



Medicare Rights Center  
Statement for the Record  
Submitted to the U.S. Senate Committee on Budget  
Regarding the September 27, 2023, hearing  
“Medicare Forever: Protecting Seniors by Making the Wealthy Pay Their Fair Share”

The Medicare Rights Center (Medicare Rights) appreciates this opportunity to submit a statement for the record on the September 27, 2023, hearing of the U.S. Senate Committee on Budget, titled “Medicare Forever: Protecting Seniors by Making the Wealthy Pay Their Fair Share.” Medicare Rights is a national, nonprofit organization that works to ensure access to affordable and equitable health care for older adults and people with disabilities through counseling and advocacy, educational programs, and public policy initiatives. Each year, Medicare Rights provides services and resources to nearly three million people with Medicare, family caregivers, and professionals.

Medicare is a vital, life-saving program that protects the health and well-being of over 63 million older adults and people with disabilities.<sup>1</sup> To strengthen the program for current and future beneficiaries, we support responsibly bolstering Medicare’s financing in ways that maintain the program’s universality, safeguard current benefits and cost protections, and modernize coverage to meet the evolving, diverse, and whole-body needs of beneficiaries.

While this will require a holistic approach that contemplates both savings and revenues, the focus of today’s hearing, and therefore our statement, is on the latter. We look forward to future opportunities to discuss cost containment, such as improving Medicare Advantage payment accuracy<sup>2</sup> and reigning in certain provider, setting, and service expenses.

### **Existing Revenue Levers**

Currently, Medicare Part A is funded through the Hospital Insurance (HI) trust fund. As its name suggests, the HI trust fund helps pay for inpatient hospital care for people with Medicare. In addition, it helps cover hospice, skilled nursing facility care, and home health services that follow a qualifying hospital stay.<sup>3</sup>

Medicare Tax. The HI trust fund is financed primarily by a dedicated payroll tax of 2.9% on covered earnings. Though it is divided equally between employers and employees, with each paying 1.45%, many

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<sup>1</sup> Centers for Medicare & Medicaid Services, “CMS Releases Latest Enrollment Figures for Medicare, Medicaid, and Children’s Health Insurance Program (CHIP)” (December 21, 2021), <https://www.cms.gov/newsroom/news-alert/cms-releases-latest-enrollment-figures-medicare-medicaid-and-childrens-health-insurance-program-chip>.

<sup>2</sup> Medicare Rights Center, “Medicare Advantage 101” (July 2023), <https://www.medicarerights.org/policy-series/medicare-advantage-101>.

<sup>3</sup> The Boards of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds, “2023 Annual Report” (March 31, 2023), <https://www.cms.gov/oact/tr/2023>.

economists believe the employer share of the tax is ultimately paid by the employee in the form of reduced compensation.<sup>4</sup>

**Additional Medicare Tax.** Due to changes in the Affordable Care Act (ACA), wages above a certain threshold (\$200,000 for individuals, \$250,000 for couples) are now subject to an additional HI payroll tax of 0.9%.<sup>5</sup> There is no employer-employee split, bringing the effective Medicare payroll tax rate for these households to 3.8%.

**Net Investment Income Tax.** Also introduced within the context of the ACA, the Net Investment Income Tax (NIIT) is a 3.8% tax on certain types of nonwage income, such as dividends and capital gains, for individuals making \$200,000 a year (\$250,000 for couples).<sup>6</sup> Despite being described as an “unearned income Medicare contribution” and originally designed to operate as such, it does not actually fund Medicare.<sup>7</sup>

## Potential Solutions

**Redirect NIIT Revenues.** That NIIT revenues go to the general fund and not the HI trust fund is widely considered the result of a legislative drafting error and procedural limitations.<sup>8</sup> Correcting this misallocation is a long overdue intervention that could considerably improve Medicare’s financial outlook.

The NIIT generates billions of dollars each year, yielding nearly \$60 billion in 2021 alone.<sup>9</sup> Redirecting its future proceeds could grow the HI trust fund by \$350 billion over ten years, alleviating more than half of its Congressional Budget Office (CBO)-estimated shortfall.<sup>10</sup> Transferring the present value of the NIIT’s past proceeds would shore up the trust fund even further, by an additional \$200 billion.

Among the revenue raisers outlined herein, properly allocating NIIT dollars to the HI trust fund is a commonsense first step. It would improve Medicare sustainability by ensuring an existing tax is operating as intended, leaving payment obligations untouched.

**Close Tax Loopholes.** As noted above, many higher-income households are subject to a 3.8% Medicare tax on their wage income and a 3.8% NIIT on their net investment income. However, owners of pass-through businesses like S-corporations and limited partnerships can bypass these taxes by classifying some of their income as “distributed profits” instead of “salary.”

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<sup>4</sup> Congressional Research Service, “Payroll Taxes: An Overview of Taxes Imposed and Past Payroll Tax Relief” (April 4, 2022), <https://crsreports.congress.gov/product/pdf/R/R47062>.

<sup>5</sup> Internal Revenue Service, “Questions and Answers for the Additional Medicare Tax” (last accessed September 22, 2023), <https://www.irs.gov/businesses/small-businesses-self-employed/questions-and-answers-for-the-additional-medicare-tax>.

<sup>6</sup> Internal Revenue Service, “Questions and Answers on the Net Investment Income Tax” (last accessed September 22, 2023), <https://www.irs.gov/newsroom/questions-and-answers-on-the-net-investment-income-tax>.

<sup>7</sup> P.L. 111-152

<sup>8</sup> Leonard E. Burman, “ACA and the Perils of Reconciliation” (March 13, 2017), <https://www.taxpolicycenter.org/taxvox/aca-and-perils-reconciliation>.

<sup>9</sup> Congressional Research Service, “The 3.8% Net Investment Income Tax: Overview, Data, and Policy Options” (June 30, 2023), <https://crsreports.congress.gov/product/pdf/IF/IF11820>

<sup>10</sup> Paul N. Van de Water, “Strengthening Medicare Financing” (December 14, 2020), <https://www.cbpp.org/research/health/strengthening-medicare-financing>.

As the experts at the Institute on Taxation and Economic Policy explain, this creates significant opportunities for tax avoidance that negatively impact Medicare financing: “If a partner of a law firm earns \$10 million through their practice, they do not need to claim all that income as salary. Instead, they could claim just \$200,000 as their salary and the rest as distributed profits. In this simplified scenario, they would save over \$200,000 in health care taxes.”<sup>11</sup>

There are several ways to address this, in whole or in part.<sup>12</sup> For example, broadening the Medicare and NIIT tax bases to cover the pass-through income for some higher-income taxpayers, such as individuals making over \$400,000 per year and couples making over \$500,000, combined with a redirection of NIIT proceeds to the HI trust fund, would raise over \$200 billion through 2031, reducing the HI deficit by over 80% based on CBO projections.<sup>13</sup>

Closing this egregious loophole improves Medicare’s finances by solving an existing problem with an existing tax. It is the next logical revenue-raising step after correcting the NIIT. We strongly urge policymakers to take such an iterative approach—to ensure all tax incentives are aligned and all proceeds are appropriately collected and directed—before contemplating any changes to individual tax rates.

Raise the Payroll Tax Rate. At the same time, we recognize the likely need for broader tax changes. As Dr. Moon has written previously, “[w]hen Medicare was enacted, it was expected that payroll tax rates would need to rise over time to meet the needs of a growing population of older adults and pay for care that was likely to become more expensive.”<sup>14</sup> However, “[t]he basic payroll tax rate that funds Part A of Medicare has remained constant since 1987 despite a doubling of the population served and a doubling of per capita spending.”<sup>15</sup> Despite being conceptualized as dynamic, Medicare taxation has been too static for too long, to the program’s detriment.

Manageable solutions are still possible. Modeling shows relatively small increases to the Medicare tax rate could generate substantial revenue. However, advance planning is necessary to minimize any potential disruptions. For example, immediately raising the Medicare payroll tax rate by one percentage point—from 1.45% to 1.95% for both employees and employers—would add \$1 trillion to the HI trust fund over the next 10 years. But such an abrupt shift may be difficult for many households to absorb, creating challenging circumstances for taxpayers and the economy.<sup>16</sup> While gradually phasing in such a shift would likely be easier to manage, it would only raise about half as much, roughly \$400 billion, over the same time frame.<sup>17</sup> Both strategies would zero out the 10-year HI financing gap the Trustees

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<sup>11</sup> Joe Hughes, “Key Reform in Build Back Better Act Would Close Loophole Used by the Rich To Avoid Funding Healthcare” (November 18, 2021), <https://itep.org/key-reform-in-build-back-better-act-would-close-loophole-used-by-the-rich-to-avoid-funding-healthcare/>.

<sup>12</sup> Karen C. Burke, “Exploiting the Medicare Tax Loophole” (June 17, 2018), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3041694](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3041694).

<sup>13</sup> Committee for a Responsible Federal Budget, “CBO Updates Major Trust Fund Baselines” (June 1, 2022), <https://www.crfb.org/blogs/cbo-updates-major-trust-fund-baselines>.

<sup>14</sup> Marilyn Moon, “Ensuring Medicare’s Future Will Require New Revenue” (January 28, 2021), <https://www.commonwealthfund.org/blog/2021/ensuring-medicares-future-will-require-new-revenue>.

<sup>15</sup> *Id.*

<sup>16</sup> Gordon B. Mermin, et al. “Options for Increasing Medicare Revenues” (February 1, 2023), <https://www.taxpolicycenter.org/publications/options-increasing-medicare-revenues/full>.

<sup>17</sup> Marilyn Moon, “Ensuring Medicare’s Future Will Require New Revenue” (January 28, 2021), <https://www.commonwealthfund.org/blog/2021/ensuring-medicares-future-will-require-new-revenue>.

currently project (\$390 billion), but that may not always be true. The longer we wait to act, the bigger hole we'll have to fill, and the fewer tools we'll have.

Any payroll tax increases must be broad-based, modest, and phased-in to prevent a worsening of income inequality or financial insecurity. They must also be part of a beneficiary-centered, comprehensive approach that includes the revenue raisers discussed above as well as important program efficiencies.

## **Conclusion**

Medicare sustainability is a critical issue for millions of Americans. The program's financing challenges are well known,<sup>18</sup> as are many of the solutions. This reality must not be used as an excuse to cut benefits, increase out-of-pocket costs, or otherwise undermine access to care in the name of "urgency." Now is the time for measured policies, not brash rhetoric.

As Dr. Moon has explained: "The Medicare Part A trust fund was intended to warn policymakers when changes were needed to sustain this crucial program for future generations. It should spur a debate on how best to protect the program rather than as a mandate for cutting this crucial benefit..."<sup>19</sup>

We agree. The Medicare Rights Center looks forward to thoughtful conversation on improving the program and its financial footing.

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<sup>18</sup> Juliette Cubanski and Tricia Neuman, "What to Know about Medicare Spending and Financing" (January 19, 2023), <https://www.kff.org/medicare/issue-brief/what-to-know-about-medicare-spending-and-financing/>.

<sup>19</sup> Marilyn Moon, "Ensuring Medicare's Future Will Require New Revenue" (January 28, 2021), <https://www.commonwealthfund.org/blog/2021/ensuring-medicares-future-will-require-new-revenue>.