Click for Table of Contents

1987 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND DISABILITY INSURANCE TRUST FUNDS

COMMUNICATION

FROM

THE BOARD OF TRUSTEES, FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND DISABILITY INSURANCE TRUST FUNDS

TRANSMITTING

THE 1987 ANNUAL REPORT OF THE BOARD, PURSUANT TO SECTION 201(c)(2) OF THE SOCIAL SECURITY ACT, AS AMENDED

LETTER OF TRANSMITTAL

BOARD OF TRUSTEES OF THE
FEDERAL OLD-AGE AND SURVIVORS INSURANCE
AND DISABILITY INSURANCE TRUST FUNDS,
Washington, D.C., March 30, 1987

HONORABLE JAMES C. WRIGHT, JR.
Speaker of the House of Representatives
Washington, D.C.

HONORABLE GEORGE BUSH
President of the Senate
Washington, D.C.

GENTLEMEN: We have the honor of transmitting to you the 1987 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund (the 47th such report), in compliance with section 201(c)(2) of the Social Security Act.

Respectfully,

JAMES A. BAKER, III, *Secretary of the Treasury, and Managing Trustee of the Trust Funds.*

WILLIAM E. BROCK, *Secretary of Labor, and Trustee.*

OTIS R. BOWEN, M.D., *Secretary of Health and Human Services, and Trustee.*

MARY FALVEY FULLER, *Trustee.*

SUZANNE DENBO JAFFE, *Trustee.*

DORCAS R. HARDY, *Commissioner of Social Security, and Secretary, Board of Trustees.*

Click on a Topic Below

CONTENTS

TABLES

TABLES (Cont.)

TABLES (Cont.)

FIGURES

1987 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND DISABILITY INSURANCE TRUST FUNDS

SUMMARY

Highlights

The actuarial estimates shown in the 1987 Annual Report indicate that the assets of the Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI) Trust Funds are expected to be sufficient to permit the timely payment of OASDI benefits for many years into the future. The long-range 75-year estimates indicate that, under the intermediate assumptions, the OASDI program will experience about three decades of positive actuarial balances, with continuing actuarial deficits thereafter. The positive actuarial balances in the first part of the 75-year projection period nearly offset the later deficits, so that the program, as a whole, is said to be in close actuarial balance.

Trust fund assets grew more rapidly in 1986 than was estimated in the 1986 Annual Report, reflecting continued growth in the economy. As a result, the trust fund levels are higher than had been expected, and the ability of the OASDI program to withstand temporary economic downturns continues to improve. The estimates for each trust fund, separately, indicate that both the OASI and the DI programs can operate satisfactorily for many years. During the next 10 years, however, if experience is very adverse, the assets of the DI Trust Fund could decline to such a low level that financial problems would occur.

For the long-range 75-year projection period, the OASDI program has an average annual deficit of 0.62 percent of taxable payroll, based on the intermediate alternative II-B assumptions. (The long-range deficit under alternative II-B in the 1986 report was somewhat smaller—0.44 percent of payroll.) The long-range deficit represents about 4.6 percent of the average annual cost rate. The program is therefore in "close actuarial balance," although imbalances occur in the 25-year subperiods.

For OASI and DI, separately, the average long-range deficits, based on the alternative II-B assumptions, are 0.43 percent and 0.19 percent of taxable payroll, respectively. The deficit for DI represents about 12 percent of the average annual cost rate; thus, the DI program is not in close actuarial balance. The DI program could be brought into close actuarial balance by a small reallocation of the contribution rate from OASI to DI, in such a way that the OASI program would remain in close actuarial balance. While such a reallocation is not being recommended, the financial condition of the DI program will need to be carefully monitored.

1. Program Description

The OASDI program consists of two separate parts which pay monthly benefits to workers and their families:

(1) Old-Age and Survivors Insurance (OASI) pays benefits after a worker retires and to survivors after a worker dies.

(2) Disability Insurance (DI) pays benefits after a worker becomes disabled.

The Board of Trustees of the trust funds is required by law to report annually to the Congress on the financial condition of the funds and on estimated future results. The Board has five members, three of whom serve in an ex officio capacity: the Secretaries of the Treasury, Labor, and Health and Human Services. The Board also includes two members of the public, Mary Falvey Fuller and Suzanne Denbo Jaffe, who are serving 4-year terms which began on September 28, 1984.

Most OASDI revenue consists of contributions paid by employees, their employers, and the self-employed. (Additional contributions are paid into a separate trust fund for the Hospital Insurance part of Medicare. This summary focuses on OASDI and does not discuss Medicare except in the context of interfund borrowing.) The contribution rates are established by law. Contributions are paid on earnings not exceeding the earnings base—$43,800 in 1987. The earnings base will rise in the future as average wages increase. The current and future OASDI contribution rates for employees and employers, each, are shown below (as percentages):

Year	OASI	DI	Total
1987	5.20	0.50	5.70
1988-89	5.53	.53	6.06
1990-99	5.60	.60	6.20
2000 & later	5.49	.71	6.20

Since 1984, a portion (not more than one-half) of OASDI benefits received by higher income beneficiaries is subject to Federal income taxation. The revenues collected as a result of this provision are transferred from the general fund of the Treasury to the trust funds.

The outgo of the OASDI trust funds consists of benefit payments and administrative expenses. Trust fund assets may not be used for any other purposes.

During periods when outgo temporarily exceeds income, trust fund assets are used to meet the shortfall. In the event of recurring shortfalls, the trust funds can allow time for legislation to be enacted to restore balance to the program. The assets of the trust funds are invested in U.S. Government securities bearing rates of interest similar to those for long-term securities issued to the general public.

2. Recent Results

During 1986, about 122 million workers made contributions to the OASDI program. At the end of September 1986, 37.5 million persons were receiving monthly OASDI benefit payments. Administrative expenses represented about 1.1 percent of benefit payments in fiscal 1986.

Income to the OASDI trust funds in fiscal 1986 was $215.5 billion, while outgo was $198.7 billion. In addition, $10.6 billion was transferred from the OASI fund to the Hospital Insurance (HI) fund, as a final repayment of interfund loans made in 1982. Thus, the assets of the OASDI funds increased by $6.1 billion during the fiscal year. A summary of the OASDI financial operations in fiscal 1986 is shown below (in billions):

Trust fund assets at end of fiscal 1985	$39.7
Income during year:	
Contributions	205.1
Revenue from taxation of benefits	3.6
Payments from general fund	3.3
Net interest	3.4
Total income	215.5
Outgo during year:	
Benefit payments	193.9
Administrative expenses	2.2
Transfer to Railroad Retirement program	2.7
Total outgo	198.7
Loan repayment to HI fund	10.6
Net increase in assets during year	6.1
Trust fund assets at end of fiscal 1986	45.9

Note: Totals may not equal sums of components, due to rounding.

3. Actuarial Estimates

The annual report contains 75-year estimates of each fund's financial operations and status. Because precise prediction of the future is impossible, alternative sets of assumptions, representing a reasonable range of possible future experience, are used to make short- and long-range estimates. Future experience could, however, fall outside the range indicated by these assumptions.

Future OASDI income and outgo will depend on a variety of economic and demographic factors, including economic growth, inflation, unemployment, fertility, and mortality. Economic factors affect the levels of workers' earnings and OASDI benefits, while demographic factors affect the numbers of people making contributions and receiving benefits.

This year's estimates were prepared using four alternative sets of assumptions. Two sets—alternatives II-A and II-B—are designated "intermediate." These sets share the same demographic assumptions, but differ with respect to economic assumptions; somewhat more robust economic growth is assumed for alternative II-A than for alternative II-B. One set—alternative I—is designated "optimistic," and another—alternative III—is "pessimistic."

No single measure is used to assess the actuarial status of the OASDI funds. Short-range measures usually focus on the adequacy of reserves available to pay benefits. Long-range measures usually focus instead on the balance between income and outgo during the projection period.

The *contingency fund ratio* is the usual measure of the OASDI program's ability to pay benefits on time in the near future. This ratio is the amount in the trust funds at the beginning of the year, including advance tax transfers for January, divided by that year's expenditures. Thus, if the trust fund ratio is 25 percent, the amount in the fund represents about 3 months' outgo. At the beginning of 1987, the fund ratio for OASDI was about 31 percent. A ratio of 8-9 percent is required to pay benefits at the beginning of each month.

In analyzing the actuarial status of OASDI for the next 75 years, several different measures are commonly used. The *income rate* is the combined OASDI employee-employer contribution rate scheduled in the law, plus the income from taxation of benefits expressed as a percentage of taxable payroll. The *cost rate* is the annual outgo expressed as a percentage of taxable payroll. Average income and cost rates can be compared directly to measure the adequacy of the program's financing.

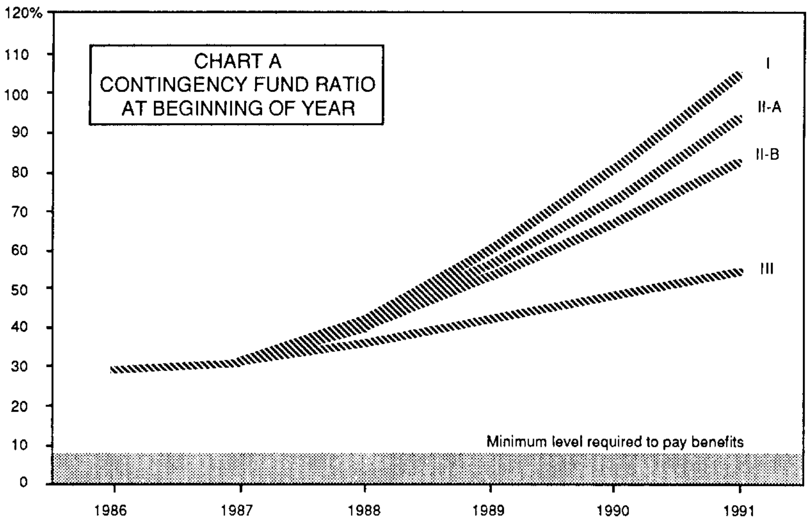
For the 75-year long-range projection period, the *actuarial balance* is the difference between the estimated average income rate and the estimated average cost rate. If this actuarial balance is negative, the program is said to have an actuarial deficit. Such a deficit is a warning that future changes may be needed in the program's financing or benefit provisions, although it does not present a complete picture without the other measures of financing discussed here. The program is in "*close actuarial balance*" for the long-range period if the average income rate is between 95 and 105 percent of the average cost rate.

4. Short-Range Financing (1987-91)

Estimates for the next 5 years are used to assess the adequacy of OASDI financing in the short range. In this period, the numbers of persons receiving OASDI benefits can be estimated fairly accurately. Changes in the national economy, however, which are difficult to predict, can have major effects on income and outgo.

The actuarial estimates shown in the 1987 report indicate that the combined assets of the OASI and DI Trust Funds will be sufficient to pay OASDI benefits on time throughout the 5-year period and for many years thereafter, based on all four sets of assumptions. In addition, the estimates based on alternatives I, II-A, and II-B indicate that the OASI and DI programs, separately, can operate satisfactorily for many years. During the next 10 years, however, if experience is very adverse, the assets of the DI Trust Fund could decline to such a low level that financial problems would occur.

Chart A shows the OASDI contingency fund ratio for 1987, 31 percent, and the projected OASDI ratios for 1988-91, on the basis of all four sets of assumptions. The fund ratios are generally estimated to increase each year.



5. Long-Range Financing (1987-2061)

Long-range 75-year estimates for OASDI, although sensitive to variations in the assumptions, indicate the trend and general range of the program's future financial status. During this long-range period, income and outgo are greatly affected by demographic, as well as economic, conditions. Most of the beneficiaries during the next 75 years have already been born, so that their numbers are projected mainly from the present population. The numbers of workers involved in these projections, however, depend on future birth rates, which are subject to more variability.

Several important demographic trends are anticipated to raise the proportion of the aged in the population during the next 75 years. First, because of the large number of persons born in the two decades after World War II, rapid growth is expected in the aged population after the turn of the century. Second, assumed declines in death rates also would increase the numbers of aged persons. At the same time, birth rates, which began to decline in the 1960s and are assumed to remain relatively low in the future, would hold down the numbers of young people.

Chart B shows the long-range trend in the number of covered workers per OASDI beneficiary. ("Beneficiaries" includes not only retired workers, but also disabled workers, spouses, children, and survivor beneficiaries.) This ratio declined from 5.1 in 1960 to 3.3 in 1986. It is estimated to reach about 2 by the middle of the next century, based on the intermediate assumptions, as the number of beneficiaries increases more rapidly than the number of covered workers.

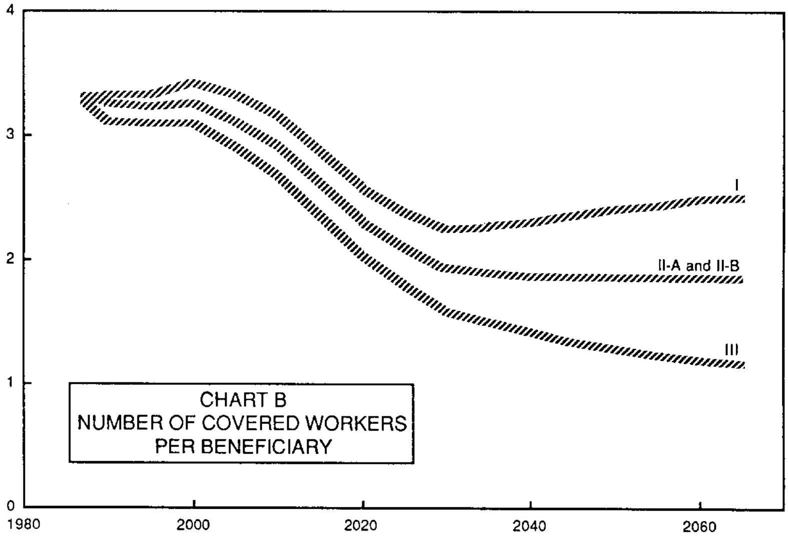
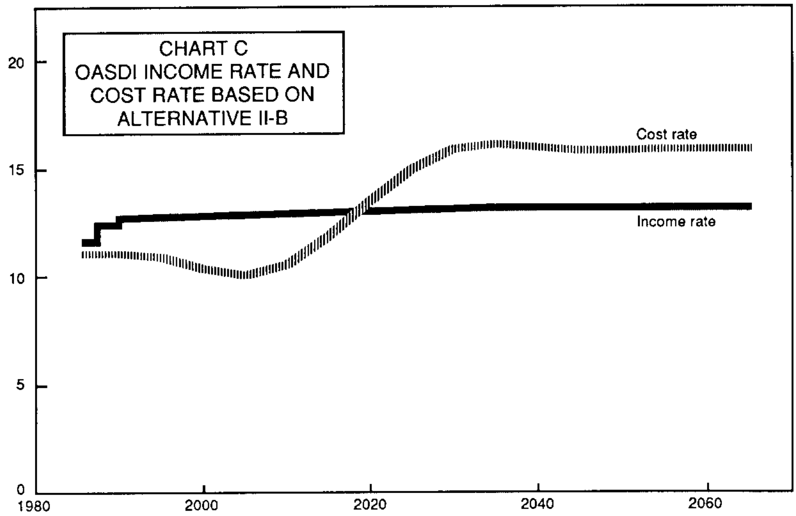


Chart C shows the estimated OASDI income and cost rates for the long-range projection period, based on the intermediate II-B assumptions. During the first three decades of this period, the estimates indicate that the income rate will generally exceed the cost rate, resulting in substantial positive actuarial balances each year. Beginning about 2015, the reverse is true, with the cost rate exceeding the income rate, thus resulting in substantial deficits. These positive actuarial balances and deficits do not reflect interest earnings, which result in trust fund growth continuing for about 15 years after the first actuarial deficits occur. The cost rate is estimated to increase rapidly after the first half of the 75-year projection period, primarily because the number of beneficiaries is projected to increase more rapidly than the number of covered workers.

The long-range OASDI actuarial deficit of 0.62 percent of taxable payroll, based on the intermediate II-B assumptions, consists of an average annual positive balance of 2.10 percent of taxable payroll for the first 25-year subperiod, and average annual deficits of 1.22 and 2.74 percent for the second and third 25-year subperiods, respectively. Thus, in the absence of other changes, the long-range actuarial balance will tend to decline slowly in future annual reports, as the valuation period moves forward and near-term years of positive balances are replaced by distant years of deficit. The actuarial deficits in the later years of the 75-year projection period are caused primarily by the demographic trends described above.



The table below presents a comparison of the average annual income and cost rates for the 75-year long-range projection period, based on the four sets of assumptions. The figures are expressed as percentages of taxable payroll. Based on the intermediate II-B assumptions, the OASDI program is in "close actuarial balance," because the estimated average income rate is between 95 and 105 percent of the average cost rate. The 0.62-percent deficit represents about 4.6 percent of the average cost rate.

Assumptions	Income rate	Cost rate	Actuarial balance
Optimistic	12.78	10.62	2.15
Intermediate II-A	12.87	12.79	.08
Intermediate II-B	12.89	13.51	-.62
Pessimistic	13.07	17.76	-4.69

Note: Income rate, cost rate, and actuarial balance are defined in the text.

I. THE BOARD OF TRUSTEES

The Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund are held by the Board of Trustees under the authority of section 201(c)(1) of the Social Security Act. The Board has five members, three of whom serve in an ex officio capacity: the Secretary of the Treasury, the Secretary of Labor, and the Secretary of Health and Human Services. The other two members, Mary Falvey Fuller and Suzanne Denbo Jaffe, are members of the public serving 4-year terms which began on September 28, 1984.

By law, the Secretary of the Treasury is designated as the Managing Trustee, and the Commissioner of Social Security is designated as the Secretary of the Board. The Board of Trustees reports to the Congress each year on the operations and status of the trust funds, in compliance with section 201(c)(2) of the Social Security Act. This annual report, for 1987, is the 47th such report.

II. SOCIAL SECURITY AMENDMENTS SINCE THE 1986 REPORT

Since the 1986 Annual Report was transmitted to the Congress on March 31, 1986, several laws affecting the OASDI program have been enacted. The more important legislative changes, from an actuarial standpoint, are described below.

The Consolidated Omnibus Budget Reconciliation Act of 1985 (Public Law 99-272, enacted into law on April 7, 1986) clarifies that, for purposes of the taxation of benefits and the calculations of various trust fund ratios under the Social Security Act, benefits for any given month that are paid in the same month will be deemed to have been paid in the following month. (Normally, benefits for a month are paid in the following month—on the third day. However, when the first, second, and third days of the following month are all days on which banks are closed, the benefits are paid on the first preceding banking day.) Also, this law required the Secretary of Health and Human Services to appoint a Disability Advisory Council, in lieu of the quadrennial Advisory Council on Social Security, to study and make recommendations on the medical and vocational aspects of disability under the Social Security and Supplemental Security Income programs. (The Council was appointed in 1986.) The Act also permanently exempts compensation received by senior-status (retired) Federal judges on active duty, for purposes of coverage under Social Security and the retirement earnings test. (Such coverage, originally required by the Social Security Amendments of 1983, had been delayed until 1986 by Public Law 98-118.)

The Federal Employees' Retirement System Act of 1986 (Public Law 99-335, enacted into law on June 6, 1986) established a new Federal retirement system effective January 1, 1987, for Federal employees hired after 1983 who are covered under the OASDI program as a result of the Social Security Amendments of 1983. Federal employees in the closed group now under the previously established Civil Service Retirement System (CSRS), who are not generally covered under the OASDI program, can elect to join the new Federal Employees' Retirement System (FERS) and, thereby, become covered under the OASDI program. The period during which such election can be made begins July 1, 1987, and ends December 31, 1987. Depending on the extent to which Federal employees now covered under the CSRS voluntarily join the new FERS, income to the OASDI program will be increased as a result of these changes. Outgo will ultimately also be increased, as these employees reach retirement age or otherwise become eligible for benefits.

The Omnibus Budget Reconciliation Act of 1986 (Public Law 99-509, enacted into law on October 21, 1986) permanently eliminated the requirement that an increase in the Consumer Price Index must be at least 3.0 percent before an automatic cost-of-living increase in OASDI benefits can become effective. As a result of the elimination of this trigger requirement, OASDI benefits were increased by 1.3 percent effective with benefits for December 1986. Also, effective January 1, 1987, the deposits of contributions resulting from State and local government employment were accelerated, and the collection of such contributions became the responsibility of the Internal Revenue Service.

This was the first of three changes which will phase the collection of State and local government contributions into the same collection schedule that applies to those resulting from private-sector employment.

The Tax Reform Act of 1986 (Public Law 99-514, enacted into law on October 22, 1986) makes extensive modifications to the Federal income tax system. Decreases in income tax rates for individuals will reduce income to the OASI and DI Trust Funds that results from the taxation of OASDI benefits. Other features of the Tax Reform Act, such as the elimination or restriction of several deductions and exemptions, will tend to raise contribution income as would possible favorable impacts on earnings and hours worked. Numerous other changes affecting business income and expenses for tax purposes may also affect Social Security contributions, especially from self-employed persons. A specific change in Social Security coverage provisions permits ministers who had received an exemption from coverage to permanently revoke the exemption, if the revocation is filed within a limited time period (generally by April 15, 1988).

The Immigration Reform and Control Act of 1986 (Public Law 99-603, enacted into law on November 6, 1986) provides for granting temporary-resident status to undocumented aliens who have been residing continuously in the United States since January 1, 1982, and to certain seasonal agricultural workers. It further provides for subsequent adjustment of such temporary-resident status to lawful-permanent-resident status if certain requirements are met. No specific effects of this Act are reflected in the actuarial estimates because none is yet anticipated.

Detailed information regarding these laws can be found in documents prepared by and for the Congress. The actuarial estimates shown in this report reflect the anticipated effects of these amendments.

III. BASIS FOR TRUST FUND RECEIPTS AND EXPENDITURES

The Federal Old-Age and Survivors Insurance Trust Fund was established on January 1, 1940, as a separate account in the United States Treasury. All the financial operations of the OASI program are handled through this fund. The Federal Disability Insurance Trust Fund is another separate account in the United States Treasury; it was established on August 1, 1956. All the financial operations of the DI program are handled through this fund.

The primary receipts of these two funds are amounts appropriated to each of them under permanent authority on the basis of contributions paid by workers, their employers, and individuals with self-employment income, in work covered by the OASDI program. Beginning January 1, 1987, these appropriated amounts include contributions paid by, or on behalf of, workers employed by State and local governments and by such employers, with respect to wages covered under the program through State agreements. (Prior to 1987, such contributions were deposited directly into each of the trust funds.) All employees, and their employers, in covered employment are required to pay contributions with respect to their wages. Employees are required to pay contributions with respect to all cash tips, if their tips are at least $20 per month, but employers are required to pay contributions on only that part of tip income deemed to be wages under the Federal minimum-wage law. All self-employed persons are required to pay contributions with respect to their covered net earnings from self-employment. In addition to making the required employer contributions on the earnings of covered Federal employees, the Federal Government also pays amounts equivalent to the employer and employee contributions that would be paid on deemed wage credits attributable to military service performed after 1956 if such wage credits were covered wages.

In general, an individual's contributions, or taxes, are computed on annual wages or net earnings from self-employment, or both wages and net self-employment earnings combined, up to a specified maximum annual amount. The contributions are determined first on the wages and then on any net self-employment earnings, such that the total does not exceed the annual maximum amount. An employee who pays contributions on wages in excess of the annual maximum amount (because of employment with two or more employers) is eligible for a refund of the excess employee contributions. The monthly benefit amount to which an individual (or his or her spouse and children) may become entitled under the OASDI program is based on the individual's taxable earnings during his or her lifetime. In computing benefits for almost all persons who first become eligible to receive benefits in 1979 or later, the earnings in each year are indexed to take account of increases in average wage levels. The maximum amount of earnings on which contributions are payable in a year, and which is also the maximum amount of earnings creditable in that year for benefit-computation purposes, is called the contribution and benefit base.

The contribution rates, or tax rates, applicable in each calendar year, and the allocation of the rates between the two trust funds, are shown in table 1. For 1988 and later, the rates shown are those scheduled in present law. The contribution and benefit bases are also shown in table 1. The bases for 1975-78 were determined under the automatic-adjustment provisions in section 230 of the Social Security Act. The bases for 1979-81 were specified in the law, as amended in 1977. The bases for 1982-87 were again determined under the automatic-adjustment provisions, as will be the bases in 1988 and later.

TABLE 1.—CONTRIBUTION AND BENEFIT BASE AND CONTRIBUTION RATES

Calendar years	Contribution and benefit base	Contribution rates (percent): Employees and employers, each: OASDI	OASI	DI	Self-employed: OASDI	OASI	DI
1937-49	$3,000	1.000	1.000	—	—	—	—
1950	3,000	1.500	1.500	—	—	—	—
1951-53	3,600	1.500	1.500	—	2.2500	2.2500	—
1954	3,600	2.000	2.000	—	3.0000	3.0000	—
1955-56	4,200	2.000	2.000	—	3.0000	3.0000	—
1957-58	4,200	2.250	2.000	0.250	3.3750	3.0000	0.3750
1959	4,800	2.500	2.250	.250	3.7500	3.3750	.3750
1960-61	4,800	3.000	2.750	.250	4.5000	4.1250	.3750
1962	4,800	3.125	2.875	.250	4.7000	4.3250	.3750
1963-65	4,800	3.625	3.375	.250	5.4000	5.0250	.3750
1966	6,600	3.850	3.500	.350	5.8000	5.2750	.5250
1967	6,600	3.900	3.550	.350	5.9000	5.3750	.5250
1968	7,800	3.800	3.325	.475	5.8000	5.0875	.7125
1969	7,800	4.200	3.725	.475	6.3000	5.5875	.7125
1970	7,800	4.200	3.650	.550	6.3000	5.4750	.8250
1971	7,800	4.600	4.050	.550	6.9000	6.0750	.8250
1972	9,000	4.600	4.050	.550	6.9000	6.0750	.8250
1973	10,800	4.850	4.300	.550	7.0000	6.2050	.7950
1974	13,200	4.950	4.375	.575	7.0000	6.1850	.8150
1975	14,100	4.950	4.375	.575	7.0000	6.1850	.8150
1976	15,300	4.950	4.375	.575	7.0000	6.1850	.8150
1977	16,500	4.950	4.375	.575	7.0000	6.1850	.8150
1978	17,700	5.050	4.275	.775	7.1000	6.0100	1.0900
1979	22,900	5.080	4.330	.750	7.0500	6.0100	1.0400
1980	25,900	5.080	4.520	.560	7.0500	6.2725	.7775
1981	29,700	5.350	4.700	.650	8.0000	7.0250	.9750
1982	32,400	5.400	4.575	.825	8.0500	6.8125	1.2375
1983	35,700	5.400	4.775	.625	8.0500	7.1125	.9375
1984[1]	37,800	5.700	5.200	.500	11.4000	10.4000	1.0000
1985[1]	39,600	5.700	5.200	.500	11.4000	10.4000	1.0000
1986[1]	42,000	5.700	5.200	.500	11.4000	10.4000	1.0000
1987[1]	43,800	5.700	5.200	.500	11.4000	10.4000	1.0000
Rates scheduled in present law:							
1988-89[1]	([2])	6.060	5.530	.530	12.1200	11.0600	1.0600
1990-99	([2])	6.200	5.600	.600	12.4000	11.2000	1.2000
2000 and later	([2])	6.200	5.490	.710	12.4000	10.9800	1.4200

[1]See text for description of tax credits.

[2]Subject to automatic adjustment.

In 1984 only, an immediate credit of 0.3 percent of taxable wages was allowed against the OASDI contributions paid by employees. In accordance with the law, this credit was implemented by a deliberate under-withholding of the employee contributions for 1984, resulting in an effective contribution rate of 5.4 percent (as compared to the employer rate of 5.7 percent). The appropriations of contributions to the trust funds, however, were based on the combined employee-employer rate of 11.4 percent, as if the credit for employees did not apply. Similar credits of 2.7 percent, 2.3 percent, and 2.0 percent are allowed against the combined OASDI and Hospital Insurance (HI) contributions on net earnings from self-employment in 1984, 1985, and 1986-89, respectively. The appropriations of contributions to the trust funds, however, are based on the contribution rates, before adjustment for the credit, that apply in each year. After 1989, self-employed persons will be allowed a deduction, for purposes of computing their net earnings, equal to half of the combined OASDI and HI contributions that would be payable without regard to the contribution and benefit base. The contribution rate is then applied to net earnings after this deduction, but subject to the base. This provision reduces contributions for those self-employed persons with earnings less than, or not greatly above, the contribution and benefit base.

All contributions, except for amounts received under State agreements for coverage under the program prior to January 1, 1987, are collected by the Internal Revenue Service and deposited in the general fund of the Treasury. The exact amount of contributions received is not known initially because amounts paid under the OASDI and HI programs and individual income taxes are not separately identified in collection reports received by the Internal Revenue Service.

Amounts representing the estimated total collections of OASDI contributions by the IRS for each month are credited to the OASI and DI Trust Funds on the first day of the month. Because these estimated collections are credited to the trust funds on the first of the month, instead of throughout the month as contributions are actually received, the trust funds pay interest to the general fund to reimburse it for the interest costs attributable to these advance transfers. Periodic adjustments (principal only) are subsequently made to the extent that the estimates are found to differ from the amounts of contributions actually payable as determined from reported earnings. Adjustments are also made to account for any refunds to employees (with more than one employer) who paid contributions on wages in excess of the contribution and benefit base.

Beginning in 1984, a portion (not more than one-half) of OASDI benefits is subject to Federal income taxation under certain circumstances. The proceeds from this taxation of benefits are credited to the trust funds, in advance, on an estimated basis, at the beginning of each calendar quarter, with no reimbursement to the general fund for interest costs attributable to the advance transfers. Subsequent adjustments are made based on the actual amounts as shown on annual income tax records. The amounts appropriated from the general fund of the Treasury are allocated to the OASI and DI Trust Funds on the basis of the income taxes paid on the benefits from each fund. (A special provision applies to benefits paid to non-resident aliens. A flat-rate tax, usually 15 percent, is withheld from the benefits before they are paid and, therefore, remains in the trust funds.)

Another source of income to the trust funds is interest received on investments held by the trust funds. That portion of each trust fund which, in the judgment of the Managing Trustee, is not required to meet current expenditures for benefits and administration is invested, on a daily basis, in interest-bearing obligations of the U.S. Government (including special public-debt obligations described below), in obligations guaranteed as to both principal and interest by the United States, or in certain federally sponsored agency obligations that are designated in the laws authorizing their issuance as lawful investments for fiduciary and trust funds under the control and authority of the United States or any officer of the United States. These obligations may be acquired on original issue at the issue price or by purchase of outstanding obligations at their market price.

The Social Security Act authorizes the issuance of special public-debt obligations for purchase exclusively by the trust funds. The Act provides that these obligations shall bear interest at a rate equal to the average market yield (computed on the basis of market quotations as of the end of the calendar month next preceding the date of such issue) on all marketable interest-bearing obligations of the United States then forming a part of the public debt which are not due or callable until after the expiration of 4 years from the end of such calendar month.

Income is also affected by provisions of the Social Security Act for (1) transfers between the general fund of the Treasury and the OASI and DI Trust Funds for any adjustments to prior payments for the cost arising from the granting of noncontributory wage credits for military service prior to 1957, according to periodic determinations made by the Secretary of Health and Human Services; (2) annual reimbursements from the general fund of the Treasury to the OASI Trust Fund for any costs arising from the special monthly cash payments to certain uninsured persons—i.e., those who attained age 72 before 1968 and who generally are not eligible for cash benefits under other provisions of the OASDI program; and (3) the receipt of unconditional money gifts or bequests made for the benefit of the trust funds or any activity financed through the funds.

The major expenditures of the OASI and DI Trust Funds are for (1) OASDI benefit payments, net of any reimbursements from the general fund of the Treasury for unnegotiated benefit checks, and (2) expenses incurred by the Department of Health and Human Services and by the Department of the Treasury in administering the OASDI program and the provisions of the Internal Revenue Code relating to the collection of contributions. Such administrative expenses include expenditures for construction, rental and lease, or purchase of office buildings and related facilities for the Social Security Administration. The Social Security Act does not permit expenditures from the OASI and DI Trust Funds for any purpose not related to the payment of benefits or administrative costs for the OASDI program.

The expenditures of the trust funds are also affected by (1) costs of vocational rehabilitation services furnished as an additional benefit to disabled persons receiving cash benefits because of their disabilities where such services contributed to their successful rehabilitation, and (2) the provisions of the Railroad Retirement Act which provide for a system of coordination and financial interchange between the Railroad Retirement program and the Social Security programs. Under these provisions, transfers between the Railroad Retirement program's Social Security Equivalent Benefit Account and the trust funds are made on an annual basis in order to place each trust fund in the same position in which it would have been if railroad employment had always been covered under Social Security.

The net worth of facilities and other fixed capital assets is not carried in the statements of the operations of the trust funds presented in this report. This is because the value of fixed capital assets does not represent funds available for the payment of benefits or administrative expenditures, and therefore is not considered in assessing the actuarial status of the trust funds.

The Social Security Act authorizes borrowing among the OASI, DI, and HI Trust Funds when necessary "to best meet the need for financing the benefit payments" from the three funds. The timing and amounts of the loans are largely at the discretion of the Managing Trustee, although no loans can be made after 1987. Loans may not be made from a trust fund if its assets (excluding any amounts borrowed) represent less than 10 percent of its current annual rate of expenditures. The law also specifies that interest on borrowed amounts will be paid monthly at a rate "equal to the rate which the lending Trust Fund would earn on the amount involved if the loan were an investment" and provides certain criteria for repaying outstanding amounts owed.

Interfund loans under the borrowing authority were made to the OASI Trust Fund from the DI and HI Trust Funds in November and December 1982. The loans were fully repaid by May 1, 1986. No additional interfund loans have been made since 1982, and none is expected to be made before the authority expires at the end of 1987. In this report, the assets of the OASI Trust Fund, as of the end of each year 1982-85, include any amounts then owed to the DI and HI Trust Funds. The assets of the trust funds to which amounts were owed do not include such amounts. This procedure is followed because the borrowed amounts were available for the payment of benefits or other obligations of the OASI fund, while such amounts were not readily available to the lending funds.