



January 22, 2010

Honorable Jeff Sessions
United States Senate
Washington, DC 20510

Dear Senator:

This letter responds to questions you posed about the Congressional Budget Office's (CBO's) analysis of the effects of H.R. 3590, the Patient Protection and Affordable Care Act (PPACA), as passed by the Senate on December 24. In particular, you asked for clarification on several issues regarding the effect of the legislation on the Hospital Insurance (HI) trust fund, from which Medicare Part A benefits are paid.

Your questions focused on the budgetary impact of the provisions of PPACA that would extend the solvency of the HI trust fund, presumably either by increasing revenues to or decreasing expenditures from that trust fund. Some specific provisions of PPACA can be identified as having such effects. However, some of those provisions would have effects beyond the HI trust fund (such as provisions addressing Medicare Advantage plans, which are paid for from both the trust fund and the Treasury's general fund), and other provisions in the act would affect the trust fund indirectly through their impact on taxable income. Because of those complexities, this letter does not address the possible impact of removing from the act all of the provisions that would affect the HI trust fund, but, rather, summarizes the net effects of the act as a whole on the trust fund.

Budgetary Impact of the Legislation

On the basis of the economic forecast and technical assumptions in CBO's March 2009 baseline, CBO projected that, under current law, the HI trust fund would be exhausted—that is, the balance of the trust fund would decline to zero—during fiscal year 2017. Enacting PPACA, including the manager's amendment, would reduce net outlays for Part A of Medicare by \$245 billion over the 2010–2019 period relative to that baseline, CBO estimates. Enacting that legislation would also increase HI payroll tax receipts by about \$113 billion over that period, according to estimates by CBO and the staff of the Joint Committee on Taxation (JCT). Together, those changes in outlays and revenues would diminish budget deficits and add to trust fund balances by \$358 billion over that 10-year period. Given those changes in the financial flows of the trust fund, CBO estimates that the HI trust fund would have a positive balance of about \$170 billion at the end of fiscal year 2019.

In the December 19, 2009, cost estimate for PPACA, CBO and JCT estimated that the direct spending and revenue effects of enacting PPACA would yield a net reduction in federal deficits of \$132 billion over the 2010–2019 period.¹ Thus, the act’s effects on the rest of the budget—other than the cash flows of the HI trust fund—would amount to a net *increase* in federal deficits of \$226 billion over the same period. Those two aspects of the legislation would have differing effects on debt held by the public: The changes to HI revenues and costs, by themselves, would reduce that debt, while changes in other revenues and costs would increase it.

For the decade beyond 2019, CBO expects that enacting PPACA would reduce federal budget deficits relative to those projected under current law—with a total effect during that decade in a broad range between one-quarter percent and one-half percent of gross domestic product.² The legislation would have positive effects on the cash flows of the HI trust fund in that decade that would be larger than its effects on federal budget deficits as a whole. Therefore, leaving aside the cash flows of the HI trust fund, CBO expects that PPACA would yield a net *increase* in budget deficits during the decade beyond 2019.

Trust Fund Accounting

However, the HI trust fund, like other federal trust funds, is essentially an accounting mechanism. In a given year, the sum of specified HI receipts and the interest that is credited on the previous trust fund balance, minus spending for Medicare Part A benefits, represents the surplus (or deficit, if the latter is greater) in the trust fund for that year. Any cash generated when there is an excess of receipts over spending is not retained by the trust fund; rather, it is turned over to the Treasury, which provides government bonds to the trust fund in exchange and uses the cash to finance the government’s ongoing activities.

The HI trust fund is part of the federal government, so transactions between the trust fund and the Treasury are intragovernmental and have no net impact on the unified budget or on federal borrowing from the public. From a unified budget perspective, any increase in revenues or decrease in outlays in the HI trust fund represents cash that can be used to finance other government activities without requiring new government borrowing from the public. Similarly, any increase in outlays or decrease in revenues in the HI trust fund in some future year represents

¹ Congressional Budget Office, letter to the Honorable Harry Reid regarding the direct spending and revenue effects of the Patient Protection and Affordable Care Act (December 19, 2009). CBO has not prepared an estimate of the budgetary impact of PPACA as passed by the Senate; the estimates used in this letter apply to the bill as introduced, incorporating the manager’s amendment but no other amendments. The relevant figures for the Senate-passed version of the legislation would not differ significantly.

² Congressional Budget Office, letter to the Honorable Harry Reid regarding an error in the cost estimate released on December 19 (December 20, 2009).

a draw on the government's cash in that year. Thus, the resources to redeem government bonds in the HI trust fund and thereby pay for Medicare benefits in some future year will have to be generated from taxes, other government income, or government borrowing in that year. The HI trust fund and other trust funds have important legal meaning but little economic or budgetary meaning.

The reductions in projected Part A outlays and increases in projected HI revenues resulting from PPACA would significantly raise balances in the HI trust fund and might suggest that significant additional resources—\$358 billion plus additional interest to be credited to the trust fund over time—had been set aside to pay for future Medicare benefits. However, only the additional savings by the government as a whole truly increase the government's ability to pay for future Medicare benefits or other programs, and those would be a much smaller (\$132 billion plus interest savings to be achieved over time). Unified budget accounting shows that the majority of the HI trust fund savings under PPACA would be used to pay for other spending and therefore would not enhance the ability of the government to pay for future Medicare benefits.

Impact on Federal Debt

You also asked about the impact of PPACA on gross federal debt. Gross federal debt consists of debt held by the public and debt issued to government accounts. Debt held by the public is the most meaningful measure for assessing the relationship between federal debt and the economy because it represents the amount that the government has borrowed in the financial markets to pay for its operations and activities; such borrowing competes with other participants in credit markets for financial resources. In contrast, debt held by trust funds and other government accounts represents *internal* transactions of the government and thus has no effect on credit markets.

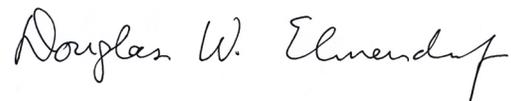
Compared with the effects of current law, enacting PPACA would increase the balance in the HI trust fund at the end of 2019 by somewhat more than \$358 billion (\$358 billion in increased revenues and reduced outlays, described above, plus interest earnings on the larger balances during the 2009–2019 period). Balances in the HI trust fund are generally held in the form of government debt. Therefore, the HI trust fund would hold more than \$358 billion of additional government debt by the end of 2019 compared with its holdings under current law. At the same time, enacting PPACA would reduce debt held by the public at the end of 2019 by somewhat more than \$132 billion (\$132 billion in increased revenues and reduced direct spending, plus interest savings from the smaller debt during the 10-year period). Therefore, enacting PPACA would increase debt held by government accounts more than it would decrease debt held by the public, and would thus increase gross federal debt.³ However, that measure of debt conveys

³ Because interest rates on debt held by the public and debt held by government accounts are not too dissimilar, accounting explicitly for the difference in interest costs between the HI trust fund and the unified government accounts would not affect this qualitative conclusion.

little information about the federal government's future financial burdens and has little economic meaning. In contrast, the effects of legislation on debt held by the public offer a more useful measure of that legislation's impact on the government's financial condition.

I hope this information is useful to you. If you have any questions, please contact me.

Sincerely,



Douglas W. Elmendorf
Director

cc: Honorable Harry Reid
Majority Leader

Honorable Mitch McConnell
Republican Leader

Honorable Max Baucus
Chairman
Committee on Finance

Honorable Chuck Grassley
Ranking Member

Honorable Tom Harkin
Chairman
Committee on Health, Education, Labor, and Pensions

Honorable Michael B. Enzi
Ranking Member

Honorable Kent Conrad
Chairman
Committee on the Budget

Honorable Judd Gregg
Ranking Member