THE WHITE HOUSE

WASHINGTON

February 16, 1999

SOCIAL SECURITY/MEDICARE EVENT

DATE:	February 17, 1999
TIME:	1:30-1:50pm (Pre-brief) 1:50-2:00pm (Meet and Greet) 2:00-3:00pm (Event)
LOCATION:	Map Room (Pre-brief) Blue Room (Meet& Greet) Event (East Room)
FROM:	Gene Sperling Mary Beth Cahill

I. PURPOSE

To highlight how your plan to save Social Security and strengthen Medicare, while maintaining fiscal discipline, is the best approach for America's young people.

II. BACKGROUND

Why Your Plan Benefits Young People:

Some commentators have stated that your plan to allocate the surpluses would redistribute more money from younger Americans to older Americans. The goal of this event is to highlight how your plan benefits younger Americans. Rather than consuming the surplus for today, you propose to reserve nearly 90 percent of the projected budget surpluses -- almost $4 trillion -- over the next 15 years for the future to help meet the long-term retirement challenge.

There are a number of reasons why this plan is good for young Americans.

First, it ensures that Social Security benefits will be there for today's young Americans. Your proposal extends the life of the Trust Fund through 2055. By working with Congress in a bipartisan way, we are working to extend Social Security for 75 years. For a worker who is 20 years old today, he/she will be assured of a strong and stable benefit when he or she retires under this framework. In addition, your framework reserves 12 percent of the projected surpluses to create new Universal Savings Accounts (USAs) so that young people can begin saving and start building wealth to meet their future retirement needs.

Second, by paying off the national debt, your plan lifts an enormous burden off future generations. As you know, during the 1980's and early 1990's, the federal debt quadrupled. As a share of GDP, the publicly held debt increased from 26 percent in 1981 to 50 percent in 1993. Today, as a result of your 1993 Economic Plan and the 1997 Balanced Budget Agreement, the debt-to-GDP ratio is 44 percent, and your proposal would cut it by more than two thirds in dollar terms and lower it to 7.1 percent, as a share of the economy, by 2014 -- its lowest level since 1917. As David Broder wrote in the *Washington Post* [2/7/99], this is "the greatest gift to our children." Here's why:

It Will Help Grow The Economy For Our Children. Your framework will cut the federal debt, thereby raising national savings. Higher national savings will mean lower interest rates, higher private-sector investment, and thus, higher economic growth in the future.

It Will Cut The Interest Payments Our Children Pay on the Federal Debt. When you took office, interest payments on the federal debt were projected to eat up 27 cents of every budget dollar in 2014. Today, interest payments on the debt take up about 13 cents of every tax dollar. Under your proposal, interest payments would shrink to just 2 cents on every dollar by 2014.

It Will Ensure That We Do Not Leave a Legacy of Debt to Our Children. Your proposal would cut the debt held by the public, as a share of the economy, to 7.1 percent in 2014. This would mean that instead of leaving a mountain of debt for our children, we would completely eliminate the national debt by 2018.

Finally, your proposal ensures that Social Security will continue to help young people today. By saying no to radical privatization, your plan promises that Social Security will continue to provide both disability and survivors insurance protection to workers and their families. For an average young family with two small children, Social Security provides benefits which are the equivalent to a payout of $600,000 from a disability and survivors insurance policy. By strengthening Social Security, your plan ensures that Social Security will continue to provide our parents and grandparents with a stable benefit -- without which many would become dependent on their children for support.

Sharon Bridgner

You will be introduced by Sharon Bridgner of McLean, Virginia. She is a 26-year old and works as a clinical research nurse of neurology at the National Institutes of Health (NIH). She formerly served as the President of the Student Nurses Association and is a member of the American Nurses Association. She also works part time at the George Mason University, School of Public Policy. As a young nurse, she sees first hand every day the importance of Social Security and Medicare to current retirees and will discuss how essential these programs are to her generation.

Audience

The audience will be filled with approximately 150 young people from all different groups, such as 2030 center, Economic Security 2000, local student groups.

III. PARTICIPANTS

Pre-brief
John Podesta
Secretary Rubin
Jack Lew
Gene Sperling
Ken Apfel
Larry Stein

Meet and Greet
John Podesta
Secretary Rubin
Jack Lew
Gene Sperling
Ken Apfel
Larry Stein
Sen. Charles Robb (D-VA)
Rep. Tammy Baldwin (D-WI)
Rep. Elijah Cummings (D-MD)
Rep. Steny Hoyer (D-MD)
Rep. Robert Matsui (D-MD)

IV. SEQUENCE OF EVENTS

- **YOU** receive briefing in the Map Room.

- **YOU** meet Members of Congress in Blue Room.

- **YOU** accompanied by the the First Lady, Secretary Rubin, Ken Apfel, Representative Tammy Baldwin, Senator Chuck Robb, Sharon Bridgner (real person), and 10 youth from James MacGregor Burns Academy of Leadership, University of Maryland are announced into the East Room.

- The First lady makes brief remarks and introduces Commissioner Apfel.

- Commissioner Apfel makes brief remarks and introduces Secretary Rubin.

- Secretary Rubin makes brief remarks and introduces Representative Tammy Baldwin.

- Representative Baldwin makes brief remarks and introduces Senator Chuck Robb.
- Senator Chuck Robb makes brief remarks and introduces Sharon Bridgner.
- Sharon Bridgner makes brief remarks and introduces **YOU**.
- **YOU** make remarks
- **YOU** depart.

V. PRESS COVERAGE

Open

VI. REMARKS

To be provided by speechwriting.

2-16-99

THE WHITE HOUSE

WASHINGTON

February 12, 1999

Copied: Sperling Podesta

MEMORANDUM FOR THE PRESIDENT

FROM: GENE SPERLING

SUBJECT: NEC WEEKLY REPORT

cc: JOHN PODESTA

USA Accounts: We held an NEC principals meeting on Thursday (2/11) to discuss details of the USA accounts. Among the issues discussed were how high up in the income distribution the flat contributions and matches should go, whether the accounts could be used for purposes other than retirement, how the accounts would be administered, and whether the proceeds from the accounts should be taxed at withdrawal. We anticipate additional principals meetings over the next week, and then hope to meet with you for final decisions.

Social Security Update: On Monday (2/8), Robert Rubin, Jack Lew, Larry Stein, Ken Apfel, David Wilcox, Chuck Brain and myself spoke with 130 Democratic members of Congress on your Social Security plan in Wintergreen, West Virginia. Robert Rubin addressed all 130 members and the others and myself were involved in 5 different breakout sessions with the members. These discussion were very substantive, we each gave a presentation to 30 members and had detailed discussions on your proposal for Social Security reform. The NEC hosted a principals meeting where we discussed creating legislation for your Social Security plan. On Tuesday (2/9), I met with Marshall Carter, Chairman and CEO of State Street Corp out of Boston and some representatives from the company where we discussed investing a portion of the Social Security trust fund in equities. On Wednesday (2/10), Robert Rubin and I met with Phil Condit, President & CEO of Boeing, Dana Mead, Chairman & CEO of Tenneco, and William Steere, Chairman & CEO of Pfizer from the Business Roundtable. We discussed a number of issues, including Social Security and "corporate governance" issues related to investing the surplus in equities. On Thursday (2/11), Robert Rubin, Larry Stein and I met with Senate Democrats and discussed Social Security reform. Finally, on Friday (2/12), I spoke at the CATO Institute and was on a panel discussing your Social Security reform proposal. Others on the panel included Henry Aaron of the Brookings Institute, Carol Cox Wait of the Committee for Responsible Federal Budget, Carolyn Weaver of the American Enterprise Institute, and Michael Tanner of the Cato Institute. You should also know that we are working on a letter of support from numerous economists, including 5 Nobel Prize winners, that is currently being circulated. The letter may be released at press conference sometime in the next two weeks.

EU Aircraft Noise Standard: The NEC is setting up an interagency process to deal with a looming dispute over a proposed EU noise regulation that would limit the use of "hushkitted" aircraft; hushkits are high-tech mufflers that allow older aircraft -- mostly Boeing planes, since Airbus aircraft are newer -- to meet Stage 3 noise requirements under the International Civil Aviation Organization (ICAO). Under the regulation, which the European Parliament approved this week, EU airlines would not be allowed to add hushkitted aircraft to their fleets after April 1, 1999. And beginning April 2002, non-EU airlines would be allowed to fly these aircraft into the EU only if they were registered before April 1, 1999 and were serving EU destinations between 1995 and 1999. We strongly oppose this regulation because it is inconsistent with internationally recognized noise standards and would undermine ICAO itself. In addition, the regulation would decrease the resale value of affected aircraft and reduce the market for hushkits themselves, a U.S. technology. Rep. Oberstar and others have introduced legislation that would prohibit the Concorde from landing here if the EU regulation takes effect. The interagency group will consider that and other possible policy options.

18-Year Financing of Airbus Aircraft: Through an NEC interagency process, we are also developing a strategy for challenging the EU on aircraft financing structures that undermine internationally agreed upon principles. OECD members agreed some years ago to limit export credit agencies (ECAs) to offering 12-year loans for commercial aircraft. However, the EU has found a way to offer 18-year financing terms for purchasers of Airbus aircraft --in flagrant violation of the spirit, if not the letter, of the OECD agreement. These distortive terms may have influenced the outcome of one or more large sales to developing countries, and we believe the EU will try to win a huge pending aircraft purchase ($3-5 billion) by Mexico by offering similar terms. (You have talking points for use with President Zedillo on the importance to the U.S. that Boeing win this sale.) We are prepared to match whatever terms the EU offers in Mexico, but we are trying to find a way to get the EU to de-escalate instead.

I want to [illegible]

Meeting with Navy Secretary on BRAC/Base Reuse: John Podesta and Dorothy Robyn on my staff met with Navy Secretary Danzig on Monday (2/8) to try to resolve a number of problems that BRAC communities face with the Navy in carrying out their base reuse plans. Although the Navy has made progress since a similar meeting two years ago, Navy officials continue to be unnecessarily slow, bureaucratic and penny-pinching in their dealings with communities (many of them in California), which often delays economic redevelopment and job creation. Among other things, Danzig proposed that Robyn meet monthly with a senior Navy official to review outstanding problems; issues that cannot be resolved at that level will be appealed directly to Navy Undersecretary Jerry Hultin.

Pensions: You should know on Thursday (2/11), Vice President Gore, accompanied by Secretaries Herman and Rubin, announced a legislative package to enhance retirement security by strengthening the private pension system. The event stressed that a secure and comfortable retirement depends on three things: social security, individual savings, and employer-sponsored pensions. At this event, we demonstrated that we continue to work to improve the private pension system, with particular emphasis on the pension needs of women. The package also includes new initiatives to expand portability by allowing rollovers between various types of pension plans and to induce small business plan start-up by lowering PBGC premiums for new plans in the early years.

Financial Modernization: This year's debate on Financial Modernization began in earnest this week, as the House Banking Committee held a series of hearings featuring Chairman Greenspan and Secretary Rubin. House Banking Committee Chairman Leach reintroduced last year's bill, H.R. 10, with minor variations. Before the hearing, Representative LaFalce introduced his own bill, with key Republican co-sponsors -- House Rules Committee Chairman Drier and Rep. Baker. Secretary Rubin expressed great enthusiasm for the LaFalce bill, demonstrating a willingness to compromise on the key issue for Treasury last year -- whether banking institutions should have the choice to conduct new financial activities (like securities and insurance) inside the bank in operating subsidiaries (the Treasury view) or must use a wholly separate bank holding company affiliate to conduct those activities (the Fed view). The LaFalce bill authorizes some, but not all, activities to be performed in operating subsidiaries. Chairman Leach and Chairman Greenspan expressed their strong opposition to the LaFalce compromise, but for the first time on this issue it was the Fed, not Treasury, that was portrayed as inflexible in press accounts.

International Labor Organization: The NEC (Lael Brainard, Sarah Rosen, and Rick Samans), Andrew Samet of Labor, and Harold Koh of State met with policy representatives of the AFL-CIO to define further the objectives of the FY2000 budget initiative regarding the ILO. To facilitate our discussions with appropriators, we are drafting a more elaborate written presentation of our objectives and expectations.

Steel Update: On Friday, Secretary Daley announced high preliminary antidumping margins on hot-rolled steel imports from Japan and Brazil that should have a significantly reduce imports from those countries. Margins ranged from 25% to 67% for Japan (trade weighted average of 35%), and from 50% to 71% (trade weighted average of 58%) for Brazil. Industry analysts believe margins over 20% will be prohibitive. Pending final determinations in June, U.S. importers of these products will be required to pay cash deposits or post a bond on imports of these products, for Japanese imports retroactive to November. Secretary Daley will announce the preliminary dumping determination on Russia next week. We are seeking a broader agreement covering all steel products that may gain the support of the steelworkers, who, like industry, oppose a suspension agreement on just hot-rolled unless it is tied to self initiation of Section 201. Senators Roth and Moynihan wrote to Secretary Daley this week stating their opposition to any suspension agreement that does not provide the same relief that allowing the dumping case to conclude would yield, stressing that to do so would "preempt the operation of law" and our efforts to advance a "forward-looking" trade strategy. They may be more receptive to a broader agreement. Secretary Daley is conferring with them and other members of the Steel Caucus. On February 24, Charlene Barshefsky, Secretary Daley, Larry Stein and I will meet with Speaker Hastert and other Republican members and then the very next day we will meet with Rep. Gephardt and other Democratic members of the Steel Caucus to continue discussions to deal with this issue.

China WTO: The NEC coordinated USTR-led interagency efforts provided for Zhu Rongji's initial review a clear sense of what we need to reach agreement on China's accession to the WTO. We worked closely with the NSC on this. Intensified talks will continue up until Zhu's visit, with Ambassador Barshefsky traveling to Beijing in the first week of March. There have been press reports that we are lowering the bar for accession. You should know that this is not true. We are sharpening our priorities through consultation with industry and Congress, but any deal has to be commercially viable, to both our exporters and import sensitive industries, and for Congress to approve permanent MFN for China.

Japan: The NEC co-chaired this week with the NSC a deputies meeting to plan for Prime Minister Obuchi's visit in late May or early April. Japan has taken meaningful steps on the fiscal and banking side, but effective implementation is key, and Treasury is not prepared to say Japan has turned the corner. Treasury, concerned that rising interest rates, a stronger yen and deflation pose a significant downside risk to the Japanese economy, is privately urging the Bank of Japan to ease monetary policy. Deregulation and market opening have stalled absent Hashimoto and amid growing concerns about dislocation. We are prioritizing deregulation and market access issues, with an eye toward resolution of some sort before the Obuchi visit. Coincidentally, Super 301 determinations must be made on April 30, just prior to the Obuchi visit. The NEC will chair an interagency subcabinet meeting with the Japanese to prepare for the summit.

5-9-99

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~~WITH CONFIDENTIAL ATTACHMENT~~

THE WHITE HOUSE

WASHINGTON

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Podesta
Spalding

March 8, 1999

MEMORANDUM FOR THE PRESIDENT

FROM: JOHN PODESTA

SUBJECT: DAILY ISSUES UPDATE

This memo provides updates on some of the issues White House offices are tracking today.

DOMESTIC POLICY COUNCIL

- **Ed-Flex.** Senator Lott's motion to invoke cloture on the Ed-Flex bill failed today, on a straight party-line vote. Another cloture vote on the bill is scheduled for tomorrow; we expect much the same vote. Immediately following the cloture vote, we issued a statement from you calling once again on the Republican Leadership to allow an up-or-down vote on the class size amendment. (See attached.) The Vice President delivered the same message at the top of his livability event and in radio interviews. Odds now are that Senator Lott will take down the bill after the failure of the second cloture vote; there is still a chance, however, that he will enter into a time agreement allowing a vote on class size and one or two other Democratic amendments. If Lott does allow a vote on class size, we expect Republicans to argue that Congress should fund no new initiatives until it fully funds special education.

NATIONAL ECONOMIC COUNCIL

- **Social Security.** Today, Alicia Munnell, Robert Solow (Nobel Laureate), and Peter Dimond held a news conference to announce the support of more than 100 of the nation's leading economists (including 5 Nobel Prize winners) for your plan to pay down the debt. United under the banner of Economists for Increased National Savings, the economists issued a statement supporting your FY'00 budget priority to save the surpluses, and your plan to direct the bulk of the $4.4 trillion of net budget surpluses away from additional spending or tax cuts, toward a more productive, long-term strategy of saving.

- **Brazil.** Today, IMF Director Camdessus recommended that the IMF Board approve Brazil's revised economic program. Key elements of the program include a strengthened fiscal adjustment -- increasing the primary surplus target by .5% to a range of 3.0-3.5% -- and an inflation target anchor for monetary policy. The U.S. Treasury released a press statement at midday welcoming the agreement and expressing the belief that firm and sustained implementation could lay the basis for restored confidence and renewed growth.

LEGISLATIVE AFFAIRS

- **House of Representatives.** Today, the House met for a *pro forma* session. On Wednesday the Ways & Means Committee will mark up the Visclosky (D-IN) -Regula (R-OH) steel imports bill. The legislation imposes quotas on the importation of foreign steel. Due to the possibility that the Kosovo Resolution, which authorizes the deployment of troops for peacekeeping, will not be considered this week, the steel imports legislation may move to the floor for consideration later this week.

- **Senate.** Today, the Senate continued debating S. 280, the Administration-supported Education Flexibility Act (Ed-Flex). Debate on the bill will continue tomorrow. A second cloture motion vote on the measure is expected tomorrow and two more are expected on Wednesday.

COUNCIL OF ECONOMIC ADVISORS

- **Productivity.** Tomorrow, at 10:00 a.m., the Bureau of Labor Statistics will release revised estimates of productivity growth in the non-farm business sector (output per hour worked) and new hourly compensation figures. The estimated fourth quarter productivity is revised up from 3.7% to 4.6%. Hourly compensation over the past four quarters increased 4%, compared to 3.7% during the same period last year. (CEA release attached.)

VICE PRESIDENT'S OFFICE

- **Liveability Agenda.** Today, the Vice President joined Sec. Slater, more than two dozen traffic reporters and nearly 150 state and local officials at an event to highlight elements of our Liveability Agenda designed to ease traffic congestion. Specifically, the Vice President: 1) called on the FCC to adopt a new, national three-digit telephone number to allow Americans immediate access to transportation information, such as road conditions and bus schedules; 2) launched a "commuter choice" initiative to all employers to offer their employees taxable cash or tax-exempt parking, transit or vanpool benefits; and 3) a series of regional transportation livability summits over the next year.

THE WHITE HOUSE

WASHINGTON

March 11, 1999

MEMORANDUM FOR JOHN PODESTA
DOUG SOSNIK
STEVE RICCHETTI
MARIA ECHAVESTE
KAREN TRAMONTANO

FROM: **GENE SPERLING**

SUBJECT: **NEC's Long-Term Policy Announcements and Message Ideas**

Per your request, we have structured this memorandum in the following manner, listing numerous policy announcements and message ideas for the President and Vice President:

- Strategic Plans
  - Saving Social Security and Strengthening Medicare
  - Promoting Greater Economic Opportunity
  - Building a New Consensus on International Trade
  - Reforming the International Financial Architecture
- Upcoming Challenges Requiring Administration Response
  - Timing
  - Responses
  - Presidential Action
- Executive and Other Non-Legislative Actions

STRATEGIC PLANS

I. <u>SAVING SOCIAL SECURITY AND STRENGTHENING MEDICARE</u>. Continuing to create an environment in which the President's Social Security and Medicare reform proposals can be enacted this year

A. ***Specific Agenda Items***

<u>Announcing Details of the President's USA Accounts Proposal</u>. We are announcing shortly the details of the President's USA accounts proposal. As part of this announcement, we will conduct a number of rollout activities on the Hill, with the press, and with groups. *Timing: March 18*

<u>Continuing Legislative Process on Our Social Security and Medicare Framework</u>. In the near term, we will be working closely with the Democrats on amendment strategies focused on Medicare vs. tax cuts. We will work longer term on a possible new configuration of our budget to unify Democrats.

<u>Create a Process for Bipartisan Negotiations</u>. Depending on several factors, such as the unfolding of the budget process and the temperature on the Hill, we could pursue creating an environment in which a negotiation process could begin on the Hill.

B. ***Possible Presidential Actions***

<u>Release the Social Security Trustees Report on March 30</u>. The 1998 Trustees report will show that our strong economy has helped improve Social Security's financial position. Last year, the report showed that economic growth had extended the life of the trust fund to 2032 -- three years beyond the previous year's report. Importantly, the report also highlights the long-term pressures facing the Social Security system and the need for reform. *Timing: March 30*

<u>Reprise of Second Day of White House Conference on Social Security</u>. We could do a reprise of the second day of the White House Conference on Social Security. Like the first conference, there could be two 1½ hour sessions, with bipartisan experts leading each. The day would close with a plenary meeting with the President. We would need at least ten days lead time in order to allow the presenters to think through what they would present. (We also want to discuss this further with Larry Stein.)

<u>Release Further Details on Widow Poverty</u>. In the coming weeks, we may be able to release further details on our anti-widow poverty initiative within our overall Social Security reform framework.

Medicare Commission. The Commission is trying to issue its report shortly. We are working on developing our overall strategy, which will depend upon the Commission's outcome.

C. *Republican Agenda and Likely Response*

As of now, it appears that the Hill Republicans will continue to push their overall budget/tax outline in the weeks ahead. In addition, they are hitting hard on our Medicare agenda, as evidenced by Sen. Gramm's charge in the Senate Finance hearing on March 10 that the Administration is "irresponsible" for proposing funding without real reforms. (The Republicans want structural reform first, then funding.) We will continue to respond pressing our positive message on our Social Security and Medicare framework and by showing how their outline fails to extend Social Security solvency, does not address Medicare's solvency, and opts for a large tax cut targeted away from the middle class. Additionally, a related major decision is whether we propose our own overall Medicare plan, which would require a very significant rollout.

D. *Timing and Strategy*

We will be unveiling the details of the USA Accounts on March 18, and will likely address Social Security and Medicare issues in other fora between now and the Easter recess, including through the release of the Social Security and Medicare Trustees Report on March 30. At the same time, hearings on both Social Security and Medicare will continue on the Hill (they have been held thus far in Senate Finance, Budget, and Aging and in House Ways & Means, Budget, and Commerce) in the weeks leading up to the Easter recess.

II. PROMOTING GREATER ECONOMIC OPPORTUNITY.

Promoting economic opportunity for all Americans by promoting development in underserved urban and rural communities, expanding worker training, increasing mentoring opportunities for pre-college students, and pressing for other initiatives for working families.

A. *Specific Agenda Items*

New Markets Initiative Legislation. In the next 4-6 weeks, we will likely have the three bills drafted for the new markets initiative (tax, APICs, and New Markets Venture Capital Firms) which the President laid out in New York in January. The delivery of this legislation at an event with members who agree to sponsor the legislation would be a good chance to push our economic empowerment message and show growing support for the initiative. *Timing: April*

Workforce Legislation. Over the next two months, we will have legislation ready to send to the Hill on re-employment, literacy, and youth employment. This will provide another opportunity for a strong message event on these issues and will help our efforts on the Hill to gain passage this year. *Timing: April-May*

B. ***Possible Presidential Actions***

Four-Day Economic Development Mission. Using a typical foreign trip as a model, the President and Vice President could tour both rural and urban areas across the United States that would benefit from the new markets initiative and other economic development initiatives that the Administration has proposed. By focusing on this issue for a sustained period of three or four days, the President and Vice President could draw attention to the fact that the Administration believes we need to do more to bring economic growth to every part of the country. This will take a significant period of time to prepare for and to do correctly. *Timing: June-July*

Addressing the Skills Gap and Training American Workers for American Jobs. One recent survey found that over 60 percent of corporate leaders say that the number one barrier to sustained economic growth is the lack of skilled workforce. The President could meet with a number of CEOs to discuss the current skills gap and what needs to be done to close it. This could obviously highlight the Administration's budget initiatives addressing the problem, such as (1) the re-employment initiative, (2) the literacy initiative, and (3) the youth employment initiative. We could also challenge high-tech companies to make specific commitments to train more American workers, which the companies pledged to do during the debate on H1-B visas. They could provide more college scholarships for women and minorities, partner with community colleges to develop cutting-edge curricula, and encourage their employees to serve as telementors for middle school students to get them excited about math and science. They could also provide matching funds for our community technology centers -- which could help train inner-city youth for high-tech jobs. *Timing: April-July*

Making College Available to All Through the GEAR UP Mentoring Initiative. We need to hold an event where the President will make several announcements regarding GEAR UP, including: the Ford Foundation's partnership with the Administration to provide technical assistance to applicants and grantees, doubling of the Ford Foundation's funding to their own grantees, the creation of the High Hopes for College Leadership Group, the President's letter to all College Presidents urging them to participate, and the unveiling of the GEAR UP application package. He will also obviously push for his proposal to double funding for the GEAR UP mentoring program. *Timing: March-April*

Focus on the Minimum Wage. Obviously, this is an issue we want to coordinate closely with the Hill. However, given that Speaker Hastert opened the door slightly on the minimum wage recently, we may want to highlight the issue soon. One possibility would be to have the Labor Department write a short report on the impact of the 1996/1997 minimum wage increase on job growth, unemployment, and wages. *Timing: TBD*

C. *Republican Agenda and Likely Response*

The Republicans will have a limited training and economic development agenda. Nonetheless, there have been some indications that key Republicans may want to move on some of our legislation. For example, Rep. Goodling made some very positive statements about our entire workforce initiative on the day the President announced it in late January. We will continue to try to forge bipartisan support around as many of these initiatives as possible.

D. *Timing and Strategy*

We would like to focus a great deal of attention on our worker training agenda and our community empowerment agenda over the next six months. In particular, though it will take a fair amount of planning, a three or four day economic development "trade" mission to underserved urban and rural areas would attract huge attention and could serve as an important catalyst in moving our related legislation.

In some instances, our timing on these issues will be dictated by movement on the Hill (e.g., when Kennedy moves on minimum wage).

III. <u>BUILDING A NEW CONSENSUS ON INTERNATIONAL TRADE</u>. Use Presidential leadership to build a new consensus on trade, delivering on his commitment to put a human face on the global economy.

A. *Specific Agenda Items*

<u>Building a New Consensus for Trade Authority:</u> We are exploring whether it is possible to work with Congressional Democrats to fashion a traditional trade authority bill that many House Democrats could support and organized labor would not feel compelled to actively oppose. It would at minimum need to treat labor and environment in parity with other trade negotiating objectives such as intellectual property and could be bolstered by supplementary commitments on international labor and the WTO negotiations. Our initial soundings suggest this will be a tough challenge this year.

<u>Launching a New WTO Round:</u> The President announced the launch of a new Round at the Seattle WTO ministerial we will host in December. This will provide an opportunity to set ambitious objectives to open foreign agricultural and services markets as well as to advance some of our "new consensus" issues, such as labor and the environment. However, many of our foreign partners will pursue opposing agendas and the ministerial

will no doubt serve as a target for NGOs and others.

China WTO Accession/MFN: This issue is both an opportunity and a challenge. We have the opportunity to conclude a WTO accession agreement with China in the run-up to Premier Zhu's visit to the United States on April 8. Such an agreement would be applauded by the multinational segment of our business and agricultural communities and would undoubtedly bolster our bilateral relationship. However, the agreement and the associated need to pursue permanent MFN will run into strong opposition from the right and the left on the Hill and organized labor has already signaled strong concerns.

Proposal for Enhanced CBI Legislation: On March 4, we transmitted to Congress enhanced CBI legislation that would provide Caribbean and Central American countries with duty-free and quota-free access for apparel made from US fabric. This legislation is likely to have greater support than in the past in the wake of Hurricane Mitch, but nonetheless is regarded negatively by organized labor and key House Democrats as evidence of our "same-old" approach to trade.

Promoting Africa Growth and Opportunity Act: This legislation is a centerpiece of the President's Africa Economic initiative and is a strong priority for Rep. Rangel. The bill would allow for duty-free and quota-free treatment of textile and apparel from African countries strongly committed to economic reform and respectful of human rights. Although it passed comfortably in the House last year, it was opposed by the Textiles Caucus. This year, Representative Jesse Jackson, Jr. has proposed an alternative that will be preferred by Textile Caucus members. On the Senate side, the Africa bill will not move unless it is wrapped up in an Omnibus trade bill.

New Arm at the ILO to Strengthen International Labor Standards: We are working with the AFL and others to design and fund a new program at the ILO that would provide assistance to developing countries to enforce core labor standards such as collective bargaining. We will seek appropriations of $25 million for the ILO and $5 million for DOL to advance this initiative. In addition, we will attempt to get G-7/8 support for this initiative at the Summit in Koln.

B. ***Possible Presidential Actions***

White House Conference or Presidential Speech on the New Consensus on Trade. The President could give a speech at a business where jobs are dependent on exports on the "new consensus," i.e., improving the connection between trade negotiations and broad based progress in living standards. It could include: a framework of trade principles developed with House Dems; international labor initiatives in the FY 2000 budget; any WTO accomplishments on trade and the environment; and success as a result of the Uruguay Round, NAFTA, and 1997-8 fast track consideration. Alternatively, we could bring together business leaders, agricultural representatives, labor and NGOs to meet with the President and Vice-President to flesh out what it means to put a human face on trade (i.e., improving the connection between trade negotiations and broad-based progress in living standards). *Timing: Early April before a trade authority bill is passed or taken up by Senate Finance as part of a Omnibus trade bill.*

Speech at ILO and Adoption of ILO Child Labor Convention: The President could deliver a speech at the annual ILO ministerial in Geneva to detail his agenda on international labor standards and child labor. He would be the first President to do so. At that time, he could express strong U.S. support -- or even promise to seek ratification of -- the new ILO convention on the most abusive forms of child labor. Whether or not he goes depends in large part on what the convention says. We are working in negotiations to make it consistent with U.S. law, but we can not be sure because of some real problems exist. *Timing: June 17 -- the day before the G-7/8 Summit in Germany.*

Presidential Statement for Opening of WTO High-Level Meeting on Trade and Environment. The President could make a statement that could be read by WTO DG Ruggiero at the opening session of this first-ever high-level meeting of trade and environmental officials, which POTUS called for at Geneva. It would emphasize the President's commitment to put in place a process that ensures sustainable development, one of fundamental mandates of WTO, becomes a priority; cite progress on transparency/accountability agenda that the President laid out at Geneva; announce our intention to include important new initiative in WTO Round negotiations to eliminate environmentally harmful subsidies in agriculture and other industries, and announce U.S. commitment to do environmental review of WTO Round & encourage other countries to do the same. *Timing: Monday, March 15!!*

Speech at Africa Partnership Forum: The President should highlight his commitment to passage of the Africa trade bill in his speech at the opening plenary of the Africa Partnership Forum. This would help garner support, which appears to be waning. *Timing: March 16*

WTO Ministerial Meeting. The President should give a speech in advance of and/or at the ministerial announcing "early harvest" results on electronic commerce, sectoral liberalization and transparency/accountability and laying out US negotiating agenda. The timing and feasibility of such an event will depend on the success of our international negotiations in the lead-up to the ministerial. *Timing: March through April 4*

C. *Republican Agenda and Likely Response*

Trade Authority: The Senate Finance Committee is planning to take up an omnibus trade bill before House Ways and Means acts, possibly in April. Chairman Roth has indicated a desire to modify last year's bill in order to make it more attractive to House Democrats; however, he is attempting to build a constituency for such changes in the business community before he issues his proposal. Chairman Archer, on the other hand, has yet to signal flexibility.

CBI: To date, the Republicans have introduced alternative bills both in the Senate and in the House. Crane's bill endorsed by Rangel provides for similar benefits but includes a provision for including regional fabric and strict transhipment enforcement. With respect to the Graham bill, the differences lie in the time period of the benefits and in the conditionality.

Africa: At this time, the Administration and congressional sponsors have been unable to locate a Republican champion in the Senate.

D. *Timing and Strategy*

Trade Authority. Our strategy is to engage House Democrats and Labor before attempting to enlist the support of Senate Finance Committee Democrats to influence the Roth bill. Senator Moynihan and other Finance Democrats are strongly committed to fast track; however, they are more prepared than last Congress to help us move Committee Republicans in our direction. Our goal is to get as much as we can out of Sen. Finance at the same time that we build confidence among House Dems. in two stages --- I) issue in April a framework of principles that embodies most of the concepts House Democrats are concerned about in the trade debate; and ii) develop specific new policy initiatives in these same areas for issuance in the run up to House consideration of the bill. These policy initiatives could include modifications to legislative language within the fast track bill as well as a series of complementary undertakings on labor, environment, debt and development, adjustment assistance, and the border economy in other areas of US international economic policy.

Africa. The Crane/Rangel bill has not been scheduled for House Ways and Means full committee mark-up. Our strategy is to work to reach consensus on an acceptable House bill if necessary, but maintain public for the Rangel legislation. Subsequently, we will then move to negotiate the controversial provisions (e.g., textiles, eligibility and transshipment) to shape a bill that will pass when it gets wrapped up into an Omnibus bill in the Senate. *Timing: April 4 to May 31*

IV. REFORMING THE INTERNATIONAL FINANCIAL ARCHITECTURE. Continue to work with the G-7 and others to advance a set of concrete, sensible reforms to the international financial architecture.

A. *Specific Agenda Items*

New Debt Policy. Treasury is working up a set of proposals to accelerate the timing and expand the scope of developing country debt forgiveness. Other G-7 members, such as Germany, the UK and France, have already announced a series of general proposals, many of which track previous US suggestions. The goal is to have significant new initiatives for the leaders to announce at the Cologne summit in June. The proposals are likely to focus on an expansion of debt relief extended by the international financial institutions; however, this will require identification of new ways to pay for the debt relief -- an issue that has not yet been resolved.

New Social Safety Net Policy. G-7 countries are discussing ways to encourage the implementation of better social safety net policies in developing countries, particularly those hit hard by the world financial crisis. An internationally accepted set of best practices or principles would be established to guide the policies of poor countries and the lending practices of MDBs. In addition, the need for crisis-stricken countries to protect budgets for social programs would be emphasized in IMF and World Bank programs.

G-7/8 Reform Agenda on International Financial Architecture: We continue work with the G-7 and in other fora to advance a set of concrete, sensible reforms to the international financial architecture. While the French and Germans have floated several specific ideas in that context (enhanced role for the IFC Interim Committee and target zones for exchange rates, both of which we propose), Treasury continues to do the real heavy lifting on systematically developing, analyzing and refining options. While the G-7 Finance Ministers did announce progress on a number of measures at their February meetings in Bonn, much work remains to be done. We are pushing to have made significant progress against the overall architecture agenda for announcement by POTUS and other leaders at G-7/8 Summit June 18 in Cologne.

B. *Possible Presidential Actions*

Speech at Africa Economic Conference to Roll Out New Debt Policy. There may be an opportunity to articulate US policy on enhanced debt relief at the Africa forum. Treasury is working on a set of policy options, which will be reviewed by a rump group of Deputies on March 12. At a minimum, the we ought to be in a position to articulate broad intentions as the UK and Germany have already done this year. *Timing: March 16*

Speech on Architecture at "Seminar" with Emerging Markets: A group of 33 industrial and emerging-market countries will meet in Germany on March 11 to discuss and provide input on questions of exchange rate regimes, responding to financial crises and strengthening the IMF and World Bank. These same countries will meet again in Washington in late April to discuss financial supervision and regulation, and ideas for shoring up social safety nets. This second meeting may provide an occasion for a Presidential speech on the topic of architectural reform, although this may be premature given the state of progress against individual reform initiatives. We will monitor progress as the date gets nearer. *Timing: April 25-26*

Speech on Architecture at World Bank/IMF meetings in April: The semi-Annual meetings of the World Bank and IMF in April may provide a similar opportunity for the President to address issues related to financial architecture reform. Again, much will depend on the state of progress against those reforms by that time. *Timing: April 27-28*

Speech on Financial Architecture at G-7/8 Summit in Cologne: The Summit will specifically take up the issue of financial architecture reform, and a Presidential speech at or around the time of the Summit will serve to highlight his continued leadership in this area. President Chirac is keen to claim some share of that leadership (although the French have contributed little of substance). We may need to finesse the timing of any POTUS address to forestall that claim. *Timing: June 18*

Speech Previewing Social Safety Net Outcomes of G-7. The President could choose to focus on social safety net issues in advance of the G-7 meeting. He could highlight the FY 2000 budget proposal providing $9.5 million to the Department of Labor to assist the many countries that have requested help in the design and implementation of unemployment, pension, health and other benefit programs. And he could give a US imprimatur to the efforts of World Bank President Wolfenson to devote more resources to this problem. *Timing: mid May*

UPCOMING CHALLENGES REQUIRING ADMINISTRATION RESPONSE

Tax Day on April 15. The Hill Republicans will hit us in the week leading up to tax day. This pattern has been played out in a similar patter for the last several years.

A. *Timing.* As occurs each year, the Hill Republicans will unleash a misleading attack on the Administration's record on taxes on the days leading up to April 15.

B. *Responses.* We plan to work with Treasury and others to develop a plan to address this shortly.

C. *Presidential Action.* It is unlikely that any Presidential action will be required.

Electricity Restructuring. Under electricity restructuring, state regulated utilities would no longer have the exclusive right to sell electricity in their geographic territories. Instead, consumers could purchase electricity from any generator that served their market, just as they currently choose their long distance telephone carrier. The bill is expected to generate $20 billion of savings and to provide important environmental benefits.

A. *Timing.* On March 18th the Department of Energy plans to submit a revised electricity restructuring bill to Congress.

B. *Responses.* Current plans are for Secretary Richardson to host an event on the steps of the Capital at which he presents the bill to Congress.

C. *Presidential Action.* We will likely not seek any Presidential or Vice Presidential action when we submit the revised legislation.

China MFN Renewal/Permanent MFN. We will face one or two MFN battles this year with Congress: annual MFN renewal and/or Congressional approval of permanent MFN for China in the wake of a China WTO deal. The first will be bruising, the second monumental, given the state of broader U.S.-China relations and the congressional and political dimensions. If China is unable to conclude its WTO negotiations with all nations until later this summer, we could be forced to vote on China twice this year because the annual MFN vote must take place by the August recess.

A. *Timing.* The President must notify Congress of his intent to renew MFN by June 3. Congress has 90 days to pass a joint resolution of disapproval. If China enters the WTO, we must pass legislation graduating China from the annual Jackson-Vanik requirement, or we will be out of compliance with our WTO obligations.

B. *Responses:* NSC, NEC, COS, State and USTR will work closely to develop a strategy for MFN renewal. If we get a WTO deal with China, Principals will need to decide whether we seek legislation to graduate China from Jackson-Vanik annual review requirements.

C. ***Presidential Action.*** We will use Premier Zhu's visit to seek to conclude a WTO deal bilaterally with China, and to advance other aspects of relationship. We will leverage that toward MFN renewal and potentially permanent MFN.

Stopping Unfairly Traded Steel and Strengthening Our Trade Laws: Unless we convincingly address the steel crisis, our overall trade agenda will be stymied this year. We have taken tough actions under our trade laws, which are beginning to show results, but many allege it took too long. A Visclosky quota bill is now moving rapidly through the House with bipartisan support. We are working on an alternative approach with Sandy Levin that aims to strengthen our trade laws but in a WTO-consistent manner. This or a similar approach may ultimately be incorporated in an Omnibus Trade Bill in the Senate.

A. ***Timing.*** The Visclosky quota bill will be voted on the week of March 14. The timing of Sen. Levin's bill is unclear. Prospects in the Senate are also unclear.

B. ***Responses.*** We are actively working with Levin and Gephardt on the Levin proposal which may gain broader support in House or Senate.

C. ***Presidential Action.*** We should continue to issue strong statements about vigorous enforcement of our trade laws and the need for our trading partners to play by the rules. Furthermore, at the right time, we should come out strongly and publicly in support of steel trade legislation we can live with that includes WTO consistent change to Section 201 injury standard.

Bankruptcy. The House is starting from a bill over which we threatened a veto last year, while the Senate is currently making some changes to gain bipartisan support for the legislation. However, even the Senate version is likely to be inadequate.

A. ***Timing.*** There could be markup in the Senate as soon as next week.

B. ***Responses.*** We are currently working with Legislative Affairs and the First Lady's office on our Hill strategy.

C. ***Presidential Action.*** We will reiterate the major changes we need to see to support bankruptcy legislation. If necessary, we will issue veto threats again.

Y2K Liability. The industry-developed consensus bill has stalled in the Senate as of now with some recognition on the Hill that it goes too far. Sen. Hatch is seeking cooperation in negotiating a bipartisan approach.

A. *Timing.* Negotiations are ongoing, and the bill is scheduled to go to the Senate floor on April 12.

B. *Responses.* We remain unconvinced that a bipartisan approach is necessary, since we would recommend a veto of the bill in its current form. We are working with the Democrats currently to move ahead.

C. *Presidential Action.* Nothing foreseeable at this time.

Class Actions. In addition to Y2K, this is the primary goal of the tort reform coalition. Last year, we had Attorney General Reno issue a veto recommendation statement.

A. *Timing.* Uncertain

B. *Responses.* We are working on more effective briefing materials now to make clear that the bill does not do what its supporters advertise.

C. *Presidential Action.* Nothing foreseeable at this time.

Financial Modernization. We are working to ensure that we can beat back any effort by Sen. Gramm and others to undermine CRA in any Financial Modernization legislation.

A. *Timing.* The Banking Committees will be marking this up soon.

B. *Responses.* If Sen. Gramm's bill moves to the floor in its current form, we will work with Treasury to reiterate the Presidential veto threat and try to promote a product in the House that the President could enthusiastically support.

C. *Presidential Action.* We may again issue veto threat.

EXECUTIVE AND OTHER NON-LEGISLATIVE ACTIONS

I. Protecting Consumers

Co: sumer Financial Right to Know. ***This is ready to go***, and we are working on how to package it together and which pieces to highlight. The thrust of the initiative is that, while innovation and technology have created great new opportunities for consumers, they also have created new challenges and opportunities for abuse. The plan contains both administrative and legislative proposals focused in five areas: disclosure/right-to-know (in credit card, banking, and other services); protection against fraud; financial privacy; expanding access to financial services; and consumer financial education. *Timing: Possibly March 25 in Cincinnati*

Promoting a "Passenger Bill of Rights". We have been working with DOT to draft the "Airline Consumer Protection Plan Act." There is significant interest in this issue on the Hill, as Sen. McCain and Rep. Shuster are both holding hearings on the subject during the week of March 8. The Vice President will announce the Administration's support of the Act in the short-term (on March 10) and then have the President conduct a larger event on the issue some time in the next several months. *Timing: March-May*

II. Building the New Economy and Advancing Technology

White House Conference on the New Economy. We could bring together top economists to meet with the President and Vice President on this issue. High profile panelists such as Alan Greenspan and a substantive discussion of major, cutting edge issues would ensure significant press coverage. Topics could include the impact of information technology on productivity, the business cycle, and inflation; the changing relationship between unemployment and inflation; and the changing relationship between regulation and international trade. *Timing: May-July*

Research Funding in a Post-Cold War World. Although there is strong support for biomedical research, there is little public or congressional understanding of the importance of investing in other research areas, such as physical sciences and engineering. In the past, DOD conducted much of the research in this area, but it has been cutting back on long-term research for the last ten years. The Administration needs to define and fund a set of research challenges for the 21st century (e.g., sustainable development) and the President could do so, just as he did at the MIT commencement in June 1998 in the context of the information revolution.

E-Society Initiative. In 1997, the Administration pulled together a set of public policy activities under the umbrella of "e-commerce." We believe that there is a value to organizing a similar effort on the social benefits and dimensions of the Information

Revolution. By launching an "e-society" initiative, the President and Vice President can continue to reinforce the message that the Information Revolution is not just about commerce, it is also about enabling Americans with disabilities to lead more independent lives, improving the way we educate our children, allowing adults to acquire new skills at a time, place and pace that is convenient for them, making government more open, efficient, and responsive, and expanding access to quality health care in rural communities. The Administration's budget makes significant contributions in this direction. We could potentially issue an Executive Order -- like the e-commerce EO -- to delegate the Administration's e-society agenda to the appropriate government agencies.

III. International Economic Issues

Child Labor. The President and Senator Harkin could hold an event to focus attention on international child labor, which would include: (1) a new executive order banning procurement of goods made with child labor (memo to Podesta for approval to be sent shortly; executive order in final clearance); (2) the DoL annual report of child labor; (3) unveiling the Administration's plan for use of $30 million IPEC Child Labor funds in FY 99; (4) arguing for continuing that level of IPEC funding in FY 2000; and (5) promoting the Administration's new $10 million program through USAID on changes to educational systems to prevent Child Labor.

Meet with Ex-Im and OPIC to Promote Manufacturing Exports. The President and Vice President could sit down with Jim Harmon at Export-Import Bank and George Munoz of OPIC to discuss everything that the two agencies are doing to address the global economic situation and to promote our initiative to boost manufacturing exports.

Announce Renewal of Super 301 By Executive Order. Super 301 enables us to take unilateral action against a country engaging in unfair trade practices that harm our exporters. In Senate testimony last month, Barshefsky announced our intention to renew this authority. The President could make a statement when he issues the executive order asserting our commitment to making sure countries play by the rules of international trade. We could try to time our announcement to coincide with the initiation or conclusion of a trade case. *Timing: (ck)*

Executive Order on Sanction Policy. The President could announce an Executive Order promising self-restraint on the imposition of economic sanctions under executive authority. This would be welcomed by the business and agriculture communities and could be used in a broader deal for similar self-restraint by Congress. We are currently working with Dodd and Lugar in the Senate and with Dooley in the House on such legislation. *Timing: (ck)*

Promoting a Southwest Borders Initiative. We could hold an event in Texas or California to announce initiatives to improve the economic hardships faced by the border regions and to fend off NAFTA criticism. *Timing: late 1999*

Agricultural Trade Policy Presidential announcement on elements of Agricultural trade policy (e.g., negotiating position for WTO, possible Section 301 for agriculture). *Timing: Summer*

APEC The President will give a speech at the APEC Leaders meeting on September 12-13 in Auckland, New Zealand, announcing the results of APEC's tariff elimination agreement and US efforts on e-commerce and information technology trade. *Timing: September 12-13*

IV. Other Initiatives and Announcements

Long-Term Care Study. We are working with HHS on pulling together information on state-by-states and women and long-term care.

IRS Oversight Board. The members of the IRS Oversight Board are almost ready to be announced (the President has the memo). This could be a good opportunity to highlight IRS reform efforts and showcase a solid board, while including members of Congress from both parties. *Timing: mid March-April*

Domestic Agricultural Labor Laws. We *may* have an announcement about new policy on domestic agricultural labor laws -- but we probably want to spend a few months making the case that there is a problem, before we suggest the solution. Labor is working on a plan. This will certainly not be ready until at least May -- and could be later. *Timing: May-July*

V. Upcoming Economic Releases that May Provide Message Opportunities

March 5	Employment Situation
March 18	International Trade
March 25 (ck)	Steel Imports
March 19	Treasury Monthly Budget
March 31	GDP (Q4--Revised)
April 1	Personal Incomes
April 2	Employment Situation
April 18	International Trade
April 21	Homeownership Numbers (Q1)
	Treasury Monthly Budget
April 25 (ck)	Steel Imports
April 29	Employment Cost Index
April 30	GDP (Q1)

March 11, 1999

TO: Gene

FROM: Jeanne

RE: MEDICARE COMMISSION: URGENT

Attached is a draft document from Laura Tyson -- she described it as a draft recommendation that could gain the support of the Commission for a positive vote. She sent it to Chris and I with a request for comments. After a quick read, it looks like it offers options -- without a strong opinion -- on financing, and some of the other critical issues (e.g., prescription drugs, age eligibility increase). It reads more like a Commission staff options paper. Chris and I will be working on a detailed set of comments tonight, but strongly recommend that you (a) read it yourself; (b) advise us how to proceed strategically as well as substantively; and (c) let us know whether you want to be on a call with Laura tomorrow to discuss this.

Also, we got calls from Daschle's office urgently requesting a detailed briefing on the President's surplus proposal for Medicare. In the wake of the Finance Committee hearing, there is a need for additional time / information for the Democratic staff. Apparently, the Senate Budget Committee is planning a hearing or mark-up on Thursday so that they want this briefing on Monday or Tuesday at the latest. I got a similar call from the House Budget Committee -- they, too, would really like help in how to defend this proposal. Chris thinks that you should do these briefings, unless you want to spend time with him so that he thoroughly understands the details of the transfer. Please advise.

Finally, I am not sure that you got a chance to review the agenda for the principals' meeting since we finished it late (attached). We would appreciate your comments / input.

Thanks.

P.S. Commission meeting officially scheduled for 3/16 at 5pm.

Tyson Draft of Statement by Medicare Commission

I. Commission Agreement on the Problems Confronting the Medicare Program

A majority of the Commission members agree that the Medicare program has four distinct problems:

Adequacy of benefits: The benefits package for Medicare was designed in 1965 to realize Medicare's basic goal—namely to provide the elderly and later the disabled with health insurance coverage similar in scope, quality and structure to that available to employed persons and their families. Consistent with this goal, the Medicare package was structured as a indemnity, fee for service insurance program covering payment for a specified list of benefits to any licensed provider choosing to provide them. Since 1965, there have been dramatic changes in both the practice of medicine and in the insurance industry, as a result of which there have been growing gaps between Medicare and the insurance programs available to the rest of the population. Employer-sponsored plans and even individual insurance products have rapidly moved from fee for service to capitated structures using closed panels of providers and management of care. Moreover, as a result of changes in the private insurance market, the average benefit packages provided by employers, by other public programs, including Medicaid, and by individual insurance options today include some prescription drug coverage, some catastrophic coverage, and even some preventive coverage, none of which are adequately provided by Medicare. In addition, Medicare deductibles and co-pays for inpatient hospital services are far higher than those for private insurance plans.

A majority of the Commission members agree that the current Medicare benefits package is no longer adequate to cover the health care needs of the elderly in ways that are consistent with the scope, quality and structure of insurance available to the rest of the population.

Inequity: As a result of the gaps in Medicare benefits, beneficiaries are exposed to large out-of-pocket expenses. Such expenses impose a much greater burden on low-income individuals than on high-income individuals. The access of many elderly Americans to necessary medical care is limited by their income, and poorer households are forced to devote a much larger fraction of their income to health spending than are richer ones.

Recognition of the financial burden of the original Medicare system on poorer beneficiaries is the reason behind the development of low-income protection programs of Medicaid—QMBs and SLMBs—to help such individuals cover their Medicare premiums, co-pays and deductibles and to provide limited coverage for prescription drugs. Participation in these programs has been limited to those with incomes below % of poverty, and participation by those eligible has been incomplete and variable across states. Thus, it is not surprising that a recent article in the New England Journal of Medicine found that even with these protections, inadequate coverage for costly drug prescriptions for low-income elderly and disabled remains a serious problem in our health care system. In addition, even with these protections, many low and moderate income participants remain exposed to large out-of-pocket expenses as a result of gaps in Medicare's benefits package.

Inefficiencies: (THIS SECTION IS CURRENTLY WRITTEN IN OUTLINE FORM ONLY—MORE WORK IS NEEDED)

The Medicare system has several features which reduce the incentives for efficiency by both beneficiaries and providers. Basic source of inefficiency—Medicare controls costs by setting prices of services covered in its standards benefits package. Several predictable results of this price-control approach: need to establish and revise huge list of allowable prices to keep up with practice of medicine; tendency of providers to encourage greater utilization of benefits to make up for their controlled prices; no or weak incentives on part of consumers to limit intensity of use; tendency to fraud in documentation of use—provider to be paid if service is performed, so provide evidence of service even when it has not occurred. Evidence of inefficiencies in system—from large regional differences that cannot be explained by differences in cost of providing the services—but differences in practice of medicine and intensity of services—more providers, more equipment, more utilization and expense per beneficiary by a factor or four.

Limitations on HCFA flexibility and reform; politics blocks competitive bidding; inability to reduce provider payments, to weed out unscrupulous providers and to restrict provider participation because of political pressures.

A majority of the Commission agrees that the efficiency of the Medicare program can and should be improved and that enhanced competition will foster this goal. At the same time, the majority of the Commission recognizes that the magnitude of the savings from greater efficiency is uncertain and that even under the most optimistic evidence currently available, realistic improvements in program efficiency by themselves will reduce but not eliminate Medicare's future financing difficulties.

Financing Needs and Program Solvency: Under current law, in the year 2000, total Medicare spending will equal $274 billion or 12% of federal spending and will be paid for by beneficiary premiums ($25 billion or 10% of the total); payroll taxes ($130 billion or 53% of the total) and general revenues ($92 billion or 37% of the total). By 2010, assuming no change in law and an annual growth rate of 7.6% (with demographics accounting for annual growth of about 4%), Medicare spending is projected to rise to $ billion or 16% of total federal spending. In that year, beneficiary premiums will account for 13%, payroll taxes for 38% and general revenues for 49% of total Medicare spending. Without changes in current law, Medicare spending will continue to rise as a share of total federal spending and general revenues will continue to rise as a share of Medicare's total financing needs through 2030, the year the Commission chose as the ending point for its projections. In 2030, Medicare spending will hit % of total federal spending, and general revenues will account for % of Medicare's total financing needs.

A majority of the Commission agrees that the Medicare program as currently structured faces substantial long-term financing difficulties, indicated by the projected insolvency of the Part A Trust Fund in (year) and by increasing program reliance on general revenues for financing.

II. Commission Agreement on the Concept of a Premium Support Approach for Restructuring Medicare

To the extent that Medicare dollars can be spent more efficiently, it will be easier to address the other problems confronting Medicare—the inadequacy of the Medicare benefits package, inequities in the access of the elderly to necessary medical services based on income, and Medicare's long-term financing needs. Savings from greater efficiency can be used to expand benefits, to increase low-income protections; and to cover projected gaps in Medicare financing. So regardless of differences among Commission members on both the extent of these other problems and the appropriate remedies for them, a majority of the Commission agrees that Medicare should be restructured in ways that will encourage more efficiency both in the HCFA fee for service program and in any other private plans that are allowed to compete with HCFA to provide Medicare services.

After hearing from a variety of experts, a majority of the Commission members agree that there are two promising approaches for enhancing the efficiency of the overall Medicare program:

first, giving HCFA both the responsibility and the statutory authority it needs to adopt management innovations developed in private health plans including flexible purchasing authority, competitive bidding, negotiated pricing authority, selective contracting for preferred providers and disease and case management techniques. In return for granting greater discretion to HCFA in managing FFS Medicare, Congress should hold HCFA to a higher standard of accountability and reporting requirements for cost and quality outcomes;

and second, allowing private plans to compete with one another and with the FFS Medicare program operated by HCFA for Medicare dollars on the basis of price and quality of service.

Based on these findings, a majority of the Commission members recommend that both of these approaches be adopted. In particular, we recommend that Medicare be restructured to allow beneficiaries to choose between a modernized fee-for service program operated by HCFA and a variety of competing private health care plans. The Medicare program would make a contribution toward the payment of the premium of the plan chosen by each Medicare beneficiary, with the remainder of the premium paid by the beneficiary. This contribution would be calculated as a certain percentage, established by law, of the weighted average of all of the plans, including the HCFA FFS plan, competing for Medicare beneficiaries. The Medicare contribution would not be set in dollar amounts—that is, Medicare would not operate as a defined contribution program—but would be set as a percentage of the weighted average of the costs of all plans certified to compete for Medicare beneficiaries. Increases in these costs over time would result in increases in both Medicare's premium contributions and the premiums paid by Medicare beneficiaries.

Under this formulation, Medicare would continue to operate under an open-ended federal spending commitment, but the risks and burdens of increases in the costs of services covered by Medicare would be automatically shared by a set percentage between Medicare and its beneficiaries. This percentage should be set at a level which provides a government contribution that is sufficiently large to assure that an adequate benefits package is available and affordable to all beneficiaries regardless of income, health status, or geographic location. Over time, both the government's premium contribution and the beneficiaries' premium payment would be expected to increase at about the same pace as the costs of overall health services to the general population.

All plans competing for Medicare beneficiaries would be required to offer at least the same standard defined benefits package as the HCFA fee-for-service plan, and this package would be established by law. In addition, both the HCFA FFS plan and the competing private plans would be required to offer a supplemental defined drugs benefit package, also established by law. The standardization of defined benefits across plans is necessary to encourage plans to compete on price and efficiency, rather than on benefits, and to reduce the likelihood of biased selection whereby less generous plans would compete to attract the healthiest beneficiaries, driving up the price of the plans available to the sickest and neediest ones. The dangers of risk selection are significant as evidenced by the experience of the Federal Employees Health Benefits Plan and Medicare's experience with HMOs; moreover, such dangers are especially strong among the elderly because of dramatic differences in the risk profiles of individuals as they age. The predictable costs of treating Medicare beneficiaries varies greatly—from a few hundred dollars per year for the healthiest beneficiaries to tens of thousands of dollars per year for those with certain chronic conditions. Although in theory effective risk adjustment techniques should be able to control such risk selection problems among plans, such techniques currently exist only in rudimentary form. If and when such techniques develop, it would be possible to allow some limited variation in the standard benefits and prescription drugs packages required by law within specified actuarial ranges. In addition, all plans, including the HCFA fee-for-service plan, could be allowed to offer supplemental packages the purchase of which would not be tied in any way to the purchase of the standard benefits packages required by law and the full price of which would be paid by the Medicare beneficiary.

The approach to restructuring the Medicare system recommended by the majority of Commission members has come to be known as a "premium support" approach in the health care literature, and many of its features bear a strong resemblance to those of the Federal Employees Health Benefit Program. A premium support approach is not a defined contribution approach under which Medicare would provide to each beneficiary a fixed dollar amount that could be used to obtain coverage from approved plans with no mandated benefits package. In contrast, under a premium support approach, each approved plan would be mandated to offer a common standards benefits package and a common prescription drug benefits package, and Medicare would provide to each beneficiary a contribution toward the premium of the approved plans, with the size of the premium reflecting the weighted average of the premiums bid by participating plans, including the HCFA fee for service plan.

Recent studies by health care experts along with the recent experience of some premium-support type programs, like FEHP, suggest that a premium support approach for Medicare could lead to a reduction in the projected increases in the cost of the Medicare program for both the government and beneficiaries. But it is necessary to be cautious about projecting substantial cost savings from restructuring Medicare into a premium support system. As the last five years have indicated, rapid changes in medical delivery systems and technology make it unwise to predict precisely where health care costs will be in five years, let alone in the more distant future. Although it is certainly reasonable to expect that on average Medicare spending per capita should track private health care spending per capita over the next thirty years as it has during the past thirty years, there is considerable uncertainty about the course of the latter. As a result of the confluence of several factors--including the aging of the population, continued technological progress in health care, and growing per capita incomes (as people become richer their spending on health care tends to increase as a share of their income)--per capita spending on health care for both the elderly and the rest of the population will almost certainty continue to grow considerably more rapidly than the overall economy—a trend which can at best be moderated but not reversed by greater efficiency realized through enhanced competition in both the Medicare system and the rest of the health care system.

Given real uncertainties in future costs, Medicare's restructuring into a premium support system requires that adequate safeguards be included to assure that unexpected developments do not have adverse consequences for beneficiaries, many of whom suffer from low incomes, chronic illnesses, and/or disabilities. Such safeguards must include a government premium rate that is high enough, along with appropriate risk adjusters, geographic adjusters, low-income protections, and strong oversight authority by an independent Medicare Board (described below), to guarantee the availability and affordability of a common standard Medicare benefits package to all beneficiaries regardless of their income or geographic location. Finally, because no safeguards mechanism can be designed to foresee all eventualities, the Medicare Board should be charged with the responsibility of providing annual reports to the Congress and the Administration, comparing Medicare's actual performance with its predicted performance, and making recommendations for changes in the Medicare system, so that it continues to honor this guarantee.

III., Particulars of a Premium Support Approach for Medicare

NOTE: WE HAVE YET TO DETERMINE WHICH OF THESE PARTICULARS HAVE MAJORITY SUPPORT AND WHICH DO NOT—I DO NOT THINK THAT ALL OF THEM WILL HAVE MAJORITY SUPPORT IN OUR FINAL REPORT

The Medicare Board: The proposed restructuring of Medicare to a premium support approach would require the establishment of a new institution—a so-called Medicare Board--charged with several responsibilities including: providing beneficiaries with information about approved plans; computing Medicare and beneficiary premiums to be paid to approved plans based on the weighted average of the bids received from such plans; and approving and negotiating with plans about their service areas and benefits packages design. The Board would operate under strict fiduciary responsibilities and would be required to submit a detailed annual report on its operations to Congress and the Administration. The Board should be designed in such a way that it is composed of health care professionals who serve for limited terms, whose decisions are guided by independent professional considerations and once approved cannot be removed for political reasons.

The Benefits Package: (Saving Medicare Today and Tomorrow Language to be Agreed Upon—Need to Check Consistency with Language above on Drug Benefits)

The Formula for Determining the Premium Contributions of the Government and of Beneficiaries: Under current law, premium payments by Medicare beneficiaries account for about 12% of the total costs of providing the standard Medicare benefits package, with the remaining 88% covered by government revenues. Under a premium support model, the government would pay a specified percentage of the weighted average price of the HCFA FFS plan and the private plans authorized to bid to serve the Medicare population, with the remainder paid by the beneficiary. In the premium support approach, actual premium payments of beneficiaries would vary depending on differences between this weighted average price and the price of the plan they selected.

In the particular premium support approach estimated by Commission staff and recommended by members of the Commission, the government would be responsible for 88% of the weighted average bid and average premium payments by beneficiaries would continue to account for about 12% of total program costs. But beneficiaries would pay all of the additional premium for plans whose price exceeded the weighted average price of all plans and would pay no premium for plans whose price fell below the weighted average price of all plans. In this basic Commission model, beneficiary premium rates would not be income-related except for additional government support for beneficiaries under 135% of poverty (see below).

NEED TO ADD DISCUSSION OF PREMIUM FORMULA FOR DRUGS BENEFITS PACKAGE: MY PROPOSAL IS THAT BOTH HCFA FFS AND PRIVATE PLANS BE REQUIRED TO OFFER A STANDARDS DRUGS BENEFITS PACKAGE. THERE WOULD BE A PREMIUM BIDDING PROCESS FOR THIS PACKAGE SIMILAR TO THE PREMIUM BIDDING PROCESS FOR THE STANDARD BENEFITS PLAN. THE ONLY DIFFERENCE WOULD BE IN THE CONTRIBUTION RATE FOR GOVERNMENT AND BENEFICIARY. WE COULD NOTE THAT THE COMMISSION MAJORITY COULD NOT AGREE ON THE CONTRIBUTION RATE FOR GOVERNMENT AND EXPLAIN REASONS FOR DISAGREEMENT. STUART AND I WOULD RECOMMEND A SUBSIDY RATE OF AT LEAST 50% FOR TWO REASONS: FRIST, A 50% SUBSIDY RATE WOULD BE SUFFICIENT TO INDUCE THE VAST MAJORITY OF BENEFICIARIES TO ENROLL FOR THE DRUG BENEFIT—AND THIS IS NECESSARY TO AVOID RISK SELECTION PROBLEM—A LOWER SUBSIDY RATE WOULD WORSEN THE RISK POOL OF INDIVIDUALS OPTING FOR DRUG COVERAGE AND MAKE IT LESS EFFICIENT. AND SECOND, AT LEAST A 50%SUBSIDY RATE IS NECESSARY TO REALIZE THE GOAL OF MAKING THE DRUG BENEFIT AFFORDABLE FOR MEDICARE BENEFICIARIES.

DISCUSSION OF DRUG BENEFIT IN HCFA FFS PLAN WOULD ALSO INCLUDE CAVEAT THAT HCFA CONTRACTS WOULD BE BASED ON PRICES AND FORMULARIES AVAILABLE IN THE PRIVATE MARKET, WITHOUT RECOURSE TO PRICE CONTROLS OR REBATES.

Geographic Adjusters to the Formula for the Premium Contribution

THIS DISCUSSION WOULD BEGIN BY NOTING THE VERY LARGE REGIONAL DIFFERENCES IN CURRENT COSTS OF PROVIDING MEDICARE PACKAGE—FOUR TO ONE DIFFERENCES, ONLY THREE –QUARTERS OF WHICH CAN BY DIFFERENCES IN INPUT PRICES, ONE QUARTER OF WHICH IS RESULT OF DIFFERENCES IN INTENSITY OF USE AND PATTERNS OF MEDICAL PRACTICE. SUCH REGIONAL DIFFERENCES ARE ONE REASON WHY PREMIUM SUPPORT MODEL WILL NEED GEOGRAPHIC ADJUSTERS IF MODEL IS BASED ON A NATIONAL BIDDING PROCESS. A SECOND REASON FOR GEOGRAPHIC ADJUSTERS IS REALITY THAT THE EXTENT OF COMPETITION AMONG PROVIDERS IS NOT SAME ACROSS ALL REGIONS --IN PARTICULAR IN SOME RURAL COMMUNITIES THERE MAY BE VERY FEW IF ANY CHOICES AVAILABLE TO BENEFICIARIES OTHER THAN THE HCFA FFS PLAN.

THE MAJORITY OF THE COMMISSION RECOMMEDNING PREMIUM SUPPORT AGREES THAT INDIVIDUAL BENEFICIARIES SHOULD NOT HAVE TO PAY MORE FOR THE SAME MEDICARE PACKAGE BASED ON THEIR GEOGRAPHIC LOCATION. IN PARTICULAR BENEFICIARES SHOULD NOT HAVE TO PAY MORE FOR THE SAME PACKAGE OF SERVICES BECAUSE THEY LIVE IN A HIGH-COST REGION OR BECAUSE OF THE MARKET POWER OF PROVIDERS

AVAILABLE IN THEIR REGION. THEREFORE, THE PREMIUM SUPPORT MODEL WILL NEED A PROCESS TO ADJUST THE SIZE OF THE GOVERNMENT'S PREMIUM PAYMENTS FOR INDIVIDUAL BENEFICIARIES SO THEY ARE HELD HARMLESS AGAINST HIGHER PRICES IN THEIR REGIONS STEEMING FROM THESE TWO FACTORS. THE DEVELOPMENT OF SUCH GEOGRPAHIC ADJUSTERS FOR THE GOVERNMENT'S PREMIUM POSES A SERIOUS TECHNICAL CHALLENGE THAT WILL HAVE TO BE ADDRESSED FOR THE PREMIUM SUPPORT MODEL TO WORK FAIRLY. INITIALLY FOLLOWING THE CURRENT FORMUAL FOR REIMBURSING MEDICARE HMOS, ADJUSTERS WHICH OFFSET 100% OF COUNTY-LEVEL VARIATIONS COULD BE SET TO FULLY REFLECT DIFFERENCES IN INPUT PRICES, MARKET POWER AND LEVELS OF CARE IN EACH COUNTY. OVER TIME, THESE ADJUSTERS COULD BE MODIFIED TO ALLOW THAT PORTION OF THE DIFFERENCE IN COUNTY PRICES DUE TO DIFFERENCES IN UTILIZATION AND PRACTICE TO BE SHARED BY THE GOVERNMENT AND THE BENEFICIARY ACCORDING TO THE OVERALL FORMULA FOR DETERMINING THEIR PREMIUM CONTRIBUTIONS.

WHILE SOME REDUCTION IN GEOGRAPHIC VARIATIONS OF MEDICARE PRICES WOULD BE EFFICIENT AND EQUITABLE, THIS WOULD HAVE BE PHASED IN GRADUALLY. FOR EXAMPLE THE PREMIUM SUPPORT SYSTEM MIGHT BEGIN WITH 100% ADJUSTMENT OF COUNTY-LEVEL DIFFERENCES IN PRICE MOVING GRADUALLY TO 75% ADJUSTMENT OF SUCH DIFFERENCES ACCORDING TO AN AGREED UPON TIMETABLE.

Special Rural Adjustment Concerns

UNDER A PREMIUM SUPPORT MODEL IT IS POSSIBLE THAT AN INSUFFICIENT NUMBER OF PRIVATE PLANS WILL ENTER SOME RURAL AREAS TO PROVIDE EFFECTIVE COMPETITION FOR HCFA FFS MEDICARE. IF SO, IT IS ALSO POSSIBLE THAT PREMIUMS WILL RISE OR QUALITY WILL FALL AS THE TRADITIONAL PROGRAM USES HIGHER PROFITS IN NONCOMPETITIVE AREAS TO OFFSET LOWER PREMIUMS AND HIGHER COSTS OF CARE IN MORE COMPETITIVE AREAS. GIVING TRADITIONAL MEDICARE FLEXIBLE MODERNIZED MANAGEMENT AUTHORITY AND THE DISCRETION TO SET PREMIUMS IN THESE AREAS COULD CREATE AN UNREGULATED MONOPOLY. THUS IT MAY BE APPROPRIATE TO RESTRICT HCFA'S DISCRETION AND TON CONTINUE TO USE THE CURRENT ADMINISTERED PRICE SYSTEM UNDER CURRNET LAW IN NONCOMPETITIVE RURAL AREAS WITH NO OR FEW PRIVATE OPTIONS. BENEFICIARY PREMIUMS COULD BE BASED ON COSTS INCURRED IN THE ADMINISTERED PRICES SYTE, WHICH ARE GENERALLY LOWER IN RURAL AREAS, SO THAT BENEFICIARIERS IN THESE AREAS WOULD BE NO WORSE OFF THAN UNDER CURRENT LAW.

Risk Adjusters to the Formula for Premium Contributions

THE PREDICTABLE COSTS OF TREATING MEDICARE BENEFICIARIES VARIES GREATLY ACROSS INDIVIDUALS—FROM A FEW HUNDRED DOLLARS A YEAR FOR THE HEALTHIEST BENEFICIARIES TO TENS OF THOUSANDS OF DOLLARS PER YEAR FOR THOSE WITH CHRONIC CONDITIONS. UNDER THESE CIRCUMSTANCES, PLANS WHICH WERE PAID THE AVERAGE COST OF TREATMENT WOULD HAVE STRONG INCENTIVES TO SHUN SICKER ENROLLEES IN FAVOR OF HEALTHIER ONES. TO THE EXTENT THAT THIS OCCURRED, PLANS THAT MADE IT RELATIVELY EASY TO OBTAIN SERVICES WOULD ATTRACT SICKER BENEFICIARIES AND WOULD HAVE TO CHARGE HIGHER PREMIUM, DRIVING THEIR HEALTHIEST BENEFICIARIES TO LOWER-COST PLANS. IF HIGH-RISK BENEFICIARIES ARE CONCENTRATED IN HIGH-COST PLANS AS A RESULT OF THIS RISK SELECTION PROBLEM, THESE BENEFICIARIES WILL BE FORCED TO PAY INAPPROPRIATELY HIGH PREMIUMS BECAUSE OF THE HIGHER LEVEL OF RISK OF THE POPULATION SERVED BY THOSE PLANS. MOREOVER, THERE WOULD BE NO INCENTIVE FOR PLANS TO PROVIDE HIGH-QUALITY

CARE TO THE CHRONICALLY ILL OR OTHER BENEFICIARES SINCE SUCH A PLAN WOULD MERELY ATTRACT MORE OF THEM.

THE MAJORITY OF THE COMMISSION RECOMMENDING PREMIUM SUPPORT APPROACH RECOGNIZES THAT THESE RISK SELECTION PROBLEMS ARE SEVERE AND THAT TO AVOID THEM ADEQUATE RISK ADJUSTMENT IS REQUIRED. A RISK ADJUSTMENT MECHANISM WOULD ADJUST THE GOVERNMENT'S PREMIUM CONTRIBUTION TO PARTICULAR PLANS ON THE BASIS OF THE RISK CHARACTERISTICS OF THE INDIVIDUALS THEY ENROLL, BUT WOULD NOT AFFECT THE BENEFICIARY CONTRIBUTION. SPECIFICALLY, A RISK ADJUSTMENT FACTOR BASED ON BENEFICIARY CHARACTERISTICS WOULD ADJUST THE PREMIUM FOR EACH PLAN BASED ON ITS TYPICAL BENEFICIARY—AND THE GOVERNMENT WOULD PAY THE DIFFERENCE BETWEEN THIS ADJUSTED PREMIUM AND THE BENEFICIARY PREMIUM.

UNFORTUNATELY, WHILE THE PRINCIPLE BEHIND RISK ADJUSTMENT IS WELL UNDERSTOOD, RISK ADJUSTMENT MECHANISMS ARE STILL RUDIMENTARY. MOST EXPERTS, FOR EXAMPLE, AGREE THAT ONLY ABOUT ONE-QUARTER OF HEALTH CARE EXPENDITURES BY A MEDICARE BENEFICIARY ARE PREDICTABLE AT THE TIME OF ENROLLMENT. THUS IT IS UNLIKELY THAT RISK ADJUSTMENT WILL ELIMINATE THE POSSIBILITY OF SIGNIFICANT RISK SELECTION PROBLEMS IN A PREMIUM SUPPORT MODEL IN THE FORESEEABLE FUTURE. HOWEVER, A NUMBER OF OTHER FEATURES OF THE PREMIUM SUPPORT APPROACH COULD BE DESIGNED IN WAYS TO DISCOURAGE RISK SELECTION. THESE INCLUDE: ADHERENCE TO STRONG STANDARDIZATION OF THE BENEFITS PACKAGES OFFERED BY PARTICIPATING PLANS; MAINTENANCE OF A HIGH GOVERNMENT SHARING RATE IN THE OVERALL PREMIUM SO THAT BENEFICIARIES HAVE A WEAKER INCENTIVE TO CHOOSE LOW-COST PLANS; ENCOURAGEMENT OF POINT OF SERVICE OPTIONS THAT ARE ATTRACTIVE TO BOTH CHRONICALLY ILL AND WEALTHY BENEFICIARIES; AND UTILIZATION-BASED RISK ADJUSTMENT TECHNIQUES BY WHICH PREMIUM PAYMENTS ARE ADJUSTED IN PART BASED ON PAST OR CONCURRENT COSTS AND UTLIZATION RATHER THAN DIAGNOSES ALONE.

Tyson Draft: Solvency and Financing Language

As numerous reports from the HCFA Actuaries, the Congressional Budget Office, and independent experts indicate, even under optimistic assumptions about the efficiency gains that might be fostered by a premium support model, Medicare spending like health care spending in the private sector is projected to grow substantially faster than the overall economy. As illustrations of this conclusion, separate estimates by the Commission staff and the HCFA actuaries of the effects of the particular premium support model proposed by Senator Breaux, exclusive of a prescription drug benefit, indicate that even after anticipated efficiency savings, Medicare spending will continue to climb rapidly.

(Need Table showing predicted Medicare spending with Breaux premium support model in 2050, 2010, 2015, 2020, 2025,2030—not including other proposed changes—want estimate of pure efficiency effect alone—also for comparison need predicted Medicare spending)

A comparison between predicted Medicare spending under Breaux's premium support model without drugs and predicted revenues available to Medicare from both the payroll tax and general revenue transfers under current Medicare law indicates that even a restructured Medicare program faces a substantial and growing financing gap in the near future. Gradually adding the costs of a prescription drug benefit of the type supported by the majority of the Commission members increases the size of this financing gap significantly. (Table needed here—can use a range of drug cost estimates to show the effect of different government subsidy rates.)

The implication of these numbers is that even with a premium support approach Medicare will have to rely increasingly on general revenues. Additional changes in the Medicare program considered by the Commission and supported by some of its members, although not a majority of them, could reduce the financing gap. These changes include: income-relating the premium contribution made by beneficiaries regardless of whether they chose to enroll in HCFA FFS Medicare or one of the authorized private plans; gradually adjusting the age of eligibility for Medicare so it conforms with increases in the age of eligibility for Social Security; and excluding direct graduate medical education charges from Medicare spending. The Commission was unable to reach majority agreement on each of these proposals reflecting the reality that each of them has its own particular disadvantages.

Adjusting the premium contribution by income is a relatively easy formulaic adjustment in a premium support approach, but would be difficult to administer in practice. In addition, although there was agreement among Commission members that high-income beneficiaries could and should pay more for their Medicare coverage, there was disagreement about what level of income would place an elderly family in the "high-income" high-premium category. The lower the level decided upon, the smaller the financing gap confronting Medicare, but the greater the risk that middle rather than high income families would face higher premium contributions, thereby threatening the social insurance nature of Medicare and weakening political support for the program. Finally, a majority of the Commission agreed that any revenues earned from income-relating the Medicare premium should be used to finance an expansion of low-income protections, not to reduce overall Medicare spending, at least for the foreseeable future.

Raising the age of eligibility to conform with the age of eligibility for Social Security could reduce Medicare spending significantly in the future but it carries a real risk of leaving many older Americans without health insurance. Almost 1 in 8 Americans aged 62-64 today have no health insurance, and the number of uninsured Americans is growing most rapidly in the 55-65 age cohort. Lack of insurance coverage in the United States is a serious policy problem: raising the age of eligibility for Medicare would aggravate this problem unless this policy were accompanied by a fair buy-in program for those who were no longer eligible for Medicare.

Carving out funding for Direct Medical Education (DME) from the Medicare program would reduce projected spending. But this approach begs the question of how to guarantee teaching hospitals with the support they need not only to provide education and research in medicine but also to cover the cost of their treatment of difficult medical cases and uninsured patients.

Finally, even if all three of these approaches to reducing Medicare spending were adopted, Commission staff estimates of the Breaux premium support plan indicate that a substantial financing gap for Medicare would remain. Substantial additional funds from general revenues would be required, over and above those currently projected under current Medicare law, to guarantee the premium contribution rates for beneficiaries proposed in the Breaux plan (as noted above these rates are:—on average beneficiaries pay 12% of the premium costs for a standard benefits package, pay no premium for plans the cost of which is less than 85% of the national weighted average, and pay all additional amounts for plans the cost of which is greater than this average.) Without the infusion of such funds, either the shares of the total premium paid by beneficiaries would have to be increased or other changes in the proposed Breaux plan would have to be made to reduce Medicare's financing gap. Moreover, the inclusion of a drug benefit of the type recommended by the majority of the Commission would require an even larger infusion of general funds, a larger increase in premiums paid by beneficiaries, or some other offsetting change in the premium support plan.

Even among the majority of Commission members who recommend a premium support approach, there is disagreement on the best way to address Medicare's projected financing gap.

Two members of this majority support the idea that the Part A Trust Fund of the current Medicare program be replaced by a Unified Medicare Trust Fund consisting of the current Part A payroll tax plus the general revenues committed to Medicare under current law. This proposal recognizes that although the Part A Trust Fund concept would no longer make sense in a premium support approach, some kind of trust fund accounting is probably the most comprehensible way to illustrate Medicare's huge future liabilities. A Unified Trust Fund approach, like a Part A Trust Fund approach, reveals that under current law Medicare would become insolvent as early as (date). To address this impending insolvency problem while allowing for a gradual transition to a premium support approach that includes an affordable prescription drug package, these two members of the majority support the President's proposal to commit 15% of the projected surpluses in the general fund to Medicare over the next years. Because the interest earned on the surplus funds committed to Medicare would accrue to Medicare over time, the total cost of covering Medicare's projected financing gaps in this way would be considerably less than the total cost of covering the same gaps at the time they developed through general revenues.

The remaining members of the majority of the Commission who recommend a premium support approach recommend that Medicare solvency be assessed by examining the increasing shift of Medicare program costs to the general fund and the changing ratios of total Medicare financing borne by the general fund, by beneficiaries, and by the payroll tax. According to this proposal, when general revenues exceed 50% of total program outlays without further Congressional approval, there should be a public debate and decision about the financing of the Medicare program focused on potential adjustments in the payroll tax, beneficiary premiums, and the percentage of general funds to be allocated to Medicare.

MEDICARE COMMISSION PRINCIPALS' MEETING
Agenda: March 10, 1999

I. UPDATE ON THE MEDICARE COMMISSION

II. BASE MEDICARE POLICIES

III. ADDITIONAL MEDICARE POLICIES

- Drug Benefit
- Income-Related Premium
- Premium Support

BASE MEDICARE POLICIES

(Calendar Years, Dollars in Billions)

POLICIES:	2000-04	2000-09
Modernizing Medicare Fee-for-Service	-9	-22
Balanced Budget Act Extenders	-7	-57
Cost Sharing Changes	-1	+1
- Combined deductible of $350		
- Removing preventive services coinsurance		
- Adding 20% lab copay, limited 10% home heath copay		
Medigap: Prohibiting Deductible Coverage	-5	-11
Interactions	+1	+4
TOTAL	**-21**	**-85**
SURPLUS REVENUE	**+120**	**+343**

* These savings exclude the President's budget proposals whose savings are used for other purposes

PRESCRIPTION DRUG BENEFIT

OPTIONS:	2000-04	2000-09
Back-End Coverage (No Cap on Benefit)		
High Option	+84	+253
No cap on benefits, $3,000 stop-loss		
$300 deductible, 10% coinsurance		
Premium in 2002: $41.50		
Low Option	+58	+176
No cap on benefits, no stop-loss		
$500 deductible, 25% coinsurance		
Premium in 2002: $28.10		
Front-End Coverage (Cap on Benefit)		
High Option	+51	+141
$2,000 cap on benefits, no stop-loss		
$250 deductible, 20% coinsurance		
Premium in 2002: $28.40		
Low Option	+37	+101
$1,000 cap on benefits, no stop-loss		
$250 deductible, 10% coinsurance		
Premium in 2002: $20.30		

For all: Voluntary, 50% premium subsidy, implemented in 2001; for all beneficiaries

INCOME-RELATED PREMIUM

OPTIONS:	2000-04	2000-09
• Health Security Act Singles: $90,000 with full payment at $100,000 Couples: $110,000 with full payment at $125,000 Beneficiaries affected: About 2 million (5%)	-16	-42
• Chafee-Breaux / Senate 1997 Singles: $50,000 with full payment at $100,000 Couples: $75,000 with full payment at $150,000 Beneficiaries affected: About 4 million (11%)	-23	-58
• Breaux / Commission Draft 1999* Single: $24,000 with full payment at $40,000 Couples: $30,000 with full payment at $50,000 Beneficiaries affected: About 13 million (33%)	-38	-95

For all: Index income thresholds to inflation; No full phase-out of subsidy; Treasury run

* Phases out at a higher subsidy level than the other options

PREMIUM SUPPORT

OPTIONS:	2000-04	2000-09
• Breaux Plan Assuming 2000 implementation Fee-for-service premium higher than current law Partial geographic adjustment; limited benefits flexibility	-26	-75
Assuming 2002 implementation	-13	-62
• Competitive Defined Benefit Assuming 2002 implementation Fee-for-service premium no higher than current law Full geographic adjustment; limited benefits flexibility	-8	-30
• Phased-In Competitive Defined Benefit Assuming 2004 implementation Fee-for-service premium no higher than current law Full geographic adjustment; limited benefits flexibility	-1	-20

SUMMARY OF PROPOSALS

OPTIONS:	2000-04	2000-09
Base	**-21**	**-85**
Income-Related Premium		
Health Security Act ($90 / 110,000)	-16	-42
Chafee-Breaux ($50 / 75,000)	-23	-58
Premium Support		
Competitive Defined Benefit	-8	-30
Phased-In Competitive Defined Benefit	-1	-20
DRUG OPTIONS		
High Uncapped Option ($250 deductible)	+84	+253
Low Uncapped Option ($500 deductible)	+58	+176
High Capped Option ($2,000 cap)	+51	+141
Low Capped Option ($1,000 cap)	+37	+101

ILLUSTRATIVE OPTIONS

OPTIONS:	2000-04	2000-09
Option 1: No Competitive Defined Benefit		
Base Plan	-21	-85
Income-Related Premium ($90/110,000)	-16	-42
Subtotal	-37	-127
Drug Benefit: Front-End, $1,000 Cap	+37	+101
Option 2: Phased-In Competitive Benefit / Lower Income-Related Premium		
Base Plan	-21	-85
Income-Related Premium ($50/75,000)	-23	-58
Phased-In Competitive Defined Benefit	-1	-20
Subtotal	-45	-163
Drug Benefit: Front-End, $1,000 Cap	+37	+101
Option 3: Competitive Defined Benefit / Lower Income-Related Premium		
Base Plan	-21	-85
Income-Related Premium ($50/75,000)	-23	-58
Competitive Defined Benefit	-8	-30
Subtotal	-52	-173
Drug Benefit: Front-End, $2,000 Cap	+51	+141

THE WHITE HOUSE

WASHINGTON

March 15, 1999

TO: Steve R., Gene S., Bruce R., Larry S., Elena K., Jack L., Dan M.
David B., Melanne V., Sarah B., Neera T., Janet M.

FROM: Chris J. and Jeanne L.

RE: BREAUX-THOMAS MEDICARE PLAN

Attached is the final Breaux-Thomas Medicare plan. They released it at a 5pm press conference. Highlights of the plan include:

- **No specific plan for Medicare financing**: The plan contains no options for raising new revenue for Medicare -- specifically it does not include the President's proposal to dedicate part of the surplus to Medicare. Instead, it states that once Medicare appears to be close to becoming insolvent (using a new definition), Congress would be notified. This would result in a Congressional debate on legislation to authorize any additional funding.

- **No meaningful prescription drug benefit**: The plan would require private managed care plans, Medigap, and possibly Medicare fee-for-service to offer a drug benefit, but only provides a subsidy for that coverage for people below 135 percent of poverty. This is troubling because it moves Medicare towards a means-tested, Medicaid-like program, and would probably result in large adverse selection in the unsubsidized Medicare fee-for-service option.

- **Age eligibility increase without a viable insurance alternative**: Although there is a suggestion that vulnerable sick people ages 65 to 67 would get Medicare, the proposal explicitly states that the Medicare buy-in would be unsubsidized and would not begin at 62 (which is truly conforming to Social Security). This plan would likely lead to an increase in the uninsured.

- **No income-related premium:** This was dropped since the last draft -- reportedly because some Republicans considered it too similar to a tax (since it is administered through Treasury).

There are probably other issues that we have not yet noticed; we will be working on a more complete memo of the issues for the morning.

Please call or page with questions.

SUMMARY OF BREAUX/THOMAS PROPOSAL

Medicare Board:
The Board would provide information to beneficiaries, negotiate with plans, compute payments to plans (including risk, geographic, and other adjustments), and compute beneficiaries premiums. Board would approve plan service areas and benefit package designs.

Benefits Package:
The standard benefits package is specified in law and would consist of all services covered under the existing Medicare statute. Plans could establish their own rules as to how the benefits would be provided. Board approval would be required for all benefit design offerings and the Board would allow variation only within a limited range as the risk adjusters were proven over time.

Prescription Drugs:
Private Plans
All private plans would be required to offer a high option that includes at least the standard benefits package plus coverage for prescription drugs.

Low-Income
The proposal would immediately extend coverage of prescription drugs for beneficiaries under 135 percent of poverty ($10,568/individual) under Medicaid with full federal funding of the additional cost. That coverage could be provided through high option plans when the premium support system was implemented.

Fee-For-Service
The government-run FFS plan could offer a high option plan which includes prescription drugs. The Medicare Board would approve the benefit package as it does for private plan offerings. HCFA would work with third-party contractors to offer its high option plan. Government contracts would be based on prices commonly available in the market, without recourse to price controls or rebates.

Medigap
All Medigap plans would include basic coverage for prescription drugs. One plan would be drug-only. Plans would vary regarding the degree Medicare coinsurance was covered.

Premium Formula Basics:
Beneficiaries would pay 12 percent of the premium for the standard benefits package on average, pay no premium for plans less than about 85 percent of national weighted average, and pay all of the additional premium for plan premiums above national weighted average. Only the cost of standard benefits (Medicare covered services) would count toward the computation of the national weighted average premium. Plans with only a high option would be required to separate out the cost of extra benefits in their submission to the Board.

In areas where only the government-run fee-for-service plan operated, the beneficiary obligation would be limited to the lower or 12 percent of the fee-for-service premium or 12 percent of the national weighted average premium.

Fee-for-Service Benefits:
The government-run fee-for-service plan would have a $400 combined deductible, indexed to the growth in Medicare costs. 10 percent coinsurance would be charged for home health, laboratory services, and certain other services not currently subject to coinsurance. No coinsurance would be charged for inpatient hospital stays and preventive care.

Special Payments:
Direct Medical Education (DME) would be carved out of Medicare. DME funding would continue through either a mandatory entitlement or multi-year discretionary appropriation program separate from Medicare. The proposal would also recommend exploring funding Indirect Medical Education (IME) and other non-insurance subsidies outside of the Medicare program and financing those items through a mandatory or multi-year discretionary appropriation program. Any special payments remaining in Medicare would not be included in the calculation of premiums for the government-run fee-for-service plan or private plans.

Retirement Age:
The normal age of eligibility would be gradually raised from 65 to 67 to conform with that of Social Security. A non-subsidized buy-in would be available at age 65. Congress should develop a special category of eligibility based on specific needs-based criteria (i.e. ADLs) for individuals between 65 and the then-current eligibility age.

Long-Term Care:
Long-term care issues should be separated from Medicare (an acute care program), and long-term care improvements should be made through pension, Social Security, and investment reforms. The proposal would require a study of various long-term care issues.

Financing:
Part A and Part B trust funds should be combined into a single Medicare Trust Fund and a new concept of solvency for Medicare should be developed. In any year in which the general fund contributions are projected to exceed 40% of annual total Medicare outlays, Congress would be required to authorize any additional contributions to the Medicare Trust Fund. This new test (40% of outlays) would probably not be reached until after 2005. Even if general revenue contributions were limited to 40% of program outlays, this proposal would extend solvency to 2013 (2017 under CBO's new baseline.)

Budgetary Impact:
Between 2000 and 2009, this proposal would save approximately $100 billion. Over the longer term, the proposal would reduce the growth of Medicare spending by approximately 1 percent a year. Although the savings would accumulate slowly over time, by 2030 the annual budgetary savings would range from $500 to $700 billion.

BUILDING A BETTER MEDICARE FOR TODAY AND TOMORROW

I. INTRODUCTION

This recommendation is in three parts:
- the design of a premium support system,
- improvements to the current Medicare program, and
- financing and solvency of the Medicare program.

We believe it is important to address the current program now because of the transition time necessary to implement this premium support system. We assume the enactment of this proposal in 1999 and that the premium support system would be fully operational in 2003.

We believe a premium support system is necessary to enable Medicare beneficiaries to obtain secure, dependable, comprehensive high quality health care coverage comparable to what most workers have today. We believe modeling a system on the one Members of Congress use to obtain health care coverage for themselves and their families is appropriate. This proposal, while based on that system, is different in several important ways in order to better meet the unique health care needs of seniors and individuals with disabilities. Our proposal would allow beneficiaries to choose from among competing comprehensive health plans in a system based on a blend of existing government protections and market-based competition. Unlike today's Medicare program, our proposal ensures that low income seniors would have comprehensive health care coverage.

Because the implementation of a premium support system will take a number of years, we recommend immediate improvements to the current Medicare program. In Section II we outline the incremental improvements to enhance the beneficiaries' security and quality of care now. We recommend immediate federal funding of pharmaceutical coverage through Medicaid for seniors up to 135% of poverty ($10,568 for an individual and $13,334 for a couple). This would also expand beneficiary participation in currently available subsidies for premiums and cost-sharing.

In reviewing the three parts of this proposal, it is important to keep in mind the different government roles in the premium support system and in current law. We believe the guarantee our society makes to every senior is to ensure that they can obtain the highest quality health care, and that their health care coverage not be allowed to fall behind that available to people in their working years. We believe that our society's commitment to seniors, the Medicare entitlement, can be made *more secure* only by focusing the government's powers on ensuring comprehensive coverage at an affordable price rather than continuing the inefficiency, inequity, and inadequacy of the current Medicare program.

I. PREMIUM SUPPORT SYSTEM TO PROVIDE COMPREHENSIVE COVERAGE

The Medicare Board
A Medicare Board should be established to oversee and negotiate with private plans and the government-run fee-for-service plan. Some examples of the Board's role are: direct and oversee periodic open enrollment periods; provide comparative information to beneficiaries regarding the plans in their areas; transmit information about beneficiaries' plan selections and corresponding premium obligations to the Social Security Administration to permit premium collection as occurs today with Medicare Part B premiums; enforce financial and quality standards; review and approve benefit packages and service areas to ensure against the adverse selection that could be created through benefit design, delineation of service areas or other techniques; negotiate premiums with all health plans; and compute payments to plans (including risk and geographic adjustment).

This Board would operate under a government charter that would describe its responsibilities and operating standards including the ability to hire without regard to civil service requirements and salary restrictions.

Ensuring Plan Performance and Dependability
All plans (private plans and the government-run FFS plan) would compete in the premium support system; all plans would have Board-approved benefit designs and premiums. The Board would ensure that the benefits provided under all plans are self-funded and self-sustaining, determining whether plan premium submissions meet strict tests for actuarial soundness, assessing the adequacy of reserves, and monitoring their performance capacity.

Management of Government-run Fee-for-service in Premium Support
The government plan would have to be self-funded and self-sustaining and meet the same requirements applied to all private plans, including whether its premium submissions meet strict tests for actuarial soundness, the adequacy of reserves, and performance capacity.

Cost containment measures would be necessary. The provisions of the Balanced Budget Act of 1997 should be extended, or comparable savings achieved. In any region where the price control structure of the government run plan is not competitive, the government-run fee-for-service plan could operate on the basis of contracts negotiated with local providers on price and performance, just as is the case with private plans. The government plan would be run through contractors as it is today; contractors in one region would be able to bid in other regions; the Board should have powers to assure that the government-run plan would not distort local markets.

Benefits Package
A standard benefits package would be specified in law. This benefits package would consist of all services covered under the existing Medicare statute. Plans would be able to offer additional benefits beyond the core package and plans would be able to vary cost sharing, including copay and deductible levels, subject to Board approval. Benefits would be updated through the annual negotiations process between plans and the Board, although the Board would not have the power to expand the standard benefit package without Congressional approval. Health plans would establish rules and procedures to assure delivery of benefits in a manner consistent with prevailing private standards and procedures offered to employer groups and other major purchasers.

The Medicare Board would approve ~~benefit~~ offerings and could allow variation within a limited range, for example not more than 10% of the actuarial value of the standard package, provided the Board was satisfied that the overall valuation of the package would be consistent with statutory objectives and would not lead to adverse or unfavorable risk selection problems in the Medicare market.

New benefit to be instituted in the premium support system: Outpatient prescription drug coverage and stop-loss protection

In Private Plans:
Private plans would be required to offer a high option that includes at least Medicare covered services plus coverage for outpatient prescription drugs and stop-loss protection. Plans would be able to vary copay and deductible structures. Minimum drug benefits for high option plans would be based on an actuarial valuation. High option and standard option plans each would be required to be self-funded and self-sustaining.

In Government-run Fee-For-Service Plan:
The government-run fee-for-service plan would be required to offer high option (including outpatient prescription drugs and stop-loss) in addition to standard option plans. The Medicare Board approval process would be the same as for private plans. High option and standard option plans would be required to be separately self-funded and self-sustaining. Government contracts would be based on prices commonly available in the market, without recourse to price controls or rebates.

Comprehensive coverage for low-income beneficiaries:
Coverage would be provided through high option plans. The federal government would pay 100% of the premiums of the high option plans at or below 85% of the national weighted average premium of all high option plans for all eligible individuals up to 135% of poverty ($10,568 for an individual and $13,334 for a couple) on a fully federally funded basis. This financial support does not limit

these beneficiaries' choice of plans nor restrict plans' design with regard to cost-sharing or other flexibility authorized by the Board. State would maintain their current level of effort, but the federal government would pay 100% of additional costs for these individuals. In this context, Congress should review DSH payments to ensure that double payments do not occur.

Premium Formula Basics
On average, beneficiaries would be expected to pay 12 percent of the total cost of standard option plans. For plans that cost at or less than 85 percent of the national weighted average plan price, there would be no beneficiary premium. For plans with prices above the national weighted average, beneficiaries' premiums would include all costs above the national weighted average.

Only the cost of the standard package would count toward the computation of the national weighted average premium. Plans with a high option, whether private plans or government-run, would separately identify the incremental costs of benefits beyond the standard package in their submissions to the Board, and the government contribution would be calculated without regard to the costs of these additional benefits.

Premium for government-run fee-for-service plans
The government-run fee-for-service plan would be treated the same as private plans.

Government-run plan premium excludes costs of special subsidies in premium calculation
All non-insurance functions and special payments now in Medicare would not be included in calculation of premiums for the government-run FFS plan or private plans.

Guaranteed premium levels where competition develops more slowly
In areas where no competition to the government-run fee-for-service plan exists, beneficiaries' obligations would be no greater than 12 percent of the FFS premium or the national weighted average, whichever is lower. The Medicare Board should periodically review those areas with a fixed percentage premium to ensure that the fixed percentage premium is not anti-competitive.

Medicare's Special Payments in a Premium Support System
Congress should examine all non-insurance functions, special payments and subsidies to determine whether they should be funded through the Trust fund or from another source. For example, payments for Direct Medical Education (DME) would be financed and distributed independent of a Medicare premium support system. Since the Part A and Part B trust funds would be combined and the traditionally separate funding sources of payroll taxes and general revenues would be blurred, Congress should provide a separate mechanism for continued funding through either a mandatory entitlement or multi-year discretionary appropriation program. On the other hand, Indirect Medical Education (IME) presents a unique problem since it is difficult to identify the actual statistical difference in costs between teaching and non-teaching hospitals.

Therefore, for now Congress should continue to fund IME from the Trust Fund as an adjustment to hospital payments.

II. IMMEDIATE IMPROVEMENTS TO THE CURRENT MEDICARE PROGRAM AND OTHER ASPECTS OF SENIORS HEALTH CARE SPENDING

Provide Outpatient Prescription Drug Coverage for 3 million more low-income beneficiaries
Immediately provide federal funding for coverage of prescription drugs under Medicaid for beneficiaries up to 135 percent of poverty ($10,568 for an individual and $13,334 for a couple). This would also expand beneficiary participation in currently available subsidies for premiums and cost-sharing. All funding obligations related to the coverage under this provision would be federal.

Improve access to outpatient prescription drug coverage for seniors
Revise federal directives to National Association of Insurance Commissioners (NAIC) to develop new Medigap state model legislation immediately. All private supplemental plans would include basic coverage for prescription drugs. One plan would be a prescription drug-only plan.

Combine Parts A and B
Health care delivery changes have blurred the distinctions originally contemplated when Parts A and B of Medicare were enacted. Parts A and B should be combined in a single Medicare Trust Fund. (See Section III on Financing and Solvency.)

Lower deductible for 8 million beneficiaries
The current Medicare program subjects beneficiaries entering the hospital to extremely high costs just at a time when they face the many other expenses associated with serious illness. Virtually no private health plan imposes such costs. We propose to combine the current Part A ($768) deductible and B ($100) deductible, and replace it with a single deductible of $400, which should be indexed to growth in Medicare costs.

Improve utilization of health care services
A fee-for-service plan is best maintained by financial incentives, without which costs spiral out of control or freedom of choice must be restricted. To protect against unnecessary rises in beneficiary Part B premiums, 10% coinsurance would be established for all services except inpatient hospital stay and preventive care, and except where higher copays exist under current law.

Revise federal directives to NAIC to develop new state model legislation to conform to the changes proposed for Medicare cost-sharing. These directives should also be designed to achieve more affordable and more efficient supplemental insurance and to minimize Medicare outlays. The new single Medicare deductible and coinsurance schedule would be insurable in part or in whole.

Eligibility Age

Medicare eligibility age should be conformed to that of Social Security. A non-subsidized buy-in should be available at age 65. In addition, Congress should develop a special category of eligibility based on specific needs-based criteria, for example selected activities of daily living, for individuals between age 65 and then-current eligibility age.

III. FINANCING AND SOLVENCY

The changes proposed in this document are intended to put Medicare on surer financial footing by creating savings due to competition, efficiency and other factors, and by slowing the growth in Medicare spending. In addition, these reforms would result in Medicare offering a benefit package that is more comparable to health care benefits offered in the private sector and would enhance our ability to meet our commitment to today's and future beneficiaries. Without these changes, quality of care could suffer, and significantly greater revenues and/or beneficiary sacrifices would be required. Beneficiaries and the taxpayers would not receive the greatest value for the total health dollars spent on seniors' behalf.

Medicare's financing needs would be dictated by the Medicare growth rate achieved under the premium support system. By moving to a premium support system, Medicare's growth rate would be reduced by 1 to 1.5 percentage points per year from the current long-term annual growth rate of 7.6 percent (Trustees Intermediate) or 8.6 (Commission's No Slowdown Baseline.) If this reduction in growth rate can be achieved, the fiscal integrity and Medicare would be significantly improved.

Even if the estimated reduction in growth rate is achieved, Medicare will require additional resources as the percent of population that is eligible for Medicare increases. As revenue is needed, how much should be funded through the payroll tax, through general revenue, and through beneficiary premiums?

The answer to this question is difficult because it would require knowing today the health care system of the future. We do not know what the future holds in terms of the evolution of the health care delivery system, or the impact that technology will have on health care costs.

At the Commission's first meeting, Federal Reserve Chairman Alan Greenspan said that "the trajectory of health spending in coming years will depend importantly on the course of technology which has been a key driver of per-person health costs" Yet he went on to underscore what could be the absurdity of attempting now to determine funding levels necessary decades into the future "technology cuts both ways with respect to both saving medical expenditures and potentially expanding the possibilities in such a manner that even though unit costs may be falling, the absolute dollar amounts could be expanding at a very rapid pace. One of the major problems that everyone has had with technology--and I could allude to all sorts of forecasts over the most recent generations--one of the largest difficulties is in forecasting the pattern of technology. It is an extremely difficult activity."

Notwithstanding the magnitude of uncertainty contained in the task, the statute establishing the Commission directed us to recommend measures to attain the long-term "solvency" of the Medicare program. Because of recent history the meaning of "solvency" has come under question. We believe a new measure of solvency must be developed that couples the uncertainty inherent in the task with the real need for the public to evaluate the cost of Medicare and how we should choose to fund this program over time.

The solvency test that has been applied to Social Security is not an apt model for Medicare. Social Security Trust Funds are funded exclusively through payroll taxes; Medicare is paid for by a combination of payroll taxes, general revenue and beneficiary premiums. These ratios have changed over time such that a greater portion of program expenses is now paid by general revenues and a relatively smaller portion is paid by payroll taxes and beneficiary premiums.

In addition, the payroll tax supporting the OASDI Trust Funds is limited both by its rate and the wage base on which that rate is applied. No portion of Medicare's funding contains these limitations. In Medicare, there is no cap on the wage base; the Part A Trust Fund is funded by a payroll tax of 2.9% on all earnings, and pays only for the Part A benefits of Medicare. Medicare's Part B benefits are paid 75% by general revenues and 25% by beneficiaries.

Consequently, the historic concept of Medicare's solvency is one that has been partially and inappropriately borrowed from Social Security and has never fully reflected the fiscal integrity, or lack thereof, of the Medicare program. In Medicare, "solvency" has meant only whether the Part A Trust Fund outlays were poised to exceed Part A reserves and collections. That is all.

Recently even this partial proof of fiscal integrity has been shattered. The notion of Part A "solvency" or rather "insolvency" has been used to shift more program costs to the general fund. An act of Congress shifted major home health expenditures from Part A to Part B in 1997, thus extending the fiction of the Part A Trust Fund "solvency" from 2002 through 2008 by shifting obligations to the general fund. The general fund, in great part, became the source of Part A "solvency".

The ever increasing estimates of general fund exposure should be part of any definition of solvency. Absent reform, general fund exposure jumps from 37% of program funding in FY2000 to 43% in FY2005 and 49% in FY2010. General fund demand will increase from $92 billion in FY2000 to $156 billion in FY2005 to $261 billion in FY2010.

Consequently, the "solvency" of the Part A Trust Fund is not useful as a guide to policy making or even as a tool to educate the public on the security and financial condition of the Medicare program.

Therefore, Part A and Part B Trust Funds should be combined into a single Medicare Trust Fund and a new concept of solvency for Medicare should be developed. This concept should more accurately reflect the implications of the program's financing structure, i.e., the ratio of relative financing burdens on the general fund, the Hospital Insurance payroll tax, and the premiums beneficiaries pay. Because beneficiary premiums and the payroll tax rate can only be amended by law, and have proved very difficult to modify over time, the only meaningful solvency test of this entitlement program is one based on the amount of general revenues needed to fund program outlays. This could be referred to as a programmatic solvency test.

Congress should enact this revised definition of Medicare solvency so that decisions can be made in the context of competing demands for general revenue. Congress should require the Trustees to publish annual projections regarding the ratio in program financing. In any year in which the general fund contributions are projected to exceed 40% of annual total Medicare program outlays, the Trustees would be required to notify the Congress that the Medicare program is in danger of becoming programmatically insolvent. The Trustees Report should provide for necessary and important public debate leading to potential adjustments to the payroll tax and/or the beneficiary premium as well as any adjustment of the general fund devoted to Medicare. Congressional approval would be required to authorize any additional contributions to the Medicare Trust Fund.

With the reforms contemplated under this proposal, that new test would probably not activated until after 2005. Even if we limit general revenue contributions to 40% of program outlays, however, this proposal would extend the solvency of Medicare to 2013. This calculation, based on the most recent CBO baseline, would indicate that solvency under this test would extend to 2017 or beyond.

Long-term care

The Commission recognizes that its proposal is focused on acute care, and does not address the issue of long-term care. In 1995, Americans spent an estimated $91 billion on long-term care, with 60 percent coming from public sources. Despite these large public expenditures, the elderly face significant uncovered liabilities. The Commission recommends that the Institute of Medicine conduct a study to 1) estimate future demands for long-term care; and 2) analyze the long-term care financing options available to seniors, including long-term care insurance, tax policy and community-based, state and federal government programs.

Actual Acturial Memo behind

MEMORANDUM TO GENE SPERLING

FROM: Natasha Bilimoria

SUBJECT: SSA releases Actuarial Memo on the Social Security Guarantee Plan (Archer/Shaw Plan)

This afternoon, Chairman Archer held a press conference releasing the Social Security Actuarial Memo stating that the Social Security Guarantee Plan (SSGP) would be expected to eliminate the estimated long-term actuarial deficit of 2.07 percent of taxable payroll. The following is a summary of this memo.

10-15 years 30%

Assumptions

- All estimates assume the elimination of the earnings test gradually from 2001 to 2006 (this has a very small effect on the overall financial status of the program.)
- Memo assumes a 5.35 rate of return, net of administrative expenses (An administrative cost of 25 basis points is assumed).

Key Points of SSA Actuaries Memo

- The Archer/Shaw plan would produce a net drain on the unified budget until 2054.
- SSGP does reach 75-year solvency.
- Transfers from the SSGP accounts to the Social Security trust funds are sufficient to allow a reduction in the payroll tax rate from 12.4 to 9.9 percent during 2050 to 2059. In 2060, payroll tax can be reduced by another 1 percent, making it 8.9 percent.
- With reductions in the payroll tax rate, the trust fund ratio is expected to stay stable at about 240 percent of annual outgo at the end of the 75 years. (Without the reductions in payroll tax, the trust fund ratio would be expected to rise to over 10 times annual outgo by the end of 75 years).
- The OASDI actuarial balance is improved by 2.15 percent of taxable payroll, leaving a balance of +0.09 percent of taxable payroll after 75 years. Without reducing the payroll tax, the deficit is improved by 2.71, leaving a balance of +0.65.
- The Social Security trust fund outgo as compared to what it takes in is expected to remain positive throughout the 75 year time period. Timely benefits made in full can be expected through 2073 and beyond.

Effect of the SSGP on Financial Status of OASDI Depends Greatly on the Actual Investment Return to the Accounts

Goss provides two examples.

The first example assumes a net yield of 1 percentage point higher, 6.35 percent.

- With this higher rate of return, the payroll tax can be reduced to 4.4 percent by 2060 and the trust fund ratio would be at 300 percent after 75 years (balance of +0.07 percent of taxable payroll).

- Without reduced payroll tax, the trust fund ratio would be expected to rise to more than 50 times annual Social Security net costs after 75 years (balance of +1.69 percent of taxable payroll).

The second example assumes a net yield of 1 percentage point lower, 4.35 percent.

- With the lower rate, the Social Security trust funds would be exhausted by 2048 (leaving a -0.08 percent payroll deficit)

SOCIAL SECURITY

MEMORANDUM

Date: April 29, 1999 Refer To: TCC

To: Harry C. Ballantyne
Chief Actuary

From: Stephen C. Goss
Deputy Chief Actuary

Subject: Long-Range OASDI Financial Effects of the Social Security Guarantee Plan--INFORMATION

This memorandum provides long-range estimates of the financial effects on the Social Security (OASDI) program for enactment of the Social Security Guarantee (SSG) Plan proposed by Representatives Archer and Shaw. This plan would provide for an annual contribution from the General Fund of the Treasury to SSG individual accounts equal to 2 percent of each worker's OASDI taxable earnings beginning with earnings in 1999.

Proceeds from these accounts would, commencing at the worker's retirement (or disability), be transferred entirely to the OASDI trust funds on a gradual basis. For workers who die before OASDI benefit entitlement without potentially eligible survivors, the account balance would go to the worker's estate, tax free. Benefits paid by the OASDI program would be the higher of benefits scheduled under current law or the scheduled SSG withdrawal rate based on a life-annuity calculation.

The combined OASDI payroll tax of 12.4 percent (6.2 percent for employees and employers, each) is assumed to be reduced in future years under the intermediate assumptions of the 1999 Trustees Report and expected investment yields. The proposal would also include the gradual elimination of the Social Security retirement earnings test between 2001 and 2006.

Enactment of this proposal, as specified, would be expected to eliminate the estimated long-range OASDI actuarial deficit (2.07 percent of taxable payroll under present law). Under assumptions described below, revenue transferred from the SSG accounts to the trust funds would be sufficient to allow reductions in the combined OASDI payroll tax rate of

2.5 percentage points in 2050 (from 12.4 to 9.9 percent) and 1 percentage point in 2060 (to 8.9 percent).

Estimates are provided for the SSG plan with and without the specified payroll tax reductions. Estimates are also provided to illustrate the sensitivity of the plan to possible variation in the yield on SSG accounts.

All estimates assume elimination of the OASDI retirement earnings test for ages 62 and older, gradually between 2001 and 2006. (This change has a very small effect on the long-range financial status of the OASDI program.) All estimates in this memorandum are based on the intermediate assumptions of the 1999 Trustees Report, except as indicated below.

The Proposal

Contributions and Investment Up To Benefit Entitlement

The proposal would provide Social Security covered workers with refundable tax credits equivalent to 2 percent of their OASDI taxable earnings for calendar years starting 1999. Credits would be increased with interest from July 1 of the year of taxable earnings, at the market yield on publicly-held Federal debt, until paid. Credits would be paid from the General Fund of the Treasury on October 15 (December 1 for self-employment earnings) in the following calendar year for the sole purpose of deposit in a SSG account. Credits for earnings in 1999 would be delayed one additional year and paid in 2001.

Accounts would be managed by mutual funds, qualified and supervised by the Social Security Guarantee (SSG) Board. The Board would consist of the six individuals appointed by the Social Security (OASDI) Trustees.

Individuals would be required to hold all SSG assets in a single fund and could change funds at most once per year. Annual SSG credits would be pooled and transmitted to the mutual fund managers by a central agency. Account holders would receive annual notice of assets in their Social Security Personal Earnings and Benefit Statements.

The proposal requires that all account balances be invested in qualified mutual funds maintained with a portfolio allocation of 60 percent stock index funds and 40 percent corporate bonds. The charge for annual administrative expenses would be limited to 25 basis points (excess expense, if any would be made up from the General Fund of the Treasury). Withdrawals prior to reaching retirement (or disability) would not be permitted.

Earnings Test Elimination at Age 62+

The Social Security retirement earnings test annual exempt amounts would be raised according to a specified schedule through 2005, and the test would be eliminated starting 2006, for all beneficiaries age 62 or older. For beneficiaries under age 62, the current test would remain unchanged. The exempt amounts would be specified for the test applicable at ages NRA through 69 as $35,000 for 2003, $40,000 for 2004, and $45,000 for 2005. For the test applicable at ages 62 up to NRA, the exempt amounts for years 2001 through 2005 would be set at $15,000, $20,000, $25,000, $30,000, and $35,000, respectively. This provision alone would have a negligible effect (between 0.005 and -0.005 percent of taxable payroll) on the OASDI actuarial balance.

SSG Account Distributions

Under the plan, the SSG account balance of workers who become entitled to OASDI retirement or disability benefits would ultimately be transferred entirely to the OASDI trust funds. Upon entitlement for Social Security retirement or disability benefits, the Social Security Administration would compute the monthly payment that could be provided from a life annuity purchased with the holdings in the SSG account. The annuity calculation would reflect the anticipated yield on the SSG account (60 percent stock and 40 percent corporate bonds, less 25 basis points for administration) and indexing of annuity payments for price inflation (as for the Social Security COLA). The annuity calculation would also reflect the expected payment of aged spouse and aged survivor benefits if the worker has a current spouse and/or a qualifying divorced spouse (marriage lasted 10 years or longer).

If the computed monthly annuity amount exceeds the level of current law scheduled OASDI benefits, then the Social Security Administration would guarantee payment from the trust funds of the computed annuity amount for life. If the computed annuity amount is less than the level of the OASDI benefit, then the OASDI benefit would be payable for life. Each month after benefit entitlement the computed annuity amount based on entitlement of the worker and any aged spouse(s) would be transferred from the SSG account to the OASDI trust funds.

Because the computed annuity amount is based on a life annuity *calculation*, the SSG account would be expected to be depleted at the point where the beneficiary(ies) reach their life expectancy, as estimated at the time of benefit entitlement. Thus, for about half of the SSG accounts, benefits will be payable after exhaustion of the SSG account entirely at the expense of the OASDI trust funds. For the other half, death before life expectancy will leave remaining SSG balances for the payment of benefits to those who lived beyond life expectancy. For workers who die prior to exhausting their SSG account, but after becoming entitled to OASDI retirement or disability benefits, the remaining balance in the SSG account will be transferred to the account of any surviving spouse potentially eligible for benefits payable by OASDI (as a surviving spouse or surviving divorced spouse). At the point at which a worker has died, and each spouse or qualifying divorced spouse has also died, any remaining SSG account balance will be transferred to the OASDI trust funds.

For workers who die before becoming entitled to OASDI retirement or disability benefits, the balance in the SSG account will be transferred to the account of any surviving spouse potentially eligible for benefits payable by OASDI (as a surviving spouse or surviving divorced spouse). If children of the worker who are eligible for survivor benefits survive the worker and any spouse, the SSG account will be maintained to cover these benefits. At the point at which a worker has died (prior to entitlement to any OASDI benefit), and each spouse or qualifying divorced spouse has also died (prior to entitlement to any OASDI benefit), and there are no eligible children, any remaining SSG account balance will go to the estate of the deceased, tax free.

OASDI Payroll Tax Rate Reduction

The plan calls for a reduction in the OASDI combined payroll tax rate from 12.4 percent to 9.9 percent in 2050 and to 8.9 percent in 2060. These reductions reflect the specified SSG portfolio allocation with the assumed asset yields described below. Payroll tax rate reductions are assumed to be implemented if transfers from the SSG accounts to the trust funds are large enough to raise the OASDI trust fund ratio above 200 percent, with continued increase thereafter.

Assumptions

SSG Account Accumulation

SSG account portfolios are required to be invested, both prior to retirement (or disability) benefit entitlement and after benefit entitlement in qualified SSG funds that are must be maintained at 60 percent stock and 40 percent corporate bonds, with an annual administrative expense charge of 25 basis points. The long-term ultimate average real yield on stocks is assumed to be 7 percent, as assumed by the 1994-96 Advisory Council. (It should be noted that while the real yield on stocks has averaged 7 percent so far this century, many speculate that future yield may average less.) The ultimate real yield on long-term corporate bonds is assumed to average 3.5 percent, or 0.5 percentage point higher than the 3.0 percent real yield for U.S. Government long-term securities, as assumed for the 1999 Trustees Report. This spread between corporate and U.S. Government bond yields is consistent with the spread experienced over the past 40 or 70 years, on average. It should be noted, however, the spread has been much smaller over the past 20 years. The expected ultimate real portfolio yield for the base projection (alternative 1) would thus be 5.35 percent, net of administrative expense,

$$(0.6*7\% + 0.4*3.5\% - 0.25\% = 5.35).$$

A range of administrative expense factors was assumed for individual accounts proposed by the 1994-96 Advisory Council on Social Security. For the Individual Account (IA) plan, individual contributions were assumed to be collected and recorded by central institution, invested in large blocks with financial institutions, and invested in a limited number of indexed funds. Based on experience of TIAA and the Federal Employee Thrift Savings Plan (TSP) it was assumed that the IA plan could be administered with an expense of 10.5 basis points per year. For the Personal Security Accounts (PSAs), individual accounts were assumed to be invested on an individual basis, resulting in an annual administrative expense of 100 basis points. Because the description of SSG individual accounts is far closer to the individual accounts for the IA plan than to the individual accounts for the PSA plan, the specified administrative expense factor of 25 basis points for SSG accounts appears to be reasonable.

Distribution of SSG Accounts

Life annuity calculations for the purpose of determining the size of monthly transfers from SSG balances to the OASDI trust funds assume a real yield equal to the net expected real yield on SSG accounts, as specified. Mortality estimates for these calculations are based on the intermediate projections of the 1999 trustees report.

Annuity calculations are assumed to be made on a unisex basis for workers with no spouse or qualified divorced spouse (marriage lasting at least 10 years). For those with a spouse, annuity calculations would be on a joint and survivor basis intended to roughly match the expected payment of OASDI benefits. For the purpose of these calculations, a joint and 2/3 survivor annuity is assumed. Thus, the amounts transferred to OASDI from the SSG account of a married beneficiary would be reduced by 1/3 upon the death of either the worker or the spouse.

Under the SSG account yields assumed for these estimates, expected transfers from SSG accounts after benefit entitlement would be less than expected OASDI benefits for virtually all future beneficiaries. However, single workers with very high earnings, close to or above the OASDI maximum taxable amount throughout their careers would have transfers from their SSG accounts greater than current law benefits if the investment return during their working years exceeded the assumed long-range average return used for these estimates. High-earning married workers would be far less likely to have transfers that exceed current-law benefits because the joint-and-survivor annuity calculation would provide lower transfers than for single workers, and current law OASDI benefits for married workers would tend to be higher.

Estimated Effect On OASDI Financing

The table below provides the estimated OASDI actuarial balance, the change in the actuarial balance, and the estimated year of combined OASDI trust fund exhaustion for the SSG Plan as described above. To illustrate the full extent of the expected value of transfers from the SSG accounts to the OASDI trust funds, the estimated financial effects of the SSG Plan without the specified reductions in the OASDI payroll tax rate are also included in the table below.

Under the SSG Plan, the OASDI actuarial balance would be improved by 2.15 percent of effective taxable payroll, from a balance of -2.07 percent under current law to a positive balance of 0.09 percent of payroll under the plan. The OASDI trust fund as a percent of annual OASDI outgo (the trust fund ratio) would be expected to remain positive throughout the long-range 75-year projection period, thus allowing timely payment of benefits in full through 2073, and beyond. The trust fund ratio would be expected to decline to about 132 percent at the beginning of 2041, and to increase thereafter. The combined OASDI payroll tax rate would be reduced from 12.4 percent to 9.9 percent for the period 2050 through 2059 and to 8.9 percent for 2060 and later. Even with these reductions in the payroll tax rate, the trust fund ratio would be expected to be stable at about 240 percent of annual outgo at the end of the long-range 75-year projection period. See table 1a attached for details.

Estimated Effects on OASDI Financial Status of the Social Security Guarantee (SSG) Plan

	Estimated OASDI Actuarial Balance	Estimated Change in OASDI Actuarial Balance	Year Exhaust OASDI Trust Funds
	(percent of taxable payroll)		
Present Law (No SSG)	-2.07	--	2034
SSG Plan 1/			
60% Stock, 40% Corp Bond			
Assess only .25% Admin Cost	+0.09	2.15	NA
Illustration of SSG Plan Without Reduced Payroll Tax			
60% Stock, 40% Corp Bond			
Assess only .25% Admin Cost	+0.65	2.71	NA

1/ Payroll tax rate would be reduced from 12.4 to 9.9 in 2050 and 8.9 in 2060.

Based on intermediate assumptions of the 1999 Trustees Report and other assumptions described in the text.

The table above also includes an illustration of the potential financial effect of the SSG Plan on Social Security if the specified reductions in the OASDI payroll tax rate were not included. This provides an indication of the full effect on OASDI of the expected transfers from SSG accounts to OASDI trust funds under the plan. Without the specified payroll tax rate reduction, the OASDI actuarial balance would be improved by 2.71 percent of taxable payroll, from a balance of -2.07 percent under current law to a positive balance of 0.65 percent of payroll under the plan without specified payroll tax rate reduction. Without the payroll tax rate reduction, the OASDI trust fund ratio would be expected to rise to over 10 times annual outgo by the end of the long-range period due to the magnitude of transfers from the SSG accounts.

Sensitivity to SSG Account Investment Yields

The effect of the SSG Plan on the financial status of the OASDI program depends greatly on the actual yield that is achieved for investments in the SSG accounts. Returns on all investments are uncertain, and returns on stocks are particularly variable over time. For this reason it is important to consider the sensitivity of the financial status of the OASDI program to possible variation in expected investment yield. Note that the 1999 Trustees Report provides this sensitivity analysis for the OASDI program under current law on page 138.

The table below provides the estimated OASDI actuarial balance, the change in the actuarial balance, and the estimated year of combined OASDI trust fund exhaustion for the SSG Plan with two different SSG yield assumptions in order to illustrate the sensitivity of the proposal to possible variation in the ultimate average returns on stock and corporate bonds.

Under sensitivity illustration 2, the average yield on SSG accounts is assumed to be 1 percentage point higher than expected for the accounts invested in 60 percent stock and 40 percent corporate bonds. Under this illustration, the OASDI trust fund ratio would be expected to decline to about 215 percent at the beginning of 2036, and to increase thereafter. The actuarial deficit would be eliminated under the SSG plan, and the combined OASDI payroll tax rate could be reduced from 12.4 percent to 9.4 percent for 2040 to2049, 6.4 percent for 2050 to 2059, and 4.4 percent for 2060 and later. Even with these reductions in the payroll tax

Sensitivity Analysis: Effect of Variation in Expected SSG Investment Yield Rates on OASDI Financial Status

	Estimated OASDI Actuarial Balance	Estimated Change in OASDI Actuarial Balance	Year Exhaust OASDI Trust Funds
	(percent of taxable payroll)		
Present Law (No SSG)	-2.07	--	2034
2: SSG Plan with 1% Higher Than Expected Yield 2/ 6.35% average net yield	+0.07	2.13	NA
2A: SSG Plan with 1% Higher Than Expected Yield Without Reduced Payroll Tax 6.35% average net yield	+1.69	3.76	NA
3A: SSG Plan with 1% Lower Than Expected Yield 3/ 4.35% average net yield	-0.08	1.98	2048

1/ Payroll tax rate reduced to 9.4 in 2040 , 6.4 in 2050, and 4.4 in 2060.
2/ No payroll tax rate reduction.

Based on intermediate assumptions of the 1999 Trustees Report and other assumptions described in the text.

rate, the trust fund ratio would be expected to be stable at about 100 percent at the end of the long-range 75-year projection period and the actuarial balance would be estimate positive 0.07 percent of payroll. Without the reduced payroll tax rate, illustration 2A, the OASDI trust fund ratio would be expected to rise to more than 50 times annual OASDI net cost (net of SSG transfers) by the end of the long-range period and the actuarial balance would be a positive 1.69 percent of payroll.

Under sensitivity illustration 3A, the average yield on SSG accounts is assumed to be 1 percentage point lower than expected for the accounts invested in 60 percent stock and 40 percent corporate bonds. Under this illustration, the OASDI trust fund ratio would be expected to become exhausted in 2048. However, the OASDI actuarial balance would be improved by about 1.98 percent of taxable payroll under this assumption, leaving an actuarial deficit of only 0.08 percent of payroll.

Annual Estimates of SSG Fund Operations and Estimated Effects on the Unified Budget Balance

Tables 1b, attached, provides estimates of aggregate SSG account balances, total contributions to and transfers from SSG accounts, and rough estimates of the effects of other changes to the OASDI program (earnings test elimination). A very rough estimate of the effects of the SSG Plan on the annual Federal unified budget balance for ***calendar years*** 2000 and later is also provided.

These estimates are based completely on the intermediate assumptions of the 1999 Trustees Report, including the trust-fund interest assumption, and thus are not consistent with projections made by CBO and OMB (which use different assumptions. However, differences in payroll and benefit estimates are not large during the first 10 projection years so these values can be viewed as very rough approximations of the magnitude of effects on the unified budget balances through this period.

Under the SSG plan with the expected yield on the specified account portfolio, amounts transferred from the SSG accounts to the OASDI trust funds would at first be small, but would exceed credits to the SSG accounts from the General Fund of the Treasury by about 2031. Including the relatively small effects of the elimination of the earnings test at ages 62 and above, the estimated change in the unified budget " cash flow" (excluding interest effects) would also be negative until 2031. Including the cumulative effects of interest and the change in the OASDI payroll tax rate, the year in which the effect of the SSG plan on the unified budget annual balance would be expected to become permanently positive is 2054.

Stephen C. Goss

Attachments

Table 1 — a 2% SSG Account, Self Ann, 100% Benefit Offset, Elim Earns Test — IA Cntrb 2 %, Ben Offset 100.0 %

SSG to Heirs — With Ult Real TF Int Rate of 3.0

at Death <65 — With Ult Real IA Yld Rate of 5.35

i, No Survivor — With Annuity Net Yld Rate 5.35

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.78	12.66	1.88	217		12.40	0.00
2001	10.86	12.68	1.81	237		12.40	4.00
2002	10.97	12.68	1.71	256		12.40	2.00
2003	11.06	12.68	1.63	273		12.40	2.00
2004	11.16	12.69	1.53	289		12.40	2.00
2005	11.25	12.70	1.46	303		12.40	2.00
2006	11.36	12.71	1.35	316		12.40	2.00
2007	11.45	12.72	1.27	327		12.40	2.00
2008	11.56	12.73	1.17	338		12.40	2.00
2009	11.70	12.74	1.04	347		12.40	2.00
2010	11.86	12.76	0.90	354		12.40	2.00
2011	12.02	12.76	0.74	361		12.40	2.00
2012	12.23	12.77	0.54	366		12.40	2.00
2013	12.46	12.79	0.33	369		12.40	2.00
2014	12.71	12.80	0.10	370		12.40	2.00
2015	12.97	12.82	-0.16	370		12.40	2.00
2016	13.24	12.84	-0.40	367		12.40	2.00
2017	13.52	12.86	-0.67	363		12.40	2.00
2018	13.80	12.87	-0.93	357		12.40	2.00
2019	14.09	12.89	-1.20	350		12.40	2.00
2020	14.38	12.91	-1.46	341		12.40	2.00
2021	14.64	12.94	-1.70	331		12.40	2.00
2022	14.86	12.96	-1.90	321		12.40	2.00
2023	15.07	12.97	-2.09	311		12.40	2.00
2024	15.26	12.99	-2.28	299		12.40	2.00
2025	15.41	13.01	-2.40	287		12.40	2.00
2026	15.55	13.03	-2.52	275		12.40	2.00
2027	15.68	13.04	-2.61	262		12.40	2.00
2028	15.73	13.06	-2.67	250		12.40	2.00
2029	15.77	13.07	-2.69	237		12.40	2.00
2030	15.77	13.09	-2.68	225		12.40	2.00
2031	15.74	13.10	-2.64	212		12.40	2.00
2032	15.70	13.11	-2.58	200		12.40	2.00
2033	15.62	13.13	-2.49	188		12.40	2.00
2034	15.49	13.13	-2.36	178		12.40	2.00
2035	15.33	13.14	-2.19	167		12.40	2.00
2036	15.14	13.15	-1.99	158		12.40	2.00
2037	14.93	13.15	-1.78	150		12.40	2.00
2038	14.69	13.16	-1.54	143		12.40	2.00
2039	14.44	13.16	-1.28	138		12.40	2.00
2040	14.18	13.17	-1.01	134		12.40	2.00
2041	13.90	13.17	-0.73	132		12.40	2.00
2042	13.64	13.18	-0.47	132		12.40	2.00
2043	13.39	13.18	-0.21	134		12.40	2.00
2044	13.15	13.18	0.04	137		12.40	2.00
2045	12.91	13.19	0.28	143		12.40	2.00
2046	12.67	13.19	0.52	150		12.40	2.00
2047	12.45	13.20	0.75	160		12.40	2.00
2048	12.24	13.20	0.97	172		12.40	2.00
2049	12.03	13.21	1.17	186		12.40	2.00
2050	11.84	10.71	-1.13	203	-2.50	9.90	2.00
2051	11.67	10.72	-0.95	201		9.90	2.00
2052	11.51	10.72	-0.79	199		9.90	2.00
2053	11.37	10.73	-0.64	199		9.90	2.00
2054	11.24	10.74	-0.50	200		9.90	2.00
2055	11.11	10.75	-0.37	201		9.90	2.00
2056	11.00	10.75	-0.25	204		9.90	2.00
2057	10.89	10.76	-0.13	208		9.90	2.00
2058	10.79	10.77	-0.02	213		9.90	2.00
2059	10.70	10.78	0.08	219		9.90	2.00
2060	10.61	9.78	-0.83	226	-1.00	8.90	2.00
2061	10.53	9.79	-0.74	224		8.90	2.00
2062	10.45	9.79	-0.65	224		8.90	2.00
2063	10.38	9.80	-0.58	223		8.90	2.00
2064	10.31	9.81	-0.51	224		8.90	2.00
2065	10.26	9.81	-0.45	224		8.90	2.00
2066	10.21	9.82	-0.39	226		8.90	2.00
2067	10.17	9.82	-0.35	227		8.90	2.00
2068	10.14	9.83	-0.31	229		8.90	2.00
2069	10.11	9.83	-0.28	231		8.90	2.00
2070	10.10	9.83	-0.26	233		8.90	2.00
2071	10.09	9.84	-0.25	236		8.90	2.00
2072	10.09	9.84	-0.25	238		8.90	2.00
2073	10.10	9.85	-0.25	240		8.90	2.00
2074	10.11	9.85	-0.26	242		8.90	2.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	12.84	12.92	0.09	2.16

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset

Office of the Actuary
Social Security Administration
April 28, 1999

Table 1 b IA Contributions, Transfers to OASDI from IA, & Unified Budget Effect

99 TR ECON | IA Cntrb 2 %, | Benefit Offset 100.0 %

Year	IA Account Balance at End of Year	Amount Contrib to IA % by GenFnx *100*	Transfer to OASDI from IA	Other Changes in OASDI CashFlow	Change in Annual UnifBudg CashFlow	Change in Debt Held by Public (EOY)	Change in Ann UnifBudg Balance
				(Billions of Current $)			
2000	0.0	0.0	0.0	0.0	0.0	0.0	0.0
2001	159.6	157.9	0.0	-1.5	-159.3	-164.1	-164.1
2002	256.1	82.2	0.2	-2.6	-84.5	-261.0	-96.8
2003	363.8	85.7	0.5	-3.4	-88.6	-367.7	-106.7
2004	483.6	89.6	1.0	-4.3	-92.9	-484.9	-117.2
2005	617.0	93.9	1.6	-5.0	-97.3	-613.5	-128.6
2006	765.2	98.4	2.6	-5.8	-101.6	-764.5	-141.0
2007	929.7	103.2	3.5	-5.7	-106.4	-907.9	-1[illegible]3.3
2008	1,112.0	108.3	4.9	-6.4	-108.8	-1,074.3	-166.5
2009	1,314.0	113.7	6.5	-5.2	-112.3	-1,255.3	-181.0
2010	1,537.7	119.3	8.6	-4.9	-116.6	-1,461.7	-196.4
2011	1,785.0	125.1	11.0	-4.6	-118.7	-1,664.6	-212.9
2012	2,057.9	131.0	14.0	-4.4	-121.5	-1,896.0	-230.4
2013	2,358.7	137.2	17.6	-4.3	-124.0	-2,144.2	-249.2
2014	2,689.0	143.6	21.6	-4.2	-126.1	-2,411.6	-267.3
2015	3,049.9	150.2	26.4	-4.0	-127.8	-2,697.7	-286.1
2016	3,443.6	157.0	32.0	-3.8	-128.8	-3,003.2	-305.6
2017	3,872.0	164.1	38.5	-3.7	-129.3	-3,328.7	-325.5
2018	4,337.7	171.5	46.1	-3.6	-129.1	-3,674.8	-346.1
2019	4,842.9	179.2	54.7	-3.5	-128.0	-4,042.0	-367.2
2020	5,390.1	187.1	64.8	-3.5	-126.0	-4,430.6	-388.5
2021	5,981.7	195.3	75.9	-3.4	-122.8	-4,840.8	-410.2
2022	6,620.3	204.0	88.8	-2.4	-117.5	-5,271.9	-431.0
2023	7,308.6	212.8	103.3	-1.2	-110.7	-5,723.4	-451.5
2024	8,049.1	222.1	119.8	0.1	-102.2	-6,195.0	-471.6
2025	8,844.7	231.8	138.4	1.5	-91.6	-6,686.2	-491.1
2026	9,698.0	241.9	159.3	3.1	-79.4	-7,195.9	-509.6
2027	10,611.9	252.4	182.5	4.2	-65.4	-7,723.8	-527.9
2028	11,589.2	263.4	209.1	5.4	-49.0	-8,268.6	-544.8
2029	12,632.7	276.1	238.4	6.6	-30.1	-8,828.6	-560.1
2030	13,745.1	287.3	271.2	7.9	-8.2	-9,402.2	-573.5
2031	14,929.2	300.0	307.5	9.2	16.8	-9,986.6	-584.3
2032	16,187.4	313.4	348.1	10.1	44.8	-10,579.4	-592.8
2033	17,522.0	327.3	393.0	11.0	76.7	-11,177.2	-597.9
2034	18,935.2	341.9	442.7	11.9	112.7	-11,776.2	-599.0
2035	20,429.0	357.2	497.8	12.8	153.3	-12,371.7	-595.5
2036	22,004.9	373.2	558.3	13.8	198.9	-12,958.3	-586.5
2037	23,664.1	390.0	625.3	14.8	250.1	-13,528.6	-571.2
2038	25,407.3	407.5	699.1	15.8	307.5	-14,078.1	-548.6
2039	27,234.4	425.7	780.4	16.9	371.6	-14,595.6	-517.5
2040	29,144.8	444.6	869.8	18.0	443.2	-15,072.4	-478.8
2041	31,136.9	464.3	968.1	19.2	523.0	-15,497.4	-425.0
2042	33,213.8	484.8	1,070.8	19.9	605.9	-15,864.1	-366.6
2043	35,376.4	506.2	1,180.6	20.6	696.0	-16,162.3	-298.2
2044	37,626.0	528.4	1,297.6	21.4	790.6	-16,381.0	-218.7
2045	39,960.0	551.5	1,422.2	22.2	892.9	-16,508.2	-127.2
2046	42,381.5	575.7	1,554.6	23.0	1,002.0	-16,531.0	-22.8
2047	44,889.2	600.7	1,695.1	23.9	1,118.3	-16,435.3	95.7
2048	47,482.8	626.8	1,843.9	24.8	1,241.9	-16,206.1	229.3
2049	50,161.5	654.0	2,001.3	25.7	1,373.0	-15,826.8	379.2
2050	52,924.5	682.2	2,167.4	-826.1	659.1	-16,159.8	-332.9
2051	55,770.5	711.6	2,342.5	-861.8	769.0	-16,400.6	-240.8
2052	58,698.3	742.2	2,526.6	-898.9	886.5	-16,536.6	-136.0
2053	61,706.1	774.0	2,720.1	-937.6	1,008.5	-16,554.5	-17.9
2054	64,792.3	807.3	2,922.9	-977.9	1,137.7	-16,440.3	114.3
2055	67,954.7	841.9	3,136.3	-1,019.9	1,273.5	-16,178.6	26[illegible].6
2056	71,191.1	878.0	3,357.3	-1,063.6	1,415.6	-15,763.7	424.9
2057	74,499.2	915.7	3,588.9	-1,109.3	1,563.9	-15,148.7	605.0
2058	77,876.4	955.0	3,830.1	-1,157.0	1,718.1	-14,345.8	802.9
2059	81,320.0	996.1	4,081.1	-1,208.8	1,879.2	-13,326.4	1,019.4
2060	84,827.3	1,038.9	4,341.7	-1,778.3	1,624.5	-12,606.6	719.8
2061	88,395.1	1,083.6	4,611.9	-1,854.9	1,673.4	-11,687.2	919.4
2062	92,020.4	1,130.3	4,891.8	-1,934.4	1,827.1	-10,550.4	1,136.8
2063	95,699.9	1,178.0	5,181.1	-2,017.2	1,984.9	-9,178.1	1,372.3
2064	99,430.4	1,228.9	5,480.0	-2,103.9	2,146.2	-7,551.6	1,626.5
2065	103,208.0	1,282.9	5,788.4	-2,194.0	2,311.5	-5,650.5	1,901.1
2066	107,028.5	1,338.1	6,106.3	-2,288.0	2,480.2	-3,463.8	2,196.8
2067	110,888.5	1,396.7	6,434.0	-2,388.0	2,652.2	-939.0	[illegible],514.6
2068	114,782.3	1,455.8	6,771.4	-2,488.2	2,827.4	1,917.4	2,856.4
2069	118,704.9	1,518.4	7,118.9	-2,594.7	3,006.8	5,140.5	3,223.2
2070	122,650.2	1,583.6	7,476.5	-2,705.6	3,187.4	8,757.3	3,616.7
2071	126,611.4	1,651.6	7,845.2	-2,821.1	3,372.5	12,788.3	4,039.1
2072	130,580.5	1,722.4	8,225.0	-2,941.4	3,561.2	17,288.5	4,492.2
2073	134,548.3	1,796.2	8,616.7	-3,066.7	3,763.5	22,286.8	4,976.3
2074	138,493.3	1,877.2	9,034.8	-3,204.4	3,953.2	27,769.4	5,502.8

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.0 TF,

Ultimate Real Yield Rate of IA 5.35
(Annuity Yield 5.35

Office of the Actuary
Social Security Administration
April 28, 1999

THE WHITE HOUSE

WASHINGTON

ECONOMIC TEAM MEETING

April 29, 1999

The Cabinet Room; 10:50am

AGENDA

I. Debt Reduction Endgames: What Would Be a Victory?
   - A. Debt reduction without extending Social Security?
   - B. Debt reduction and Medicare reform?
   - C. Only debt reduction that extends Social Security?

II. Extending the Trust Fund by 75 Years Within the State of the Union Framework

III. Plans that Combine Trust Fund Investments with Progressive Individual Accounts
   - A. SOTU plan with add-on individual accounts
   - B. Mirror account approach to trust fund investments

IV. Archer-Shaw Plan

V. Process Options for Moving Forward

1. Possible Endgames Without a Social Security Deal

A. Could Claim Victory for Debt Reduction Even Without Extending the Social Security Trust Fund

- Announce that we agree that Social Security should be taken out of the budget, and that the Social Security surplus should be used only for debt reduction.

Advantages:

- Huge win for fiscal discipline -- especially when compared with the large tax cuts the Republicans were proposing last year using the unified surpluses.

- This could be seen as the next, most impressive, step by a fiscally responsible President who not only eliminated the unified budget deficit, but is now taking a historic step to pay off the national debt and make the Social Security trust funds "real."

Disadvantages:

- If we embrace this now, we may lose our leverage for obtaining bond transfers to extend the Social Security trust fund.

- Reaching a budget deal without surplus transfers for Social Security would increase the chance that any future Social Security reform will rely more heavily on benefit cuts, tax increases, or carve-out style individual accounts.

- Cutting a deal at the end of the year to allocate the on-budget surplus to discretionary spending and tax cuts could be seen as abandoning commitment to "Save Social Security First."

Two Key Issues:

- **Getting Credit for Debt Reduction Victory.** If at the end of the year the main accomplishment is dramatic debt reduction, it will clearly be a Clinton accomplishment spurred primarily by the President's Save Social Security agenda. Yet if we are seen as repeatedly attacking Republican lockbox proposals, this outcome could ironically be seen as a Republican win and a White House loss.

- **USA Accounts without Social Security Reform.** Would we still be in favor of USA accounts in the absence of extending the Social Security trust fund? This outcome could be seen as giving individual accounts (and a tax cut) to Republicans without receiving anything for Social Security in exchange.

B. Claim Victory if We Get Debt Reduction and Extend Medicare Even Without an Extension of Social Security.

- If we can reach an agreement to commit substantial new resources to the Medicare trust fund, it may be worth cutting a deal to allocate the rest of the on-budget surplus -- even without extending the Social Security trust fund.

Advantages:

- Strengthening Medicare and putting the country on a path to eliminating the national debt would be a major accomplishment even in the absence of a Social Security deal.

Disadvantages:

- Would violate "Save Social Security First" commitment.

Key Issues:

- Would this be enough of a win to let Republicans have some tax cuts?

- Would we be in favor of USA accounts in this context, or would we be giving the Republicans individual accounts without getting a stronger traditional Social Security system in return?

C. Require That Debt Reduction Be Combined With Crediting The Benefits of Debt Reduction to Social Security.

- If comprehensive Social Security reform falters, this could be a partial victory in a larger end-of-the-year budget negotiation.

Advantages:

- Would lock in debt reduction, show partial progress on Social Security, and make irresponsible tax cuts and radical privatization less likely in the future.

- Provides a way to get a partial Social Security victory at the end of the year if the process has broken down.

Disadvantages:

- Would extend the trust fund by less than under any full reform plan and by significantly less than the 2055 we initially described as a partial victory in our SOTU package.

- Could let Republicans off the hook on tax cuts, without ensuring a long term fix for Social Security.

Key Issues:

- Would partial extension of the trust fund be enough of a Social Security victory to relax our Social Security first requirement and allow for tax cuts or USA accounts?

  -- We could offer Republicans a deal such as $1 of tax cuts for every $4 of bonds given to the Social Security and Medicare trust fund.

ALTERNATIVE WAYS OF TRANSFERRING BONDS TO THE TRUST FUNDS: POSSIBLE OPTIONS TO GAIN MORE SUPPORT FOR USING DEBT REDUCTION TO EXTEND SOCIAL SECURITY

Mechanisms to Strengthen the Case for Using Debt Reduction to Extend Social Security Solvency:

1. Justify annual transfers based on the interest savings from debt reduction.
2. Make large transfers equal to the total amount of debt reduction accomplished only after the fact and only if debt reduction actually occurs.

Key Challenge:

- Under conventional budget accounting, the transfers (and the interest on past transfers) will reduce the on-budget surplus available for other purposes.
- We will need to postpone most or all of the actual transfers until after 2014 if we want to afford the rest of your SOTU package using only the on-budget surpluses.

New Options:

- **One time transfer of bonds.** Record every year the amount of debt reduction that occurs. At the end of 15-years, make a one time transfer of bonds to Social Security in the amount of the total debt reduction achieved. (Will cause a large on-budget deficit in the year of the transfer). Will extend solvency until around 2046.

- **Transfer interest savings starting in 2015.** Record every year the amount of debt reduction that occurs. At the end of the 15-year period, begin transferring the interest savings from the debt reduction that occurred in the first 15 years. (Another option would be to simply call for general revenue transfers after 2015 unlinked to debt reduction). Will extend solvency until 2043 or 2044.

- **Accumulate annual interest savings, then transfer starting in 2015.** For the first 15-years, record the interest savings that occur from paying down debt. In the 15th year, make a one-time transfer of the total interest savings. From that year on, make additional transfers of the annual interest savings from the debt reduction that has occurred. Will extend solvency until around 2046. However, the interest owed to the trust fund will lead to on-budget deficits between 2027 and 2037.

Note: All of these options improve the 75-year actuarial balance by roughly one-third - from -2.07 to around -1.40.

II. Completion of President's SOTU Plan: Real Reforms, Including Expanded Widow Benefit and Repeal of Earnings Test

- Do trust fund transfers and equity investments as in the President's State of the Union plan (extends trust fund to 2060 with 7 percent real return on equities).

- Include new widow benefit at 75 percent of the combined benefits the married couple received when both spouses were alive (capped at the average worker-only benefit), repeal earnings test, and do traditional reforms to extend trust fund to 2075

Issue:

- This approach requires us to win on both equity investments and bond transfers.

SOTU PLAN	
Current 75-year OASDI balance	- 2.07
Change from surplus transfer and equity investment	+1.52
Remaining Balance	**-0.56**
Without equities the remaining balance would be -1.05.	

SOME REAL REFORMS	
Enhanced Widow Benefit	**- 0.07**
• Will lessen poverty for this group.	
Repeal Earnings Test	**0.00**
• Has some short term revenue impact.	
Maintain Share of All Earnings Taxed at 85.65 Percent of Payroll	**+0.11**
• A tax increase of $645 for someone making $78,000 or more.	
Change Formula for Calculating Benefits So That Benefits Grow Slightly Slower than Wages (But Still More than Inflation)	**+0.15**
• A benefit cut of 3 percent by 2045.	
Eliminate the hiatus in the normal retirement age	**+0.15**
• Raises the retirement age by a year for someone retiring between 2011 and 2017.	
Remaining Balance	**- 0.30**

SOME OPTIONS FOR LAST PORTION (CHOOSE ANY 2)	
Further Raise Share of Earnings Taxed to 87.5 Percent of Payroll	**+0.19**
• A further tax increase of $1847 for those earning over $92,700.	
Progressive Benefit Cut for Those with Average Earnings Above $36,000	**+0.19**
• Would cut benefits by about 5 percent for the top third of earners.	
Cover New State and Local Hires Starting in 2020	**+0.16**
Increase Number of Years Used in Calculating Benefits from 35 to 38	**+0.17**
• Disproportionately impacts low-wage workers and women.	

Using Automatic Indexing and Triggers to Make Program Changes

Description:

- Legislate the benefit reductions or revenue increases in out years that would be required to achieve 75-year actuarial balance, but allow such cuts or revenue increases to be nullified or "triggered off" if stronger economic performance or improved demographics make the measures unnecessary.

Possible Justifications:

- Significant uncertainty concerning future requires prudent assumptions but also recognition that one should not impose needless sacrifice if assumptions prove pessimistic.

- Clinton plan calls for significant increase in national savings, without building growth dividend into assumptions.

- Some feel long term assumptions do not recognize improved productivity trends due to technological advances.

Advantages:

- Reasonable policy response to long term policy making under uncertainty.

- Possibility that measures requiring sacrifice will not happen may dampen intensity of opposition to measures.

Disadvantages:

- **Not taken seriously.** Elite media could see as way to duck the need to tell people that sacrifice is required.

- **Taken too seriously.** "Trigger off" provisions ignored and mechanism attacked as benefit cuts and tax increases.

III. Plans that Combine Reform of Traditional Social Security with the Establishment of Progressive Individual Accounts

III.A Combine SOTU plan with Individual Accounts to Give Both Sides a Win

- Our message would be that we are strengthening the traditional Social Security system in the way that Ball and others have urged.

- Could insist that any individual accounts make the overall system more progressive.
  - -- Individual accounts could look a lot like USA accounts.

- Could let description of individual accounts be ambiguous enough that Republicans could claim that they got individual accounts within Social Security, while we claimed we protected the entire 12.4 percent payroll tax for the traditional benefit and set up USAs outside of Social Security.

Change in Benefits in 2045
(as percentage of current law benefits)

	Low Earner ($13,000)	Moderate Earner ($30,000)	High Earner ($48,000)
Approximate Benefit Cuts in 75-year version of SOTU plan	3 to 7 percent	3 to 6 percent	3 to 8 percent
Impact of 1 percent individual account	+9 percent	+12 percent	+14.5 percent
Impact of $300 per worker individual account	+17 percent	+12 percent	+9 percent
Impact of maximum USA account	+56 percent	+40 percent	+30 percent
Impact of automatic portion of USA accounts.	+17 percent	+6 percent	+ 0 percent

III.B Have Trust Fund Investments "Mirror" Investment Choices Made by Individuals in Their Individual Accounts

- Our goal is to take resources from the surplus and to invest them for higher returns on behalf of the Social Security Trust Fund so as to strengthen the traditional Social Security guaranteed benefit. However, as we had feared, the collective approach to investing has run into significant political opposition.

- We need a mechanism for investing on behalf of the trust fund while providing more individual choice over the investments.

- With an acceptable mechanism, it might be possible to do even more equity investment than occurs in your State of the Union plan. For example, the Archer-Shaw plan reaches 75-year actuarial balance because it relies more heavily on equity investments than your plan does (and because it receives general fund transfers for a longer period of time).

<u>Possible Mechanisms:</u>

- **Have Trust Fund Investments Mirror the Investments in Individual Accounts or USAs.**
  - -- For example, if there were 10 authorized private sector mutual funds in which the individual accounts could be invested, the trust fund could invest with the same managers in proportion to how the individual accounts were allocated.
  - -- Might be more acceptable form of investment for trust fund because:
    - Would create perception of equity investments arising from aggregation of individual choices as opposed to from central government control.
    - Could be less potential for political interference because individual investors would resist attempts to restrict the portfolios in which their individual accounts were invested.

- There are likely to be other similar mechanisms that would allow the Social Security trust fund in invest in equities while providing the perception of individual choice.

An Example of a Possible Plan

- Same transfers from surplus to the trust fund as in the State of the Union plan.
- Equity investments occur in same stock index fund that will be used for USAs.
- With half of the trust fund invested like individual accounts, we would have around 25 percent of the trust fund in stocks rather than 14.6 percent,
  - -- The Social Security trust fund would be extended until 2068 and the remaining actuarial balance would be -0.22 percent of payroll.
  - -- Investments in the market would constitute up to 11 percent of the stock market.

- **Refundable tax credit equal to 2 percent of payroll coming out of Social Security surpluses and general revenues and directed into individual accounts.**

  -- The plan description says that the tax credits will be financed out of the Social Security surpluses (without reducing the amount of bonds given to the trust fund). There is some ambiguity about what this means. However, conventional scoring would say that the financing is coming out of general revenues.

- **Social Security Trust Fund Buffers Individual Accounts to Guarantee Current Law Benefit Levels**

  -- Most individuals will receive exactly the same Social Security benefit they would receive under current law. The individual account will be annuitized and provide part of the Social Security benefit. The Social Security trust fund will make up the rest using financing from the 12.4 percent payroll tax.

  -- In the occasional case in which the income from the individual account is greater than the current law Social Security benefit, the individual receives the income from the individual account and therefore receives more than their current-law benefit.

- **Individuals will be able to pick fund managers, but not investment mix.** All accounts will be required to be invested in index fund portfolios providing a 60-40 split between stocks and bonds. This mandated investment portfolio was necessary to get the 5.3 percent rate of return required to extend the trust fund for 75 years.

- **Plan will Require Mandatory Annuitization at Retirement.** No withdrawal will be permitted for any purpose other than retirement income. In the event of death before age 65, the accounts could be bequeathed so long as the individual has not previously received Social Security benefits (including disability benefits).

Advantages:

- Sets aside large portions of budget surplus to strengthen the traditional Social Security benefit.

- Obtains higher returns to help strengthen the traditional Social Security benefit.

- The entire 12.4 percent of the payroll tax continues to go to fund the traditional benefit.

- Retains progressivity of the traditional benefit. General revenue financing adds more progressive financing to the system.

- Serious attempt to deal with corporate governance and political interference issues that arise from investing on behalf of the trust fund.

- Pro-savings plan which locks up surpluses to pay for existing Social Security commitments. By prefunding now, reduces the need to issue debt to finance benefits later.

Disadvantages:

- May create the appearance that the individual account is providing most of the Social Security benefit using revenue equal to only 2 percent of payroll, compared to the 12.4 percent of payroll which funds the balance of the benefit. This could create pressure for later privatization of Social Security.

- The relatively small fraction of people who will receive benefits 30 or 40 years down the road that are greater than current law Social Security benefits will be concentrated among higher income beneficiaries. In contrast, our USA account concentrates its benefits on low-income households.

- Unnecessarily spends billions of dollars on administrative costs to create the perception of individual accounts when the investments could be done far more efficiently through collective investment with protections against political interference.

- Heavy reliance on equity financing of traditional benefit creates stock market risk for the government -- though some would say the trust fund is unlikely to be worse off than from investing in bonds.

- Relies completely on general revenues and higher returns, instead of seeking tougher choices that would free more resources for other priorities.

- By taking 2 percent in perpetuity regardless of surpluses, it could force deficits down the road that would lead to reductions in investments in other key priorities.

Some Process Options for Moving Forward

Option 1: Announce Marginal Adjustments within SOTU Plan

1.A Release details on how to achieve 75-year balance within the SOTU framework.

1.B Show new approaches to transferring bonds based upon the gains from debt reduction.

1.C Embrace taking Social Security out-of-the-budget, and show how to fit the SOTU program within the out-of-the-budget framework.

Option 2: Make Offer to Pass Legislation on USA-type Individual Accounts and Social Security Solvency at the Same Time.

- Would still require that individual USA accounts be outside of Social Security, but by linking passage of Social Security solvency legislation and USAs, it would allow Republicans to claim a win on individual accounts and Democrats to claim a win on protecting Social Security without any privatization.

Option 3: Seek to Work to Get Some Democrats to Float Possible Common Ground Proposals That the President Could Send Encouraging Signals about.

- Potential people could include Conrad, Lieberman, Cardin, and Pomeroy.

Option 4: Cardin Suggestion: Announce that we would accept a USA-type account as a supplementary Social Security account if 12.4 percent is protected for defined benefits and we can make an equivalent collective equity investment.

THE WHITE HOUSE

WASHINGTON

May 5, 1999

MEMORANDUM FOR JOHN PODESTA
STEPHANIE STREETT
KAREN TRAMONTANO

FROM: GENE SPERLING

SUBJECT: Social Security/Medicare Meetings Request

I would like to propose a list of four upcoming meetings we need to have with the President on two of our more pressing economic issues – Social Security and Medicare.

I appreciate the scheduling burden all of you are under with respect to Kosovo, Columbine, Oklahoma, and other pressing matters, but delaying these meetings will soon begin to have a seriously negative impact on our strategy for these two issues.

The four meetings I would propose for the period of May 10-21 are:

- **Social Security Strategy Meeting.** We need to sit down with the President and further discuss several strategic and tactical options for moving ahead.

- **House Ways & Means Democrats on Social Security.** We need to schedule a meeting – following the strategy meeting discussed above -- with the President and Democratic members of the Ways & Means Committee. We could consider adding some Senate Democrats, but we need to ensure that we allow Rangel and Matsui the same time we will give to Chairman Archer and Representative Shaw.

- **Meeting or Call with Archer, Shaw.** Following the President's meeting with Ways & Means Democrats, he will need to meet with or call two critical Republicans on Social Security -- Chairman Archer and Rep. Shaw.

- **Medicare Meeting.** We need to hold a one and a half hour meeting with the President and his economic/budget advisors to discuss preliminary options for the President's Medicare proposal and our basic choices over premium support, prescription drugs, and savings. We need to get guidance from the President so we can proceed expeditiously on final choices for a plan. We have prepared a briefing book for him that we can send to him a few days prior to the meeting.

I appreciate your attention to this, and would be happy to discuss it further with any or all of you.

THE WHITE HOUSE

WASHINGTON

ECONOMIC TEAM MEETING

May 12, 1999

The Cabinet Room; 2:00-3:00pm

AGENDA

I. POSSIBLE GOALS

II. OPTIONS:

1a. 75-Year Solvency Plus USAs
1b. Variation with Adjustments to the SOTU Plan

2a. Incremental Plans To Lock in Debt Reduction and Partially Extend Solvency
2b. Variation with Equity Investment
2c. Variation with Scaled-Back Program

3a. An Incremental Plan
3b. Incremental Plan Compromise

POSSIBLE GOALS

- **To extend Social Security solvency for 75 years.**

  -- If real reform is possible, this is the prize.

- **To extend Social Security solvency enough to allow use of the surplus.**

  -- "Saving Social Security first" will provide flexibility for other goals: seeking adequate funding of core government, advancing USAs, using surplus for Medicare reform and prescription drugs.

- **To demonstrate leadership.**

  -- Proposing Social Security reform would show that you are moving forward, setting the agenda.

- **To avoid being tarred as the ones who killed Social Security reform.**

  -- Democrats need to avoid being seen as the ones who stood in the way of reform that people see as needed.

- **To maintain the roadblock to too-large tax cuts.**

  -- Allowing use of the surplus without effectively reserving or displacing it could pave the way for tax cuts so large that they create deficits well into the future.

- **To keep Democrats together.**

OPTION 1:: 75-YEAR SOLVENCY PLUS USAs

- **SOTU Plan.** Do trust fund transfers and equity investments as in the State of the Union plan -- extends Trust Fund solvency to 2060 if one assumes a 7 percent return on equities.

- **Additional reforms.** Do traditional reforms to extend Trust Fund solvency to 2075, include a new widow benefit at 75 percent of the combined benefits the married couple received when both spouses were alive (capped at the average worker-only benefit), and repeal the earnings test.

- **Offer to pass a Social Security solvency plan at the same time with USA-type accounts to give both sides a win.** Individual USAs would still be outside of Social Security. Republicans could claim a win on individual accounts and Democrats could claim a win on protecting Social Security without privatization. We must be willing to work with Republicans on the exact design of the accounts and solvency plan.

The SOTU Plan	
Current 75-year OASDI balance	-2.07
Transfer surplus and invest in equities	+1.52
Remaining balance	**-0.56**

Additional Reforms	
Enhance widow benefit (lessens poverty in this group)	-0.07
Repeal earnings test (a short-term revenue loss)	0
Maintain share of earnings taxed at 85.65 percent of payroll -- a $645 tax increase for workers making $78,000 or more	+0.11
Change formula for calculating benefits so that benefits go up faster than prices but slightly slower than wages -- a 3 percent benefit cut by 2045	+0.19
Eliminate the hiatus in the normal retirement age -- raises retirement age by as much as a year for workers retiring between 2011 and 2017	+0.15
Remaining balance	**-0.21**

Options for the Last Piece (Choose any 2)	
Further raise the share of earnings taxed to 87.5 percent of payroll -- a further tax increase of $1847 for workers earning over $92,700	+0.19
Progressive benefit cut for those with earnings above $36,000 -- about a 5 percent benefit cut for the top third of earners	+0.19
Increase number of years used in calculating benefits from 35 to 38 -- disproportionately affects low-wage workers and women	+0.17
Fill the remaining gap or avoid any revenue measures by progressive benefit cuts that would be waived if solvency strengthens due to economic or demographic improvement	

Components do not add to total because of interactive effects.

VARIATIONS OF THE ADDITIONAL REFORMS

- **We could change the mixes of additional reforms to one of the following:**

A: Additional Reforms Without Revenues	
Eliminate the hiatus in the normal retirement age -- raises retirement age by as much as a year for workers retiring between 2011 and 2017	+0.15
Reduce growth in benefits for new retirees by 0.33 percent a year starting in 2012 and later. -- a 9.7 percent benefit cut by 2045	+0.61

B: Additional Reforms Without Changes to Normal Retirement Age	
Maintain share of earnings taxed at 85.65 percent of payroll -- a $645 tax increase for workers making $78,000 or more	+0.11
Reduce growth in benefits for new retirees by 0.33 a year starting in 2012 and later. -- a 9.7 percent benefit cut by 2045	+0.61

C: Additional Reforms With Greater Progressivity	
Maintain share of earnings taxed at 85.65 percent of payroll -- a $645 tax increase for workers making $78,000 or more	+0.11
Progressive benefit cut for those with earnings above $29,000 and Reduce the indexing of the second bend point by 2 percent a year starting 2012 through 2021	+0.61

Advantages

- **Leaves almost everyone better off:**

Change in Benefits in 2045 (as percentage of current law benefits)			
	Low Earner ($13,000)	Moderate Earner ($30,000)	High Earner ($48,000)
Approximate changes in 75-year solvency plan	0 to -4 percent	-3 to -6 percent	+2 to -7 percent
USA benefit*	+26 to +87 percent	+9 to +58 percent	0 to +47 percent

* assuming USA parameters grow at the rate of the Gross Domestic Product; benefit for a couple

- **Achieves 75-year solvency.**

- **Creates progressive individual accounts, outside of Social Security.**

- **Demonstrates leadership.**

- **Makes it easier to do Medicare reform.** Putting forward a 75-year solvency plan will make it easier to use some surplus for prescription drugs while maintaining Social Security first pledge.

Disadvantages

- **Some Congressional Democrats may argue** that it neutralizes a potential advantage in protecting the existing Social Security program against benefit cuts, and exposes Members to a potential attack for supporting Social Security benefits cuts.

- **Despite costs, could result in no real reform enacted.**

  -- Senator Lott may not want reform, and Speaker Hastert may not have the power to negotiate it.

- **Linking individual accounts to Social Security risks unfavorable comparisons of the two rates of returns.**

- **Linking individual accounts to Social Security will look more like an add-on.** Some Democrats will fear the slippery slope. It may highlight USA administrative problems.

OPTION 1(B): VARIATION WITH ADJUSTMENTS TO THE SOTU PLAN

- **Same as above, only adjust some features of the SOTU plan that received criticism.**

Possible Adjustment 1: Alleviate corporate governance concerns about centralized investment.

- Have trust fund investments mirror the investments in USAs.

- For example, if there were 10 authorized private sector mutual funds in which the USAs could be invested, the trust fund could invest with the same managers in proportion to how the USAs were allocated.

- Might be more acceptable form of investment for trust fund because:

  -- Would create perception of equity investments arising from aggregation of individual choices as opposed to from central government control.

  -- Could be less potential for political interference because individual investors would resist attempts to restrict the portfolios in which their individual accounts were invested.

- There are likely to be other similar mechanisms that would allow the Social Security trust fund in invest in equities while providing the perception of individual choice.

An Example of a Possible Plan
• For every dollar put into USAs by individuals, the government could invest 50 cents in the same stock index fund as used by the USAs.

Possible Adjustment 2: Clarify debt reduction for solvency plan.

- **Offer to work with Republicans to develop means to achieve debt reduction in a way that avoids perception of double-counting.**

  -- Do debt reduction as in the State of the Union plan, but make trust fund transfers after 15 years of paying down the debt.

  -- Shows transfers only after debt reduction has been achieved from off-budget surplus and may help combat the perception of double-counting.

  -- Will require additional reforms to make up for savings lost by delaying transfers from the timing in the SOTU plan.

OPTION 2: INCREMENTAL PLANS TO LOCK IN DEBT REDUCTION AND PARTIALLY EXTEND SOLVENCY

- **You could embrace the goal of achieving on-budget balance after a limited transition period.**

- **Devote on-budget surpluses for next 15 years to needed discretionary spending, phased-in USAs, and delayed Medicare transfers.**

  -- Under current projections, we would run on-budget deficits averaging $20 billion during the first 6 years, but would then achieve on-budget balance with full USAs and the same cumulative Medicare transfers as under the SOTU plan.

- **Begin transfers to Social Security in 2015 *if an only if* debt has been paid down.**

  -- If we transferred each year an amount equal to the interest savings from paying down debt, we would extend Social Security solvency until 2043.

Advantages

- It would block overly large tax cuts by taking resources off the table.

- It would ensure that benefit cuts and revenue increases actually add to national savings and thereby enhance our ability to pay Social Security benefits down the road.

- It would reinforce your reputation for fiscal discipline and responsibility.

- It would address criticisms of the SOTU plan and show movement toward the Republican budget resolution without giving up the key features of the SOTU plan.

- It would garner support from fiscal conservatives, elite media, and a variety of validators.

- It could move us toward an endgame like option 3.

Disadvantages

- It would make it harder to put forward a plan with 75-year solvency.

- It would leave less money for making transfers to Social Security and Medicare and for other priorities because the on-budget surpluses are smaller than the unified surpluses for many years.

- We would show an on-budget deficit during the first 6 years under OMB numbers.

OPTION 2(B): VARIATION WITH EQUITY INVESTMENT

- **Do the same as in option 2, only have the Trust Fund make equity investments.**

  -- We may have to employ the means in Option 1(B) to alleviate corporate governance concerns about centralized investment.

  -- If we invested 15 percent of the trust fund in equities, we would extend solvency further into the 2040s.

OPTION 2(C): VARIATION WITH SCALED-BACK PROGRAM

- **Do the same as in option 2, only scale back discretionary spending and USAs by one-third each to allow some Social Security transfers within the 15-year window. Use equity investment as necessary.**

OPTION 3: AN INCREMENTAL PLAN

- **Seek some amount of general-revenue transfers to the trust fund to extend solvency in exchange for locking in the entire Social Security surplus for debt reduction.**
  - -- You say that you will embrace the off-budget treatment of Social Security and the Republican point-of-order lock box (not the debt limit lock box) if we can agree on some method for extending solvency at least 15 years.

Advantages

- It is achievable.
- It would allow you to claim a clear victory for a result you more than any other have brought about – elimination of the on-budget deficit.
- It would be a huge win for fiscal responsibility. It would preserve a large fraction of the surpluses for debt reduction.
- It potentially sets up a Medicare-vs.-tax cut fight.

Disadvantages

- It does not address long-term solvency issues presented by the retirement of the baby boom generation.
- It could be criticized by fiscal conservatives as avoiding hard choices and failing to lead.
- It may not be enough to unblock access to the surpluses; that is, it may not meet the test of "saving Social Security first."
- We may not be able to get to this result simply by seeking it directly.

OPTION 3(B): INCREMENTAL PLAN COMPROMISE

- In order to get a final deal, in exchange for some amount of general-revenue transfers to the trust fund to extend solvency, we may have to allow both locking in the entire Social Security surplus for debt reduction plus some amount of tax cuts (perhaps in combination with some amount of Medicare and discretionary funding).