S.C. § (continued...)

Part D participants may choose to have their Part D premiums deducted from their benefits or to pay them directly to their prescription drug plan sponsors.

**Growth in Social Security Benefits and Part B Premiums**

Historically, the growth in Medicare Part B premiums has greatly exceeded the growth in Social Security benefits. Over the past decade, Social Security’s annual COLA resulted in a cumulative benefit increase of about 27%; average worker benefits have increased by about 36%. At the same time, standard Part B premiums have more than doubled, from $45.50 in 2000 to $96.40 in 2009. By law, all Part B premiums are set as a proportion of projected Part B program costs. Part B costs—like all health-care costs—have been rising dramatically. This cost growth is driven by many factors, including increasing life expectancy, new medical technology, program expansion, increases in the earnings of health professionals, and other medical price growth (which has been higher than overall inflation).

The cumulative growth in standard Part B premiums has been dramatic, but annual changes have been somewhat erratic. During the past 10 years, annual Part B premium increases have ranged from 0% to more than 17%. Social Security COLAs, meanwhile, have ranged from 1.4% to 5.8%. **Figure 1** shows the annual rates of increase in Medicare premiums and Social Security benefits from 2000 to 2009.

![Figure 1. Annual Increase in Social Security Benefits and Standard Medicare Part B Premiums, 2000-2009](image)

**Source:** 2009 Medicare Trustees Report and the 2009 Social Security Trustees Report.

**Note:** There were no increases in the Part B premium in 2000 and 2009.

(...continued)

1840(b)(1)).

28 The COLA increases the benefits paid to current beneficiaries. In contrast, average Social Security benefits (those paid to new and current beneficiaries) have risen at a faster rate than the annual COLA, because the formula for calculating initial Social Security benefits is linked to wage growth, whereas the COLA is based on price growth. Generally, wages rise faster than prices.
Hold Harmless Provision

A *hold harmless* provision reduces the Part B premium for most beneficiaries whose Social Security COLAs are not sufficient to cover the standard Part B premium increase.\(^29\) If, in a given year, the increase in the standard Part B premium would cause a beneficiary’s Social Security check to be less, in dollar terms, than it was the year before, then the premium is reduced to ensure that the nominal amount of the individual’s Social Security check stays the same.\(^30\) However, high-income individuals who must pay income-related Part B premiums are *not* covered by the hold harmless provision. This means that for these high-income beneficiaries, Social Security checks can be reduced from one year to the next as a result of an increase in the Part B premium. New enrollees, as well as low-income beneficiaries who are not required to pay Part B premiums, are also not affected by the hold harmless provision.\(^31\)

SSA determines which beneficiaries will be held harmless. Whether a beneficiary is held harmless depends on the amount of the standard Part B premium increase relative to the amount of his or her Social Security COLA in a given year. An individual’s Social Security COLA is determined by multiplying his or her benefit amount by the inflation rate (i.e., the CPI-W). Part B premiums are determined by projected Part B program costs. Thus, the number of people held harmless can vary widely from year to year, depending on annual inflation rates and projected Part B costs.\(^32\)

In some cases, a beneficiary may be held harmless one year but not the next. In other cases, a beneficiary will be held harmless in a current year because his or her Part B premium was reduced in an earlier year. The cumulative effect of the hold harmless provision can produce substantial savings for individuals with low benefits.

A beneficiary is *not* held harmless if the increase in his or her Part D premium (or the combined increase in Part B and Part D premiums) causes his or her Social Security check to decline. In other words, a person’s Social Security check may decrease from one year to the next as a result of Part D premium increases.

\(^{29}\) 42 U.S.C. § 1839(f). The hold harmless provision was first implemented in January 1987.

\(^{30}\) To be held harmless in a given year, a beneficiary must have had Part B premiums deducted from both the December check of the prior year and the January check of the current year. Changes in a beneficiary’s benefit amount (other than the COLA) do not affect whether the beneficiary is held harmless. If a beneficiary’s benefit amount changes during a year in which he or she is held harmless (e.g., a beneficiary starts to receive a government pension offset), the Part B premium amount does *not* change. For more information on the hold harmless provision, see CRS Report R40561, *How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?*, by Jim Hahn and Alison Shelton.

\(^{31}\) For more information on the hold harmless provision and the impact on Part B premiums if there is no Social Security COLA during 2010 and 2011, see CRS Report R40561, *How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?*, by Jim Hahn and Alison Shelton.

\(^{32}\) For example, about 1.8 million Part B participants (6% of those paying premiums) were held harmless in 2005, and roughly 1 million participants (3% of those paying premiums) in 2006 (SSA Actuarial Note No. 147).
Figure 2. Approximate Thresholds for Hold Harmless Provision, 2000-2009

**Source:** Congressional Research Service calculations, based on figures from the 2009 Medicare Trustees Report and the 2009 Social Security Trustees Report.

**Note:** There were no increases in the Medicare Part B premium in 2000 or 2009.

Figure 2 shows the approximate Social Security monthly benefit amounts beneath which Social Security beneficiaries who paid Part B premiums were held harmless from 2000 to 2009. The Part B premium increase is reduced for most beneficiaries with monthly Social Security benefits below the threshold in a given year.33 If a beneficiary had benefits above the threshold in a given year, he or she would pay the full Part B premium increase in that year. In 2009, Medicare Part B premiums did not increase, so the hold harmless provision did not apply.

No Social Security COLA Scenario

SSA announced on October 15, 2009, that there will be no Social Security COLA in 2010. Furthermore, both SSA and the Congressional Budget Office predict that there will be no COLA in 2011. Over the same period, total Medicare Part B program costs and premiums are expected to increase.34 In a typical year, the hold harmless provision affects a small fraction of beneficiaries and has a limited impact on program finances. However, in a scenario where Medicare Part B premiums increase but Social Security benefits do not, the effects of the hold harmless provision are larger and more complex. For more information on this issue, please see CRS Report R40561, *How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?*, by Jim Hahn and Alison M. Shelton.

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33 Some beneficiaries with benefits below these thresholds would not have had their Part B premiums reduced because their benefit checks would not have declined as a result of the Part B premium increase, due to the fact the Social Security benefits are rounded down to the nearest dollar. These thresholds apply only to beneficiaries who were not held harmless in the previous year. For more information, see SSA Actuarial Note No. 147.

34 By law, Medicare Part B premiums cover 25% of annual program costs.
Impact of Medicare Premiums on Social Security Beneficiaries

Actual Impact, 2000-2009

During the past decade, Medicare Part B premiums have absorbed a growing fraction of beneficiaries’ Social Security benefits. The deduction of Part B premiums does not affect all beneficiaries equally. Paying the standard Part B premium, as most beneficiaries do, requires a relatively larger deduction from small Social Security benefits than from large benefits. Although Social Security benefits are progressive, they are also based on a workers’ lifetime earnings; consequently, low earners are disproportionately affected by the deduction of Medicare premiums.

Effect of Part B Premiums on Social Security Benefits

The following section illustrates how the deduction of Medicare Part B premiums would have affected the Social Security benefits of three hypothetical workers who retired in 2000: a low earner, a medium earner, and a high earner. The low earner is assumed to have earned 45% of the average wage during each year of his or her career (about $19,000 in 2009) and to receive a monthly Social Security benefit of about $800 in 2009. The medium earner is assumed to have earned the average wage during each year of his or her career (about $42,000 in 2009) and to receive a monthly Social Security benefit of about $1,400 in 2009. The high earner is assumed to have earned 160% of the average wage during each year of his or her career (about $67,000 in 2008) and to receive a monthly Social Security benefit of $1,800 in 2009. All of the hypothetical workers are assumed to have been born in 1935, to have worked full-time each year from age 22 to 65 with no interruptions, to have retired in 2000 at age 65, and to pay the standard Part B premium without low-income assistance or protection under the hold harmless provision. Figure 3 shows the percentage of each hypothetical worker’s Social Security benefits deducted to pay the standard Part B premium from 2000 to 2009.

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35 The hypothetical workers were developed by SSA’s actuaries. See Social Security Administration, Office of the Chief Actuary, Actuarial Note Number 144, Internal Rates of Return Under the OASDI Program for Hypothetical Workers, by Orlo R. Nichols, et al., June 2001, at http://www.ssa.gov/OACT/NOTES/note2000s/note144.html.


37 The low earner could potentially qualify for assistance in paying Part B premiums if he or she had little or no income besides Social Security benefits, had assets below the statutory limit ($4,000 for an individual and $6,000 for a couple), and applied for assistance.
As shown in Figure 3, a growing proportion of Social Security benefits have been deducted to pay Part B premiums over the 10-year period. In 2000, the medium earner needed approximately 5% of his or her Social Security benefits to pay the Part B premium each year. As the Part B premium increased, particularly during the mid-2000s, the proportion of Social Security benefits needed to pay the Part B premium rose substantially. By 2009, the Part B premium absorbed about 8% of the medium earner’s benefits. The proportion of benefits needed to pay the standard Part B premium rose by about two-thirds over the past decade.

Lower earners need a greater fraction of their Social Security benefits to pay the Part B premium than do higher earners. For example, in 2009 the low earner in this illustration needs about 13% of his or her Social Security benefits to pay the Part B premium. In contrast, the high earner needs about 6% of his or her benefits to pay the Part B premium.

Effect of Part B Premium Increases on Social Security COLAs

The Social Security COLA is designed to ensure that Social Security benefits keep up with overall inflation. However, a larger share of the COLA is absorbed by the increase in the Part B premium in some years than in others. In years when the Part B premium increase absorbs a larger share of the COLA, beneficiaries’ ability to pay for all other goods and services decreases.

Using the same three hypothetical workers as examples, Figure 4 shows the percentage of the Social Security COLA absorbed by the annual increase in Medicare premiums in each year from 2000 to 2009. The proportion of the COLA needed to pay the increase in the Part B premium has varied substantially over time. In some years, a large proportion of beneficiaries’ COLAs have been absorbed by the Part B premium increase. For example, in 2004 and 2005, the Part B premium increase absorbed more than half of the medium earner’s COLA. In 2009, there was no Part B premium increase, so beneficiaries kept their entire Social Security COLAs. In years with...
premium increases, those with lower benefits need a greater fraction of their Social Security COLAs to cover the Part B premium increase than those with higher benefits.

**Figure 4. Percentage of Social Security COLAs Absorbed by Standard Part B Increase, 2000-2009**

![Graph showing percentage of Social Security COLAs absorbed by Part B increase from 2000 to 2009 for low, medium, and high earners.]

**Source:** Congressional Research Service calculations, based on figures from the 2009 Medicare Trustees Report and the 2009 Social Security Trustees Report.

**Notes:** The calculations in this figure are based on individuals who retired in 2000. Estimates for other cohorts would vary. There were no increases in the Medicare Part B premium in 2000 or 2009.

**Future Impact, 2010-2078**

Most experts agree that Medicare cost growth will continue to outstrip growth in prices (and thus Social Security COLAs) and wages (and thus initial Social Security benefits). The trustees of Social Security and Medicare project that over the long term, annual inflation will average 2.8%, annual wage growth will average 3.9%, and annual increases in Parts B and D costs per beneficiary will average 5% or more. Long-range projections are inherently imprecise; the further into the future one looks, the wider the range of possible outcomes. Projections of Medicare cost growth are particularly uncertain. Sources of uncertainty range from the difficulty of predicting medical breakthroughs to the ongoing implementation of Part D.

**Projected Effect of Part B and Part D Premiums on Social Security Benefits**

If Part B costs rise at the rate the trustees have projected, premiums will absorb an increasing share of beneficiaries’ Social Security benefits. In fact, many experts believe that Part B costs will grow faster than the trustees have projected.
Why the Trustees’ Projections of Medicare Part B Premiums May Be Too Low

Trustees Assume Cuts to Physician Payments. The Medicare trustees make their projections of future program costs and premiums based on the provisions of the law that authorizes Medicare. The law requires a sustainable growth rate (SGR) formula to be used to calculate Medicare physician payments, which account for about 50% of Part B costs. Application of this formula would result in cuts to physician fees of about 21% in 2010 and 5% in each of the following years. The Medicare trustees assume that these cuts will be made.

However, congressional action has prevented cuts to physician fees for 2003 to 2009. Many Members of Congress were concerned about the impact of potential payment reductions on beneficiaries’ access to services. The trustees acknowledge that “multiple years of significant reductions in physician payments per service are very unlikely to occur before legislative changes intervene.” If the trustees had not assumed that physician payments would be cut, projected Part B costs would be significantly higher. Consequently, projected Part B premiums would be higher, because they are proportionate to projected program costs.

Trustees Assume Medicare Cost Growth Will Slow. The Medicare trustees assume that the growth in Medicare costs (and thus premiums) will slow in the future. The Congressional Budget Office (CBO) explains that “in their long range forecasts, the Medicare trustees assume that the development and increasing use of new medical technologies will cause spending per enrollee to continue to grow faster than [inflation and wages] but that significant pressures will be brought to bear on the entire health-care system to reduce [costs].” Consequently, the trustees project that the growth in Medicare premiums will also slow. The trustees’ intermediate projection is that Part B premiums will increase by an average annual rate of at least 5% over the long term.

Many experts believe this projected growth rate is too low. One reason is that the trustees’ projections are significantly lower than past growth rates for Part B premiums. If Part B premiums continue to rise at the same rate as they have in the past, they will increase much more rapidly than the Medicare trustees project.


It is also difficult to project how Medicare Part D premiums, implemented in 2006, might change over time. (See the text box.) Early estimates of Part D costs varied widely. The nature of Part D makes it difficult to project premiums, because individual plans set premiums for their beneficiaries. In general, prescription drug spending has been rising at least as much as overall health spending; this trend is expected to continue.38

Uncertainties in Projecting Part D Premiums

How will drug prices and utilization change? Changes in drug prices and utilization could have a significant impact on Part D premiums. If generic drugs become increasingly available or more widely used, premiums could be lower than expected. Alternatively, pharmaceutical breakthroughs or increased use of expensive prescriptions could lead to higher premiums.

How many prescription drug plans will compete for beneficiaries? In the first several years of implementation, a greater-than-expected number of plans offered Part D benefits. If a large number of plans continue to offer Part D benefits, competition to attract beneficiaries could drive down premiums. Alternatively, some analysts believe that the fierce competition for beneficiaries will force some plans out of Part D in future years, reducing competition and leading to higher premiums.

Figure 5 shows the proportion of the average Social Security benefit that would be needed to pay standard Part B premiums from 2010 to 2078. It also shows the proportion of the average Social Security benefit that would be needed to pay the standard Part B and the average premium for standard Part D coverage, combined. The graph is based on the trustees’ intermediate projections. Each year in the graph shows the projected percentage of average Social Security benefits that would be needed to pay Medicare premiums for a person who turned 65 and retired in January of that year. In interpreting Figure 5, it is important to note that Part D premiums vary widely by

plan, and that Part D premiums may be deducted from beneficiaries’ Social Security checks or be paid directly to the plan.

The estimates in Figure 5 show the proportion of initial Social Security benefits needed to pay Medicare premiums for a series of different cohorts retiring in each year from 2010 to 2078. Initial Social Security benefits are indexed to wages. In contrast, the estimates in Figure 3 show the proportion of Social Security benefits needed to pay Medicare premiums for a single cohort over time. After the initial year, benefits are indexed to inflation using the COLA. This difference is important because Figure 3 compares Medicare premium growth to price growth (i.e., inflation) for average (“medium”) earners, whereas Figure 5 compares Medicare premium growth to wage growth in the average Social Security benefit. On average, Medicare premiums have grown faster than both wages and prices and are projected to do so in the future.

**Figure 5. Percentage of Initial Social Security Benefits Deducted for Standard Medicare Part B and Part D Premiums, 2010-2078**

<table>
<thead>
<tr>
<th>Year</th>
<th>Part B premiums</th>
<th>Part B + Part D premiums</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>9%</td>
<td>12%</td>
</tr>
<tr>
<td>2075</td>
<td>22%</td>
<td>31%</td>
</tr>
</tbody>
</table>

*Source: 2009 Medicare Trustees Report, Figure III.C1.*

**Note:** Part B premiums are not expected to decrease as a proportion of Social Security benefits, as they are shown to do in the early years of Figure 5. Figure 5 is based on the trustees’ projections; the trustees acknowledge that their short-run projections of Part B costs are “unreasonably reduced” due to the assumption that physician payments will be cut (2009 Medicare Trustees Report, p. 31). In addition, Figure 5 shows a cohort of hypothetical workers each year in the first year of their retirements, whereas Figure 3 shows a single cohort of hypothetical workers over time.

Beneficiaries are projected to need a much larger fraction of their Social Security benefits to pay Part B premiums in the future. For example, in 2010 it is projected that the Part B premium will absorb 9% of the average Social Security benefit in the first year of retirement, and the combined Parts B and D premiums will absorb 12% of the average initial benefit. In 2078 premiums are projected to absorb more than twice that share, with 22% going to pay the Part B premium in the first year of retirement, and 31% of the average benefit in the first year of retirement going to pay combined Parts B and D premiums. In the future, as in the past, low earners will need a greater fraction of their benefits to pay the Part B premium than will high earners.
Legislation in the 111\textsuperscript{th} Congress

As a result of SSA’s announcement that no COLA will be paid in 2010, and if, as projected, there is no Social Security COLA in 2011, then a range of issues may potentially be addressed through legislation. These issues may include the impact of the hold harmless provision on the Part B premiums paid by beneficiaries who are not held harmless, the impact on seniors who will pay higher Part D premiums and higher out-of-pocket medical costs, and other issues. Several bills before the 111\textsuperscript{th} Congress would address one or more of these issues. For more information, please see CRS Report R40561, \textit{How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?}, by Jim Hahn and Alison M. Shelton.

Conclusion

Rising Medicare premiums are consuming a growing share of beneficiaries’ Social Security benefits. An increasing number of Americans will be affected by this interaction as the number of Social Security and Medicare beneficiaries grows over time. The Social Security trustees project that by 2040, the proportion of Americans aged 65 and older—most of whom are eligible for both Social Security and Medicare—will almost double.\footnote{2009 Social Security Trustees Report, Table V.A2.}

Low-income beneficiaries and those who rely primarily on Social Security may see a decline in their standard of living as their Medicare expenses rise. Premiums for Parts B and D are projected to increase significantly faster than Social Security benefits. The hold harmless provision protects most beneficiaries from a drop in the dollar value of Social Security benefits; however, the Part B and Part D premiums are projected to consume a growing share of the annual Social Security COLA, which was designed to maintain beneficiaries’ living standards.

Out-of-pocket costs for Parts B and D are projected to grow at the same rates as premiums, contributing to the growing health-care expenses of beneficiaries. Most beneficiaries are likely to have income apart from their Social Security benefits. However, many of tomorrow’s beneficiaries, like today’s, are likely to rely mostly on Social Security, especially as traditional pension coverage declines and many Americans save little or nothing for retirement.\footnote{CRS Report RL30122, \textit{Pension Sponsorship and Participation: Summary of Recent Trends} and CRS Report RL30922, \textit{Retirement Savings and Household Wealth in 2007}, both by Patrick Purcell.} Some beneficiaries will be protected from rising Medicare premiums: Medicaid covers premiums for some persons who meet income and asset tests, and the hold harmless provision protects most Social Security beneficiaries against Part B increases (although not Part D increases) that exceed the annual Social Security COLA. Many beneficiaries could struggle to cover their health-care expenses, however, including new enrollees who are not covered by the hold harmless provision.\footnote{For more information on the hold harmless provision and the impact on Part B premiums if there is no Social Security COLA for 2010 and 2011, see CRS Report R40561, \textit{How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?}, by Jim Hahn and Alison Shelton.}

Finally, it is important to remember that Social Security beneficiaries gain from their participation in the Medicare program. Medicare provides health-care coverage to the vast majority of

\footnote{2009 Social Security Trustees Report, Table V.A2.}
\footnote{For more information on the hold harmless provision and the impact on Part B premiums if there is no Social Security COLA for 2010 and 2011, see CRS Report R40561, \textit{How Would Medicare Part B Premiums Be Affected If There Were No Social Security COLA?}, by Jim Hahn and Alison Shelton.}
Americans aged 65 and older and to most disability beneficiaries. Together, Medicare and Medicaid cover a majority of participating Social Security beneficiaries' health-care expenses. Although Social Security beneficiaries are affected by rising health-care costs, the benefits of participating in Medicare are substantially greater than the costs.

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