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THE 1993 ANNUAL REPORT OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND DISABILITY INSURANCE TRUST FUND

COMMUNICATION

FROM

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

TRANSMITTING

THE 1993 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND THE FEDERAL DISABILITY INSURANCE TRUST FUNDS, PURSUANT TO 42 U.S.C. 401(c)(2)

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LETTER OF TRANSMITTAL

BOARD OF TRUSTEES OF THE
FEDERAL OLD-AGE AND SURVIVORS INSURANCE
AND DISABILITY INSURANCE TRUST FUNDS,
Washington, D.C., April 6, 1993

HONORABLE Thomas S. Foley
Speaker of the House of Representatives
Washington, D.C.

HONORABLE Albert Gore, Jr.
President of the Senate
Washington, D.C.

GENTLEMEN: We have the honor of transmitting to you the 1993 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 53d such report), in compliance with section 201(c)(2) of the Social Security Act.

Respectfully,

Lloyd M. Bentsen, *Secretary of the Treasury, and Managing Trustee of the Trust Funds.*

Robert B. Reich, *Secretary of Labor, and Trustee.*

Donna E. Shalala, *Secretary of Health and Human Services, and Trustee.*

Stanford G. Ross, *Trustee.*

David M. Walker, *Trustee.*

Louis D. Enoff, *Acting Commissioner of Social Security, and Secretary, Board of Trustees.*

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I. OVERVIEW

A. INTRODUCTION

The Old-Age, Survivors, and Disability Insurance (OASDI) program in the United States provides protection against the loss of earnings due to retirement, death, or disability. The OASDI program consists of two separate parts which pay monthly benefits to workers and their families. Under the Old-Age and Survivors Insurance (OASI) program, monthly benefits are paid to retired workers and their families, and to survivors of deceased workers. Under the Disability Insurance (DI) program, monthly benefits are paid to workers who become disabled and to their families.

The Social Security Act establishes a Board of Trustees to oversee the financial operations of the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund. The Board is composed of five members, three of whom serve automatically by virtue of their positions in the Federal Government: the Secretary of the Treasury, who is the Managing Trustee, the Secretary of Labor, and the Secretary of Health and Human Services. The other two members are appointed by the President and confirmed by the Senate to serve as public representatives: Stanford G. Ross and David M. Walker are currently serving 4-year terms that began on October 2, 1990.

The Social Security Act requires, among other duties, that the Board report annually to the Congress on the financial and actuarial status of the OASI and DI Trust Funds. This annual report, for 1993, is the 53d such report.

B. HIGHLIGHTS

This section summarizes the more important developments since the 1992 Annual Report was issued and describes the major features of this report. (Throughout this report totals do not necessarily equal the sums of rounded components.)

- At the end of December 1992, 41.5 million people were receiving monthly benefits under the OASDI program. During 1992, an estimated 132 million people worked in jobs covered by the OASDI program and paid OASDI taxes on their earnings. The following table summarizes the financial transactions of the OASI and DI Trust Funds in fiscal year 1992 which ended September 30, 1992 (in billions):

	OASI	DI	Combined
Assets at beginning of year	$255.4	$13.0	$268.4
Income	307.1	31.2	338.3
Expenditures	256.2	31.3	287.5
Net increase in assets	50.9	–.1	50.7
Assets at end of year	306.3	12.9	319.2

- The invested assets of the OASI and DI Trust Funds, combined, earned interest amounting to $23.6 billion during fiscal year 1992. The effective annual rate of interest earned by the combined assets during calendar year 1992 was 8.7 percent. During the same period, the average interest rate on new securities purchased by the trust funds was 7.1 percent.

- Administrative expenses for the OASDI program during fiscal year 1992 were $2.7 billion, which is equal to 0.9 percent of benefit payments for the year.

- An automatic benefit increase of 3.0 percent became effective for December 1992. Effective for 1993, the OASDI "contribution and benefit base" was increased from $55,500 to $57,600. In addition, the annual exempt amounts under the "retirement earnings test" were raised from $7,440 to $7,680 for beneficiaries under age 65, and from $10,200 to $10,560 for beneficiaries aged 65 to 69. (The retirement earnings test does not apply to beneficiaries aged 70 and over.)

- On April 2, 1992, in compliance with Section 709 of the Social Security Act, the Board reported to Congress that the reserves of the DI Trust Fund were then expected to be exhausted in

1997 and could possibly be exhausted as early as 1995. Following a careful analysis of the DI program by the Department of Health and Human Services, the ex officio members of the Board of Trustees, on December 16, 1992, submitted a report "The Social Security Disability Insurance Program: An Analysis," to Congress. The ex officio members of the Board recommended that a payroll tax rate reallocation should be used to enable the DI fund to pass the test of short-range financial adequacy, but that the specific amount of the reallocation be determined after the Board's 1993 Annual Report is issued. The ex officio members also recommended that a significant research effort be undertaken to establish more clearly whether the DI program's recent rapid growth is temporary or a longer term trend.

The Public Trustees, because of their positions as independent trustees, did not consider it appropriate to participate with the ex officio trustees in the analysis of the DI program experience or the development of specific legislative recommendations. However, the Public Trustees reviewed both the analysis and the recommendations of the ex officio trustees and concurred in the recommendations both for a tax rate reallocation and for the best possible research to assist policymakers in formulating solutions to the projected long-range DI deficit.

To evaluate the financial status of the OASDI program under a broad range of possible future conditions, actuarial estimates are prepared under three alternative sets of economic and demographic assumptions. Alternative II is the "intermediate" set of assumptions, and represents the Trustees' "best estimates" of future economic and demographic conditions. Alternative I is characterized as a more "optimistic" set—it assumes relatively rapid economic growth, low inflation, and favorable (from the standpoint of program financing) demographic conditions. Alternative III is more "pessimistic," with slower economic growth, more rapid inflation, and financially disadvantageous demographic conditions.

The Trustees prepare both "short-range" and "long-range" estimates of the financial and actuarial status of the trust funds. Short-range estimates are prepared for the next 10 years (1993-2002). Long-range estimates cover the next 75 years, in keeping with the long-term financial obligations incurred by the OASDI program. Specific tests are applied to evaluate the overall actuarial status of the program.

Overview

There is a short-range test of financial adequacy and a long-range test of close actuarial balance. The following statements summarize the actuarial estimates:

- The assets of the DI Trust Fund are estimated to decline steadily from $12.3 billion at the beginning of calendar year 1993 until the fund is exhausted in 1995, based on both the intermediate and more pessimistic assumptions. Based on alternative I, the DI Trust Fund would become exhausted in 1997.

  The DI Trust Fund fails to meet the short-range test of financial adequacy.

- Because the short-range test of financial adequacy is not met by the DI Trust Fund, and the fund is expected to be exhausted in 1995, legislative action is needed promptly to strengthen the financing of the DI Trust Fund. As noted earlier, the members of the Board of Trustees recommended in December 1992 a tax rate reallocation between the OASI and DI Trust Funds to remedy the projected financial shortfall in the DI Trust Fund in the next few years. The current Trustees are separately recommending to the Congress a reallocation from OASI to DI effective with 1993.

- The assets of the OASI Trust Fund grow steadily under all three sets of assumptions during 1993 to 2002. OASI assets are estimated to increase from their current level of $319.1 billion, or 117 percent of annual expenditures, to $1,096 billion, or 254 percent of annual expenditures at the beginning of the year 2002, based on the intermediate assumptions.

  The OASI Trust Fund passes the short-range test of financial adequacy by a wide margin.

- Over the next 10 years, the estimated assets of the OASI and DI Trust Funds, if combined, would increase substantially. At the beginning of calendar year 1993, OASDI assets amounted to $331.5 billion or 107 percent of annual OASDI expenditures. By the year 2002, the assets are estimated to increase to $1,010 billion, or 199 percent of annual expenditures, based on the intermediate assumptions. In the 1992 Annual Report, based on the intermediate assumptions, assets were estimated to increase to 206 percent of annual expenditures by the year 2001.

  The OASI and DI Trust Funds, on a combined basis, pass the short-range test of financial adequacy by a wide margin. However, legally the OASI and DI programs are separate and each has its own trust fund. As a result, separate projections for the OASI and DI funds are required.

- In the long range, income and expenditures are generally expressed as a percentage of the total amount of earnings subject to taxation under the OASDI program (referred to as "taxable payroll"). Summarized income and cost rates over the 75-year long-range period are determined through present-value calculations and by taking into account actual beginning fund balances and targeted ending fund balances of 100 percent of annual expenditures.

  Overall, for the period 1993-2067, the difference between the summarized income and cost rates is a deficit of 1.46 percent of taxable payroll based on the intermediate alternative II assumptions. This is the same as the estimated deficit shown in the 1992 Annual Report for the period 1992-2066, based on the intermediate assumptions. Based on alternative I the difference is a positive actuarial balance of 1.16 percent of taxable payroll; and based on alternative III, the difference is a deficit of 4.96 percent of taxable payroll.

  On a combined basis, the OASDI program does not meet the requirements for the long-range test of close actuarial balance. Individually, the OASI and DI Trust Funds also fail the long-range test. These results are also the same as those shown in the 1992 Annual Report.

- Income from OASDI payroll taxes represents 12.4 percent of taxable payroll—made up of the 6.2 percent tax rate paid by employees and a matching amount paid by their employers. (Self-employed workers pay OASDI taxes at the combined employee-employer rate.) Since these tax rates are not scheduled to change in the future under present law, OASDI payroll tax income as a percentage of taxable payroll remains constant at 12.4 percent.

  Under present law, up to one-half of a beneficiary's OASDI benefits may be subject to Federal income taxation. The income tax revenues from this provision are transferred to the OASI and DI Trust Funds and are currently equivalent to about 0.2 percent of taxable payroll. Adding these income sources together yields a total "income rate" of 12.6 percent. This rate is estimated to increase gradually to 13.2 percent of taxable payroll by the end of the 75-year projection period based on the intermediate assumptions. The growth is attributable, in part, to the increasing proportion of beneficiaries who will pay income taxes on their OASDI benefits in the future.

- OASDI expenditures for benefit payments and administrative expenses currently represent about 11.6 percent of taxable payroll. This "cost rate" is estimated to remain below the corresponding income rate for the next 24 years, based on the intermediate assumptions. Under alternatives I and III, the estimated cost rate is lower than the income rate for the next 34 and the next 4 years, respectively. With the retirement of the "baby-boom" generation starting in about 2010 OASDI costs will increase rapidly relative to the taxable earnings of workers. By the end of the 75-year projection period, OASDI cost rates are estimated to reach 12.4 percent, 18.0 percent, and 27.1 percent of taxable payroll under alternatives I, II, and III, respectively.

- Under the intermediate assumptions, the excess of OASDI tax revenues over expenditures for the next 24 years, together with interest earnings on the trust funds, will result in a rapid accumulation of assets for the combined OASI and DI Trust Funds during this period. However, total income is estimated to fall short of expenditures in 2025 and later, under the intermediate assumptions. In this circumstance, trust fund assets would be redeemed to cover the difference. The assets of the combined OASI and DI Trust Funds are estimated to be depleted under present law in 2036 based on the intermediate assumptions. Under the more favorable conditions assumed in alternative I, the combined OASI and DI assets would continue growing throughout the long-range projection period, reaching about 10 times annual expenditures. Under the more pessimistic assumptions in alternative III, the combined assets are estimated to be exhausted in 2017.

  Because the assets of the trust funds are generally invested in special securities of the U.S. Treasury, the initial accumulation of assets will result in a substantial cash flow from the trust funds to the general fund of the Treasury. The subsequent redemption of securities will cause this cash flow to reverse. The magnitude and pattern of these cash flows have important public policy and economic implications that extend beyond the operation of the OASDI program itself.

- Because the long-range test of close actuarial balance is not met by either the OASI or DI Trust Funds, nor by the two funds, combined, appropriate options to strengthen the long-range financing of these funds should be developed.

C. TRUST FUND FINANCIAL OPERATIONS

The various sources of income to the OASDI program, and categories of expenditures, can be illustrated by reference to the actual transactions during fiscal year 1992. The following table summarizes these transactions.

Type of transaction	Amount of transaction in fiscal year 1992 (in billions)
Sources of income:	
Payroll taxes	$308.4
Taxation of benefits	6.2
General fund reimbursements	(1)
Interest	23.6
Categories of expenditures:	
Benefit payments	281.6
Railroad Retirement financial interchange	3.2
Administrative expenses	2.7

[1] Less than $50 million.

1. Income

Most OASDI income consists of the taxes paid by employees, employers, and the self-employed on earnings in employment covered by the OASDI program. These taxes represent a portion of the Social Security payroll taxes collected under the Federal Insurance Contributions Act (FICA) and the Self-Employment Contributions Act (SECA). The balance of the Social Security payroll tax is used to finance Hospital Insurance (HI), commonly referred to as "Part A" of the Medicare program. Such taxes are paid on earnings up to specified maximum annual amounts. The following table shows the earnings bases, tax rates, and maximum tax amounts by program for 1993.

For 1993...	OASI	DI	OASDI	HI	Total for OASDI and HI
Maximum taxable amount of earnings	$57,600	$57,600	$57,600	$135,000	—
Tax rate for employees and employers, each (in percent)	5.60	0.60	6.20	1.45	7.65
Tax rate for self-employed persons (in percent)	11.20	1.20	12.40	2.90	15.30
Maximum tax payable by an employee or employer	$3,225.60	$345.60	$3,571.20	$1,957.50	$5,528.70
Maximum tax payable by a self-employed person	$6,451.20	$691.20	$7,142.40	$3,915.00	$11,057.40

The tax rates for OASDI and for HI are not scheduled to change from their current values under present law. (The allocation of the OASDI tax rate between OASI and DI is scheduled to change in the year 2000, as shown in table II.B.1.) The maximum amounts of earnings subject to OASDI and HI taxes increase automatically each year, based on the increase in the average wages for all workers (as described in section II.E).

In fiscal year 1992, OASDI payroll tax income amounted to $308.4 billion. Payroll taxes represented 91 percent of the total income received by the OASDI program during the year.

Beneficiaries whose "adjusted gross income" exceeds certain threshold amounts must pay income taxes on up to one-half of their annual OASDI benefits. The revenue from this requirement is credited to the OASI and DI Trust Funds and totaled $6.2 billion in fiscal year 1992.

The trust funds receive relatively small amounts of reimbursement from the general fund of the Treasury for certain special categories of benefits for which there is no other financing. In fiscal year 1992, the trust funds were reimbursed for the costs of paying benefits to certain uninsured persons. The total amount of the reimbursement was about $19 million.

The final source of income to the trust funds is from interest on the invested assets of the funds. The portion of each fund that is not needed to meet current expenditures is invested. By law, these investments must be in interest-bearing securities of the U.S. Government, in securities guaranteed by the U.S., or in certain securities issued by Federally sponsored agencies. In practice, trust fund assets are invested almost entirely in special U.S. Treasury securities. Interest from all investments in fiscal year 1992 amounted to $23.6 billion.

2. Expenditures

The primary type of expenditure by the OASDI program is the payment of benefits. In fiscal year 1992, benefit payments totalling $281.6 billion were made to retired and disabled workers and their families,

and to survivors of deceased workers. These payments represented 98 percent of total OASDI expenditures for the year.

By law, there is a financial interchange between the OASDI program and the Railroad Retirement program. As a result of this requirement, $3.2 billion was transferred from the OASI and DI Trust Funds to the Railroad Retirement program in fiscal year 1992.

The last category of expenditure is for the cost of administering the OASDI program. In fiscal year 1992, administrative expenses were $2.7 billion, or about 0.9 percent of total benefits paid during the year.

3. Trust Fund Assets

For fiscal year 1992, total income was $338.3 billion and total expenditures were $287.5 billion. Thus, the assets of the OASI and DI Trust Funds increased by a net total of $50.7 billion during the year, from $268.4 billion to $319.2 billion.

The trust funds serve as a mechanism to accommodate for a period of time imbalances between income and expenditures. For example, the expenditures of the DI Trust Fund exceeded income to the fund in fiscal year 1992 (for reasons that will be described subsequently), necessitating a redemption of assets to cover the difference. In the event of recurring shortfalls, the trust funds can allow a period of time for the development, enactment, and implementation of legislation to restore financial stability to the program.

The invested assets of the trust funds are backed by the full faith and credit of the U.S. Government, in the same way as other public-debt obligations of the U.S. Government. As these invested assets continue to increase, interest earnings will play an increasingly important role in program financing. In particular, over the next 20 to 30 years, interest earnings on the invested assets of the trust funds will become a larger share of total income. In fiscal year 1992, interest income to the combined OASI and DI Trust Funds represented 7.0 percent of total OASDI income. If both funds were combined (avoiding the exhaustion of the DI fund in 1995), interest income in fiscal year 2002 would represent an estimated 10.6 percent of total income.

D. INTRODUCTION TO ACTUARIAL ESTIMATES

The financial and actuarial status of the OASDI program is traditionally evaluated both for the "short range" (the next 10 years) and for the "long range" (the next 75 years). Each of the various income and expenditure items described in the previous section is estimated for the future, and combined to form estimates of the future level of trust fund assets.

The long-range period of 75 years is used in order to evaluate the full range of financial commitments that will be incurred on behalf of current program participants. For example, a group of workers now entering the labor force at age 22 will work and pay OASDI taxes for the next 45 years before reaching age 67, when full-rate retirement benefits (i.e., not reduced for early retirement) will first become payable. At that time, the surviving workers may retire and receive benefits. Some of these workers might live and receive benefits for as long as 30 years or more. Thus, a 75-year projection period will include the entire working and retired life span of the great majority of workers now contributing to the program, as well as those currently receiving benefits.

Because of the inherent uncertainty in estimates for as many as 75 years into the future, projections are shown in this report for three alternative sets of assumptions regarding future economic and demographic trends. Designated as alternatives I, II, and III, the assumptions range from optimistic (alternative I) to pessimistic (alternative III), with alternative II representing the intermediate, or "best estimates" in the opinion of the Trustees.

From the estimated income, expenditure, and asset amounts, a number of different measures are calculated for use in evaluating the financial status of the program. Because of the difficulty in comparing dollar values from one period to another, these measures are generally based on relative scales (although financial operations in nominal and inflation-adjusted dollar amounts are also available). These measures include (1) the annual amounts of future income and outgo as a percentage of the amount of earnings subject to the OASDI payroll tax, (2) the annual differences between these income and outgo figures, and (3) summary comparisons of these figures over various periods. The level of trust fund assets relative to annual program expenditures and the year in which trust fund exhaustion may be projected to occur are additional measures for evaluating the financial status of the program. Careful review of these measures provides a reasonably complete picture of the financial outlook for the OASDI program.

The program is also subject to two explicit tests of financial status (see section II.F)—a short-range test and a long-range test. The purpose of these tests is to provide objective summary judgments as to whether or not the projected financial status of the OASDI program is considered satisfactory in each time period. The tests help highlight the need for corrective action to restore financial balance when their requirements are not met.

As with any analysis of a complex subject, these summary tests should be used in conjunction with a full understanding of the year-by-year patterns, trends, and other characteristics revealed by the underlying financial projections.

E. ECONOMIC AND DEMOGRAPHIC ASSUMPTIONS

Actual future income from OASDI payroll taxes and other sources, and actual future expenditures for benefits and administrative expenses, will depend upon a large number of factors: the size and composition of the population which is receiving benefits, the level of future benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers' earnings in the future. These factors will depend in turn upon future marriage and divorce rates, birth rates, death rates, migration rates, labor force participation and unemployment rates, disability incidence and termination rates, retirement age patterns, productivity gains, wage increases, cost-of-living increases, and many other economic and demographic circumstances affecting the OASDI program.

It is not possible to know precisely what the future holds with respect to these economic and demographic factors. In recognition of this uncertainty, actuarial estimates are prepared under three alternative sets of economic and demographic assumptions. An "intermediate" set of assumptions, alternative II, is selected to provide a single "best estimate" of future economic and demographic conditions. Alternative I is a more "optimistic" set of assumptions from the standpoint of OASDI financing and alternative III is a more "pessimistic" set of assumptions. The assumptions vary from year to year during the first 5 to 25 years, in most cases, before reaching their ultimate assumed values for the remainder of the 75-year projection period.

While it may be reasonable to assume that actual trust fund experience will fall within the range defined by these alternatives, no assurance can be given because of the uncertainty inherent in projections of this type and length. In general, the degree of confidence that can be placed in the assumptions and estimates is greater for the earlier years than for the later years. Nonetheless, even for the earlier years, the estimates are only an indication of the expected trend and general range of future program experience.

The following table summarizes the ultimate values assumed for the key economic and demographic factors underlying the actuarial estimates shown in this report. These ultimate values apply for years after 2015, with the exception of life expectancy which is assumed to continue improving throughout the projection period.

Ultimate assumptions	Alternative I	Alternative II	Alternative III
Percentage change in:			
Average wage in covered employment	4.7	5.1	5.6
Consumer Price Index (CPI)	3.0	4.0	5.0
Real-wage differential (percent)	1.7	1.1	0.6
Unemployment rate (percent)	5.0	6.0	7.0
Interest rate (percent)	6.0	6.3	6.5
Fertility rate (children per woman)	2.2	1.9	1.6
Life expectancy at birth in 2070 (combined average for men and women, in years)	77.7	80.7	84.3
Annual net immigration (in thousands)	1,100.0	850.0	700.0

These key assumptions for the 1993 Annual Report are largely unchanged, as compared to the assumptions used in the 1992 report. The only major change in an ultimate assumption is an increase in the level of annual net immigration, by 100,000 for each of the three alternatives, consistent with a recent reassessment of the expected effect of the Immigration Act of 1990 by the Immigration and Naturalization Service. Revisions of other assumptions for the early years of the projection period, based on data collected since the 1992 report, had little or no effect on these ultimate annual rates. The values for life expectancy are slightly different because they reflect the accumulated difference in annual-mortality-rate assumptions for all years through the year 2070.

These assumptions reflect a careful assessment of past data and future prospects. No major change other than that made for annual net immigration was deemed necessary at this time to ensure that the financial projections continue to be based on the most plausible range of economic and demographic conditions.

F. SHORT-RANGE ACTUARIAL ESTIMATES

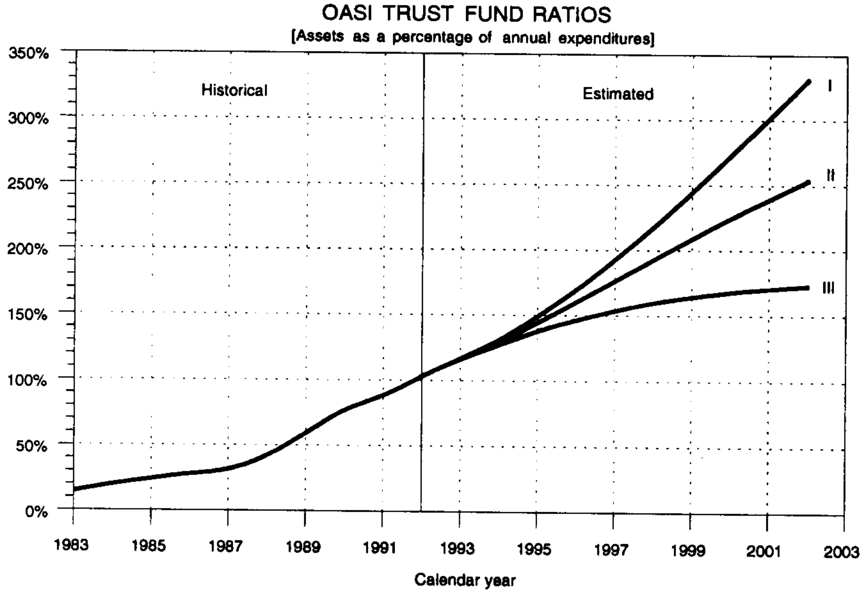
The financial status of the OASDI program during the next 10 years (1993-2002) is generally evaluated by examining the adequacy of the estimated future level of trust fund assets. Because of inflation, economic growth, and growth in the OASDI program, asset levels expressed in nominal dollar amounts are not comparable over long periods of time. For this reason, it is more informative to consider a relative measure of the program's financial condition.

For example, OASDI assets at the beginning of calendar year 1993 totaled $331 billion, while assets at the beginning of 1960 were $22 billion. The asset level in 1993 would be sufficient to cover almost 13 months of expenditures in the absence of other income. Assets in 1960, although much smaller in nominal dollars, could have covered about 22 months of expenditures and thus represented a much stronger contingency reserve.

The ratio of trust fund assets at the beginning of a year to expenditures during the year is termed the "trust fund ratio." The trust fund ratio serves as the primary measure of the fund's financial adequacy in the short range. It is also used when applying the explicit short-range test of financial adequacy, as will be illustrated in the next subsection. (Annual reports for prior years have sometimes referred to this ratio as the "contingency fund ratio.")

1. OASI Trust Fund

The following chart presents trust fund ratios for the OASI Trust Fund. Actual past values for 1983 through 1992 are shown, together with estimated values for 1993-2002 based on the alternative sets of assumptions.



The estimates indicate that the OASI trust fund ratio would generally increase by a substantial amount in every year of the short-range projection period under each of the three sets of assumptions. Based on the alternative II assumptions, the ratio is estimated to increase from 117 percent at the beginning of calendar year 1993 to 254 percent by the year 2002. Under the more optimistic conditions assumed for alternative I, the ratio would reach 331 percent at the beginning of 2002. Despite the more pessimistic conditions under alternative III, OASI assets would still increase steadily to 173 percent of annual expenditures at the beginning of 2002.

As noted previously, an explicit test of short-range financial adequacy is applied to each trust fund. The conditions required to meet this test are as follows:

- If the trust fund ratio for a fund exceeds 100 percent at the beginning of the projection period, then it must be projected to remain at or above 100 percent throughout the 10-year projection period;
- Alternatively, if the fund ratio is initially less than 100 percent, it must be projected to reach a level of at least 100 percent within 5 years (and not be depleted at any time during this

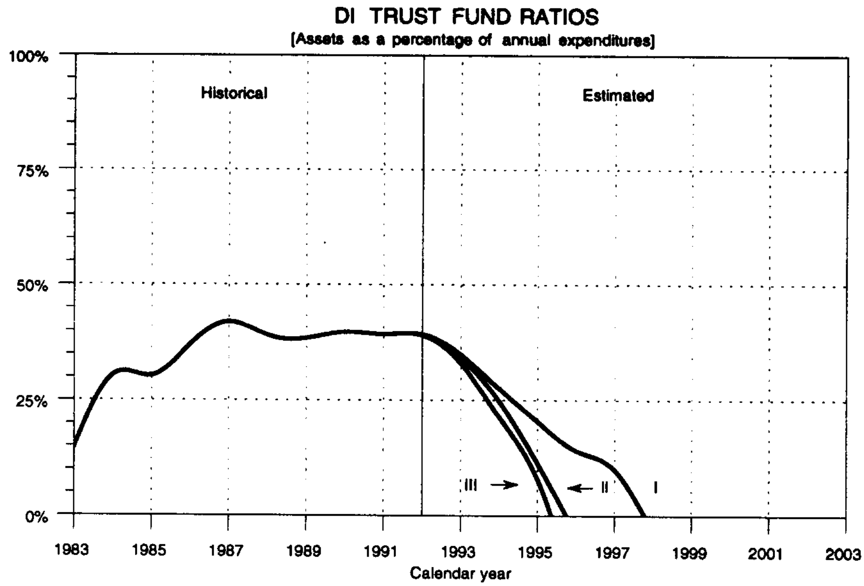
period) and then remain at or above 100 percent throughout the remainder of the 10-year period.

This test is applied on the basis of the intermediate (alternative II) estimates. Failure to meet this test by a trust fund is an indication that solvency of the program over the next 10 years is in question and that action is needed to improve the short-range financial adequacy of the program.

Based on the alternative II assumptions, the assets of the OASI Trust Fund exceed 100 percent of annual expenditures at the beginning of 1993 and would remain well above the 100-percent level through the end of the year 2002. Consequently, the OASI Trust Fund satisfies the short-range test of financial adequacy. The estimates shown above also indicate that the test would be satisfied even under the adverse conditions assumed in alternative III.

2. DI Trust Fund

As shown in the following chart, at the beginning of 1993 DI assets represented only about 35 percent of annual DI expenditures. Under all three sets of assumptions, DI assets would decline steadily to the point of exhaustion within the next 2-4 years. In the absence of corrective legislation, the assets of the DI Trust Fund are expected to become insufficient to meet benefit payments on a timely basis in 1995. This result is projected under both the intermediate and pessimistic sets of assumptions (alternatives II and III). Based on the more favorable conditions assumed in alternative I, DI assets would decrease at a somewhat slower rate but the trust fund would still be exhausted late in 1997 without corrective legislation.



The unfavorable financial outlook for the DI program is primarily attributable to an increasing trend since 1982 in the proportion of workers who are awarded disability benefits and a decreasing trend since 1970 in the annual proportion of beneficiaries whose disability benefits terminate as a result of recovery, death, or attainment of age 65. In particular, the annual number of new disability awards has increased very rapidly in the last several years, from about 415,000 in 1988 to over 640,000 in 1992. During 1983 through 1988, the adverse financial consequences of these trends were largely offset by the favorable economic growth that was experienced during that period. The economy has slowed since then, however, with the result that growth in tax income has failed to keep pace with growth in benefits.

The DI estimates shown in this report represent a worsening of the program's financial outlook compared to the estimates shown in the 1992 Annual Report.[1] The change is primarily attributable to the very rapid increase in new benefit awards experienced in 1992. A range of 518,000 to 598,000 awards had been projected but the actual

[1] In the 1992 Trustees Report, the assets of the DI Trust Fund were projected under the intermediate assumptions to be depleted in 1997. The more pessimistic projections indicated depletion in 1995.

number proved to be significantly greater than even the pessimistic projection.

The unusually large increase in awards in 1992 is partly attributable to the continuing rapid increase in the number of workers applying for disability benefits and partly to a special administrative initiative adopted early in 1992. This initiative addressed the growing number of applications awaiting adjudication and authorized special expedited claims-processing procedures. These procedures, which had not been implemented at the time the 1992 Annual Report projections were prepared, have had the effect of accelerating disability determinations in cases where an allowance is expected, thereby causing a one-time increase in awards. This effect is expected to diminish as the backlogs are reduced and, in fact, benefit awards in the fourth quarter of 1992 and first quarter of 1993 have decreased significantly. Therefore, the disability incidence assumptions developed for this annual report have not been adjusted to reflect this administrative initiative.

Because DI assets fail to reach the level of 100 percent of annual expenditures under the alternative II assumptions (and would, in fact, be depleted in the third year of the projection period), the DI Trust Fund does not satisfy the short-range test of financial adequacy. Because of the imminent depletion of the DI Trust Fund, it is imperative that corrective action be taken in the very near future to strengthen the financial position of the DI program. As noted in other sections of this report, the Board of Trustees has recommended such action to the Congress.

3. OASI and DI Trust Funds, Combined

The following chart summarizes the actual past and estimated future values of the trust fund ratio for the OASI and DI Trust Funds, combined. At the beginning of 1993, combined OASDI assets represented about 107 percent of combined expenditures for 1993. This ratio is projected to increase steadily during 1993-2002 under both the alternative I and II sets of assumptions, reaching projected levels of 284 percent and 199 percent, respectively, at the beginning of 2002. Based on the more pessimistic alternative III assumptions, the trust fund ratio for the combined funds would reach a maximum of

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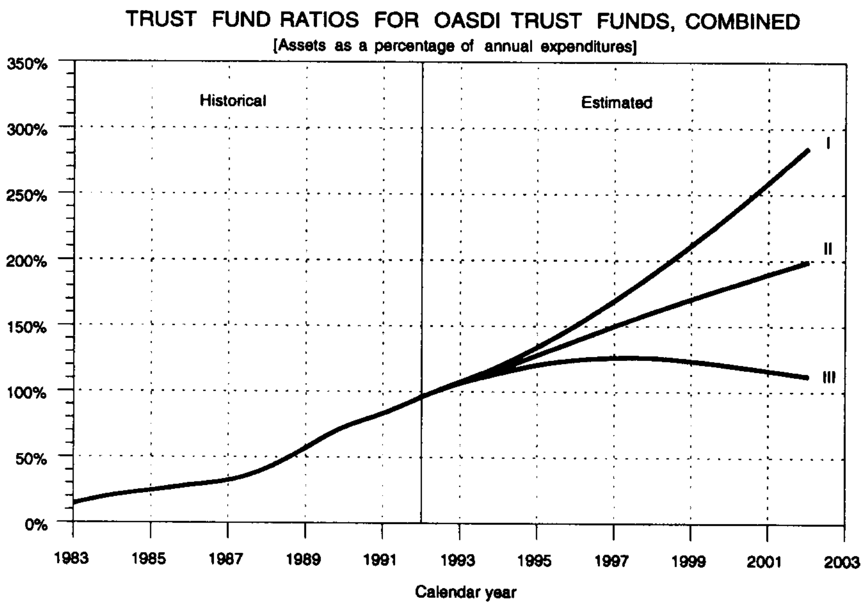
126 percent in 1997-98 and then decline gradually to 112 percent at the beginning of 2002.



Under the alternative II assumptions, the total assets of the OASI and DI Trust Funds at the beginning of 1993 exceed 100 percent of annual OASDI expenditures and would remain above that level throughout the short-range projection period. Therefore, the combined trust funds meet the requirements of the short-range test of financial adequacy. Under the less favorable conditions assumed in alternative III, the fund ratio for OASI and DI combined would still remain above the 100-percent level through 2002. Thus, the combined funds would pass the short-range test even under adverse conditions, although only by a narrow margin.

These projections indicate that the overall financial position of the OASI and DI Trust Funds, on a combined basis, is satisfactory. Thus, the near-term depletion of the DI fund could be avoided through a reallocation of tax rates between OASI and DI without jeopardizing the short-range financial status of the OASI Trust Fund. Such a reallocation would, of course, worsen the long-range financial outlook for OASI. Because the OASI program is substantially larger than DI, however, the negative impact on OASI would be small whereas the improvement for DI would be considerable.