

# ***PERSONALLY SPEAKING***

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## **AMERICA: A BROKEN WELFARE STATE**

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*Permission to quote is granted when the source is acknowledged*

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A welfare state operates on the premise that there will be sufficient tax revenues to pay for the benefits promised. The American welfare state is broken because benefit expenditures are expanding faster than tax revenues and abuse grows as program spending increases. Our attention in the following focuses on the symptoms of that collapse in terms of four programs: Social Security retirement, Medicare, Medicaid, and unemployment insurance. We do not address the related problem of corporate welfare.

**Direct Symptoms.** The trustees of Social Security retirement state that the program will exhaust all of its more than \$2.2 trillion in assets by 2037 and will be able to pay retirees only 75 cents on every \$1 in benefits promised. The program's own actuary estimates that under the current tax/benefit schedule, the rate of return for a two-earner couple both of whom reach age 65 in 2038 with annual earnings of \$86,000 is 0.77 percent. Under a regime of higher taxes to prevent the exhaustion of trust fund reserves by 2037, the rate of return for single males who reach age 65 in 2038 with \$86,000 in annual earnings turns *negative!*

Responding to a Mayo Research Institute information request, SS stated that there are 50,314 retirees whose monthly benefit in 2010 has been cut to zero because their required Medicare contribution is greater than their retirement benefit. SS will bill these retirees for the difference.

The trustees of the Medicare Hospital Insurance Trust Fund estimate that the fund's assets will be exhausted by 2017. The trustees assert that reversing this outcome "will require very substantial increases in tax revenues and/or reductions in expenditures." The chief financial officer of the Centers for Medicare and Medicaid Services states that the net cost of Medicare, Medicaid, and the Children's Health Insurance Program in fiscal year 2009 was \$691 billion – 15 percent higher than in FY 2008. Medicare overpayments in FY 2009 amounted to \$23 billion, an error rate of 7.4 percent. Medicaid overpayments added up to \$28.7 billion for an 8.7 percent error rate. This combined M&M overpayment estimate of \$51.7 billion prepared by the CMS chief financial officer understates the problem because it does not include CHIP overpayments or *undetected* overpayments.

The U.S. Department of Labor reported that in calendar year 2008 a total of \$41.6 billion was paid to unemployment insurance beneficiaries (data for CY 2009 will be available in August 2010). Overpayments of unemployment insurance benefits totaled \$1.2 billion, a nationwide

fraud rate of 2.81 percent. California led the nation with \$260 million in fraudulent payments. Louisiana posted a fraud rate of 11.7 percent, the highest in the nation and more than 4 times higher than the national average. These figures too represent underestimates of fraud because they do not reflect the amount of *undetected* fraud.

**Indirect Symptoms.** Overall 40 percent of America's lower-income households pay no federal income taxes. Indeed, they receive substantial direct federal tax subsidies mainly through refundable tax credits. Mayo Research Institute estimates that 121 million persons reside in these households. Under *The Make Work Pay* tax credit, couples with incomes up to \$190,000 are eligible for at least a partial credit. Under the *Additional Child Tax Credit*, couples with incomes up to \$110,000 are eligible for partial credit.

Nearly 84 million Americans receive cash or in-kind benefits from the federal government. Almost 56 million of them have incomes above the poverty level.

Of the 36.0 million members of poor households with income below \$35,000, 16.2 million reported that they did not work at all in 2008.

Persons in the top 20 percent of all U.S. households according to income pay 90.5 percent of all federal income taxes.

A large but unknown number of Americans hide their incomes from the tax collector and manage to escape paying taxes on that hidden income. The amount of GDP in the "underground economy" is estimated by University of Wisconsin professor Edgar Feige at nearly \$2 trillion. Feige puts the annual loss of federal income taxes at upwards of \$500 billion.

**Consequences.** Social Security retirement can be salvaged only through higher taxes or lower benefits. Under those circumstances persons with higher earnings will have to accept rates of return below 1 percent in order to make available full benefits to persons with lower earnings.

The solution to Medicare and Medicaid funding is virtually the same -- higher taxes or lower benefits (reimbursements). M&M cuts involve reducing reimbursements to hospitals, physicians, and other health care providers. These cuts, however, will reduce access to health care because increasingly physicians will refuse to accept M&M patients. If they are forced to accept these patients, the next generation of bright college students will think twice about completing a pre-med undergraduate program and committing themselves to four years in medical school followed by four or more years in specialty training. More primary health care will be provided by nurse practitioners.

By extending benefits from 26 weeks to 99 weeks, unemployment insurance has morphed from an *insurance* program in which benefit duration depends on administrative formulae that incorporate the beneficiary's work history to an *assistance* program where work history is set aside and duration depends on the needs of the unemployed and public sympathy. Workers who would have exhausted their regular benefits after 26 weeks, or after 39 or 52 weeks under temporary extended benefit programs, and would be forced to lower their employment

expectations, enter a training program, or relocate, now are able to postpone those decisions. Extending benefits to nearly two years affords more opportunities for working violators to draw benefits by not reporting that they have found work and for nonworking violators to receive benefits without making a reasonable effort to find work. It will be difficult in the next recession to limit benefit duration to less than 99 weeks.

To many Americans it is obvious that adding a new health-care entitlement doesn't fix a broken system. To others, it seems that it doesn't matter because whether it is broken or not they do not have to pay for it. For them, the new entitlement will be free.

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