SUMMARY OF THE OPERATIONS OF THE TRUST FUND, FISCAL YEAR 1989

A statement of the income and disbursements of the Federal Hospital Insurance Trust Fund in fiscal year 1989, and of the assets of the fund at the beginning and end of the fiscal year, is presented in table 2.

The total assets of the trust fund amounted to $65,877 million on September 30, 1988. During fiscal year 1989, total receipts amounted to $75,116 million, and total disbursements were $58,238 million. The assets of the trust fund thus increased $16,878 million during the year to a total of $82,755 million on September 30, 1989.

Included in total receipts during fiscal year 1989 was $67,742 million representing contributions appropriated to the trust fund. As an offset, $217 million was transferred from the trust fund into the Treasury as repayment for the estimated amount of contributions subject to refund to employees who worked for more than one employer during the course of a year and paid contributions on wages in excess of the statutory maximum earnings base, and $3 million was transferred to the trust fund from State and local governments for underpayments from previous State agreements for coverage of State and local government employees.

Net contributions amounted to $67,527 million, representing an increase of 9.1 percent over the amount of $61,901 million for the preceding 12-month period. This growth in contribution income resulted primarily from (1) the higher level of earnings in covered employment and (2) the two increases in the maximum annual amount of earnings taxable from $43,800 to $45,000 and from $45,000 to $48,000 that became effective January 1, 1988, and January 1, 1989, respectively.

The section entitled "Nature of the Trust Fund" referred to provisions under which the HI trust fund is to be reimbursed from the general fund of the Treasury for costs of paying benefits under this program on behalf of certain uninsured persons. The reimbursement in fiscal year 1989 amounted to $515 million, consisting of $488 million for benefit payments, $7 million for administrative expenses, and $20 million for interest on adjustments to costs in prior fiscal years.

The section entitled "Nature of the Trust Fund" referred to provisions of the Social Security Act under which certain persons aged 65 and over but not otherwise eligible for HI protection may obtain such protection by enrolling in the program and paying a monthly premium. Premiums collected from such voluntary participants in fiscal year 1989 amounted to about $42 million.

In accordance with the provisions of the Railroad Retirement Act which coordinate the railroad retirement and the HI programs and which govern the financial interchange arising from the allocation of costs between the two systems, the Railroad Retirement Board and the Secretary of Health and Human Services determined that a transfer of about $345 million in principal and about $13 million in interest from the railroad retirement program's Social Security Equivalent Benefit Account to the HI trust fund would place this fund in the same position, as of September 30, 1988, in which it would have been if railroad employment had always been covered under the Social Security Act. This amount, together with interest to the date of transfer amounting to about $21 million, was transferred to the trust fund in June 1989.

In accordance with provisions for the appropriation to the trust fund of HI taxes on noncontributory military wage credits as discussed in the section entitled "Nature of the Trust Fund," the trust fund was credited on July 1, 1989 with $86 million for calendar year 1989 taxes on wage credits.

The remaining $6,567 million of receipts consisted almost entirely of interest on the investments of the trust fund.

Of the $58,238 million in total disbursements, $57,433 million represented benefits paid directly from the trust fund for health services covered under title XVIII of the Social Security Act. Benefit payments increased 10.4 percent in fiscal year 1989 over the corresponding amount of $52,022 million paid during the preceding 12 months.

The remaining $805 million of disbursements was for net administrative expenses. Administrative expenses are allocated and charged directly to each of the four trust funds --OASI, DI, HI, and SMI--on the basis of provisional estimates. Similarly, the expenses of administering other programs of the Health Care Financing Administration are also allocated and charged directly to the general fund of the Treasury on a provisional basis. Periodically, as actual experience develops and is analyzed, adjustments to the allocations of administrative expenses and costs of construction for prior periods are effected by interfund transfers, including transfers between the HI and SMI trust funds and the program management general fund account, with appropriate interest allowances.

Table 3 compares the actual experience in fiscal year 1989 with the estimates presented in the 1988 and 1989 annual reports. The 1989 annual report was completed after the end of the fiscal year. Therefore, preliminary actual figures were available at that time. The estimates in the 1988 report understated tax contributions somewhat. The benefit payments estimated, also understated, were completed prior to the enactment of the Medicare Catastrophic Coverage Act of 1988. If the estimated $1,952 million which would have been spent for catastrophic benefits in fiscal year 1989 had been known at the time, then the 1988 estimate for fiscal year 1989 benefit payments would have been $57,835. The actual amount of benefit payments would have then been less than one percent below the estimated amount.

The assets of the HI trust fund at the end of fiscal year 1988 totaled $65,877 million, consisting of $66,080 million in the form of obligations of the U.S. Government or of federally-sponsored agency obligations and, as an offset, an extension of credit of $203 million against securities to be redeemed. The assets of the HI trust fund at the end of fiscal year 1989 totaled $82,755 million, consisting of $82,914 million in the form of obligations and, as an offset, an extension of credit of $159 million against securities to be redeemed. Table 4 shows the total assets of the fund and their distribution at the end of fiscal years 1988 and 1989.

New securities at a total par value of $94,669 million were acquired during the fiscal year through the investment of receipts and the reinvestment of funds made available from the redemption of securities. The par value of securities redeemed during the fiscal year was $77,833 million. Thus, the net increase in the par value of the investments held by the fund during fiscal year 1989 amounted to $16,836 million.

The effective annual rate of interest earned by the assets of the HI trust fund during the 12 months ending on June 30, 1989, was 9.9 percent. (This period is used because interest on special issues is paid semiannually on June 30 and December 31.) The interest rate on public-debt obligations issued for purchase by the trust fund in June 1989 was 8.75 percent, payable semiannually.

TABLE 2.--**STATEMENT OF OPERATIONS OF THE HOSPITAL INSURANCE TRUST FUND DURING FISCAL YEAR 1989**
(In thousands of dollars)

Total assets of the trust fund, beginning of period	$65,876,905
Receipts:	
Appropriation of employment taxes	$67,741,556
Refunds of employment taxes	-217,350
Deposits arising from State agreements	2,505
Interest on investments	6,557,835
Amortization of premium and discount (Net)	-1,315
Premiums collected from voluntary participants	42,119
Transfer from railroad retirement account	344,600
Transitional uninsured coverage	515,000
Military service credits of 1989	85,728
Interest on reimbursements, SSA 1/	5
Interest on reimbursements, HCFA 1/	10,811
Interest on reimbursements, Railroad	34,232
Total receipts	$75,115,725
Disbursements:	
Benefit payments	$57,432,968
Administrative expenses:	
Treasury administrative expenses	46,285
Salaries and expenses, SSA	293,166
Salaries and expenses, HCFA 2/	434,649
Salaries and expenses, Office of Secretary	15,180
Construction	7,309
Professional Standards Review Organization	330
Reimbursement of SSA expenses	0
Reimbursement of HCFA expenses	0
Payment Assessment Committee	3,077
Public Health Service	4,565
Total disbursements	$58,237,528
Total assets of the trust fund, end of period	$82,755,102

1/ A positive figure represents a transfer to the HI trust fund from the other trust funds. A negative figure represents a transfer from the HI trust fund to the other trust funds.
2/ Includes administrative expenses of the intermediaries.

NOTE: Totals do not necessarily equal the sums of rounded components.

TABLE 3.--**COMPARISON OF ACTUAL AND ESTIMATED OPERATIONS OF THE HOSPITAL INSURANCE TRUST FUND, FISCAL YEAR 1989**
(Dollar amounts in millions)

		Comparison of actual experience with estimates for fiscal year 1989 published in--			
		1989 report 1/		1988 report 1/	
Item	Actual amount	Estimated amount	Actual as percentage of estimate	Estimated amount	Actual as percentage of estimate
Net contributions	$67,527	$67,527	100	$64,773	104
Benefit payments	$57,433	$57,433	100	$55,883	103

1/ Alternative II-B.

TABLE 4.--ASSETS OF THE HOSPITAL INSURANCE TRUST FUND, BY TYPE, AT THE END OF FISCAL YEARS 1988 AND 1989 1/

	September 30, 1988	September 30, 1989
Investments in public-debt obligations sold only to the trust funds (special issues):		
Certificates of indebtedness:		
8 3/8-percent, 1990	------	$2,484,226,000.00
9 1/4-percent, 1989	$5,581,465,000.00	------
Bonds:		
8 1/4-percent, 1993	622,286,000.00	622,286,000.00
8 3/8-percent, 1990	1,231,586,000.00	------
8 3/8-percent, 1991-2001	14,066,078,000.00	14,066,078,000.00
8 5/8-percent, 1990	686,250,000.00	683,175,000.00
8 5/8-percent, 1991-2002	10,744,154,000.00	10,744,154,000.00
8 3/4-percent, 1990-1992	------	3,643,052,000.00
8 3/4-percent, 1993-1994	972,757,000.00	3,401,457,000.00
8 3/4-percent, 1995-2004	------	16,373,444,000.00
9 1/4-percent, 1990-2003	17,678,981,000.00	17,678,981,000.00
9 3/4-percent, 1993-1995	1,240,090,000.00	1,240,090,000.00
10 3/8-percent, 1989	427,022,000.00	------
10 3/8-percent, 1990-2000	3,412,678,000.00	3,412,678,000.00
10 3/4-percent, 1989	588,410,000.00	------
10 3/4-percent, 1990-1998	2,353,640,000.00	2,353,640,000.00
13 -percent, 1993-1996	1,770,094,000.00	1,770,094,000.00
13 1/4-percent, 1993-1997	2,541,541,000.00	2,541,541,000.00
13 3/4-percent, 1989	262,135,000.00	------
13 3/4-percent, 1990-1999	1,899,081,000.00	1,899,081,000.00
Total public-debt obligations sold only to the trust funds (special issues)	$66,078,248,000.00	$82,913,977,000.00
Investments in federally-sponsored agency obligations:		
Participation certificates:		
Federal Assets Liquidation Trust-		
Government National Mortgage Association:		
6.40-percent, 1987	------	------
6.05-percent, 1988	------	------
6.45-percent, 1988	------	------
6.20-percent, 1988	------	------
Unamortized Premium & Discount (Net)	1,315,002.00	------
Total investments	$66,079,563,002.00	$82,913,977,000.00
Undisbursed balance	-202,658,416.91	-158,875,425.33
Total assets	$65,876,904,585.09	$82,755,101,574.67

1/ Certificates of indebtedness and bonds are carried at par value, which is the same as book value. Book value for participation certificates is par value plus net unamortized premium and discount.

EXPECTED OPERATIONS AND STATUS OF THE TRUST FUND DURING THE PERIOD OCTOBER 1, 1989 TO DECEMBER 31, 1992

The expected operations of the trust fund during fiscal years 1990-92 are shown in table 5, together with the past experience of the program. The projection shown in table 5--and the entirety of this section--is based on two intermediate sets of projection assumptions labeled "Alternative II-A" and "Alternative II-B," which are presented in detail in appendix A.

Income received through the financial interchange between the railroad retirement account and the trust fund under the provisions of the Railroad Retirement Act is estimated on the same basis as income from HI contributions. Estimates of the corresponding outgo are included in the disbursement items.

Estimated income to the trust fund which is appropriated from general revenues to reimburse the program for the cost of coverage of noninsured persons is the same as the estimates of disbursements for such persons, net of corrections for differences between costs and amounts transferred for previous years. Premium income and disbursements for other noninsured persons over age 65 who may enroll in the HI program on a voluntary basis are based on an estimated enrollment of 29,000 in fiscal year 1990.

The transfers from general revenues for military wage credits are based on provisions of the Social Security Amendments of 1983 (Public Law 98-21), as described in the "Nature of the Trust Fund" section.

The investment of new assets received during fiscal years 1990-92 is assumed to be in the form of special public-debt obligations bearing interest rates ranging from 7.375 percent to 8.25 percent, payable semiannually. The average effective annual rate of interest on the assets held by the HI trust fund on September 30, 1989, was 9.5 percent.

Disbursements for benefits are projected to increase in fiscal years 1990-92, primarily as a result of the increase in hospital payment rates and hospital admissions under the program. The expenditures for benefit payments shown in table 5 differ from those shown in the 1991 Federal Budget. These estimates are based on more recent demographic and economic projections, and they do not reflect the implementation of proposed changes in regulations which were included in the budget. The expenditures for benefit payments shown in this section are based on the assumption that for fiscal years 1991 and later, the prospective payment rates will be increased in accordance with Public Law 100-203, the Omnibus Budget Reconciliation Act of 1987; for fiscal year 1990, the prospective payment rates have already been determined.

The actual operations of the HI program are organized, in general, on a calendar year basis. Earnings subject to taxation and the applicable tax rates are established by calendar year, as are the inpatient hospital deductible and other cost-sharing amounts. The projected operations of the trust fund on a calendar year basis are shown in table 6, according to the same assumptions as used in table 5. A preliminary estimate of the December 1990 lump sum transfer, to be determined in the 1990 quinquennial Military Service Determination, is also included; the provisions prescribing this transfer are described in the "Nature of the Trust Fund" section. The ratios of assets in the trust fund at the beginning of each calendar year to total disbursements during that year are shown in table 7 for past years and as projected through 1992.

TABLE 5.--OPERATIONS OF THE HOSPITAL INSURANCE TRUST FUND DURING FISCAL YEARS 1967-92
(In millions)

	Income							Disbursements				Trust fund	
Fiscal year 1/	Payroll taxes	Transfers from railroad retirement account	Reimbursement for uninsured persons	Premiums from voluntary enrollees	Payments for military wage credits	Interest on investments and other income 2/	Total income	Benefits payments 3/	Administrative expenses 4/	Total disbursements	Interfund borrowing transfers 5/	Net increase in fund	Fund at end of year
Historical Data:													
1967	$2,689	$16	$327		$11	$46	$3,089	$2,508	$89	$2,597		$492	$1,343
1968	3,514	44	273		11	61	3,902	3,736	79	3,815		88	1,431
1969	4,423	54	749		22	96	5,344	4,654	104	4,758		586	2,017
1970	4,785	64	617		11	137	5,614	4,804	149	4,953		661	2,677
1971	4,898	66	863		11	180	6,018	5,442	150	5,592		426	3,103
1972	5,226	66	503		48	188	6,031	6,108	167	6,276		-245	2,859
1973	7,663	63	381		48	196	8,352	6,648	194	6,842		1,510	4,369
1974	10,602	99	451	$4	48	405	11,610	7,806	259	8,065		3,545	7,914
1975	11,291	132	481	6	48	609	12,568	10,353	259	10,612		1,956	9,870
1976	12,031	138	610	8	48	709	13,544	12,267	312	12,579		966	10,836
T.Q.	3,366	143	0 6/	2	0	5	3,516	3,315	89	3,404		112	10,948
1977	13,649	0 7/	803 6/	11	141	770	15,374	14,906	301	15,207		167	11,115
1978	16,677	214 7/	688	12	143 8/	809	18,543	17,411	451	17,862		681	11,796
1979	19,927	191	734	17	141	901	21,910	19,891	452	20,343		1,567	13,363
1980	23,244	244	697	17	141	1,072	25,415	23,790	497	24,288		1,127	14,490
1981	30,425	276	659	21	141	1,341	32,863	28,907	353	29,260		3,603	18,093
1982	34,390	351	808	25	207	1,829	37,611	34,343	521	34,864		2,747	20,840
1983	36,387	358	878	26	3,663 9/	2,629	43,940	38,102	522	38,624	-$12,437	-7,121	13,719
1984	41,364	351	752	35	250	2,812	45,563	41,476	633	42,108		3,455	17,174
1985	46,490	371	766	38	86	3,182	50,933	47,841	813	48,654	1,824	4,103	21,277
1986	53,020	364	566	40	-714 10/	3,167	56,442	49,018	667	49,685	10,613	17,370	38,648
1987	57,820	368	447	40	94	3,982	62,751	49,967	836	50,803		11,949	50,596
1988	61,901	364	475	42	80	5,148	68,010	52,022	707	52,730		15,281	65,877
1989	67,527	379	515	42	86	6,567	75,116	57,433	805	58,238		16,878	82,755
Projection:													
Alternative II-A													
1990	71,002	369	413	60	90	6,567	78,501	63,145	954	64,099		14,402	97,157
1991	75,759	363	605	64	-436 11/	9,170	85,525	66,783	1,019	67,802		17,723	114,881
1992	80,443	361	374	69	89	10,476	91,812	74,774	1,098	75,872		15,940	130,820
Alternative II-B													
1990	70,952	369	413	60	90	6,567	78,451	63,145	954	64,099		14,352	97,107
1991	75,252	363	605	64	-267 12/	9,167	85,184	66,773	1,016	67,789		17,395	114,503
1992	79,675	358	375	70	89	10,490	91,057	74,884	1,093	75,977		15,080	129,582

1/ Fiscal years 1976 and earlier consist of the 12 months ending on June 30 of each year; the three-month interval from July 1, 1976, through September 30, 1976, labeled "T.Q.," is the transition quarter; fiscal years 1977 and later consist of the 12 months ending on September 30 of each year.
2/ Other income includes recoveries of amounts reimbursed from the trust fund which are not obligations of the trust fund and a small amount of miscellaneous income.
3/ Includes costs of Peer Review Organizations (beginning with the implementation of the Prospective Payment System on October 1, 1983).
4/ Includes costs of experiments and demonstration projects.
5/ A negative amount is a loan to the OASI trust fund; a positive amount is a repayment of loan principal to the HI trust fund.
6/ The 1977 transfer is for benefits and administrative expenses during the five-quarter period covering the transition quarter and fiscal year 1977.
7/ The 1978 transfer is for contributions during the five-quarter period covering the transition quarter and fiscal year 1977.
8/ Includes $2 million in reimbursement from general revenues for costs arising from the granting of deemed wage credits to persons of Japanese ancestry who were interned during World War II.
9/ Includes the lump sum general revenue transfer of $3,456 million, as provided for by section 151 of P.L. 98-21.
10/ Includes the lump sum general revenue adjustment of -$805 million, as provided for by section 151 of P.L. 98-21.
11/ Includes the preliminary estimate of the lump sum general revenue adjustment of -$525 million, as provided for by section 151 of P.L. 98-21.
12/ Includes the preliminary estimate of the lump sum general revenue adjustment of -$357 million, as provided for by section 151 of P.L. 98-21.

NOTE: Totals do not necessarily equal the sums of rounded components.

TABLE 6.--OPERATIONS OF THE HOSPITAL INSURANCE TRUST FUND DURING CALENDAR YEARS 1966-92
(In millions)

Calendar year	Income: Payroll taxes	Income: Transfers from railroad retirement account	Income: Reimbursement for uninsured persons	Income: Premiums from voluntary enrollees	Income: Payments for military wage credits	Income: Interest on investments and other income 1/	Income: Total income	Disbursements: Benefits payments 2/	Disbursements: Administrative expenses 3/	Disbursements: Total disbursements	Interfund borrowing transfers 4/	Trust fund: Net increase in fund	Trust fund: Fund at end of year
Historical Data:													
1966	$1,858	$16	$26		$11	$32	$1,943	$891	$108	$999		$944	$944
1967	3,152	44	301		11	51	3,559	3,353	77	3,430		129	1,073
1968	4,116	54	1,022		22	74	5,287	4,179	99	4,277		1,010	2,083
1969	4,473	64	617		11	113	5,279	4,739	118	4,857		422	2,505
1970	4,881	66	863		11	158	5,979	5,124	157	5,281		698	3,202
1971	4,921	66	503		48	193	5,732	5,751	150	5,900		-168	3,034
1972	5,731	63	381		48	180	6,403	6,318	185	6,503		-99	2,935
1973	9,944	99	451	$2	48	278	10,821	7,057	232	7,289		3,532	6,467
1974	10,844	132	471	5	48	523	12,024	9,099	272	9,372		2,652	9,119
1975	11,502	138	621	7	48	664	12,980	11,315	266	11,581		1,399	10,517
1976	12,727	143	0 5/	9	141	746	13,766	13,340	339	13,679		88	10,605
1977	14,114	0 6/	803 5/	12	143 7/	784	15,856	15,737	283	16,019		-163	10,442
1978	17,324	214 6/	688	13	141	834	19,213	17,682	496	18,178		1,035	11,477
1979	20,768	191	734	16	141	975	22,825	20,623	450	21,073		1,751	13,228
1980	23,848	244	697	18	141	1,149	26,097	25,064	512	25,577		521	13,749
1981	32,959	276	659	22	207	1,603	35,725	30,342	384	30,726		4,999	18,748
1982	34,586	351	808	24	207	2,022	37,998	35,631	513	36,144	-$12,437	-10,583	8,164
1983	37,259	358	878	27	3,456 8/	2,593	44,570	39,337	540	39,877		4,693	12,858
1984	42,288	351	752	33	250	3,046	46,720	43,257	629	43,887		2,834	15,691
1985	47,576	371	766	41	-719 9/	3,362	51,397	47,580	834	48,414	1,824	4,808	20,499
1986	54,583	364	566	43	91	3,619	59,267	49,758	664	50,422	10,613	19,458	39,957
1987	58,648	368	447	38	94	4,469	64,064	49,496	793	50,289		13,775	53,732
1988	62,449	364	475	41	80	5,830	69,239	52,517	815	53,331		15,908	69,640
1989	68,369	379	515	55	86	7,317	76,721	60,011	792	60,803		15,918	85,558
Projection:													
Alternative II-A													
1990	71,637	369	413	62	-435 10/	8,529	80,575	62,843	962	63,805		16,770	102,328
1991	76,836	363	605	65	89	9,828	87,786	69,408	1,039	70,447		17,339	119,667
1992	81,877	361	374	70	89	11,054	93,825	76,547	1,117	77,664		16,161	135,828
Alternative II-B													
1990	71,429	369	413	62	-267 11/	8,520	80,526	62,844	962	63,806		16,720	102,278
1991	76,252	363	605	65	90	9,812	87,187	69,409	1,035	70,444		16,743	119,021
1992	81,041	358	375	71	89	11,034	92,968	76,706	1,112	77,818		15,150	134,171

1/ Other income includes recoveries of amounts reimbursed from the trust fund which are not obligations of the trust fund and a small amount of miscellaneous income.
2/ Includes costs of Peer Review Organizations (beginning with the implementation of the Prospective Payment System on October 1, 1983).
3/ Includes costs of experiments and demonstration projects.
4/ A negative amount is a loan to the OASI trust fund; a positive amount is a repayment of loan principal to the HI trust fund.
5/ No transfer is made in 1976 because of the change in transfer dates from December to March. The 1977 transfer is for benefits and administrative expenses during the 15-month period beginning July 1976 and ending September 1977.
6/ No transfer is made in 1977 because of the change in transfer dates from August to June. The 1978 transfer is for contributions during the 15-month period beginning July 1976 and ending September 1977.
7/ Includes $2 million in reimbursement from general revenues for costs arising from the granting of deemed wage credits to persons of Japanese ancestry who were interned during World War II.
8/ The lump sum general revenue transfer, as provided for by section 151 of P.L. 98-21.
9/ Includes the lump sum general revenue adjustment of -$805 million, as provided for by section 151 of P.L. 98-21.
10/ Includes the preliminary estimate of the lump sum general revenue adjustment of -$525 million, as provided for by section 151 of P.L. 98-21.
11/ Includes the preliminary estimate of the lump sum general revenue adjustment of -$357 million, as provided for by section 151 of P.L. 98-21.

NOTE: Totals do not necessarily equal the sums of rounded components.

TABLE 7.--**RATIO OF ASSETS IN THE FUND AT THE BEGINNING OF THE YEAR TO DISBURSEMENTS DURING THE YEAR FOR THE HOSPITAL INSURANCE TRUST FUND**
(In percent)

Calendar year	Ratio
Historical data:	
1967	28%
1968	25
1969	43
1970	47
1971	54
1972	47
1973	40
1974	69
1975	79
1976	77
1977	66
1978	57
1979	54
1980	52
1981	45
1982	52
1983	20
1984	29
1985	32
1986	41
1987	79
1988	101
1989	115
Projection:	
Alternative II-A	
1990	134
1991	145
1992	154
Alternative II-B	
1990	134
1991	145
1992	153

ACTUARIAL STATUS OF THE TRUST FUND

The Board of Trustees recommends that it is advisable to maintain a balance in the trust fund equal to a minimum of one-half year's expenditures. This principle reflects the view that a small fund is needed for the contingency that future income and outgo may differ substantially from projected levels, and to provide time for legislative action to remedy unexpected imbalances. At the beginning of 1990, the trust fund balance was above the minimum desired level.

In previous reports, the cost of the program for projected years was defined as the sum of (1) expenditures under the program and (2) an allowance for building and maintaining the fund at the level of at least a half year's disbursements after accounting for the offsetting effect of the interest earnings of the fund. Beginning in 1988, however, the cost of the program was defined as expenditures only, without an allowance for building and maintaining the fund and without recognition of the interest earnings of the fund. In projecting expenditures under the program, only costs attributable to insured beneficiaries are considered, since benefits and administrative costs for noninsured persons are financed through general revenue transfers and premium payments rather than through payroll taxes.

The historical costs of the HI program, expressed as percentages of taxable payroll, are shown in table 8. The ratio of expenditures to taxable payroll has increased from 0.94 percent in 1967 to 2.60 percent in 1989, reflecting both the higher rate of increase in program costs than in earnings subject to HI taxes and the extension of HI benefits to disabled and end-stage renal disease beneficiaries.

The projected costs of the program under alternatives II-A and II-B, expressed as percentages of taxable payroll, and the tax rates scheduled under current law for selected years over the 75-year period 1990-2064, are shown in table 9. Further increases in the ratio of expenditures to taxable payroll under both alternative II-A and alternative II-B result from the projection that the cost of the HI program will continue to increase at a higher rate than taxable earnings. (See appendix A for a description of the methodology and assumptions used in these projections.)

Table 9 also indicates additional amounts needed for the cost of trust fund building and maintenance over the course of the 75-year projection period. During the early years of the projection period, income exceeds expenditures and the trust fund (expressed as a percent of the following year's outlays) increases, indicating that the tax rates scheduled in the law are already sufficient for trust fund building and maintenance. Once the trust fund declines below the level of fifty percent, there is an additional cost of maintaining the fund at the minimum level of fifty percent of the following year's outlays. In the last part of the projection period, the interest earned on the fifty percent balance is more than enough to cover the increases in the balance necessary to keep the fund ratio at fifty percent. This yields a negative cost of maintaining the fund for these years.

The adequacy of the financing of the HI program under current law is measured by comparing on a year-by-year basis the actual tax rates specified by law with the corresponding costs of the program, expressed as percentages of taxable payroll. If these two items are exactly equal in each year of the projection period and all projection assumptions are realized, tax revenues will be sufficient to provide for benefits and administrative expenses for insured persons. A small additional amount would be needed to maintain the trust fund at the level of one-half year's expenditures. In practice, however, tax rate schedules generally are designed with rate changes occurring only at intervals of several years, rather than with continual yearly increases to match exactly with projected cost increases. To the extent that small differences between the yearly costs of the program and the corresponding tax rates occur for short periods of time and are offset by subsequent differences in the reverse direction, the substance of the financing objectives will have been met.

While the year-by-year comparisons discussed are necessary to measure the adequacy of the financing of the HI program, the financial status of the program is often summarized, over a specific projection period, by a single measure known as the actuarial balance. The actuarial balance of the HI program is defined to be the excess of the average tax rate for the valuation period over the average expenditures of the program, expressed as a percentage of taxable payroll, for the same period. Until this year, the average expenditures, average tax rates, and actuarial balances were computed on an average-cost basis. Under this methodology, the difference between the arithmetic means of the annual cost rates (expenditures expressed as a percentage of taxable payroll) and the annual tax rates is defined as the actuarial balance. Thus, under the average-cost method, the cost and tax rates for each year are given equal weights when summarized into a single measure. Beginning with this report, however, another basis, known as the level-financing method, is used to calculate average cost rates, tax rates, and actuarial balances, unless otherwise indicated. (For comparison purposes, several tables in this report display results under both methods.) This approach is the same as the reporting methods of the OASDI report. The level-financing calculations are based on the present value of future income, outgo, and taxable payroll. The present value is calculated by discounting the future annual amounts at the assumed rate of interest. The income and cost rates over the projection period are then obtained by dividing the present value of the taxable payroll into the present values of income and outgo, respectively. The difference between the income rate and cost rate over the long-range projection period, after an adjustment to take into account the fund balance at the valuation date, is computed to obtain the long-range actuarial balance. Thus, the level-financing method uses weighted averages to arrive at summary measures. In this report, the trust fund balance is targeted to be zero at the end of the 75-year projection period under this method. It should be noted that these two methods for summarizing values over the entire 75-year projection period, and subperiods thereof, are based on the same annual projections of expenditures and tax rates; their difference consists in the way in which these projected annual values are summarized into single measures. The actuarial balance in any one-year period is identical under either method. Average costs, tax rates, and actuarial balances are shown in table 9 for multi-year periods, under both the average-cost and level-financing bases, as well as for selected single years, as already discussed.

The actuarial balances under alternatives II-A and II-B, as well as those under alternatives I and III which are described later, for the 75-year period 1990-2064 are shown in table 10. The average tax rate for the period is 2.90 percent. The average cost of the program under alternative II-A is 5.73 percent of taxable payroll. The average cost of the program under alternative II-B is 6.16 percent of taxable payroll.

Since future economic, demographic, and health care usage and cost experience may differ considerably from either set of intermediate assumptions on which the cost estimates were based, projections have also been prepared on the basis of two additional alternative sets of assumptions. The estimated operations of the HI trust fund during calendar years 1989-2014 are summarized in table 11 for all four alternatives. Table 12 compares the actuarial balances for the first 25-year period, the first 50-year period, and the whole 75-year period 1990-2064, under each of the four alternatives. The assumptions underlying alternatives II-A and II-B, the intermediate projections, are presented in substantial detail in appendix A. The assumptions used in preparing projections under alternatives I and III are also summarized in appendix A.

The four alternative sets of assumptions were selected in order to indicate the general range in which the cost of the program reasonably might be expected to fall. The alternative I assumptions are somewhat more optimistic than both alternative II assumptions, resulting in a lower average cost over the projection period and a stronger trust fund development. The alternative III assumptions are somewhat more pessimistic than both alternative II assumptions, resulting in a higher average cost over the projection period and a weaker trust fund development. Alternative III thus reflects the possible impact, in the near future, of conditions which are significantly more adverse than those assumed under either of the intermediate alternatives. Alternatives I and III provide for a fairly wide range of possible experience. Actual experience reasonably may be expected to fall within the range, but no guarantee can be made that this will be the case, particularly in light of the wide variations in experience that have occurred since the beginning of the program. The projected trust fund development under alternative III also provides a measure of the strength of the financing of the program. An adequate financing schedule ought to be sufficiently strong to withstand, for a reasonable period of time, conditions in the general economy and in the hospital sector which are substantially more adverse than anticipated under either alternative II-A or alternative II-B.

Under both alternatives II-A and II-B, the trust fund as a percent of a year's disbursements is projected to increase until 1994 and then decline steadily until it is completely exhausted shortly after the turn of the century. Under alternative I, the trust fund is projected to remain solvent throughout the first 25-year projection period, with trust fund exhaustion occurring in 2018. Under alternative III, the trust fund as a percent of a year's disbursements is projected to increase to a level of about 146 percent in 1992 and then decrease rapidly until the fund is exhausted in 1999. These projections do not reflect any reduction in disbursements due to proposed changes in regulations which were included in the 1991 Federal Budget but which have not been implemented.

The divergence in outcomes among the four alternatives is reflected both in the estimated operations of the trust fund and in the 75-year average costs. The variations in the underlying assumptions, as shown in appendix A, can be characterized as (1) moderate in terms of magnitude of the differences on a year-by-year basis, and (2) persistent over the duration of the projection period. During the first 25-year projection period, under both sets of intermediate assumptions, program expenditures are projected to increase faster than taxable payroll, at a rate which gradually declines to slightly above two percent more per year than taxable payroll by 2010. However, program expenditures are expected to grow about four percent more than taxable payroll for alternatives II-A and II-B in 2014, the last year of the first 25-year projection period. This is just after the major demographic shift, as described below, begins. Under alternative I, program expenditures are also projected to increase faster than taxable payroll, but at a somewhat lower rate, which gradually declines to about one-half percent more per year than taxable payroll by 2010; the rate then increases, reaching almost two and one-half percent more per year than taxable payroll in 2014. Similarly, alternative III follows a pattern whereby program expenditures initially increase faster than taxable payroll and at a somewhat higher rate than the intermediate assumptions, gradually declining to about four percent more per year than taxable payroll by 2010, and then increasing to over six percent more than taxable payroll in 2014. Past experience has indicated that conditions producing results as adverse as those under alternative III can occur. In view of this and because of the wide range of possible experience, it is important that a balance be maintained in the HI trust fund as a reserve for contingencies.

A valuation period of 75 years is needed to present fully the future contingencies that reasonably may be expected, such as the impact of the large shift in the demographic composition of the population which occurs after the turn of the century. As table 9 indicates, estimated expenditures under the program, expressed as percentages of taxable payroll, increase rapidly during the second 25 years of the projection period. This rapid increase in costs occurs because the relatively large number of persons born during the period between the end of World War II and the early 1960's (known as the "baby boom") will reach retirement age and begin to receive benefits, while the relatively small number of persons born during later years will comprise the labor force. During the last 25 years of the projection period, the projected expenditures under the program stabilize.

Costs beyond the initial 25-year projection period for alternatives II-A and II-B are based upon the assumption that costs per unit of service will increase at the same rate as earnings increase. Thus, changes in the last fifty years of the projection period primarily reflect the impact of the changing demographic composition of the population. Costs beyond the initial 25-year projection period for alternatives I and III begin by assuming that program cost increases, relative to taxable payroll increases, are approximately 2 percent less rapid and 2 percent more rapid, respectively, than the results under both sets of intermediate assumptions. The 2 percent differentials gradually decrease until the year 2039 when program cost increases, relative to taxable payroll, are approximately the same as under both sets of intermediate assumptions.

The 75-year actuarial balance of the HI program, under alternative II-B, is estimated to be -3.26, as shown in table 10. The actuarial balance as reported in the 1988 Annual Report was -2.35. The actuarial balance in this report is compared to that in the 1988 report because the long-range actuarial status of the trust fund was not presented in the 1989 report, for reasons given therein. The major reasons for the change in the 75-year actuarial balance are:

(1) Changes in valuation period: Deletion of 1988 and 1989 and the addition of 2063 and 2064 to the 75-year projection period substitutes deficit years for

surplus years with respect to the operations of the HI trust fund. The net effect on the actuarial balance is -0.17.

(2) Legislation since the 1988 report: Several major legislative changes were enacted since the 1988 report. These are described in the "Social Security Amendments Since the 1989 Report" section in this report and in the analogous section of the 1989 report. The net effect of all legislative changes is -0.81.

(3) Economic and demographic assumptions: Changes in the economic and demographic assumptions described in appendix A result in a -0.24 change in the actuarial balance. Projections of the population covered by the program are higher than in the 1988 report, while projections of taxable payroll are lower.

(4) Updating the projection base: The cost as a percent of payroll for 1989, excluding catastrophic expenditures, was less than estimated in the 1988 report. The net effect of this change on the actuarial balance is +0.34.

(5) Hospital assumptions: Changes in the hospital assumptions described in appendix A result in a -0.39 change in the actuarial balance. The primary factor contributing to the change is longer continuations of the current trends toward treating less complicated (and thus expensive) cases in outpatient settings, resulting in an increase in the average prospective payment per admission.

(6) Recognition of the beginning trust fund balance and interest earnings on the projected trust fund balances: Recognizing these two items and allowing them

to cover some of the cost of the program results in a +0.05 change in the actuarial balance.

(7) Change in weights: The change in weights associated with each year in the projection period results in a -1.67 change in the actuarial balance. Under the average-cost method, the cost and tax rates for each year are given equal weightings when summarized into a single measure. Under the level-financing method, the cost and tax rates for each year are weighted (before adjustment for interest) by the ratio of the taxable payroll in that year to total taxable payroll for the entire 75-year projection period.

(8) Recognition of assumed interest: Under the level-financing method, hypothetical interest earnings (in addition to interest earnings on the projected trust fund balances) are assumed to offset about 24 percent of the long-range cost of the HI program. The effect of this change on the actuarial balance is +1.98.

TABLE 8.--**COST OF THE HOSPITAL INSURANCE PROGRAM, EXPRESSED AS A PERCENT OF TAXABLE PAYROLL**

Calendar year	Expenditures under the program 1/
1967	0.94%
1968	1.04
1969	1.12
1970	1.20
1971	1.32
1972	1.30
1973	1.33
1974	1.42
1975	1.69
1976	1.83
1977	1.95
1978	2.01
1979	1.99
1980	2.19
1981	2.39
1982	2.65
1983	2.67 2/
1984	2.64
1985	2.64
1986	2.57
1987	2.49
1988	2.48
1989	2.60

1/ Costs attributable to insured beneficiaries only, on an incurred basis. Benefits and administrative costs for noninsured persons are financed through general revenue transfers and premium payments, rather than through payroll taxes. Gratuitous credits for military service after 1956 are included in taxable payroll.

2/ Deemed credits for military service before 1984 were attributed to the year in which such service had occurred. If all such credits had been attributed in 1983, expenditures under the program in 1983 would have been lower by .18 percent of taxable payroll.

TABLE 9.--COST AND TAX RATES OF THE HOSPITAL INSURANCE PROGRAM, EXPRESSED AS A PERCENT OF TAXABLE PAYROLL

Calendar year	Expenditures under the program 1/	Tax rates scheduled in the law 2/	Actuarial balance 3/	Trust fund building and maintenance 4/	Cost plus fund mainten-ance 5/	Augmented balance 6/
Alternative II-A						
1990	2.56%	2.90%	0.34%	0.34%	2.90%	0.00%
1995	3.05	2.90	-0.15	-0.15	2.90	0.00
2000	3.51	2.90	-0.61	-0.61	2.90	0.00
2005	3.87	2.90	-0.97	0.04	3.91	-1.01
2010	4.35	2.90	-1.45	0.04	4.39	-1.49
2015	5.06	2.90	-2.16	0.03	5.09	-2.19
2020	5.72	2.90	-2.82	0.04	5.76	-2.86
2025	6.47	2.90	-3.57	0.04	6.51	-3.61
2030	7.13	2.90	-4.23	0.02	7.15	-4.25
2035	7.54	2.90	-4.64	0.00	7.54	-4.64
2040	7.74	2.90	-4.84	-0.02	7.72	-4.82
2045	7.86	2.90	-4.96	-0.03	7.83	-4.93
2050	7.95	2.90	-5.05	-0.03	7.92	-5.02
2055	8.06	2.90	-5.16	-0.03	8.03	-5.13
2060	8.17	2.90	-5.27	-0.02	8.15	-5.25
Average-cost basis:						
1990-2014	3.67	2.90	-0.77	-0.06	3.61	-0.71
1990-2039	5.14	2.90	-2.24	-0.02	5.12	-2.22
1990-2064	6.09	2.90	-3.19	-0.02	6.07	-3.17
Level-financing basis:						
1990-2014	3.50	2.90	-0.60			
1990-2039	4.90	2.90	-2.00			
1990-2064	5.73	2.90	-2.83			
Alternative II-B						
1990	2.56%	2.90%	0.34%	0.34%	2.90%	0.00%
1995	3.13	2.90	-0.23	-0.23	2.90	0.00
2000	3.69	2.90	-0.79	-0.36	3.33	-0.43
2005	4.12	2.90	-1.22	0.04	4.16	-1.26
2010	4.68	2.90	-1.78	0.05	4.73	-1.83
2015	5.47	2.90	-2.57	0.04	5.51	-2.61
2020	6.18	2.90	-3.28	0.05	6.23	-3.33
2025	6.99	2.90	-4.09	0.05	7.04	-4.14
2030	7.69	2.90	-4.79	0.02	7.71	-4.81
2035	8.12	2.90	-5.22	0.00	8.12	-5.22
2040	8.32	2.90	-5.42	-0.03	8.29	-5.39
2045	8.42	2.90	-5.52	-0.03	8.39	-5.49
2050	8.52	2.90	-5.62	-0.03	8.49	-5.59
2055	8.63	2.90	-5.73	-0.03	8.60	-5.70
2060	8.75	2.90	-5.85	-0.03	8.72	-5.82
Average-cost basis:						
1990-2014	3.86	2.90	-0.96	-0.05	3.81	-0.91
1990-2039	5.50	2.90	-2.60	-0.02	5.48	-2.58
1990-2064	6.52	2.90	-3.62	-0.02	6.50	-3.60
Level-financing basis:						
1990-2014	3.69	2.90	-0.79			
1990-2039	5.25	2.90	-2.35			
1990-2064	6.16	2.90	-3.26			

1/ Costs attributable to insured beneficiaries only, on an incurred basis. Benefits and administrative costs for noninsured persons are financed through general revenue transfers and premium payments, rather than through payroll taxes. Gratuitous credits for military service after 1956 are included in taxable payroll.

2/ Rates for employees and employers combined.

3/ Difference between the tax rate scheduled in the law and program expenditures.

4/ Allowance for building and maintaining the trust fund balance at the level of at least a half-year's outgo after accounting for the offsetting effect of interest earnings.

5/ Sum of program expenditures and trust fund building and maintenance. Totals do not necessarily equal the sums of rounded components.

6/ Difference between the tax rate scheduled in the law and the cost plus fund maintenance of the program.

TABLE 10.--SEVENTY-FIVE YEAR ACTUARIAL BALANCE OF THE HOSPITAL INSURANCE PROGRAM, UNDER ALTERNATIVE SETS OF ASSUMPTIONS 1/

	Alternative			
	I	II-A	II-B	III
Average contribution rate 2/	2.90%	2.90%	2.90%	2.90%
Average-cost basis:				
Average program expenditures 3/ 4/	3.74	6.09	6.52	12.01
Actuarial balance 5/	-0.84	-3.19	-3.62	-9.11
Trust fund building and maintenance 3/ 6/	-0.02	-0.02	-0.02	+0.02
Program cost including trust fund building and maintenance 3/ 7/	3.72	6.07	6.50	12.03
Augmented balance 8/	-0.82	-3.17	-3.60	-9.13
Level-financing basis:				
Average program expenditures 3/ 9/	3.65	5.73	6.16	11.26
Actuarial balance 10/	-0.75	-2.83	-3.26	-8.36

1/ For the 75-year period 1990-2064.
2/ As scheduled under present law.
3/ Expressed as a percentage of taxable payroll.
4/ Expenditures for benefit payments and administrative costs for insured beneficiaries, on an incurred basis, computed on the average-cost basis.
5/ Difference between the average contribution rate (tax rate scheduled in the law) and program expenditures (computed on the average cost-basis).
6/ Allowance for building and maintaining the trust fund balance at the level of at least a half-year's outgo after accounting for the offsetting effect of interest earnings.
7/ Sum of program expenditures and trust fund building and maintenance.
8/ The augmented balance is the difference between the average contribution rate and the average cost of the program, including trust fund building and maintenance.
9/ Expenditures for benefit payments and administrative costs for insured beneficiaries, on an incurred basis, computed on the level-financing basis.
10/ Difference between the average contribution rate and program expenditures (computed on the level-financing basis).

TABLE 11.--ESTIMATED OPERATIONS OF THE HOSPITAL INSURANCE TRUST FUND DURING CALENDAR YEARS 1989-2014, UNDER ALTERNATIVE SETS OF ASSUMPTIONS
(Dollar amounts in billions)

Calendar year	Total income	Total disbursements	Net increase in fund	Fund at end of year	Ratio of assets to disbursements 1/ (percent)
ALTERNATIVE I					
1989 2/	$ 76.7	$ 60.8	$ 15.9	$ 85.6	115
1990	80.2	63.7	16.5	102.0	134
1991	88.0	69.3	18.7	120.7	147
1992	94.1	75.4	18.6	139.3	160
1993	100.3	81.8	18.5	157.8	170
1994	106.4	88.5	17.9	175.7	178
1995	112.1	95.4	16.7	192.3	184
2000	142.2	132.8	9.3	256.1	186
2005	178.5	174.1	4.3	288.1	163
2010	221.3	229.3	-8.0	276.3	124
2014	256.6	291.4	-34.8	187.3	76
ALTERNATIVE II-A					
1989 2/	$ 76.7	$ 60.8	$ 15.9	$ 85.6	115
1990	80.6	63.8	16.8	102.3	134
1991	87.8	70.4	17.3	119.7	145
1992	93.8	77.7	16.2	135.8	154
1993	100.1	85.3	14.8	150.6	159
1994	106.3	93.7	12.6	163.3	161
1995	112.2	102.6	9.6	172.8	159
1996	118.2	112.0	6.2	179.0	154
1997	124.0	121.9	2.1	181.1	147
1998	129.9	132.5	-2.6	178.5	137
1999	135.8	144.2	-8.4	170.1	124
2000	142.4	156.4	-14.0	156.1	109
2001	148.2	168.2	-20.0	136.0	93
2002	153.9	181.0	-27.1	108.9	75
2003	159.5	194.6	-35.1	73.8	56
2004	165.0	209.1	-44.1	29.7	35
2005	170.5	224.6	-54.2	3/	13
ALTERNATIVE II-B					
1989 2/	$ 76.7	$ 60.8	$ 15.9	$ 85.6	115
1990	80.5	63.8	16.7	102.3	134
1991	87.2	70.4	16.7	119.0	145
1992	93.0	77.8	15.2	134.2	153
1993	99.1	85.8	13.2	147.4	156
1994	105.2	94.7	10.5	157.9	156
1995	111.3	104.5	6.7	164.6	151
1996	117.5	114.8	2.7	167.3	143
1997	123.7	126.0	-2.3	165.0	133
1998	129.8	138.0	-8.1	156.8	120
1999	135.9	151.2	-15.3	141.5	104
2000	141.6	165.5	-23.9	117.6	86
2001	147.1	179.5	-32.3	85.3	66
2002	152.6	194.5	-41.9	43.4	44
2003	157.8	210.6	-52.8	4/	21
ALTERNATIVE III					
1989 2/	$ 76.7	$ 60.8	$ 15.9	$ 85.6	115
1990	79.8	63.7	16.1	101.7	134
1991	83.4	70.0	13.3	115.0	145
1992	89.0	78.6	10.4	125.4	146
1993	95.0	88.5	6.5	131.9	142
1994	98.8	98.3	0.5	132.4	134
1995	104.6	110.7	-6.1	126.3	120
1996	110.2	124.6	-14.3	112.0	101
1997	115.0	139.7	-24.7	87.2	80
1998	119.2	156.4	-37.1	50.1	56
1999	122.6	174.8	-52.1	5/	29

1/ Ratio of assets in the trust fund at the beginning of the year to disbursements during the year.
2/ Figures for 1989 represent actual experience.
3/ Trust fund depleted in calendar year 2005.
4/ Trust fund depleted in calendar year 2003.
5/ Trust fund depleted in calendar year 1999.

NOTE: Totals do not necessarily equal the sums of rounded components.

TABLE 12.--ACTUARIAL BALANCES OF THE HOSPITAL INSURANCE PROGRAM, UNDER ALTERNATIVE SETS OF ASSUMPTIONS

	Alternative			
	I	II-A	II-B	III
1990-2014:				
Average contribution rate 1/	2.90%	2.90%	2.90%	2.90%
Average program expenditures 2/	2.90	3.50	3.69	4.80
Actuarial balance 3/	0.00	-0.60	-0.79	-1.90
1990-2039:				
Average contribution rate 1/	2.90	2.90	2.90	2.90
Average program expenditures 2/	3.35	4.90	5.25	8.85
Actuarial balance 3/	-0.45	-2.00	-2.35	-5.95
1990-2064:				
Average contribution rate 1/	2.90	2.90	2.90	2.90
Average program expenditures 2/	3.65	5.73	6.16	11.26
Actuarial balance 3/	-0.75	-2.83	-3.26	-8.36

1/ As scheduled under present law.
2/ Expenditures for benefit payments and administrative costs for insured beneficiaries, on an incurred basis, expressed as a percentage of taxable payroll, computed on the level-financing basis.
3/ Difference between the average contribution rate (tax rate scheduled in the law) and program expenditures.

CONCLUSION

The balance in the Federal Hospital Insurance Trust Fund at the beginning of 1990 was 134 percent of estimated outgo for calendar year 1990. This is above the minimum 50 percent level recommended by the Board of Trustees. The tax rates specified in the law are sufficient, along with interest earnings and assets in the fund, to support program expenditures over the next thirteen to fifteen years under the intermediate assumptions. However, any significant adverse deviation from these projections could result in the inability of the fund to meet its obligations much sooner than projected. In order to bring the HI program into actuarial balance even for the first 25-year projection period under the alternative II-B assumptions, either outlays will have to be reduced by 21 percent or income increased by 27 percent (or some combination thereof).

Over the 75-year projection period, the average tax rate necessary to provide for benefits and administrative expenses exceeds the average tax rate scheduled in the law. For the first 25-year projection period, the actuarial balance is -0.60 and -0.79 for alternative II-A and alternative II-B, respectively. The actuarial balance is -2.00 and -2.35 for alternatives II-A and II-B, respectively, during the first 50-year projection period, and -2.83 and -3.26 for alternatives II-A and II-B, respectively, over the entire 75-year projection period.

There are currently over four covered workers supporting each HI enrollee. This ratio will begin to decline rapidly early in the next century. By the middle of that century, there will be only about two covered workers supporting each enrollee. As the post-World

War II "baby boom" becomes eligible for benefits, the annual increase in program costs as a percentage of taxable payroll rises dramatically, from 2.2 percent in 2010 to 4.2 percent in 2014 under alternative II-B (see appendix A). Not only are the anticipated reserves and financing of the HI program inadequate to offset this demographic change, but under all but the most optimistic assumptions, the HI trust fund is projected to become exhausted even before the major demographic shift begins to occur. Exhaustion is projected to occur shortly after the turn of the century, in 2003 under the alternative II-B assumptions, and could occur as early as 1999 if the pessimistic assumptions are realized.

The Board notes that promising steps to begin reducing the rate of growth in payments to hospitals have already been taken, including the implementation of prospective payment and diagnosis-related groups. Initial experience under the prospective payment system for hospitals suggests that this payment mechanism is an effective means of constraining the growth in hospital payments and improving the efficiency of the hospital industry. Efforts focused on improving the efficiency and reducing the costs of the health care delivery system need to be continued, in close combination with mechanisms that will assure that the quality of health care is not adversely affected.

Because of the magnitude of the projected actuarial deficit in the HI program and the probability that the HI trust fund will be exhausted shortly after the turn of the century, the Board believes that early corrective action is essential in order to avoid the need for later, potentially precipitous changes. The Board, therefore, urges that the Congress take early remedial measures to bring future HI program costs and financing into balance, and to maintain an adequate trust fund against contingencies.