THE MISSING INGREDIENT IN THE BUDGET DEBATE: PHASING OUT SOCIAL SECURITY AND MEDICARE FOR HIGH INCOME RETIREES

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Draft May 18, 2011

BY

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\(^1\) I would like to thank the following for their helpful comments on this paper: the faculty members at the Penn State Dickinson School of Law who participated in a forum on the paper; Professor Richard Kaplan of the University of Illinois College of Law, an expert in income tax and elder law; Professor Joel Handler of the UCLA School of Law; and my Research Assistants at the Penn State Dickinson School of Law: Stephen Anderson, Marc Boiron, Jake Mattinson, and Becky Sue Thompson. Also, during the development of this paper, I benefited from discussions I had with Professor Kaplan and Professor Preston Green of the Penn State Dickinson School of Law. The ideas discussed and any mistakes are, of course, my own.
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I. Introduction

A. Three Deficit and Debt Proposals

The concern with the Federal budget deficits\textsuperscript{2} and the growing Federal debt\textsuperscript{3} has brought forth three principal proposals: (1) the December 2010 proposal by the bipartisan National Commission on Fiscal Responsibility and Reform (the Deficit Commission Proposal);\textsuperscript{4} (2) the April 2011 Fiscal Year 2012 Budget Resolution, The Path to Prosperity,\textsuperscript{5} advanced by Congressman Paul Ryan, the Republican chairman of the House Committee on the Budget (the Ryan Proposal); and (3) the proposal of President Obama set out in a speech\textsuperscript{6} he gave at George Washington University on April 13, 2011 (the Obama Proposal). These proposals are sometimes referred to here as the Three Proposals.

B. Introduction to the Proposal Here for “Phasing Out” Social Security and Medicare

As discussed below, the three main reasons for the long-term problem with budget deficits and debt are (1) Social Security, a Federal retirement program for the elderly; (2) Medicare, a Federal health care program for the elderly; and (3) Medicaid, a Federal health care program for low

\textsuperscript{2} Budget deficits are the annual differences between revenues collected and expenditures made by the Federal government.
\textsuperscript{3} Debt is the aggregate Federal government debt held by the public, including foreigners.
\textsuperscript{4} The Moment of Truth, Report of the National Commission on Fiscal Responsibility (December 2010) [the Deficit Commission Proposal]. The Commission, which was appointed by President Obama, was chaired by former Republican Senator, Alan Simpson of Wyoming and Democrat Erskine Bowles, former Chief of Staff to President Clinton.
\textsuperscript{5} The Path to Prosperity, Fiscal Year 2012 Budget Resolution, House Committee on the Budget, Chairman Paul Ryan of Wisconsin [the Ryan Proposal].
\textsuperscript{6} Remarks of President Obama on Fiscal Policy, George Washington University (April 13, 2011) [the Obama Proposal].
income persons. In this article, I set forth proposals for reforming Social Security and Medicare that none of the Three Proposals address: a “phase-out” of benefits. Under the phase-out proposed here, retirees with high incomes would (1) have to pay a portion (and in some cases, all) of the cost of Medicare insurance, and (2) receive a reduced (and in some cases, no) Social Security payment.

The phase-out reforms proposed here are not even discussed in the Congressional Budget Office’s March 2011 publication: *Reducing the Deficit: Spending and Revenue Options.* However, a March 2011 study on the means testing of Social Security by the Center for Economic and Policy Research reports that “[m]ore than 90 percent of [Social Security] benefits go to individuals with non-Social Security incomes of less than $50,000 a year.” As indicated below, the phase-outs proposed here would begin at approximately $50,000 of non-Social Security income and, therefore, could be expected to result in savings of less than 10% of Social Security payments.

These reforms are consistent with the fundamental “safety net” principles underlying Medicare and Social Security, and if adopted, these proposals would be a positive step in putting Medicare and Social Security on a sustainable fiscal basis. Even with these changes, however, efforts should continue to be made to enhance the operational efficiency and cost effectiveness of each of these and other programs.

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Before elaborating on these proposed reforms, Section II briefly discusses background information on deficits and debt and the potential harm they may cause to the economy. The article next outlines how the issues with Social Security, Medicare and Medicaid are addressed in the Deficit Commission Proposal (Section III), the Ryan Proposal (Section IV), and the Obama Proposal (Section V). The article then (1) discusses the phase-out proposal for Social Security and Medicare (Section VI), (2) briefly touches on the political problem raised by this proposal (Section VII), and (3) provides a conclusion (Section VIII). Although the approaches to Medicaid set out in the Three Proposals are discussed, this article does not make any suggestions for reforming Medicaid. Also, this article does not discuss potential changes in the structure of the tax system applicable to Social Security and Medicare. The phase-out proposals set out here should be adopted without regard to potential changes in the tax structures supporting these programs.
II. Background Information on the Problem with Deficits and Debt

A. The CBO’s Projections of Deficits and Debt

In its January 2011 *Budget and Economic Outlook*, the bipartisan Congressional Budget Office (CBO) paints the following picture of the annual budget deficits the country faces and the impact of these deficits on the nation’s outstanding debt for the 10-year projection period, 2011-2021:

The amount of federal debt held by the public has varied markedly over the past few decades. After reaching nearly 50 percent of GDP in 1993, it dropped to 33 percent in 2001 as a result of several years of declining budget deficits and then surpluses . . . . The surpluses and declining debt were short-lived, however, as deficits between 2002 and 2007 boosted debt held by the public by $1.7 trillion; still, economic growth in that period kept debt as a percentage of GDP fairly steady, at around 37 percent.

In 2008, the United States experienced its most severe financial crisis since the Great Depression. The next year, federal revenues dropped sharply and outlays increased substantially, pushing the deficit to $1.4 trillion. The budget deficit in 2010 was nearly $1.3 trillion because of continued low revenues and elevated spending. Overall, in the three years between 2008 and 2010, the Treasury added nearly $4 trillion to its outstanding borrowing, increasing debt held by the public as a percentage of GDP from 36 percent at the end of 2007 to 62 percent at the end of 2010. Under the assumptions of the baseline (in particular, [1] that tax provisions [*i.e.*, the Bush tax cuts and relief under the alternative minimum tax (AMT)] expire as scheduled, [2] that Medicare’s payment
rates to physicians drop sharply as scheduled [the “doc fix” doesn’t happen], and [3] that discretionary spending grows at the rate of inflation), debt held by the public is projected to rise to 69 percent of GDP this year and 77 percent of GDP by 2021 . . . . That amount of debt relative to GDP would be the highest recorded since 1950.9

Obviously, the budget deficits and the outstanding debt would be higher if (1) the Bush tax cuts are extended, which is almost certain for taxpayers making less than $250,000;10 (2) the AMT is indexed for inflation, which is a sensible and almost certain policy change;11 and (3) the planned reduction in Medicare payments to doctors is reversed, which is highly likely (i.e., the “doc fix” likely will happen).12

The CBO gives the following explanation of the likely explosion in deficits and debt that could occur beyond the 10-year projection period used in its January 2011 *Budget and Economic Outlook*:

> Beyond the 10-year projection period, further increases in federal debt relative to the nation’s output almost certainly lie ahead if current policies remain in place. The aging of the population and rising costs for health care will push federal spending as a percentage of GDP well above that in recent decades. In particular, spending on the government’s major mandatory health care programs—Medicare, Medicaid, CHIP [(the Federal Children Health Insurance Program)], and health insurance subsidies to be provided

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10 The President wants to extend them for married taxpayers making less than $250,000 and the Republicans want to extend them for all taxpayers.
11 There is a lot of support for this change.
12 There is a lot of support for the doc fix.
through the new insurance exchanges—along with Social Security will increase from roughly 10 percent of GDP in 2011 to about 16 percent over the next 25 years. If revenues stay close to their average share of GDP for the past 40 years, that rise in spending will lead to rapidly growing budget deficits and surging federal debt.\textsuperscript{13}

The following table shows the expected spending over the 2011 to 2021 forecast period on Social Security, Medicare, and Medicaid:

<table>
<thead>
<tr>
<th>Federal Program</th>
<th>Expected Spending, 2011-2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>Social Security</td>
<td>$9.8 Trillion</td>
</tr>
<tr>
<td>Medicare</td>
<td>$7.6 Trillion</td>
</tr>
<tr>
<td>Medicaid</td>
<td>$4.2 Trillion</td>
</tr>
</tbody>
</table>

\textbf{Source:} CBO Budget and Economic Outlook, \textit{supra} note 9, at Table 3-3, p. 58.

The CBO elaborates as follows on the impact of these programs on the deficit:

CBO estimates that Social Security, Medicare, Medicaid, and other health programs will account for nearly 70 percent of mandatory spending (excluding offsetting receipts) in 2011. In the absence of any changes in law, outlays for those programs will exceed 80 percent of mandatory spending by 2021. Spending for those programs will equal 10.6 percent of GDP in 2011 but will grow to 12.7 percent by 2021, in large part because federal outlays related to health care are projected to increase rapidly.\textsuperscript{14}

\textsuperscript{13} Budget and Economic Outlook, \textit{supra}, note 9, at 25.
\textsuperscript{14} Id. at 60.
The importance of addressing Social Security and Medicare was highlighted in the May 13, 2011 report of the Social Security and Medicare Boards of Trustees. In discussing the findings in the Report, Treasury Secretary Geithner explains:

The Social Security program has dedicated resources that will cover benefits for the next 25 years. But in 2036, one year earlier than was projected in last year’s report, the Social Security Trust Fund will exhaust its assets and incoming revenues will be insufficient to maintain payment of full benefits. Due to technical changes in the economic assumptions underlying the projections, Medicare’s Hospital Insurance Trust Fund will exhaust its assets in 2024, five years earlier than was projected in last year’s report.

**B. Assessment of the Impact of Deficits and Debt on Economic Growth by the CBO, the President, the Deficit Commission, and Congressman Ryan**

In evaluating the impact of deficits and debt on the economy, the CBO first points out that “deficits during or shortly after a recession generally hasten economic recovery . . . .” The CBO then discusses several reasons, “[s]ome of [which] would arise gradually,” why we should be concerned with rising deficits and debt.

The gradual consequences include potential harms from “crowding out” private investment and higher marginal tax rates:

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17 Budget and Economic Outlook, supra, note 9, at 25.
18 Id.
A growing portion of people’s savings would go to purchase government debt rather than toward investments in productive capital goods such as factories and computers; that “crowding out” of investment would lead to lower output and incomes than would otherwise be the case. In addition, if the payment of interest on the extra debt was financed by imposing higher marginal tax rates, those rates could discourage work and saving and further reduce output; alternatively, the growing interest payments might force reductions in spending on government programs. Moreover, rising debt would increasingly restrict the ability of policymakers to use fiscal policy to respond to unexpected challenges, such as economic downturns or international crises.19

In addition to these potential gradual consequences, the CBO points out that there is also concern that “a growing federal debt . . . would increase the probability of a sudden fiscal crisis, during which investors would lose confidence in the government’s ability to manage its budget and the government would thereby lose its ability to borrow at affordable rates.”20 However, the CBO goes on to explain: “because interest rates on Treasury securities are unusually low today, such a crisis does not appear imminent in the United States.”21 The CBO elaborates as follows on this crisis point:

[A]s other countries’ experiences show [e.g., Greece], investors can lose confidence abruptly and interest rates on government debt can rise sharply and unexpectedly.

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19 Id.
20 Id.
21 Id.
The exact point at which such a crisis might occur for the United States is unknown, in part because the ratio of federal debt to GDP is climbing into unfamiliar territory and in part because the risk of a crisis is influenced by other factors, including the government’s long-term budget outlook, its near-term borrowing needs, the amount of private saving, and foreign investors’ willingness to invest in U.S. assets. Thus, there is no way to predict with any confidence whether and when such a crisis might occur and no identifiable tipping point of debt relative to GDP. However, the risk of a crisis probably will increase when investors’ growing confidence in the global recovery and the stability of the financial system increases their desire to hold private securities and foreign debt rather than Treasury securities. Moreover, the risk would probably become much larger if debt grew substantially more relative to GDP and if that debt-to-GDP ratio was poised to continue to rise.22

Although this evaluation by the CBO does not necessarily mean that our projected deficits and debt will ruin our economy, it is commonly accepted that they may have an adverse effect on our economy if they are not addressed. For example, in his April 2011 Budget Speech, President Obama explained as follows the risk to the economy from large deficits and debt:

> Ultimately, all this rising debt will cost us jobs and damage our economy. It will prevent us from making the investments we need to win the future. We won’t be able to afford good schools, new research, or the repair of roads — all the things that create new jobs and businesses here in America. Businesses will be less likely to invest and open shop in a country that seems unwilling or unable to balance its books. And if our

22 Id.
creditors start worrying that we may be unable to pay back our debts, that could drive up interest rates for everybody who borrows money — making it harder for businesses to expand and hire, or families to take out a mortgage.\(^\text{23}\)

And, the Deficit Commission gave the following similar explanation of the impact of deficits and debt on the economy:

Federal debt this high is unsustainable. It will drive up interest rates for all borrowers — businesses and individuals — and curtail economic growth by crowding out private investment. By making it more expensive for entrepreneurs and businesses to raise capital, innovate, and create jobs, rising debt could reduce per-capita GDP, each American’s share of the nation’s economy, by as much as 15 percent by 2035.\(^\text{24}\)

The Ryan Proposal has an even more apocalyptic projection of the adverse effects of debt on the economy:

The economic effects of a debt crisis on the United States would be far worse than what the nation experienced during the financial crisis of 2008. For starters, no entity on the planet is large enough to bail out the U.S. government. Absent a bailout, the only solutions to a debt crisis would be truly painful: massive tax increases, sudden and disruptive cuts to vital programs, runaway inflation, or all three. This would create a huge hole in the economy that would be exacerbated by panic.

Even if high debt did not cause a crisis, however, the nation would still be in for a long and grinding period of economic decline if it stayed on its current path. A recent study

\(^{23}\) The Obama Proposal, \textit{supra} note 6.

\(^{24}\) The Deficit Commission Proposal, \textit{supra} note 4, at 11.
completed by Reinhart and economist Ken Rogoff of Harvard confirms this common-sense conclusion. The study found conclusive empirical evidence that total debt exceeding 90 percent of the economy has a significant negative effect on economic growth.\textsuperscript{25}

The Ryan Proposal overstates the prediction of the Reinhart and Rogoff study, which finds: “[I]t is evident that there is no obvious link between debt and growth until public debt reaches a threshold of 90 percent [of GDP].”\textsuperscript{26} As indicated above, the CBO predicts that in 2021 debt will be only 77\% of GDP.

C. Standard and Poor’s Rating of U.S. Debt, April 18, 2011

On April 18, 2011, Standard and Poor’s affirmed its triple A rating (the highest rating) of U.S. debt, while at the same time stating that its “Outlook was Revised to Negative.”\textsuperscript{27} S&P gives the following reason for the negative outlook:

We believe there is a material risk that U.S. policymakers might not reach an agreement on how to address medium- and long-term budgetary challenges by 2013; if an agreement is not reached and meaningful implementation does not begin by then, this would in our view render the U.S. fiscal profile meaningfully weaker than that of peer 'AAA' sovereigns.\textsuperscript{28}

\textsuperscript{25} The Ryan Proposal, \textit{supra} note 5, at 21.
\textsuperscript{27} Standard and Poor’s Global Credit Portal, \textit{United States of America, AAA/A-1+ Rating Affirmed, Outlook Revised to Negative} (April 18, 2011) [S&P April 2011 Report].
\textsuperscript{28} \textit{Id.} at 2.
If U.S. debt were to be downgraded by S&P and other rating agencies, the government would have to pay higher interest rates when issuing new debt.

The S&P report makes it clear that the principal contributors to the long-term budgetary issues are Social Security, Medicare, and Medicaid:

Beyond the short- and medium-term fiscal challenges, we view the U.S.’s unfunded entitlement programs (such as Social Security, Medicare, and Medicaid) to be the main source of long-term fiscal pressure. These entitlements already account for almost half of federal spending (an estimated 42% in fiscal-year 2011), and we project that percentage to continue increasing as long as these entitlement programs remain as they currently exist (see "Global Aging 2010: In The U.S., Going Gray Will Cost A Lot More Green," Oct. 25, 2010, RatingsDirect).29

The phase-out for Social Security and Medicare proposed here would address, at least in part, S&P’s concern that the percentage of Federal spending for these programs will “continue increasing as long as these entitlement programs remain as they currently exist . . . .”30

D. Possible Overstatement of the Concern with Debt

Two final points on debt: First, as indicated in the CBO’s Budget and Economic Outlook, the recent increase in budget deficits and debt arose from a combination of (1) a reduction in revenues resulting from the most severe downturn in economic activity since the great depression, and (2) an increase in government spending to offset the decline in spending by individuals and firms. Many, if not most, economists agree that (1) without the increase in short-term spending by our Federal government, our economy would have been worse off than it is

29 Id. at 5.
30 Id.
now, and (2) it does not make sense economically to be cutting short-term government spending as our economy is recovering from a recession. One economist recently made the point as follows:

Virtually all experts agree that the deficits that must be brought under control are the looming large future deficits, not the temporary deficit caused by the recession itself or the temporary fiscal stimulus enacted to combat it.\textsuperscript{31}

Another economist recently had the following harsh assessment of the rush to cut current government spending:

We are cutting government spending with little thought to the value of the public services forgone, and no thought at all to the effect on production, jobs and incomes.

Fiscal prudence matters. But the helter skelter rush to cut this year’s and next year’s budget deficits is high-priced folly. For want of enough spending overall by households, businesses and government taken together, i.e., for want of enough buying, a huge amount of production capacity is standing idle, producing nothing. . . . If anyone tells you that cutbacks in this year’s and next year’s federal spending will encourage enough additional private spending to make up the difference . . . [i]t’s nonsense.\textsuperscript{32}


It should be crystal clear to any objective observer that the problem with debt is not a short-term problem; rather, it is a long term problem, principally caused by the aging of the American population and the rising per capita costs of medical care.

Second, the ratio of Federal debt to GDP is in some ways analogous to the ratio of an individual’s debt to his or her income. Most individuals who have a home mortgage have a ratio of debt to income of 3 or 4 to 1, much higher than the ratio of Federal debt to GDP. However, the ratio of an individual’s debt to home and asset value may be at most 70%-80%. At the Federal level the ratio of debt to the value of all of the assets in the U.S is significantly lower than 70%-80%. Although, this could mean that the concern with Federal debt may be overstated, it is prudent to act peremptorily in addressing the projected growth in long-term debt.
III. Treatment of Medicaid, Medicare, and Social Security in the Deficit Commission Proposal

A. Medicaid Proposals

In its chapter on Health Care Savings, the Deficit Commission makes the following technical recommendations relating to Medicaid:

Medicaid Savings

3.3.8 Eliminate state gaming of Medicaid tax gimmick.

(Saves $5 billion in 2015, $44 billion through 2020) . . .

3.3.9 Place dual eligibles in Medicaid managed care.

(Saves $1 billion in 2015, $12 billion through 2020) . . .

3.3.10 Reduce funding for Medicaid administrative costs.

(Saves $260 million in 2015, $2 billion through 2020) . . .

None of these proposals would have a significant impact on the broad range of people receiving Medicaid payments. The total savings would be $58 billion through 2020. This is a little more

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33 Deficit Commission, supra note 4, at 39.
than 1% of the $4.2 trillion the CBO estimates will be spent on Medicaid during the 10-year forecast period, 2011-2021.\textsuperscript{34}

B. Medicare Proposals

In its chapter on Health Care Savings, the Deficit Commission makes the following rather technical recommendations relating to Medicare:

\textbf{Medicare Savings}

3.3.1 Increase government authority and funding to reduce Medicare fraud.

\textit{(Saves $1 billion in 2015, $9 billion through 2020)} . . .

3.3.2 Reform Medicare cost-sharing rules.

\textit{(Saves $10 billion in 2015, $110 billion through 2020)} . . .

3.3.3 Restrict first-dollar coverage in Medicare supplemental insurance.

\textit{(Medigap savings included in previous option. Additional savings total $4 billion in 2015, $38 billion through 2020.) . . .}

3.3.4 Extend Medicaid drug rebate to dual eligibles in Part D.

\textit{(Saves $7 billion in 2015, $49 billion through 2020)} . . .

3.3.5 Reduce excess payments to hospitals for medical education.

\textit{(Saves $6 billion in 2015, $60 billion through 2020)} . . .

\textsuperscript{34} See Table A, \textit{supra}.}
3.3.6 Cut Medicare payments for bad debts.

*(Saves $3 billion in 2015, $23 billion through 2020)* . . .

3.3.7 Accelerate home health savings in ACA.

*(Saves $2 billion in 2015, $9 billion through 2020)* . . .

The total cost savings would be $298 billion through 2020, which is about 4% of the $7.6 trillion the CBO estimates will be spent on Medicare during the 10-year forecast period, 2011-2021. None of the changes would seem to have a significant adverse impact on the benefits Medicare recipients receive.

**C. Overall Spending on Health Care**

The Deficit Commission makes the following recommendation for containing the growth of spending on health care by the Federal government:

**RECOMMENDATION 3.6: ESTABLISH A LONG-TERM GLOBAL BUDGET FOR TOTAL HEALTH CARE SPENDING.** Establish a global budget for total federal health care costs and limit the growth to GDP plus 1 percent. . .

**D. Social Security**

In its chapter on Social Security, the Deficit Commission makes the following recommendations regarding Social Security Reform:

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36 See Table A, *supra*.
37 Deficit Commission, *supra* note 4, at 41.
RECOMMENDATION 5.1: MAKE RETIREMENT BENEFIT FORMULA MORE PROGRESSIVE. Modify the current three-bracket formula to a more progressive four-bracket formula, with changes phased in slowly. Change the current bend point factors of 90%|32%|15% to 90%|30%|10%|5% by 2050, with the new bend point added at median lifetime income. . .

RECOMMENDATION 5.2: REDUCE POVERTY BY PROVIDING AN ENHANCED MINIMUM BENEFIT FOR LOW-WAGE WORKERS. Create a new special minimum benefit that provides full career workers with a benefit no less than 125 percent of the poverty line in 2017 and indexed to wages thereafter. . .

RECOMMENDATION 5.3: ENHANCE BENEFITS FOR THE VERY OLD AND THE LONG-TIME DISABLED. Add a new “20-year benefit bump up” to protect those Social Security recipients who have potentially outlived their personal retirement resources. . .

RECOMMENDATION 5.4: GRADUALLY INCREASE EARLY AND FULL RETIREMENT AGES, BASED ON INCREASES IN LIFE EXPECTANCY. After the Normal Retirement Age (NRA) reaches 67 in 2027 under current law, index both the NRA and Early Eligibility Age (EEA) to increases in life expectancy, effectively increasing the NRA to 68 by about 2050 and 69 by about 2075, and the EEA to 63 and 64 in lock step. . .
RECOMMENDATION 5.5: GIVE RETIREES MORE FLEXIBILITY IN CLAIMING BENEFITS AND CREATE A HARDSHIP EXEMPTION FOR THOSE WHO CANNOT WORK BEYOND 62. Allow Social Security beneficiaries to collect half of their benefits as early as age 62, and the other half at a later age. Also, direct the Social Security Administration to design a hardship exemption for those who cannot work past 62 but who do not qualify for disability benefits.

RECOMMENDATION 5.6: GRADUALLY INCREASE THE TAXABLE MAXIMUM TO COVER 90 PERCENT OF WAGES BY 2050.

RECOMMENDATION 5.7: ADOPT IMPROVED MEASURE OF CPI. Use the chained CPI, a more accurate measure of inflation, to calculate the Cost of Living Adjustment for Social Security beneficiaries.

RECOMMENDATION 5.8: COVER NEWLY HIRED STATE AND LOCAL WORKERS AFTER 2020. After 2020, mandate that all newly hired state and local workers be covered under Social Security, and require state and local pension plans to share data with Social Security.

RECOMMENDATION 5.9: DIRECT SSA TO BETTER INFORM FUTURE BENEFICIARIES ON RETIREMENT OPTIONS. Direct the Social Security Administration to improve information on retirement choices, better inform future beneficiaries on the financial implications of early retirement, and promote greater retirement savings.
RECOMMENDATION 5.10: BEGIN A BROAD DIALOGUE ON THE IMPORTANCE OF PERSONAL RETIREMENT SAVINGS.\textsuperscript{38}

Although no costs estimates are included with these changes, Figure 17 to the Deficit Commission Report shows that the “Total Deficit Effect of Social Security Reform” is to increase the deficit by $238 billion over the 2012-2020 forecast period. This increase arises because many of these proposals, including the proposal to make the benefit formula more progressive, would enhance the Social Security payments received by lower income workers.

\textbf{E. General Observations}

The Deficit Commission essentially keeps in place the current structure of Medicaid, Medicare, and Social Security. Its changes are on the margins of these programs and do not adversely impact the “safety net” role these programs provide.

\textbf{IV. Treatment of Medicaid, Medicare, and Social Security in the Ryan Proposal}

\textbf{A. Medicaid}

The Ryan Proposal would make major reforms to Medicaid, the medical program for the poor. The changes are described as follows in the Ryan Proposal:

\textsuperscript{38} \textit{Id.} at 49-53.
**Major proposals**

- Secure the Medicaid benefit by converting the federal share of Medicaid spending into a block grant tailored to meet each state’s needs, indexed for inflation and population growth. This reform ends the misguided one-size-fits-all approach that has tied the hands of so many state governments. States will no longer be shackled by federally determined program requirements and enrollment criteria. Instead, they will have the freedom and flexibility to tailor a Medicaid program that fits the needs of their unique populations.

- Improve the health-care safety net for low-income Americans by giving states the ability to offer their Medicaid populations more options and better access to care. Medicaid recipients, like all Americans, deserve to choose their own doctors and make their own health care decisions, instead of having Washington dictate those decisions for them.

- Save $750 billion over ten years, contributing to the long-term stabilization of the federal government’s fiscal path and encouraging fiscal responsibility at the state level.\(^{39}\)

The last bullet, the $750 billion savings, is the most important proposed reform. As indicated above, the CBO estimates that over its 10-year forecast period (2011-2021), spending on Medicare would equal $4.2 trillion, and the Ryan proposal would cut this by $750 billion, which is an 18% cut in the spending on health care for the poor.

B. Medicare

The Ryan Proposal sets out the following proposed changes to Medicare:

Saving Medicare

Major proposals

• Save Medicare for current and future generations while making no changes for those in and near retirement. For younger workers, when they reach eligibility, Medicare will provide a Medicare payment and a list of guaranteed coverage options from which recipients can choose a plan that best suits their needs. These future Medicare beneficiaries will be able to choose a plan the same way members of Congress do. Medicare will provide additional assistance for lower-income beneficiaries and those with greater health risks.

• Ensure that the cost of frivolous litigation is not passed on to consumers in the form of higher health-care premiums by capping non-economic damages in medical liability lawsuits.

• Stop the raid on the Medicare trust fund that was going to be used to pay for the new health care law. Any current-law Medicare savings must go to saving Medicare, not financing the creation of new open-ended health-care entitlements.
• Fix the Medicare physician payment formula for the next ten years so that Medicare beneficiaries continue to have access to health care [the “doc fix”].

The first bullet-point is the most important; it would result in the partial privatization of Medicare. It is referred to here as the Ryan Medicare Voucher Proposal, although the Ryan Proposal describes it as a “premium-support” program. The Ryan Proposal explains that wealthier retirees would receive less premium-support than low income retirees:

The Medicare premium-support payment would be adjusted so that wealthier beneficiaries would receive a lower subsidy, the sick would receive a higher payment if their conditions worsened, and lower-income seniors would receive additional assistance to cover out-of-pocket costs.

The Ryan Proposal would apply to people who are now 55 or under.

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40 Id. at 44.
41 Id. at 46. Henry Aaron, an outstanding public finance economist, explains why the Ryan Proposal is a voucher system and not a premium support plan:

Of late, various sponsors of plans [including the Ryan Proposal] to change the terms of Medicare have applied the term “premium support” to plans that provide vouchers, but lack one or more of the protections that distinguish the two approaches. People are, of course, free to redefine terms: trying to avoid tainted terms is commonplace—people are no longer ‘fired’ but are given ‘new career opportunities.’ But it is important that the affective trappings of the term ‘premium support’ not protect the harsher realities of voucher plans from the scrutiny they deserve.

Henry Aaron, Vouchers Or Premium Support: What’s In A Name?, Posted By Henry Aaron On April 6, 2011 @ 3:56 pm In All Categories, Competition, Consumers, Health Reform, Insurance, Medicare, HealthAffairs.org, at http://healthaffairs.org/blog/2011/04/06/vouchers-or-premium-support-whats-in-a-name/ [Aaron, Vouchers].
42 Ryan Proposal, supra note 5, at 46.
It does not seem clear from the Ryan Proposal how much of a reduction in Medicare benefits would result from adoption of the Ryan Medicare Voucher Proposal. However, in addressing this reduction in benefits issue in his Budget speech, President Obama asserts:

[The Ryan Medicare Voucher Proposal] says that 10 years from now, if you’re a 65-year-old who’s eligible for Medicare, you should have to pay nearly $6,400 more than you would today. It says instead of guaranteed health care, you will get a voucher. And if that voucher isn’t worth enough to buy the insurance that’s available in the open marketplace, well, tough luck — you’re on your own. Put simply, it ends Medicare as we know it.  

Also, in an analysis of the Ryan Proposal, the Congressional Budget Office, estimates that in 2022, under that Proposal, “a typical 65-year-old would pay 61 percent of the [the costs] of benchmark [medical services].” On the other hand, under the current Medicare rules, the CBO estimates that “the typical 65-year-old would pay 27 percent of the benchmark . . . .” Thus, the

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43 The Obama Proposal, supra note 6.
44 Congressional Budget Office, Long-Term Analysis of a Budget Proposal by Chairman Ryan, 23 (April 5, 2011).
45 Id. Henry Aaron describes the differences between the present system and the Ryan Proposal as follows:

It is not surprising . . . that the Congressional Budget Office estimates that [under the Ryan Proposal] the share of health care expenses that a typical elderly beneficiary would have to pay out of pocket would go up in 2030—from 25-30 percent under current law, to 68 percent under the Ryan plan. Since the same adjustment factor would be used for Medicaid, which Ryan would convert into a block grant, it is also not surprising that federal health care spending would be reduced by approximately two-thirds by 2050.

Aaron, Vouchers, supra note 41.

And, a report of the Center for Economic and Policy Research points out that the Ryan Proposal will become much more onerous on beneficiaries as they age:

According to the CBO analysis, [under the Ryan Proposal] rising health care costs will quickly make a Medicare equivalent plan unaffordable to most beneficiaries. Also, since costs rise as beneficiaries age, a Medicare equivalent plan will become less affordable to the same beneficiary as she gets older. Finally, this plan implies a huge transfer of income from beneficiaries to health care providers and insurers, since the
Ryan Proposal would increase the cost of benchmark services that the typical 65-year-old would have to bear from 27%, under the current law, to 61% under the Ryan Proposal.

Finally, in view of the fact that (1) the last bullet point (the 10-year “doc fix”) would result in higher spending, and (2) Table S-4 of the Ryan Proposal indicates that there will not be a significant change in overall spending on Medicare, it would appear that the Ryan Medicare Voucher Proposal in essence pays for the doc fix by reducing the payments for medical care. If this is so, then the Ryan Proposal would result in a wealth transfer from those receiving Medicare to doctors providing medical care services.\footnote{In making a similar point, the report of the Center for Economic and Policy Research states:}

\begin{quote}
Finally, [the Ryan] plan implies a huge transfer of income from beneficiaries to health care providers and insurers, since the cost of delivering the same quality care will be substantially higher under Representative Ryan’s plan than under the existing Medicare system.
\end{quote}

The bottom line is that less would be spent on medical coverage for those receiving Medicare, but the overall spending on Medicare, estimated at $7.6 trillion by the CBO over its 10-year forecast period would not be significantly changed.

\section*{C. Social Security}

The Ryan Proposal sets out the following general principles regarding the need for Congress and the President to reform Social Security:

\begin{quote}
Advancing Social Security Reforms
\end{quote}

\footnotetext{In making a similar point, the report of the Center for Economic and Policy Research states:}

\begin{quote}
Finally, [the Ryan] plan implies a huge transfer of income from beneficiaries to health care providers and insurers, since the cost of delivering the same quality care will be substantially higher under Representative Ryan’s plan than under the existing Medicare system.
\end{quote}

CEPR on Ryan Plan, \textit{supra} note 45.
Major proposals

• Force policymakers to come to the table and enact common-sense reforms to keep the program solvent for current beneficiaries and make it stronger for future generations. Social Security must be reformed to prevent severe cuts in future benefits.

• Set in motion the process of reforming Social Security by establishing a requirement that in the event that the Social Security program is not sustainable, the President, in conjunction with the Board of Trustees, must submit a plan for restoring balance to the fund. The budget then requires congressional leaders in both the U.S. House of Representatives and U.S. Senate to put forward their best ideas as well.

• Move the conversation to solutions that save Social Security, thus providing the space to forge a bipartisan path forward and ensure that Social Security remains a key part of retirement security for the future.47

Table S-4 of the Ryan Proposal indicates that his proposal would result in no change to Social Security payments over the forecast period.

D. General Observations

First, the Ryan Proposal takes on the weakest group in society by proposing an 18% cut in medical benefits for the poor through cuts in Medicaid. Second, without stating it directly, the Ryan Proposal uses cuts in medical benefits resulting from the privatization of Medicare as a way of paying for the doc fix; this would be a wealth transfer from many poor and middle class

47 Ryan Proposal, supra note 5, at 47.
elderly receiving health care to much better off doctors. The CBO makes it clear that the Ryan Medicare Voucher Proposal is a “stealth” attempt to shift a significant portion of the cost of Medicare to the retired. Third, to avoid a fight with one of this nation’s most powerful constituencies, the retired, the Ryan Proposal “punts the ball down the field” on Social Security. The Ryan Proposal would thus erode the “safety net” function of Medicaid and Medicare, but not of Social Security.
V. Treatment of Medicaid, Medicare, and Social Security in the Obama Proposal

A. Medicaid and Medicare

The Obama Proposal addresses Medicare and Medicaid in the same way. First, the President rejects out of hand the Ryan Proposal to move to a voucher system for Medicare and to cut back on Medicaid spending:

[The Ryan Proposal is] a vision that says America can’t afford to keep the promise we’ve made to care for our seniors. . . .

It’s a vision that says up to 50 million Americans have to lose their health insurance in order for us to reduce the deficit. Who are these 50 million Americans? Many are somebody’s grandparents -- may be one of yours -- who wouldn’t be able to afford nursing home care without Medicaid. Many are poor children. Some are middle-class families who have children with autism or Down’s syndrome. Some of these kids with disabilities are -- the disabilities are so severe that they require 24-hour care. These are the Americans we’d be telling to fend for themselves. . . .

To meet our fiscal challenge, we will need to make reforms. We will all need to make sacrifices. But we do not have to sacrifice the America we believe in. And as long as I’m President, we won’t.48

48 The Obama Proposal, supra note 6.
And, the President reiterates his strong opposition to the Ryan Proposals for reforming Medicaid and Medicare:

But let me be absolutely clear: I will preserve these health care programs as a promise we make to each other in this society. I will not allow Medicare to become a voucher program that leaves seniors at the mercy of the insurance industry, with a shrinking benefit to pay for rising costs. I will not tell families with children who have disabilities that they have to fend for themselves. We will reform these programs, but we will not abandon the fundamental commitment this country has kept for generations.49

Second, the President proposes cost savings reforms with both Medicaid and Medicare without fundamentally altering the benefits. He contrasts as follows his cost containment approach with the Ryan Proposal to reduce benefits:

The third step in our approach is to further reduce health care spending in our budget. Now, here, the difference with the House Republican plan could not be clearer. Their plan essentially lowers the government’s health care bills by asking seniors [Medicare recipients] and poor families [Medicaid recipients] to pay them instead. Our approach lowers the government’s health care bills by reducing the cost of health care itself.50

The President elaborates as follows on his cost cutting plan:

Already, the reforms we passed in the health care law will reduce our deficit by $1 trillion. My approach would build on these reforms. We will reduce wasteful subsidies

49 Id.
50 Id.
and erroneous payments. We will cut spending on prescription drugs by using Medicare’s purchasing power to drive greater efficiency and speed generic brands of medicine onto the market. We will work with governors of both parties to demand more efficiency and accountability from Medicaid.

We will change the way we pay for health care — not by the procedure or the number of days spent in a hospital, but with new incentives for doctors and hospitals to prevent injuries and improve results. And we will slow the growth of Medicare costs by strengthening an independent commission of doctors, nurses, medical experts and consumers who will look at all the evidence and recommend the best ways to reduce unnecessary spending while protecting access to the services that seniors need.

Now, we believe the reforms we’ve proposed to strengthen Medicare and Medicaid will enable us to keep these commitments to our citizens while saving us $500 billion by 2023, and an additional $1 trillion in the decade after that. But if we’re wrong, and Medicare costs rise faster than we expect, then this approach will give the independent commission the authority to make additional savings by further improving Medicare.\footnote{Id.}

Even if the cost of Medicare and Medicaid can be brought under control, as the President expects, there is still a sound reason for adopting the Medicare reforms proposed here because the current system is providing a large benefit to high income people who do not need it.

**B. Social Security**

Like the Deficit Commission Proposal and the Ryan Proposal, the Obama Proposal acknowledges the long-term problem with Social Security but does not make any concrete
proposals for addressing the problem, other than rejecting the privatization of Social Security. The President explains:

While Social Security is not the cause of our deficit, it faces real long-term challenges in a country that’s growing older. As I said in the State of the Union, both parties should work together now to strengthen Social Security for future generations. But we have to do it without putting at risk current retirees, or the most vulnerable, or people with disabilities; without slashing benefits for future generations; and without subjecting Americans’ guaranteed retirement income to the whims of the stock market. And it can be done.\(^{52}\)

\textbf{C. Observations}

The President acknowledges that changes must be made to preserve Medicare, Medicaid and Social Security:

Finally, there are those who believe we shouldn’t make any reforms to Medicare, Medicaid, or Social Security, out of fear that any talk of change to these programs will immediately usher in the sort of steps that the House Republicans have proposed. And I understand those fears. But I guarantee that if we don’t make any changes at all, we won’t be able to keep our commitment to a retiring generation that will live longer and will face higher health care costs than those who came before.\(^{53}\)

Although the President has acknowledged that changes are needed, he has not proposed changes to the current benefit structure of these programs. Thus, he too has “punted the ball down the field” on the entitlement issue.

\(^{52}\) Id.  
\(^{53}\) Id.
VI. Proposals for Phasing-Out Medicare and Social Security for High Income Retirees

A. Introduction to this “Phase-Out” Proposal

1. Basic Principles

The Deficit Commission Proposal, the Ryan Proposal, and the Obama Proposal all acknowledge that, in view of the aging of the American population, there are long-term funding problems with Social Security and Medicare. Although the Ryan Proposal suggests the adoption of a voucher system for Medicare, none of these proposals directly addresses the fundamental problem with entitlements under these programs.

While there is no one solution, it is proposed here that at least a partial solution to the funding problem is to “phase-out” the entitlements under these programs for high income individuals. This “phase-out” principle can be illustrated by analyzing the treatment of the following two hypothetical retirees, Joe and Bill, who are polar opposites when it comes to assets and income.

Under the phase-out proposal here, income is broadly measured and includes income excluded from gross income under the Federal income tax, such as interest on state and local bonds and income earned in tax exempt retirement accounts. It does not include a payout of principal in a retirement account. This income is referred to here as Broadly Measured Income. Joe and Bill are both retired and have the following assets and income:
Joe is a 70 year old retired bus driver, who has $500,000 in investable assets and $50,000 in annual Broadly Measured Income, including his Social Security, and

Bill is a 70 year old retired executive who has $5 million in investable assets and $250,000 in annual Broadly Measured Income, including his Social Security.

Under the phase-out proposal set out below, Joe would get his full Social Security payment and would be covered under Medicare as he presently is under current law. On the other hand, because of his financial resources, Bill would not receive any Social Security payment and would have to pay 100% of a premium covering the economic costs of his Medicare benefits if he chose to participate in Medicare. As discussed below, under the proposal here (1) the Social Security Benefit would be phased out as individuals move from $75,000 of annual Broadly Measured Income to $175,000 (the Social Security Phase-Out Requirement); and (2) to participate in Medicare, retired persons would be required to pay an increasing portion of the economic costs of a premium for Medicare benefits as they move from $75,000 of annual Broadly Measured Income to $175,000 (the Medicare Premium Payment Requirement).

If at some point in the future, Bill’s income drops below the $75,000 threshold, he would then be entitled to full participation in Medicare and Social Security. Thus, these programs would be there as safety nets for any individual who was initially not covered but because of, for example, a significant decrease in the fair market value of investable assets, his or her income drops below $75,000.

54 Investable assets do not include personal residences and other personal property. They include investments such as stocks and bonds, whether or not held in retirement accounts.
55 The “economic costs” would include the cost of benefits and administrative costs.
56 Although the Medicare Premium Payment Requirement is not labeled a phase-out, it has the economic effect of phasing out the Medicare benefit.
2. Justification for the Social Security Phase-Out Requirement

The Social Security Phase-Out Requirement is similar to the approach in Canada, which begins to reduce Social Security payments once a retiree’s income exceeds approximately $67,000 in Canadian dollars. The Social Security payment is completely eliminated at approximately $150,000 in Canadian dollars. This is a sensible approach that is consistent with the safety-net purpose of Social Security. Interestingly, this phase-out feature of the Canadian Social Security system is apparently one of the reasons Canada does not face the same long-term budgetary problems the U.S. faces. For example, an April 2011 Wall Street Journal article reports:

Canada's budget deficit for the last 11 months shrank by nearly a third . . . from the year-ago period—boosted by strong economic growth and higher commodity prices, and providing a stark foil to the current budget and debt woes south of the border.

Certainly, the Canadian budget deficit would not have shrunk as much if there were not a phase-out of Social Security payments for high income retirees.

Bill, the executive, does not need a safety net from the government, and the government should not provide him with one. He would not suffer a material adverse effect from elimination of the Social Security payment because it is a small percentage of his income and will not have a material impact on his standard of living. In fact, Bill is unlikely to spend the Social Security payment at any time during his life, and the most likely disposition of any Social Security benefit he receives will be to increase his heirs’ inheritances. This illustrates that for many high income

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retirees, the economic impact of current Social Security benefits is to increase the inheritances their heirs receive. No sensible retirement policy could support such a bizarre economic effect.

On the other hand, the Social Security payment received by Joe is a material part of his income, and his living standard likely would be adversely affected in a material way if he did not receive it. Unlike Bill, the executive, Joe is likely to spend his Social Security payment on the current needs of his family. Also, it is likely that Joe’s life expectancy will be shorter than Bill’s, and as a consequence, under the current system, Joe will get a smaller aggregate benefit from Social Security than Bill. The proposal here would eliminate much of this type of regressivity (i.e., giving the wealthy proportionately more benefits) in the current system.

3. Justification for the Medicare Premium Payment Requirement

Turning to Medicare, why should the Federal government provide free Medicare benefits to Bill just because he is older than 65? Bill can easily pay for his own medical insurance. Also, the money Bill saves as a result of receiving Medicare benefits under the current system will likely not be spent by Bill on his family; rather, such money likely will go to Bill’s heirs in the form of increased inheritances. Thus, like the Social Security benefit Bill receives under the current system, the Medicare benefits Bill currently receives are likely to merely increase the inheritances his heirs receive.

In any event, under the Medicare Premium Payment Requirement, Bill could purchase Medicare insurance if he chose to do so; however, he would have to pay the full cost of the premium. As an alternative, Bill could buy private insurance or choose not to buy any insurance and, in essence, self-insure. If it would be beneficial to the overall Medicare system for Bill to be included (because, for example, he is less likely to need benefits), then Bill could be offered a
discounted premium sufficient to induce him and similarly situated retirees to voluntarily participate in the Medicare system as contrasted with purchasing private insurance. However, the Medicare Premium Payment Requirement system proposed here does not have such an incentive.

Interestingly, the Medicare Premium Payment Requirement is similar to the Ryan Proposal for Medicare vouchers in that (1) retirees earning between $75,000 and $175,000, and who are, therefore, subject to the Medicare Premium Payment Requirement, can purchase Medicare insurance at a discount to the actual cost,\textsuperscript{59} and (2) many retirees with earnings over $175,000 would opt for private insurance rather than Medicare. However, the Medicare Premium Payment Requirement proposed here only applies to well-off retirees, whereas the Ryan Proposal’s voucher system applies to all retirees, albeit treating high-income retirees less favorably than low income retirees.

In discussing the purpose of Medicare, the Ryan Proposal explains: “In urging the creation of Medicare, President Kennedy said that such a program was chiefly needed to protect, not the poor, but people who had worked for years and suddenly found all their savings gone because of a costly health problem.”\textsuperscript{60} The phase-out of benefits under Medicare is certainly consistent with this purpose, and under the proposal here, no person otherwise eligible for Medicare would “suddenly [find] all [of his or her] savings gone because of costly health problems.” As a practical matter, any person who was not initially covered would be entitled to full coverage once his or her investable assets dropped below approximately $1 million. This can be illustrated as follows.

\textsuperscript{59} See Table B, infra.

\textsuperscript{60} The Ryan Proposal, supra, note 5, at 45, citing President John F. Kennedy. \textit{Address at a New York Rally in Support of the President’s Program of Medical Care for the Aged}. May 20, 1962.
Assuming an average 5% return (i.e., income and capital gains) on investments, under the phase-out proposed here, only individuals with more than approximately $1 million in investable assets would have to pay a portion and in some cases all of the cost of Medicare. For example, assume that a person initially had $4 million in investable assets producing $200,000 in Broadly Measured Income, before taking into account any Social Security Benefit. Because this person’s Broadly Measured Income exceeds $175,000, he or she would have to pay the full cost of participating in Medicare. Assume further that this person does not purchase Medicare or other insurance and as a result must spend his or her personal resources to address a catastrophic health issue. Once this person’s assets have dropped to approximately $1 million, which under the 5% assumption here would produce approximately $50,000 in Broadly Measured Income, he or she would qualify for full participation in Medicare without making any payment as long as the Social Security benefit, which is also included in Broadly Measured Income, did not exceed $25,000. This is because Broadly Measured Income includes the $50,000 of earnings on investable assets plus the Social Security benefit, and as long as the total is less than $75,000, there would be no phase-out. Thus, by limiting any such depletion in assets to approximately $1 million, the proposal here addresses the concern expressed by President Kennedy and highlighted in the Ryan Proposal.

**B. Proposed Phase-Out of Social Security Benefit**

Under the Social Security Phase-Out Requirement proposed here, any person otherwise eligible for Social Security who has greater than $75,000 in annual Broadly Measured Income would receive a declining portion of the Social Security benefit that would otherwise be payable, and if
the person’s annual Broadly Measured Income exceeds $175,000, no Social Security payment would be made.

Table B shows the amount that a person with more than $75,000 in annual Broadly Measured Income would receive as a Social Security benefit, under the assumption that the Social Security benefit that would otherwise be payable is $20,000.
Table B: Social Security Phase-Out Requirement for Income Levels Running from below $75,000 to above $175,000

<table>
<thead>
<tr>
<th>Broadly Measured Income</th>
<th>Percentage Decrease in Social Security Payment</th>
<th>Social Security Payment Otherwise Due</th>
<th>Actual Social Security Payment Due</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to $75,000</td>
<td>-0%</td>
<td>$20,000</td>
<td>$20,000</td>
</tr>
<tr>
<td>Over $75,000 and up to $100,000</td>
<td>20%</td>
<td>$20,000</td>
<td>$16,000</td>
</tr>
<tr>
<td>Over $100,000 and up to $125,000</td>
<td>40%</td>
<td>$20,000</td>
<td>$12,000</td>
</tr>
<tr>
<td>Over $125,000 and up to $150,000</td>
<td>60%</td>
<td>$20,000</td>
<td>$8,000</td>
</tr>
<tr>
<td>Over $150,000 and up to $175,000</td>
<td>80%</td>
<td>$20,000</td>
<td>$4,000</td>
</tr>
<tr>
<td>Over $175,000</td>
<td>100%</td>
<td>$20,000</td>
<td>-0%</td>
</tr>
</tbody>
</table>

Thus, as income rises from $75,000 to above $175,000, the Social Security payment would drop from $20,000 to zero. Some may argue that this schedule is much too generous, because, for example, an individual with $150,000 in Broadly Measured Income, which is likely to be backed
up by approximately $3 million in investable assets (i.e., 5% annual return \times \$3 \text{ million} = \$150,000), will be receiving a \$4,000 Social Security payment from the government.

C. Proposed Phase-Out of Medicare Benefits

Under the Medicare Premium Payment Requirement proposed here, any person otherwise eligible for Medicare who has greater than $75,000 in annual Broadly Measured Income would, if such person wanted to participate in Medicare, have to pay a portion, and in some cases all, of a premium covering the economic costs of the Medicare benefits. As opposed to purchasing Medicare insurance, a person making more than $75,000 in such income could decide to purchase private medical insurance or could choose to purchase no health insurance and, thereby expose his or her assets to the risk of depletion as a result of paying health care cost.

Table C shows the amount that a person with more than $75,000 in annual Broadly Measured Income would have to pay to receive Medicare benefits, under the assumption that the economic costs of a premium for such benefits is $10,000.
Table C: Medicare Premium Payment Requirement for Medicare Benefits for Income Levels Running from below $75,000 to above $175,000

<table>
<thead>
<tr>
<th>Broadly Measured Income</th>
<th>Percentage Required to Be Paid for Medicare Benefit</th>
<th>Premium Covering the Economic Costs of Medicare Benefit</th>
<th>Actual Payment Due</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to $75,000</td>
<td>-0%</td>
<td>$10,000</td>
<td>-0-</td>
</tr>
<tr>
<td>Over $75,000 and up to $100,000</td>
<td>20%</td>
<td>$10,000</td>
<td>$2,000</td>
</tr>
<tr>
<td>Over $100,000 and up to $125,000</td>
<td>40%</td>
<td>$10,000</td>
<td>$4,000</td>
</tr>
<tr>
<td>Over $125,000 and up to $150,000</td>
<td>60%</td>
<td>$10,000</td>
<td>$6,000</td>
</tr>
<tr>
<td>Over $150,000 and up to $175,000</td>
<td>80%</td>
<td>$10,000</td>
<td>$8,000</td>
</tr>
<tr>
<td>Over $175,000</td>
<td>100%</td>
<td>$10,000</td>
<td>$10,000</td>
</tr>
</tbody>
</table>

Thus, as income rises from $75,000 to above $175,000, the required payment for the $10,000 premium covering the economic costs of the Medicare benefit would increase from -0- to $10,000. Some may argue that this schedule is much too generous, because, for example, a retiree with $150,000 in Broadly Measured Income, which is likely backed up by approximately
$3 million in investable assets (i.e., 5% annual return X $3 million = $150,000), will be receiving a 20% subsidy for the purchase of Medicare insurance.

D. Phase-Out Based on Prior Year’s Income, Married Couples, Hardship Exceptions, Inflation Adjustments, and Coordination with Current Means Testing of Premiums for Medicare Part B and Part D

In general, the phase-out would be done on the basis of the person’s Broadly Measured Income in the prior year, and the Broadly Measured Income would be determined by a schedule that would be filed with the income tax return. Although the phase-out proposed here is based on gross Broadly Measured Income, it might be appropriate to compute the phase-out after allowing for certain deductions. However, it would not be appropriate, for example, to permit a deduction for mortgage interest, because that would discriminate against retirees that decided to rent or owned homes without a mortgage.

Separate phase-out tables would be developed for, inter alia, married and unmarried persons in accordance with principles governing the tax rates for such persons in the Internal Revenue Code. The administrators of Social Security and Medicare would be given authority to grant hardship relief in accordance with regulations to be adopted. The ranges of Broadly Measured Income in Tables B and C would be adjusted for inflation, and it might be appropriate to have the tables reflect differences in the cost of living between various areas of the country.

Rules would be developed for coordinating the Medicare Premium Payment Requirement with the current “means testing” of the premiums for Medicare Part B, non-hospitalization coverage,61

and Part D, prescription coverage. Under the current means testing of these programs, high
income retirees are required to pay more for benefits than low income retirees. The phase-out
proposed here provides for a much greater degree of means testing for all Medicare benefits.

E. Effective Date and Transition

Implementation of this phase-out proposal should be effectuated on a delayed basis so as not to
significantly interfere with the reasonable expectations of those planning for retirement. The
Ryan Proposal for changes in Medicare would only apply to individuals 55 and younger, and that
may be a good starting point for implementing this proposal. However, for individuals with very
high levels of income (e.g., above $250,000), the proposal could be phased in sooner.

F. Budgetary Impact

As indicated, the phase-out of Social Security and Medicare has not been addressed by the CBO
or any of the three budget proposals discussed here. However, as discussed above, an analysis
by the Center for Economic and Policy Research indicates that with a phase-out like the one
proposed here, which effectively begins at approximately $50,000 of non-Social Security income
(i.e., $75,000 of Broadly Measured Income including Social Security), the revenue savings
would be less than 10% of the overall cost of Social Security. In any event, it could be
expected that the adoption of the proposals made here would significantly reduce the costs of
Medicare and Social Security and make a significant contribution to putting those programs on a
sustainable basis. This is particularly the case in view of the fact that the high income retirees
who will not be receiving benefits, or will be receiving reduced benefits, under the proposals

62 See generally Richard L. Kaplan, Analyzing the Impact of the New Health Care Reform Legislation on Older
here are also likely to live longer than lower income retirees. Therefore, under the current system, these high income retirees would likely receive benefit payments under Social Security and Medicare for longer periods than lower income retirees. To be clear, however, adoption of these proposed phase-outs will not be the “silver bullet” that eliminates the long term funding problem with Social Security and Medicare.64 Even with the adoption of these proposals, efforts should continue to be made to enhance the operational performance and effectiveness of these programs.

VII. The Political Issue: The Likely Response of Many High-Income Retirees to the Phase-Out

Of course, many high-income retirees, like Bill, the retired executive discussed above, will likely argue that since they have paid into Social Security and Medicare, they should be entitled to receive full Social Security and Medicare benefits. The answer is simple: yes, you will be entitled to full Social Security and Medicare benefits if your income ever drops below $75,000 and partial benefits if your income is ever between $75,000 and $175,000. But, as long as your income is higher than $175,000 you cannot participate in these programs, which, after all, have a safety net purpose and are not defined contribution plans where you get back what you put in.65

Further, without these and other changes, the current level of Social Security and Medicare taxes and benefits is unsustainable. As indicated in the S&P report discussed above, the Social

64 Id.
Security, Medicare, and Medicaid “entitlements already account for almost half of federal spending . . . , and [the] percentage [will] continue increasing as long as these entitlement programs remain as they currently exist . . . .” 66 (emphasis added) Thus, under the proposal here, Bill and other future well-off retirees will be subject to limited or no participation in Social Security and Medicare, unless as a result of falling on hard times, their investable assets are depleted to about $1 million, which could be expected to produce approximately $50,000 in income before taking into account Social Security.

Adoption of this proposal will likely erode some of the political support for Social Security and Medicare from high income retirees and those who expect to become high income retirees. Also, the phase outs proposed here will likely be opposed by left leaning Democrats and right leaning Republicans for the same reasons these polar opposite political groups opposed means testing of the premiums for Medicare Part B, the non-hospitalization benefit.

With respect to the Democratic opposition, Professor Kaplan explains:

Democrats in the House opposed means testing Medicare because they thought that such a concept was contrary to the social insurance role that they wanted Medicare to play. Democrats wanted everyone to be in the Medicare risk pool and wanted the program’s benefits to be shared as broadly as possible. This approach was undoubtedly a reaction, in part, to what had happened the year before when the Personal Responsibility and Work Opportunity Reconciliation Act (better known as welfare reform) was passed. That is, House Democrats opposed means-testing Medicare Part B because they were concerned that if Medicare Part B began to take on certain characteristics of a welfare program—

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e.g., fewer benefits (or higher costs) for persons with greater income—then Medicare might become vulnerable to the sort of attack that federal welfare programs had endured the previous year.67

The reasoning behind this opposition by some Democrats seems to me to be the equivalent of a decision to bribe high income individuals into supporting Medicare. The proposal here does not bribe high income individuals; rather, the proposal directly states that high income individuals will receive Social Security and Medicare only if they need them in the future. This is part of the costs they must bear to ensure that Social Security and Medicare are there for those who need it.

With respect to the Republican opposition, Professor Kaplan explains:

House Republicans believed that calibrating Medicare Part B premiums according to income was a back-door tax on retirees who had worked and invested conscientiously throughout their working lives. In other words, means-testing Medicare was just one more penalty on effort or a “success tax” in their view. Accordingly, House Republicans opposed means-testing Medicare Part B to avoid imposing a stealth tax on upper-income retirees.68

High income individuals are not the only ones who “work and invest conscientiously.” The well-off in this country do not have a monopoly on hard work. Indeed it is commonly understood that many, if not most, high income individuals have benefited from “head-starts” provided by their parents. Thus, this belief by some House Republicans that the well-off in this country somehow “picked themselves by their boot straps,” should be challenged for what it is, a myth.

67 Kaplan, Means--Testing Medicare Part B, supra note 61, at 34.
68 Id.
Notwithstanding the likely left and right opposition to the phase-out proposal here, if politicians from across the political spectrum are truly concerned with long-term debt, then in the interest of retaining the current benefit structures of Social Security and Medicare for those retired Americans who are in need of them, these debt-concerned politicians should coalesce around this, or a similar, proposal.

The discussions that could lead to this type of coalescence could be beginning. For example, an article published by MSNBC in April 2011 states: “Calling Social Security ‘broken,’ three Republican senators unveiled a plan . . . to overhaul the 75-year old entitlement program by raising the retirement age and reducing benefits for some wealthier Americans.” (emphasis added) Under this proposal, “seniors making over $43,000 a year would have their monthly benefits reduced by $300 to $400 by 2032.” It is noteworthy that the means-testing in the Senator’s plan would (1) begin at a much lower threshold ($43,000) than the threshold for the means-test proposed here ($75,000), and (2) would only cut back, and not phase-out benefits, which is proposed here.

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70 Id.
VIII. Conclusion

The Deficit Commission Proposal, the Ryan Proposal, and the Obama Proposal do not effectively address the long-term problem with the funding of Social Security and Medicare. As a tool for limiting the costs of these two entitlements and thereby helping to put these programs on a sustainable basis without reducing the effectiveness of their “safety net” function, Congress should phase-out the benefits under these programs for high income retirees. Under the phase-outs proposed here:

(1) the Social Security benefit would be phased out as individuals move from $75,000 of annual Broadly Measured Income to $175,000 (Social Security Phase-Out Requirement), and

(2) to participate in Medicare, retired persons would be required to pay an increasing portion of the premium covering the economic costs of Medicare benefits as they move from $75,000 of annual Broadly Measured Income to $175,000 (Medicare Premium Payment Requirement).

Similar to the effective date of the Ryan Proposal, these provisions in general would only apply to people who are 55 years old or younger.

Both of these changes are sensible and will not undermine the safety net function of these programs. The Social Security Phase-Out Requirement is similar to the phase-out for such payments under Canadian law, which is apparently one of the reasons Canada’s debt problem is not as significant as ours. The Medicare Premium Payment Requirement is structured so that
even a high income person who elected to be self-insured would not see all of his or her assets completely depleted as a result of the cost of health care. Thus, the Medicare structure proposed here addresses President Kennedy’s argument, also advanced in the Ryan Proposal, that Medicare should be adopted because it would prevent “people who had worked for years [from] suddenly [finding] all their savings gone because of a costly health problem.”71

The future retirees who will be subject to the Social Security Phase-Out Requirement and the Medicare Premium Payment Requirement will lose benefits they would otherwise have received. However, as the Deficit Commission Proposal, the Ryan Proposal, and the Obama Proposal acknowledge, the system cannot continue as it is currently structured. Consequently, as a practical matter, benefits will have to be significantly cut back, or taxes will have to be significantly raised. The phase-out proposal advanced here significantly cuts benefits, but only for those future retirees who will not suffer a material financial hardship as a result of a reduction or elimination of their Social Security and Medicare benefits.

As a practical matter, adoption of the proposal here will, in most cases, simply mean that the heirs of the affected high income retirees will get smaller inheritances, because under the current system, the Social Security and Medicare benefits received by these high income retirees do not generally result in higher spending. Rather, in many instances, the benefits merely increase the assets passed on to their heirs. Politicians of all political persuasions should have the courage to bring his government funding of inheritances to an end, thereby reducing the adverse impact these programs have on long-term debt.

71 The Ryan Proposal, supra, note 5, at 45, citing President John F. Kennedy. Address at a New York Rally in Support of the President’s Program of Medical Care for the Aged. May 20, 1962.
One final point: I believe the overwhelming majority of Americans agree with me that it is economic folly for the Federal government to be providing to Warren Buffet, one of the richest people in the world, Social Security and Medicare benefits. If this is so, then for these Americans, the adoption of a phase-out along the lines proposed here is just a matter of line-drawing. This proposal draws the line at $75,000 for beginning the phase-outs. Some will argue that this is too high; others will argue that this is too low. Americans need to have an honest discussion of where to draw the line.