

Republican Prescription Drug Plan Erodes Cost of Living Protection, Cuts Social Security Benefits

H.R. 4910 Protects the Social Security COLA

Background

Social Security has a valuable feature for retirees, disabled workers and survivors: an annual cost of living adjustment (COLA). This benefit is all the more important because it is missing from many private pensions. However, rising health care costs in the past three years of Republican control have forced up the premiums for Medicare Part B so much that a large part of the COLA is now absorbed by the annual increase in those premiums. Under current law, individuals for whom the increase in the Part B premium would exceed their COLA do not have to pay the excess premium. But even that protection is missing for the new Part D prescription drug premium. Without a legislative change, millions of Social Security beneficiaries will see a substantial erosion in the purchasing power of their benefit check and some will even see their check shrink.

The Problem

The Social Security COLA is based on the previous year's change in the consumer price index (CPI), a measure of overall inflation in the economy. The goal of the COLA is to maintain the purchasing power of the benefit check in the face of rising prices. But that objective is undermined if the Medicare premium, which is typically deducted from a retiree's Social Security check, is growing very rapidly.

The current Medicare premium rises with spending in the program. In the past four years, the increases in Medicare Part B premiums have been substantial because health care costs have risen rapidly. As a result, for many beneficiaries, the additional deduction in their monthly benefit check to cover the higher Medicare premium has offset much of their COLA increase, leaving an inadequate amount to cover increases in the costs of all other goods and services.

The \$11.60 per month increase in the Medicare Part B premium for 2005 is the largest ever. This means that in the four years of the Bush Administration, the cumulative increase in the monthly premium will be \$28.20, more than twice as much as the cumulative increase of \$13.40 over the entire eight years of the Clinton Administration. Next year, for example, a widow with a \$600 monthly Social Security check will have 72 percent of her COLA used up by the increase in the Medicare premium.

Republican insensitivity to the problem of Medicare premiums undermining the Social Security COLA is reflected in their design of the new prescription drug benefit. An average senior is expected to spend five to six percent of his or her income on combined Medicare Part B and D premiums in 2006. But far more than six percent of the COLA will be used up by increases in the premiums.

For example, in 2005 the average retiree will see nearly half of his or her COLA eaten up by the Medicare premium increase. And 7 percent of beneficiaries will see no COLA at all: it will be entirely spent on just the premium increase. The following table shows the fraction of beneficiaries who have significant portions of their COLA used up by the premium increase:

Amount of COLA spent on 2005 Medicare Increase	Number of beneficiaries (in millions)	Percent of beneficiaries¹
All of the COLA	2.1	7
More than 75 percent	5.6	19
More than 50 percent	12.6	42
More than 25 percent	29.2	98
Less than 25 percent	0.5	2
TOTAL²	29.7	100

1. Among those who pay medicare premiums. Table excludes beneficiaries whose Part B premiums are paid by Medicaid. Assumes a COLA of 2.7 percent.

2. Totals may not add due to rounding.

Source: Congressional Budget Office.

In 2007, the Congressional Budget Office estimates that two out of every five beneficiaries (43 percent) will have more than 25 percent of their COLA used up by Medicare premium increases. This rises to 66 percent—23 million beneficiaries—by 2014.

The Solution: H.R. 4910, the “Social Security COLA Protection Act of 2004”

The “Social Security COLA Protection Act” would ensure that no more than 25 percent of a retiree’s annual COLA could be absorbed by increases in Part B and Part D Medicare premiums. Doing so would reserve 75 percent of the COLA for price increases in other goods and services, such as food, clothing, shelter, energy, and other health expenditures. In 2005, some 29 million Social Security beneficiaries would be protected by this legislation.

How the COLA Protection Bill Works

Example 1. Widow with \$500 in monthly Social Security benefits in 2004

Her annual Social Security benefit is \$6,000, and the COLA will increase her income by \$162 in 2005 (a 2.7 percent increase).

However, Medicare Part B premiums are projected to rise by at least \$139 that year. *Without* the bill's protection, a premium increase of \$139 will eat up 86 percent of her COLA.

With the bill's protection, only 25 percent of her COLA will be absorbed by Medicare premium increases, leaving 75 percent (\$122 per year) to cover other increases in her cost of living. The bill preserves an additional \$99 of COLA to be used for other expenses.

By 2009, the bill will save \$197 of her COLA. In 2014, \$545 of her COLA will be protected. Over 10 years, the projected total savings for this beneficiary will reach \$2,640.

Example 2. Retired couple with \$1,100 in combined monthly Social Security benefits in 2004.

Their annual benefits are \$13,200: \$8,400 for the husband and \$4,800 for the wife. A 2.7 percent COLA would increase their income by \$356 in 2005.

However, the Medicare Part B premiums paid by this couple are projected to rise by at least \$278 in 2005. *Without* the bill's protection, a premium increase of \$278 will eat up 78 percent of their combined COLA.

With the bill's protection, only 25 percent of their COLAs will be absorbed by Medicare premium increases, leaving 75 percent (\$267 per year) to cover other increases in their cost of living. The bill preserves an additional \$189 of COLA to be used for other expenses.

By 2009, the bill will protect \$358 of their COLA. In 2014, \$1,016 of their COLA will be protected. Over 10 years, the projected total savings for this couple will reach \$4,879.

How much would others save?

<u>Annual Benefit Amount</u>	<u>Savings Over 10 years</u>	<u>Average Annual Savings*</u>
\$7,200 (\$600 per month)	\$2,239	\$224
\$9,000 (\$750 per month)	\$1,636	\$164
\$9,600 (\$800 per month)	\$1,435	\$144

* The particular amount in each year could differ from this average because each year, the amount of protection provided by the bill would depend on the interaction between the Medicare premium increase and that individual's COLA increase. If the premium increase is large while the COLA is small, savings would be larger. If the premium increase is modest while the COLA is large, then savings would be smaller.

What fraction of those who pay Medicare premiums would benefit from the bill?

Year	Percent of Beneficiaries Helped by H.R. 4910 (of those who pay premiums)
2005	98
2007	43
2009	64
2011	67
2014	66

Source: Congressional Budget Office