

UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE

FISCAL AND HEALTH CARE CHALLENGES

**The Honorable David M. Walker
Comptroller General of the United
States**

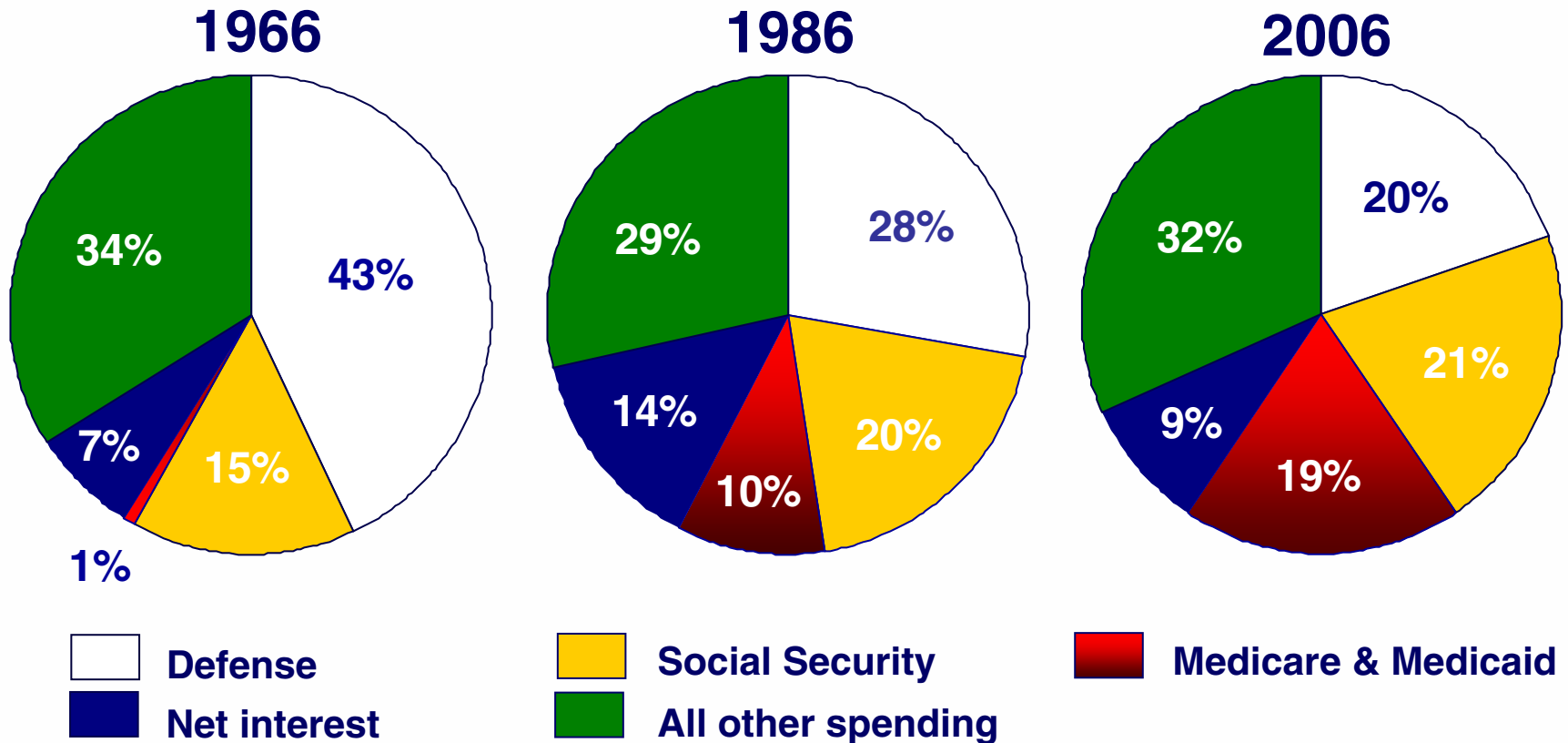
Federation of American Hospitals
Annual Public Policy Conference

March 5, 2007

GAO revised this document on March 13, 2007, to clarify that the 2006 figures are final and not preliminary (slide 2) and that note "a" relates to the unified deficit and not to the on-budget deficit (slide 3).



Composition of Federal Spending



Sources: Office of Management and Budget and the Department of the Treasury.

Note: Numbers may not add to 100 percent due to rounding.

Fiscal Year 2005 and 2006 Deficits and Net Operating Costs

	Fiscal Year 2005	Fiscal Year 2006
	(\$ Billion)	
On-Budget Deficit^a	(494)	(434)
Unified Deficit	(318)	(248)
Net Operating Cost^b	(760)	(450)

Sources: The Office of Management and Budget and the Department of the Treasury.

^aIncludes \$173 billion in Social Security surpluses for fiscal year 2005 and \$185 billion for fiscal year 2006; \$2 billion in Postal Service surpluses for fiscal year 2005 and \$1 billion for fiscal year 2006.

^bFiscal year 2005 and 2006 net operating cost figures reflect significant but opposite changes in certain actuarial costs. For example, changes in interest rates and other assumptions used to estimate future veterans' compensation benefits increased net operating cost by \$228 billion in 2005 and reduced net operating cost by \$167 billion in 2006. Therefore, the net operating costs for fiscal 2005 and 2006, exclusive of one-time actuarial gains, were (\$532) billion and (\$617) billion, respectively.

Major Fiscal Exposures

(\$ trillions)

	2000	2006	% Increase
• Explicit liabilities	\$6.9	\$10.4	52
<ul style="list-style-type: none"> • Publicly held debt • Military & civilian pensions & retiree health • Other 			
• Commitments & contingencies	0.5	1.3	140
<ul style="list-style-type: none"> • E.g., PBGC, undelivered orders 			
• Implicit exposures	13.0	38.8	197
• Future Social Security benefits	3.8	6.4	
• Future Medicare Part A benefits	2.7	11.3	
• Future Medicare Part B benefits	6.5	13.1	
• Future Medicare Part D benefits	--	7.9	
Total	\$20.4	\$50.5	147

Source: 2000 and 2006 Financial Report of the United States Government.

Note: Totals and percent increases may not add due to rounding. Estimates for Social Security and Medicare are at present value as of January 1 of each year and all other data are as of September 30.

How Big is Our Growing Fiscal Burden?

This fiscal burden can be translated and compared as follows:

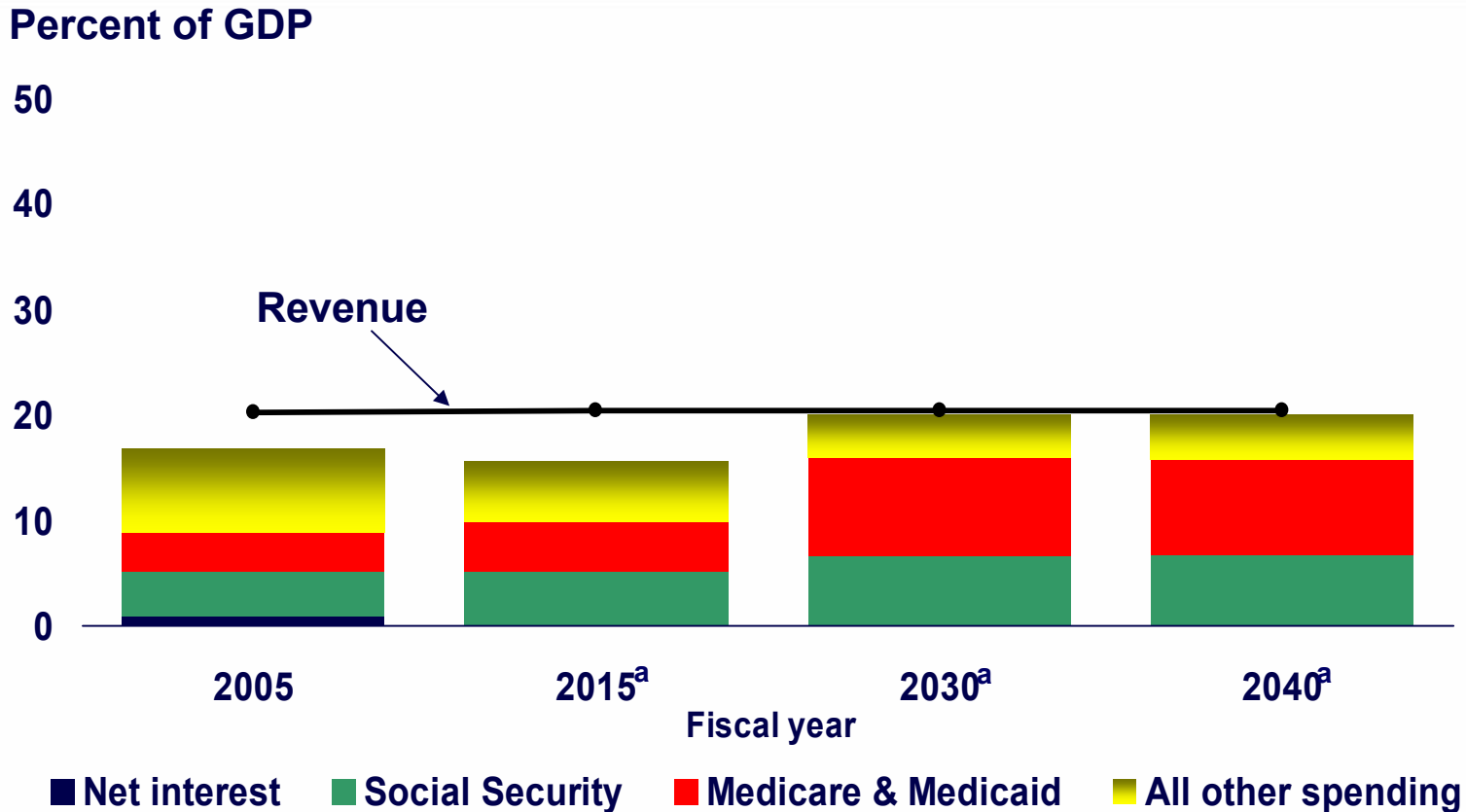
Total –major fiscal exposures	\$50.5 trillion
Total household net worth¹	\$53.3 trillion
Burden/Net worth ratio	95 percent
Burden²	
Per person	\$170,000
Per full-time worker	\$400,000
Per household	\$440,000
Income	
Median household income³	\$46,326
Disposable personal income per capita⁴	\$31,519

Source: GAO analysis.

Notes: (1) Federal Reserve Board, Flow of Funds Accounts, Table B.100, 2006:Q2 (Sept. 19, 2006); (2) Burdens are calculated using estimated total U.S. population as of 9/30/06, from the U.S. Census Bureau; full-time workers reported by the Bureau of Economic Analysis, in NIPA table 6.5D (Aug. 2, 2006); and households reported by the U.S. Census Bureau, in [Income, Poverty, and Health Insurance Coverage in the United States: 2005](#) (Aug. 2006); (3) U.S. Census Bureau, [Income, Poverty, and Health Insurance Coverage in the United States: 2005](#) (Aug. 2006); and (4) Bureau of Economic Analysis, [Personal Income and Outlays: October 2006](#), table 2, (Nov. 30, 2006).

Potential Fiscal Outcomes Under Baseline Extended (January 2001)

Revenues and Composition of Spending as a Share of GDP



Source: GAO's January 2001 analysis.

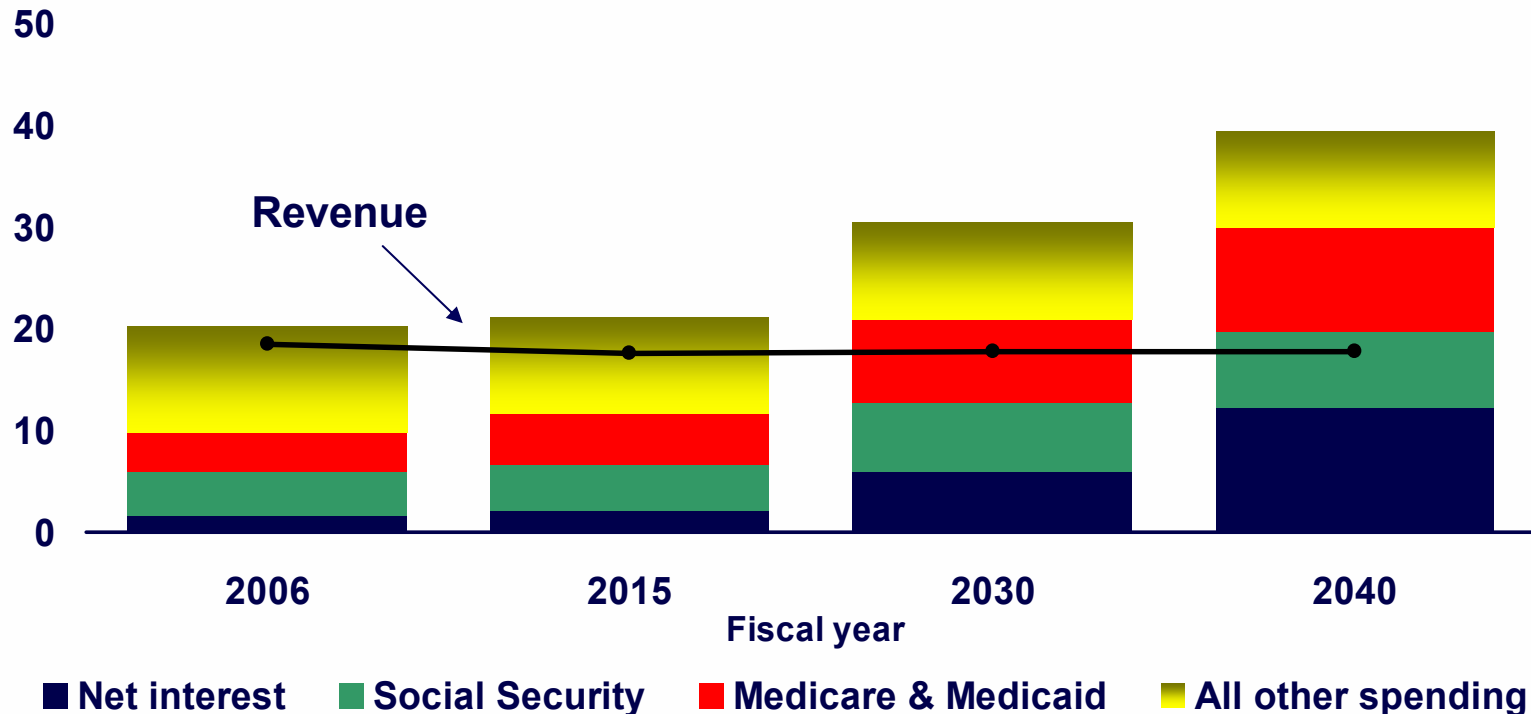
Notes: Revenue as a share of GDP increases through 2011 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2011, revenue as a share of GDP is held constant—implicitly assuming action to offset the increased revenue from real bracket creep, the AMT, and tax-deferred retirement accounts.

^aAll other spending is net of offsetting interest receipts.

Potential Fiscal Outcomes

Alternative Simulation—Discretionary Spending Grows with GDP and Expiring Tax Provisions Extended (January 2007)
Revenues and Composition of Spending as a Share of GDP

Percent of GDP

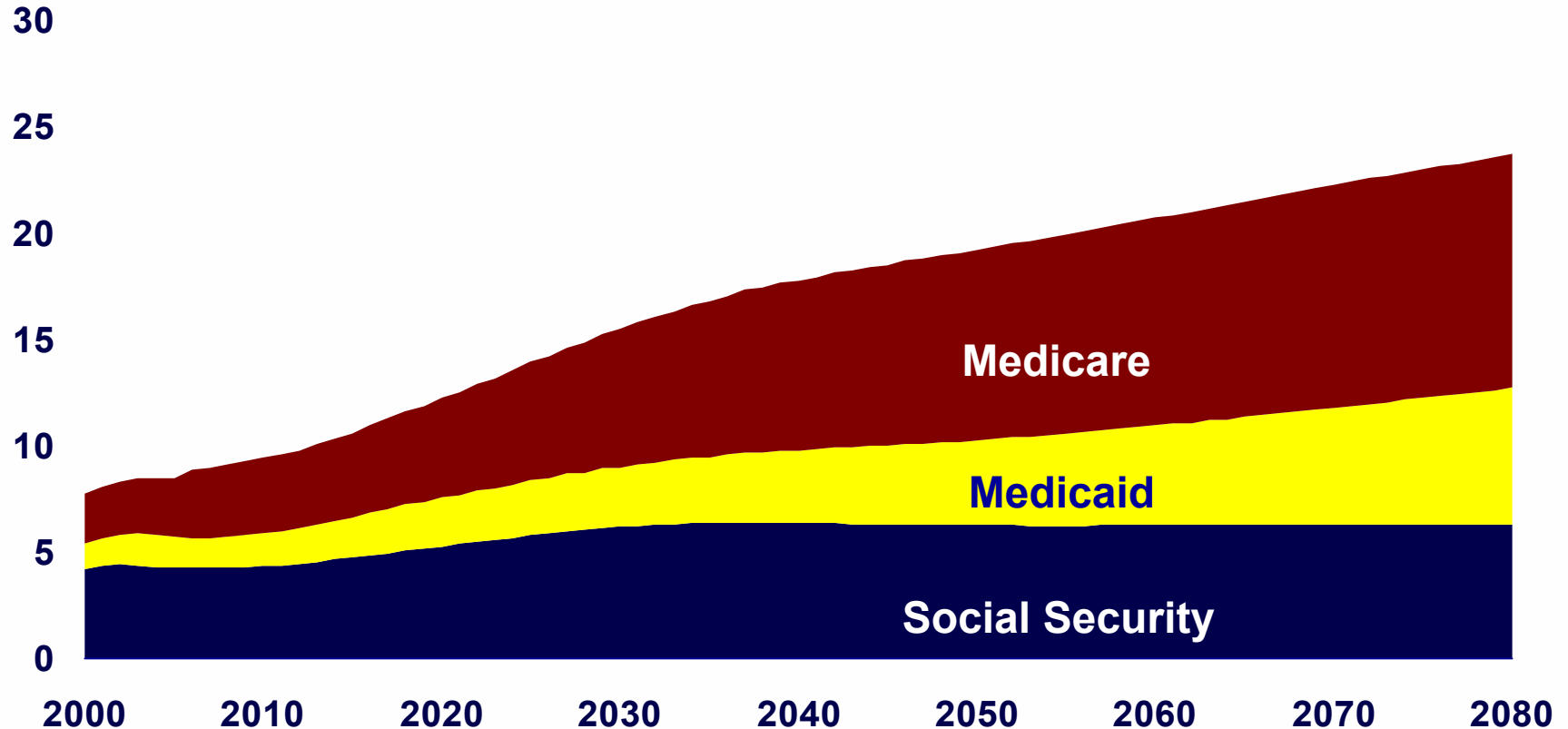


Source: GAO's January 2007 analysis.

Notes: AMT exemption amount is retained at the 2006 level through 2017 and expiring tax provisions are extended. After 2017, revenue as a share of GDP is held constant—implicitly assuming that action is taken to offset increased revenue from real bracket creep, the AMT, and tax-deferred retirement accounts.

Social Security, Medicare, and Medicaid Spending as a Percent of GDP

Percent of GDP

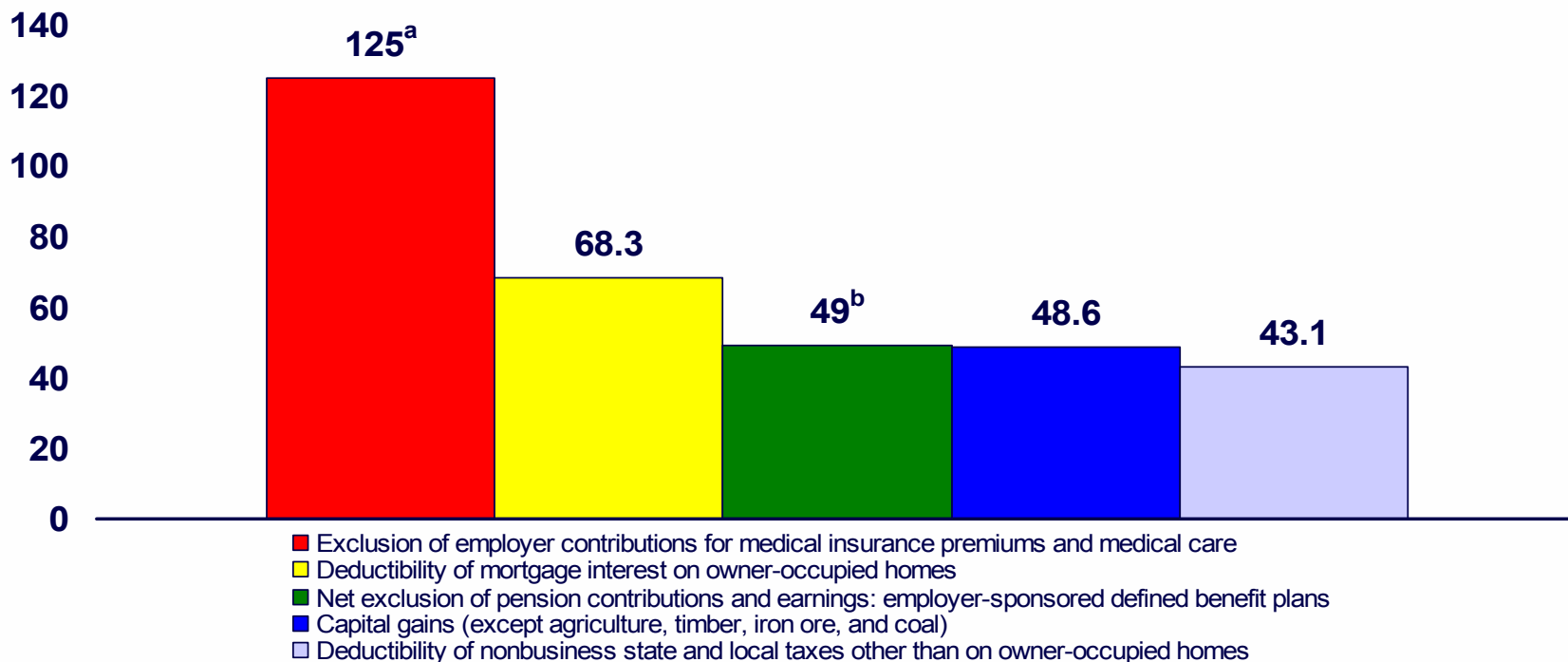


Sources: GAO analysis based on data from the Office of the Chief Actuary, Social Security Administration, Office of the Actuary, Centers for Medicare and Medicaid Services, and the Congressional Budget Office.

Notes: Social Security and Medicare projections based on the intermediate assumptions of the 2006 Trustees' Reports. Medicaid projections based on CBO's August 2006 short-term Medicaid estimates and CBO's December 2005 long-term Medicaid projections under mid-range assumptions.

Health Care Is the Nation's Top Tax Expenditure in Fiscal Year 2006

Estimated dollars in billions



Source: Office of Management and Budget (OMB), *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2008*.

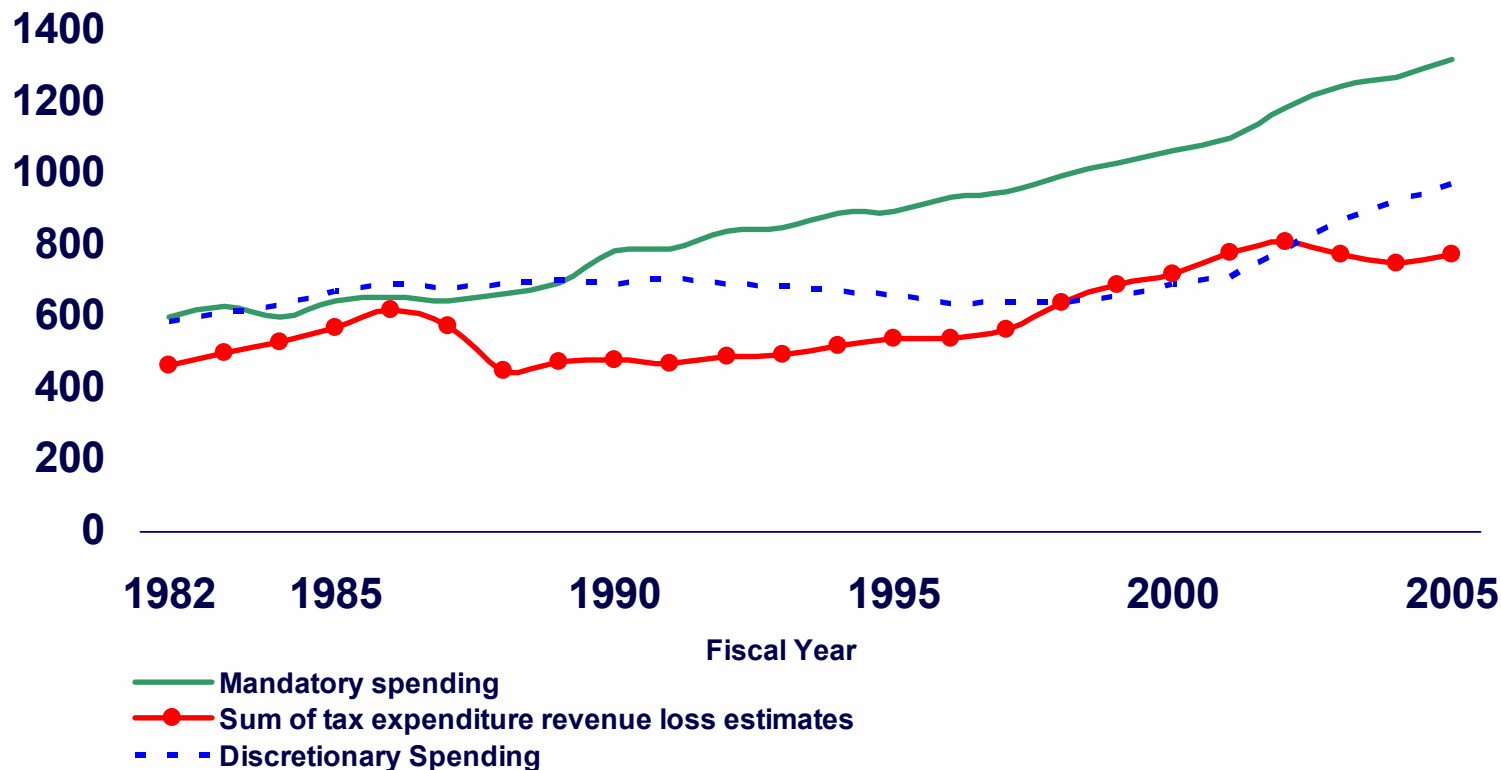
Note: "Tax expenditures" refers to the special tax provisions that are contained in the federal income taxes on individuals and corporations. Treasury does not include forgone revenue from other federal taxes such as Social Security and Medicare payroll taxes.

^aIf the payroll tax exclusion were also counted here, the total tax expenditure for employer contributions for health insurance premiums would be about 50 percent higher or \$187.5 billion.

^bThis tax expenditure does not include \$40.8 billion in revenue losses due to defined contribution plans.

Federal Tax Expenditures Exceeded Discretionary Spending for Half of the Last Decade

Dollars in billions (in real 2005 dollars)



Source: GAO analysis of OMB budget reports on tax expenditures, fiscal years 1976-2007.

Note: Summing tax expenditure estimates does not take into account interactions between individual provisions. Outlays associated with refundable tax credits are included in mandatory spending.

Current Fiscal Policy Is Unsustainable

- **The “Status Quo” is Not an Option**

- We face large and growing structural deficits largely due to known demographic trends and rising health care costs.
- GAO’s simulations show that balancing the budget in 2040 could require actions as large as
 - Cutting total federal spending by 60 percent or
 - Raising federal taxes to 2 times today's level

- **Faster Economic Growth Can Help, but It Cannot Solve the Problem**

- Closing the current long-term fiscal gap based on reasonable assumptions would require real average annual economic growth in the double digit range every year for the next 75 years.
- During the 1990s, the economy grew at an average 3.2 percent per year.
- As a result, we cannot simply grow our way out of this problem. Tough choices will be required.

The Way Forward: A Three-Pronged Approach

1. Improve Financial Reporting, Public Education, and Performance Metrics
2. Strengthen Budget and Legislative Processes and Controls
3. Fundamental Reexamination & Transformation for the 21st Century (i.e., entitlement programs, other spending, and tax policy)

*Solutions Require Active Involvement from
both the Executive and Legislative Branches*

The Way Forward:

Improve Financial Reporting, Public Education, and Performance Metrics

- Improve transparency & completeness of President's budget proposal:
 - Return to 10-year estimates in budget both for current policies and programs and for policy proposals
 - Include in the budget estimates of long-term cost of policy proposals & impact on total fiscal exposures.
 - Improve transparency of tax expenditures
- Consider requiring President's budget to specify & explain a fiscal goal and a path to that goal within 10-year window--or justify an alternative deadline
- Require annual OMB report on existing fiscal exposures [liabilities, obligations, explicit & implied commitments]
- Require enhanced financial statement presentation and preparation of summary annual report that is both useful and used
- Increase information on long-range fiscal sustainability issues in Congressional Budget Resolution & Budget Process.
- Develop key national (outcome-based) indicators (e.g. economic, security, social, environmental) to chart the nation's posture, progress, and position relative to the other major industrial countries

The Way Forward: Strengthen Budget and Legislative Processes and Controls

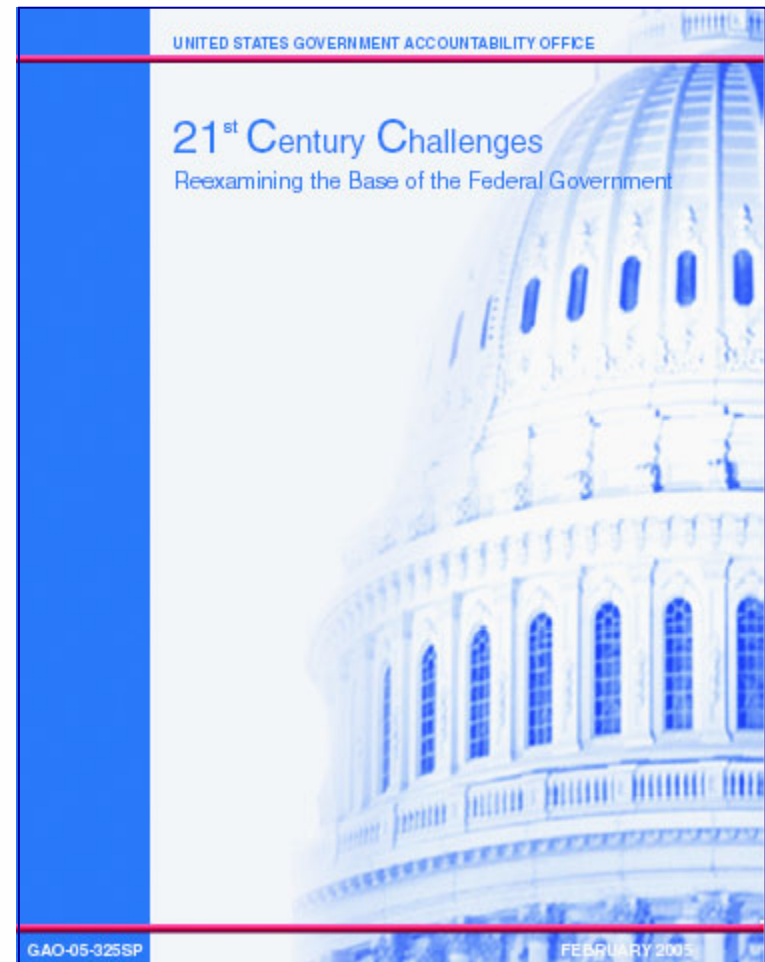
- Restore discretionary spending caps & PAYGO rules on both spending and tax sides of the ledger
- Develop mandatory spending triggers [with specific defaults], and other action-forcing provisions (e.g., sunsets) for both direct spending programs and tax preferences
- Develop, impose & enforce modified rules for selected items (e.g., earmarks, emergency designations, and use of supplementals)
- Require long-term cost estimates (e.g. present value) for any legislative debate on all major tax and spending bills, including entitlement programs. Cost estimates should usually assume no sunset
- Extend accrual budgeting to insurance & federal employee pensions; develop techniques for extending to retiree health & environmental liabilities
- Consider biennial budgeting
- Consider expedited line item rescissions from the President that would only require a majority vote to override the proposed rescission(s)

The Way Forward: Fundamental Reexamination & Transformation

- Restructure existing entitlement programs
- Reexamine and restructure the base of all other spending
- Review & revise existing tax policy, including tax preferences and enforcement programs
- Expand scrutiny of all proposed new programs, policies, or activities
- Reengineer internal agency structures and processes, including more emphasis on long-term planning, integrating federal activities, and partnering with others both domestically and internationally
- Strengthen and systematize Congressional oversight processes
- Increase transparency associated with government contracts and other selected items
- Consider a capable, credible, bi-partisan entitlement and tax reform commission along the lines proposed by Sen. Voinovich and Cong. Wolf

21st Century Challenges Report

- Provides background, framework, and questions to assist in reexamining the base
- Covers entitlements & other mandatory spending, discretionary spending, and tax policies and programs
- Based on GAO's work for the Congress



Source: GAO.

Twelve Reexamination Areas

MISSION AREAS

- Defense
- Education & Employment
- Financial Regulation & Housing
- Health Care
- Homeland Security
- International Affairs
- Natural Resources, Energy & Environment
- Retirement & Disability
- Science & Technology
- Transportation

CROSSCUTTING AREAS

- Improving Governance
- Reexamining the Tax System

Illustrative 21st Century Questions: Health Care

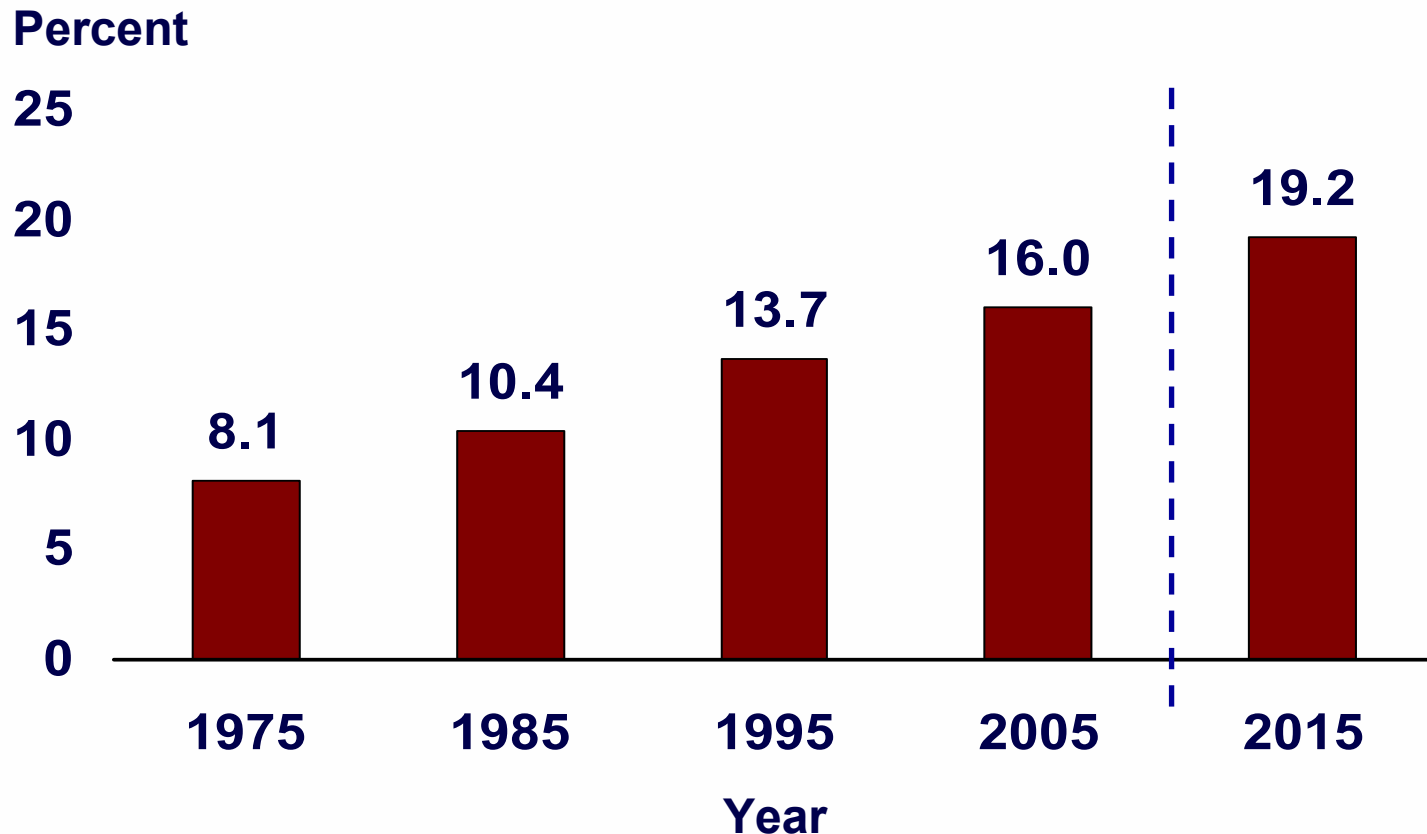
- How can we make our current **Medicare and Medicaid** programs sustainable? For example, should the eligibility requirements (e.g., age, income requirements) for these programs be modified?
- How can we perform a **systematic reexamination of our current health care system**? For example, could public and private entities work jointly to establish formal reexamination processes that would (1) define and update as needed a minimum core of essential health care services, (2) ensure that all Americans have access to the defined minimum core services, (3) allocate responsibility for financing these services among such entities as government, employers, and individuals, and (4) provide the opportunity for individuals to obtain additional services at their discretion and cost?

Key Dates Highlight Long Term Challenges of the Medicare Program

Date	Event
2006	Medicare Part A outlays exceed cash income
2007	Estimated trigger date for “Medicare funding warning”
2012	Projected date that annual “general revenue funding” for Part B will exceed 45 percent of total Medicare outlays
2018	Part A trust fund exhausted, annual income sufficient to pay about 80% of promised Part A benefits

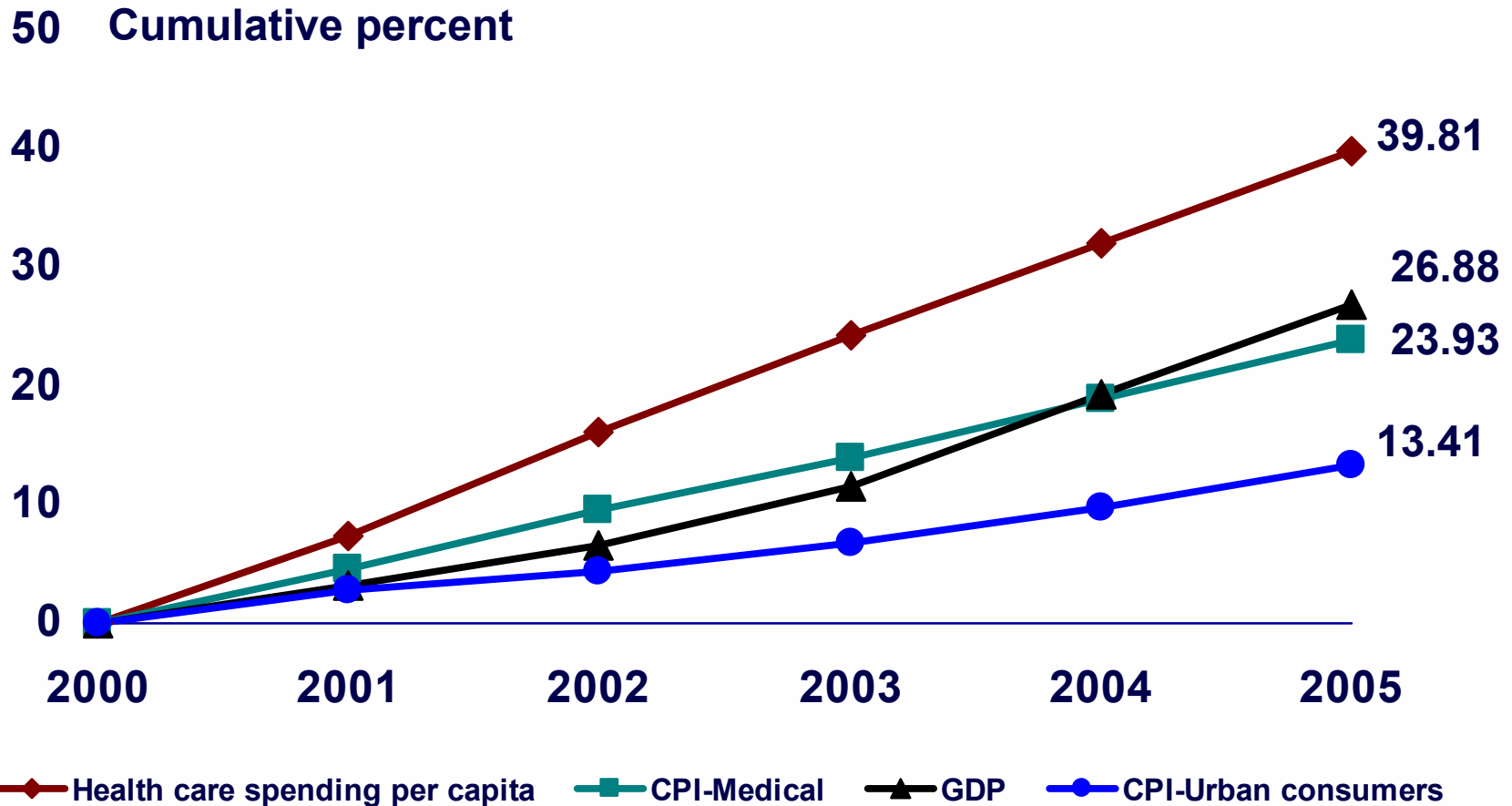
Source: 2006 Annual Report of The Boards of Trustees of The Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds (Washington, DC, May 2006).

Growth in Health Care Spending: Health Care Spending as a Percentage of GDP



Source: The Centers for Medicare & Medicaid Services, Office of the Actuary.
Note: The figure for 2015 is projected.

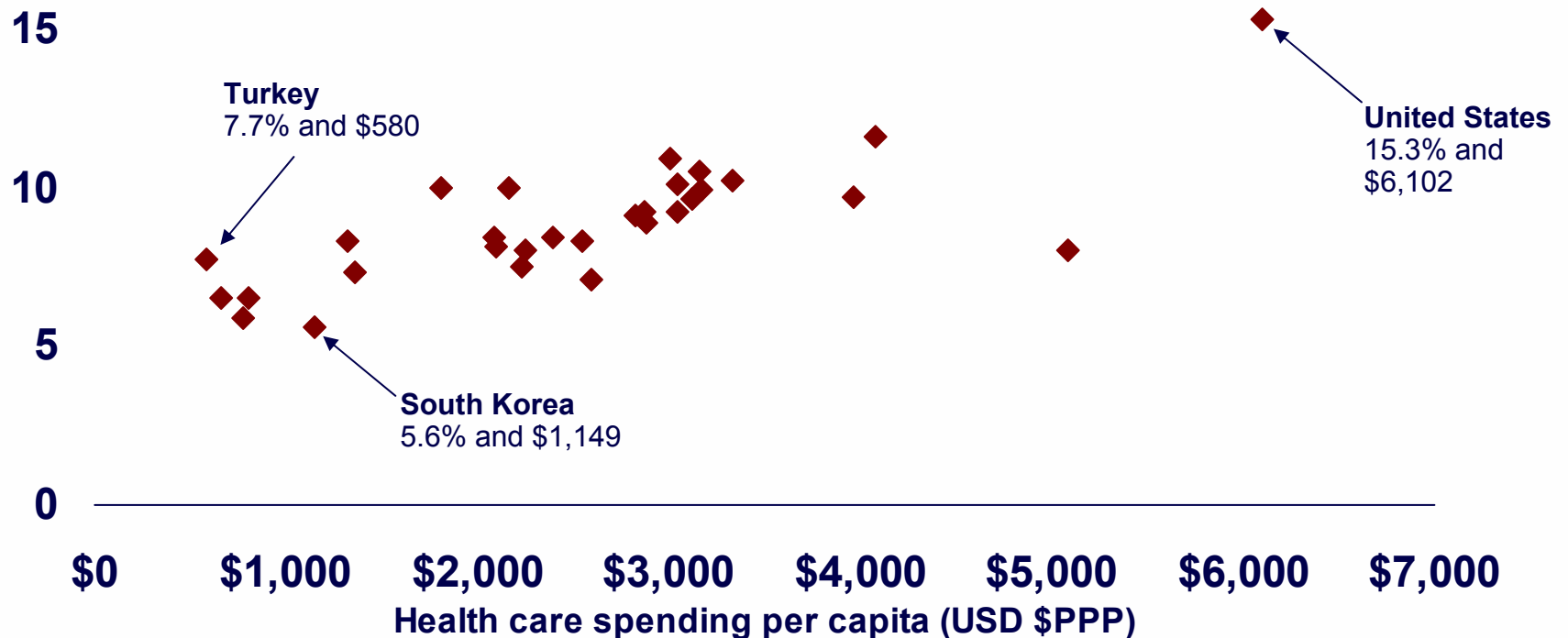
Growth in Health Care Spending: Cumulative Growth in Health Care Spending Per Capita, Medical Inflation, GDP, and General Inflation, 2000-2005



Source: Bureau of Labor Statistics, The Centers for Medicare & Medicaid Services, Office of the Actuary, and the Bureau of Economic Analysis.

Growth in Health Care Spending: U.S Compared to Other OECD Countries, 2004

20 Percent of GDP spent on health care

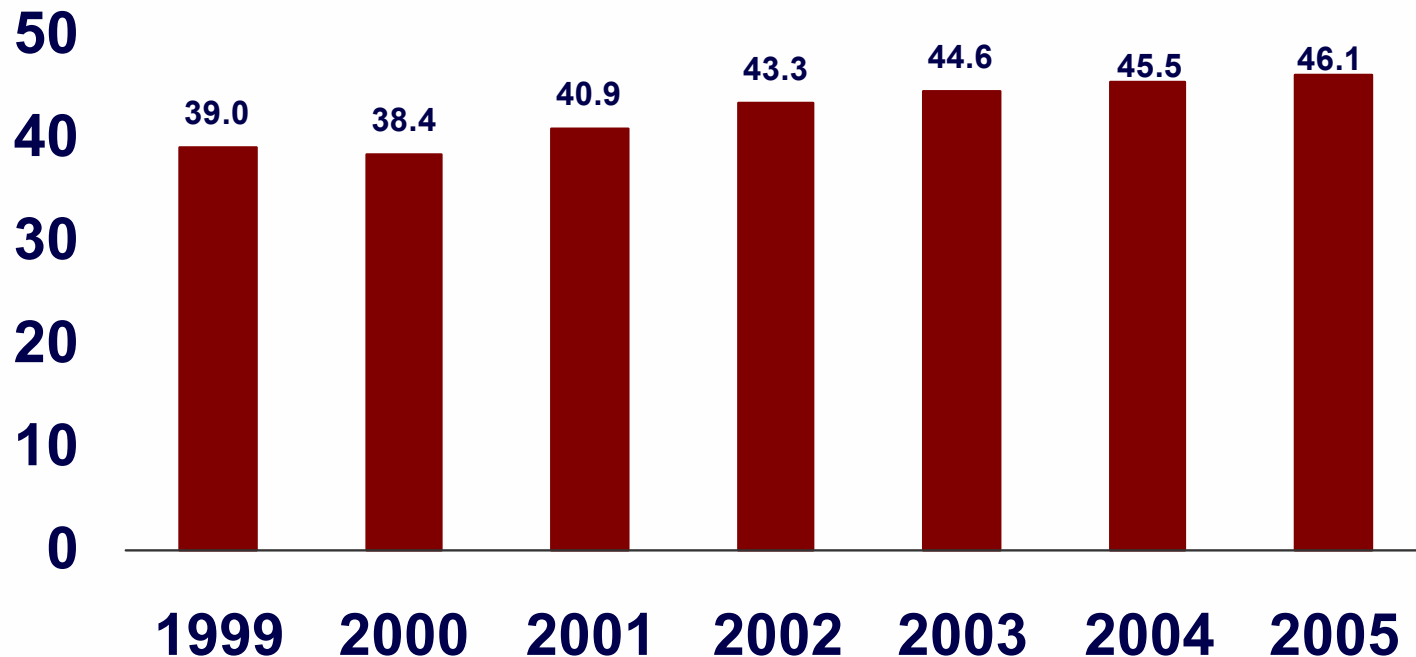


Source: *OECD Health Data, 2006*

Notes: All of the data on per capita spending and GDP have been translated into U.S. dollar equivalents, with exchange rates based on purchasing power parities (PPPs) of the national currencies

Number of Non-elderly Uninsured Americans, 1999-2005

Population in millions



Sources: GAO and Urban Institute and Kaiser Commission on Medicaid and the Uninsured analyses.

Notes: Figures for 1999-2000 are from Urban Institute and Kaiser Commission on Medicaid and the Uninsured. The figures for 2001-2005 are from GAO analyses of the Bureau of the Labor Statistics and the Bureau of the Census Current Population Survey, Annual Social and Economic Supplement.

Where the United States Ranks on Selected Health Outcome Indicators

Outcome	Rank
Life expectancy at birth <i>U.S. = 77.5 years in 2003</i>	23 out of 30 in 2003
Infant Mortality <i>U.S. = 6.9 deaths in 2003</i>	25 out of 30 in 2003
Potential Years of Life Lost <i>U.S. = 5,066 in 2002</i>	23 out of 26 in 2002

Source: OECD Health Data 2006.

Notes: Data are the most recent available for all countries. Life expectancy at birth for the total population is estimated by the OECD Secretariat for all countries, as the unweighted average of the life expectancy of men and women. Infant mortality is measured as the number of deaths per 1,000 live births. Potential years of life lost (PYLL) is the sum of the years of life lost prior to age 70, given current age-specific death rates (e.g., a death at 5 years of age is counted as 65 years of PYLL).

The Administration's Health Care Reform Proposals

Reduce the tax preference for employer-sponsored coverage

- Replace the current exclusion for employer-provided health insurance with a new standard deduction for health insurance of \$15,000 for families (\$7,500 for singles). (Deduction applies to insurance purchased individually or provided by an employer. Employees are required to include the value of employer-provided health coverage in their gross income)

Slow the annual growth in Medicare spending over 10 years from 7.4% to 6.7%

- Reduce provider payments and allow scheduled physician fee reductions to occur
- Automatically reduce reimbursements by 0.4 percent when general revenue funding for Medicare exceeds 45 percent

Increase Medicare revenues through expansion of income-related premiums

- Eliminate annual inflation adjustments to income thresholds governing Part B premium levels
- Implement income-based premium for prescription drug benefit

Slow the annual growth in Medicaid spending over 10 years from 7.7% to 7.6%

- Limit Medicaid matching rates for administrative costs to 50 percent
- Reduce Medicaid reimbursements to government providers
- Eliminate certain reimbursements for school-based services
- Revise coverage of rehabilitation services
- Eliminate reimbursements for graduate medical education

Reauthorize SCHIP for 5 years

- Maintain current enrollment levels for targeted low income children
- Refocus the program on low-income, uninsured children below 200 percent of Federal poverty level
- Target SCHIP funds to states with most need

Examples of Other Recent Health Care Reform Proposals

Sponsor	Reform Proposal or Strategy
Senator Susan Collins	Access to Affordable Health Care Act
Senator Ron Wyden	Healthy Americans Act
Senator Voinovich, Senator Bingaman, and Representative Baldwin	Health Partnership Act
Health Coverage Coalition for the Uninsured	Kids 1 st Initiative, state innovation, other reforms
New America Foundation	Fully portable health insurance for all Americans
Newt Gingrich	21 st Century Intelligent Health System
America's Health Insurance Plans	A Vision for Reform
Federation of American Hospitals	Health Coverage Passport

Issues to Consider in Examining Our Health Care System

- The public needs to be educated about the differences between **wants, needs, affordability, and sustainability** at both the individual and aggregate level
- Ideally, health care reform proposals will:
 - **Align Incentives** for providers and consumers to make prudent decisions about the use of medical services,
 - **Foster Transparency** with respect to the value and costs of care, and
 - **Ensure Accountability** from insurers and providers to meet standards for appropriate use and quality.
- Ultimately, we need to address four key dimensions: **access, cost, quality, and personal responsibility**

Selected Potential Health Care Reform Approaches

Reform Approach	Short-term action	Long-term action
Revise the government's payment systems and leverage its purchasing authority to foster value-based purchasing for health care products and services	✓	
Consider additional flexibility for states to serve as models for possible health care reforms	✓	
Consider limiting direct advertising and allowing limited importation of prescription drugs	✓	
Foster more transparency in connection with health care costs and outcomes	✓	
Create incentives that encourage physicians to utilize prescription drugs and other health care products and services economically and efficiently	✓	
Foster the use of information technology to increase consistency, transparency, and accountability in health care	✓	
Encourage case management approaches for people with chronic and expensive conditions to improve the quality and efficiency of care delivered and avoid inappropriate care	✓	
Reexamine the design and operational structure of the nation's health care entitlement programs—Medicare and Medicaid, including exploring more income-related approaches	✓	✓

Selected Potential Health Care Reform Approaches

Reform Approach	Short-term action	Long-term action
Revise certain federal tax preferences for health care to encourage more efficient use of health care products and services.	✓	✓
Foster more preventative care and wellness services and capabilities, including fighting obesity and encouraging better nutrition	✓	✓
Promote more personal responsibility in connection with health care	✓	✓
Limit spending growth for government-sponsored health care programs (e.g., percentage of the budget and/or economy)		✓
Develop a core set of basic and essential services. Create insurance pools for alternative levels of coverage, as necessary		✓
Develop a set of evidence-based national practice standards to help avoid unnecessary care, improve outcomes, and reduce litigation		✓
Pursue multinational approaches to investing in health care R&D		✓

Four National Deficits

- *Budget*
- *Balance of Payments*
- *Savings*
- *Leadership*

Key Leadership Attributes Needed for These Challenging and Changing Times

- ***Courage***
- ***Integrity***
- ***Creativity***
- ***Stewardship***

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Web site: www.gao.gov/cghome.htm

Contact

Paul Anderson, Managing Director, Public Affairs
AndersonP1@gao.gov (202) 512-4800
U.S. Government Accountability Office
441 G Street NW, Room 7149
Washington, D.C. 20548

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