

United States Government Stewardship Information for the Years Ended September 30, 2001 and September 30, 2000 (Unaudited)

Stewardship Assets

The Government holds “Stewardship Assets” for the benefit of the Nation. Because the Government has been entrusted with, and made accountable for, these resources and responsibilities, they are recognized in this *Financial Report*.

When acquired, stewardship assets are generally treated as expenses in the financial statements. This section provides more detailed stewardship information on these resources to highlight their long-term benefit and to demonstrate accountability. This information facilitates the understanding of the operations and financial condition of the Government.

National Defense Assets

“National Defense Assets” consist of property, plant and equipment that the Department of Defense (DOD) requires to perform military missions, such as combat operations, peacekeeping, and support of civilian authorities during civil emergencies, and vessels held in a preservation status by the Maritime Administration’s National Defense Reserve Fleet.

While standards presently exist for reporting information on national defense assets, DOD is aware that FASAB, at DOD’s request, is considering modifications to its national defense asset standard. DOD will not report any information on national defense assets until FASAB concludes its consideration of this matter and retains or changes existing standards.

Stewardship Land

“Stewardship Land” refers to federally-owned land that is set aside for the use and enjoyment of present and future generations and land on which military bases are located. Except for military bases, this land is not used or held for use in general Government operations. Stewardship land is land that the Government does not expect to use to meet its obligations, unlike the assets listed in the Balance Sheets. Stewardship land is measured in nonfinancial units such as acres of land and lakes, miles of parkways, and miles of wild and scenic rivers. Examples of stewardship land include national parks, national forests, wilderness areas, and land used to enhance ecosystems to encourage animal and plant species and to conserve nature. This category excludes lands administered by the Bureau of Indian Affairs and held in trust.

Most stewardship land managed by the Government was once part of the 1.8 billion acres of public domain land acquired between 1781 and 1867. Stewardship land accounts for 28 percent of the current U.S. land mass. Stewardship land acquired totaled \$373.0 million and \$306.5 million for the years ended September 30, 2001, and September 30, 2000, respectively. The table below depicts the stewardship land owned by the Government and administered by the Department of Interior, the Department of Defense, and the Department of Agriculture. Detailed information concerning stewardship land can be obtained in the financial statements of the Departments of Interior, Agriculture and Defense.

United States Government Stewardship Land as of September 30

Agency	Predominate Use	Millions of Acres		Percentage	
		2001	2000	2001	2000
Bureau of Land Management	Public land	261.8	264.4	40.5	40.9
U.S. Forest Service.....	National forest system	192.4	192.2	29.8	29.8
U.S. Fish and Wildlife Service	National wildlife refuge system	90.1	88.7	14.0	13.7
National Park Service	National park system	78.9	78.2	12.2	12.1
Department of Defense.....	Defense facilities	16.8	16.8	2.6	2.6
Bureau of Reclamation	Water, power, and recreation	5.7	5.8	0.9	0.9
Total acres.....		<u>645.7</u>	<u>646.1</u>	<u>100.0</u>	<u>100.0</u>

Heritage Assets

“Heritage Assets” are Government-owned assets that have one or more of the following characteristics:

- Historical or natural significance.
- Cultural, educational, or artistic importance.
- Significant architectural characteristics.

The cost of heritage assets often is not determinable or relevant to their significance. Like stewardship land, the Government does not expect to use these assets to meet its obligations. The most relevant information about heritage assets is nonfinancial. The public entrusts the Government with these assets and holds it accountable for their preservation. Examples of heritage assets include Mount Rushmore National Memorial, Yosemite National Park, and museum objects on display at the Smithsonian Institution. Other examples of heritage assets include the Declaration of Independence, the U.S. Constitution, and the Bill of Rights preserved by the National Archives. Also included are national monuments/structures such as the Vietnam Veterans Memorial, the Jefferson Memorial, and the Washington Monument, as well as art and cultural treasures at the Smithsonian Institution and the Library of Congress (LC). Many other sites such as battlefields, historic structures, and national historic landmarks are also placed in this category.

Some heritage assets are used both to remind us of our heritage and for day-to-day operations. These assets are referred to as Multi-use Heritage Assets. One typical example is the White House. The cost of acquisition, betterment or reconstruction of all multi-use heritage assets is capitalized as general property, plant and equipment and is depreciated.

The following discussion of the Government’s heritage assets is not all-inclusive. Rather, it highlights significant heritage assets reported by Federal agencies.

The Government classifies heritage assets into three broad categories:

- Collection-type.
- Natural.
- Cultural.

“Collection-type Heritage Assets” include objects gathered and maintained for museum and library collections. “Natural Heritage Assets” include national wilderness areas, wild and scenic rivers, natural landmarks, forests, and grasslands. “Cultural Heritage Assets” include historic places and structures, memorials and monuments, national cemeteries, and archeological sites.

Collection-Type Heritage Assets

The Smithsonian Institution holds some of the most prominent Federal museum collections. The Smithsonian acquires, protects, and preserves approximately 140 million individual objects for public exhibition, education, and research.

Similarly, the LC holds the world's largest library collection, comprising more than 115 million items. The LC receives two copies of every book, pamphlet, map, print, photograph, and piece of music registered for copyright in the United States.

The National Archives hold more than 2 million cubic feet of records. These records ensure ready access to essential information documenting the rights of citizens, the actions of Federal officials, and the effects of those actions on the national experience. These records include text and legislative records; cartographic and architectural records; motion picture, sound, and video records; and still pictures and graphics. The National Archives also maintains historically important documents such as the U.S. Constitution and the Louisiana Purchase Treaty.

Collection-type heritage assets acquired totaled \$13.2 million and \$61.4 million for the years ended September 30, 2001, and September 30, 2000, respectively.

Natural Heritage Assets

Congress has designated several wilderness areas to preserve their natural conditions. The Department of Interior (DOI) manages approximately 71 million acres of these wilderness areas comprised of almost 68.3 percent of the Nation's 104 million wilderness acres. The Cebolla Wilderness in New Mexico is one such area.

The "national wild and scenic rivers system" includes protected free-flowing rivers. The Government protects these areas because of their fish and wildlife, or for their scenic, recreational, geologic, historic, or cultural value. DOI manages 52.5 percent of these 11,294 river miles, including the Bluestone National Scenic River in West Virginia.

The Government also sets aside natural landmarks that exemplify a region's natural characteristics. The National Park Service manages 18 national natural landmarks, such as the Garden of the Gods in Colorado.

The U.S. Forest Service manages 155 national forests and 20 national grasslands on over 192 million acres of public land. These areas encompass significant heritage resources. Examples include the White Mountain National Forest in New Hampshire and the Thunder Basin National Grassland in Wyoming.

Natural heritage assets acquired totaled \$51.0 million and \$106.8 million for the years ended September 30, 2001, and September 30, 2000, respectively.

Any acreage cited above for natural heritage assets, such as wilderness areas, are also included in the acreage cited in the Stewardship Land section.

Cultural Heritage Assets

The National Register of Historic Places lists historic sites and structures. This is America's official list of cultural resources worthy of preservation. Official properties include districts, sites, buildings, structures, and objects significant to American history. It also includes significant architectural, archaeological engineering, and cultural properties. Forest Service land encompasses 887 such properties.

The Nation's monuments and memorials include the Washington Monument, the Vietnam Veterans Memorial, and the Jefferson Memorial in Washington, D.C. The National Park Service manages these. In addition, the American Battle Monuments Commission administers, operates, and maintains 24 permanent American Military Cemeteries on foreign soil and 27 stand-alone memorials, monuments, and markers around the world. This includes the Belleau Wood Marine Monument in France.

Archeological sites contain the remains of human activity. DOI manages numerous archaeological sites. The National Park Service manages 63,000 archeological sites; the Bureau of Land Management, the U.S. Fish and Wildlife Service and the Bureau of Reclamation manage 269,159 archaeological and historical properties. The ancient earthen mounds at the Hopewell Culture National Historic Site in Ohio are a notable example.

National cemeteries include the Arlington National Cemetery in Virginia and the Fort Logan National Cemetery in Colorado. The Department of the Army (Army) manages the Arlington National Cemetery. The Department of Veterans Affairs (VA) manages Fort Logan National Cemetery and other cemeteries.

Stewardship Responsibilities

“Stewardship Responsibilities” provides information on the social insurance programs: Social Security, Medicare, Railroad Retirement, Black Lung and Unemployment Insurance. The purpose of this information is to assist the American people in evaluating the financial condition and sustainability of these programs.

Social Insurance Update

The following table gives financial report users updated information on selected financial aspects of the Social Security and Medicare programs that became available subsequent to the preparation of the related data presented in the detailed social insurance disclosures on pages 57 to 74.

Specifically, the social insurance programs’ actuarial analysis and assumptions that are included on pages 65 to 68 were prepared based on estimates as of January 1, 2001. On March 26, 2002, the Boards of Trustees for the Social Security and Medicare Trust Funds released annual reports that present information for these programs as of January 1, 2002. The table below compares selected key data elements from these sources.

Comparison of Trustees’ Reports Updated Estimates with the Financial Report Estimates

	Trustees’ Report Estimates as of January 1, 2002	Financial Report Estimates as of January 1, 2001
First Year Expenditures Exceed Tax Revenue:		
Social Security (OASI and DI).....	2017	2016
Federal Old-Age and Survivors Insurance (OASI)	2018	2016
Federal Disability Insurance (DI)	2009	2008
Federal Hospital Insurance (Medicare Part A).....	2016	2016
Year Trust Fund Assets Are Exhausted:*		
Social Security.....	2041	2038
Federal Old-Age and Survivors Insurance	2043	2040
Federal Disability Insurance	2028	2026
Federal Hospital Insurance	2030	2029
Actuarial Deficit as a Percentage of Taxable Payroll Over the 75-Year Projection Period:		
Social Security.....	1.87%	1.86%
Federal Old-Age and Survivors Insurance	1.54%	1.53%
Federal Disability Insurance	0.34%	0.33%
Federal Hospital Insurance	2.02%	1.97%
Annual Deficit as a Percentage of Taxable Payroll for the 75th Year of the Projection Period:		
Social Security.....	6.42%	6.05%
Federal Old-Age and Survivors Insurance	5.64%	5.33%
Federal Disability Insurance	0.78%	0.72%
Federal Hospital Insurance	7.37% ¹	7.35%
Present Value of Resources Needed Over the 75-Year Projection Period:		
Social Security.....	\$4,562 billion ¹	\$4,207 billion
Federal Hospital Insurance	\$5,126 billion ¹	\$4,730 billion

*See page 61 for more information on how trust funds are financed.

¹Amount derived by the Office of the Actuary at SSA and CMS, respectively, for Trustees’ Report projections.

In their 2002 Reports, the Trustees for the Social Security (OASDI) and Federal Hospital Insurance (Medicare Part A) programs reported some near-term improvement in the financial status of these programs. However, they continued to caution that long-term sustainability issues still need to be addressed, and that timely action to deal with the continuing long-term shortfall is needed. As the Trustees point out, "... the sooner adjustments are made the smaller and less abrupt they will have to be."

One factor with a large effect on this year's projections compared to last year was an increase in the long-term productivity assumption from a 1.5 percent annual growth rate to a 1.6 percent annual growth rate. In addition, the CPI inflation rate assumption was lowered (from 3.3 percent to 3.0 percent), there were several relatively small changes in the demographic assumptions, and some improvements in projection methods were incorporated into the estimates.

On balance, these changes extend the exhaustion date for the OASDI Trust Fund by three years (from 2038 to 2041) and for the HI Trust Fund by one year (from 2029 to 2030). Revenues fall behind expenditures a year later than last year (2017) for the OASDI Trust Fund but in the same year as last year (2016) for the HI Trust Fund. The 75-year actuarial deficits were slightly larger for both trust funds, as the changes in assumptions and methods didn't fully offset the addition of a new deficit year at the end of the 75-year projection period. Both funds remain substantially out of long-term actuarial balance. Compared to last year, the annual deficit (as a percentage of payroll) in the 75th projection year (2076) increased noticeably for the OASDI fund and was about the same for the HI fund.

The First Year Expenditures Exceed Tax Revenue represents the point at which the trust funds would have to start using interest income to make payments. Interest income is paid in the form of Treasury securities. In order to use the interest, the trust funds would have to redeem the securities. To finance redemption, the Government must raise taxes, increase borrowings from the public, cut spending for other programs, retire less debt, or some combination thereof. The Year Trust Fund Assets Are Exhausted represents the point at which all trust fund assets (Treasury securities) have been redeemed. After this date, these respective programs will not have adequate resources to pay promised benefits or obligations in a timely manner. In the year of trust fund exhaustion, 2041 for Social Security (OASDI) and 2030 for Medicare Part A, tax income is estimated to cover 73 percent and 68 percent of program expenditures, respectively. The Actuarial Deficit as a Percentage of Taxable Payroll Over the 75-Year Projection Period can be interpreted as the percentage that, if added to the current scheduled tax rates, would cover projected trust fund shortfalls over the 75-year period and have enough assets on hand at the end of the 75-year period to pay scheduled benefits in the following year. Similarly, the Annual Deficit as a Percentage of Taxable Payroll for the 75th Year of the Projection Period represents the increase in payroll taxes needed in year 2076 and 2075, respectively, to cover projected cash shortfalls for each 1-year period. The Present Value of Resources Needed Over the 75-Year Projection Period represents the discounted net excess of projected cash expenditures (outflow) over cash income (inflow) during the 75-year projection period. The trust fund assets at the beginning of the period are not reflected in the calculation of this amount.

Social Insurance

The social insurance programs were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the Government. Because taxpayers rely on social insurance in their long-term planning, social insurance programs should show their sustainability as currently constructed, as well as what their effect will be on the Government's financial condition. The resources needed to run these programs are raised through taxes and fees collections. Eligibility for benefits rests in part on earnings and time worked by the individuals. Social insurance program benefits sometimes are redistributed intentionally toward lower-wage workers. In addition, social insurance programs have uniform sets of entitling events and schedules that apply to all participants.

United States Statement of Social Insurance

The following table presents estimates for several key indicators of the status of the Social Security and Medicare programs. These estimates are based on long-range actuarial projections of the range of persons who are participants or eventually will participate in the programs as contributors or beneficiaries during a projected period of time sufficient to illustrate the financial status and sustainability of the program. The projection includes current workers, retirees, survivors, disabled persons who have not attained retirement age, as well as the participants who have attained retirement age, and those expected to become new participants in the future.

United States Government Statement of Social Insurance Present Value of Long-Range Actuarial Projections¹

(In billions of dollars)	Contributions and Earmarked Taxes ²		Benefit Payments ³		Benefit Payments in Excess of Contributions and Earmarked Taxes	
	2001	2000	2001	2000	2001	2000
Participants Who Are Currently Receiving Benefits:						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	309	266	4,255	4,020	3,946	3,754
Federal Hospital Insurance (Medicare Part A)	113	97	1,693	1,681	1,580	1,584
Federal Supplementary Medical Insurance (Medicare Part B)	258	234	1,159	1,051	901	817
Railroad Retirement	56	2	81	27	25	25
Black Lung (Part C) ⁴	8	8	4	4	(4)	(4)
Participants Who Are Not Currently Receiving Benefits:						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	12,349	11,335	18,944	17,217	6,595	5,882
Federal Hospital Insurance (Medicare Part A)	4,136	3,757	8,568	6,702	4,432	2,945
Federal Supplementary Medical Insurance (Medicare Part B)	1,845	1,527	7,415	6,094	5,570	4,567
Railroad Retirement	57	26	67	39	10	13
Future Participants:⁵						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	11,035	10,088	4,700	4,297	(6,335)	(5,791)
Federal Hospital Insurance (Medicare Part A)	3,507	3,179	2,225	1,349	(1,282)	(1,830)
Federal Supplementary Medical Insurance (Medicare Part B)	593	404	2,206	1,514	1,613	1,110
Railroad Retirement	29	40	13	10	(16)	(30)
			Valuation Period	Valuation Date	Net Present Value of Negative Cashflow⁶	
Federal Old-Age, Survivors and Disability Insurance (Social Security) 2000			1/1/2000 – 12/31/2074	1/1/2000	3,845	
Federal Old-Age, Survivors and Disability Insurance (Social Security) 2001			1/1/2001 – 12/31/2075	1/1/2001	4,207	
Federal Hospital Insurance (Medicare Part A) 2000			1/1/2000 – 12/31/2074	1/1/2000	2,699	
Federal Hospital Insurance (Medicare Part A) 2001			1/1/2001 – 12/31/2075	1/1/2001	4,730	
Federal Supplementary Medical Insurance (Medicare Part B) 2000			1/1/2000 – 12/31/2074	1/1/2000	6,494	
Federal Supplementary Medical Insurance (Medicare Part B) 2001			1/1/2001 – 12/31/2075	1/1/2001	8,084	
Railroad Retirement 2000			9/30/2000 – 12/31/2073	12/31/1998	8	
Railroad Retirement 2001			1/1/2001 – 12/31/2076	1/1/2001	19	
Black Lung (Part C) 2000			9/30/2000 – 9/30/2040	6/30/2000	(4)	
Black Lung (Part C) 2001			9/30/2001 – 9/30/2040	6/30/2001	(4)	

The following notes are an integral part of this financial statement.

Notes to the Statement of Social Insurance

- ¹ Present values are computed based on the economic and demographic assumptions believed most likely to occur (the intermediate assumptions) as set forth in the related Trustees' reports.
- ² Contributions and earmarked taxes consist of payroll taxes from employers, employees, and self-employed persons; revenue from Federal income taxation of OASDI and railroad retirement benefits; monthly Medicare Part B premiums paid by, or on behalf of, beneficiaries; railroad work-hour tax; and excise tax on coal (Black Lung). Contributions and earmarked taxes for the Medicare Part B program presented in this report are presented on a consolidated perspective. Interest payments and other intragovernmental transfers have been eliminated. The Centers for Medicare & Medicaid Services' (CMS), formerly known as the Health Care Financing Administration (HCFA), 2001 Annual Report presents income from the trust fund's perspective, not a Governmentwide perspective. Therefore, CMS's Annual Report includes \$8,084 billion for the present value of transfers from the general fund of the Treasury to the Medicare Part B Trust Fund that have been eliminated in this *Financial Report*.
- ³ Benefit payments include administrative expenses.
- ⁴ Black Lung disability benefits for current and future miners are not expected to be material.
- ⁵ Includes births during the period and individuals below age 15 as of January 1 of the valuation year.
- ⁶ The net present value of negative cashflow is the current amount of funds needed to cover projected shortfalls, excluding trust fund balances, over the 75-year period. The trust fund balances at the beginning of the valuation period that were eliminated for this consolidation were: \$1,049 billion – Social Security, \$177 billion – Medicare Part A, \$44 billion – Medicare Part B, \$19 billion – Railroad Retirement, and Black Lung Trust Fund, which had a negative balance of \$7.2 billion.

The projection period for new entrants covers the next 75 years for the Social Security and Medicare programs. The projection period for current participants (or "closed group") would theoretically cover all of their working and retirement years, a period that could be greater than 75 years in a few instances. As a practical matter, the present values of future payments and contributions for/from current participants beyond 75 years are not material.

The actuarial present value of the excess of future benefit payments to current participants (that is, to the closed group of participants) over future contributions and tax income from them or paid on their behalf is calculated by subtracting the actuarial present value of future contributions and tax income by and on behalf of current participants from the actuarial present value of the future benefit payments to them or on their behalf. For Social Security and Medicare, further information can be obtained from the Social Security Administration and the Department of Health and Human Services: The 2001 Report of the Board of the Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, and The 2001 Report of the Board of the Trustees of the Federal Hospital Insurance Trust Fund.

Program Sustainability

Social Security (OASDI)

Under the intermediate assumptions (best estimates) of the Board of Trustees of the Federal OASDI Trust Funds, OASDI income from contributions on taxable earnings and from income taxes on benefits is expected to exceed total expenditures for this year and each of the next 14 calendar years. From 2010 through 2030, however, OASDI costs, relative to taxable earnings, are expected to increase rapidly as the "baby-boom" generation reaches retirement age. In contrast, the program's income from contributions due on taxable earnings and income taxes on benefits will remain a relatively constant percentage of taxable payroll.

In view of the size of the financial shortfall in the OASDI program over the next 75 years, the Board of Trustees of the Federal OASDI Trust Funds urges that the long-range deficits of both the OASI and DI Trust Funds be addressed in a timely way.

Medicare

Medicare has generally been viewed as a program in greater financial difficulty than Social Security because it will combine the rising costs of health care over time with the increase in beneficiaries as baby boomers become eligible. The approach of the last two decades, that of seeking improvements in the efficiency and effectiveness of

health care delivery, will continue to be an important contributor to Medicare's future. The challenge facing the future financing of this program is how we will, as a society, share the costs of health care for a much larger aging population.

The Medicare Part A program is substantially out of financial balance in the long range. Under the intermediate assumptions of the Board of Trustees of the Medicare Part A Trust Fund, income is projected to continue to exceed expenditures moderately for the next 14 years, but to fall short by steadily increasing amounts in 2016 and later. The long-range outlook, however, remains extremely unfavorable, in large part as a result of the impending retirement of the baby boom generation. Over the full 75-year projection period, substantially greater changes in income and/or outlays are needed to bring the program into actuarial balance.

These projections indicate that without additional legislation, the fund would be exhausted in the future—initially producing payment delays, but very quickly leading to a curtailment of health care services to beneficiaries. In its 2001 annual report to Congress, the Board of Trustees of the Medicare Part A Trust Fund urged the Nation's policy makers to address the remaining financial imbalance facing the Medicare Part A Trust Fund by taking "further effective and decisive action, building on the strong steps taken in recent reforms." They also stated, "Consideration of further reforms should occur in the relatively near future."

The recent improvements in projected expenditures for Medicare Part B, while welcome, are not sufficiently large to diminish serious concerns with expenditure growth. The Board of Trustees of the Medicare Part B Trust Fund note that program costs have generally grown faster than the GDP and that this trend is expected to continue under present law. The projected increases are attributable in part initially to assumed continuing growth in the volume and intensity of services provided per beneficiary. Starting in 2010, the retirement of the post-World War II baby boom generation will also have a major influence on the growth in program costs.

Prior to the Balanced Budget Act of 1997, Medicare Part A Trust Fund assets were projected to be exhausted in the very near future. The urgency of this situation prompted considerable attention and led directly to the provisions in the Act to slow Medicare Part A expenditure growth. In contrast, the financing provisions for Medicare Part B prevent such crises. While Medicare Part B is in fact running a shortfall since premiums only cover about 25 percent of program costs, Part B remains solvent because of a growing infusion of general revenue funds. As a result, there has been substantially less attention directed toward the financial status of the Medicare Part B program than to the Medicare Part A program, even though Medicare Part B expenditures have increased faster than Medicare Part A expenditures in most years and are expected to continue to do so in the future.

Given the past and projected cost of the Medicare Part B program, the Board of Trustees of the Medicare Part B Trust Fund urges the Nation's policy makers to consider effective means of controlling Medicare Part B costs in the near term. For the longer term, legislative proposals need to be developed to address the large increases in Medicare Part B costs associated with the baby boom's retirement in partnership with Medicare Part A cost increases.

Railroad Retirement

The Railroad Retirement program is projected to have an \$18.5 billion negative cashflow, based on a projection through 2076, on a consolidated basis. This negative cashflow will be financed through the redemption of securities that resulted from past program surpluses. The long-term stability of the program, however, is still questionable. Under the current financing structure, actual levels of railroad employment over the coming years will largely determine whether corrective action is necessary.

Subsequent event: On December 21, 2001, President Bush signed the "The Railroad Retirement and Survivors' Improvement Act of 2001" (RRSIA) into law. The new law enhances benefits and changes the funding of the retirement program.

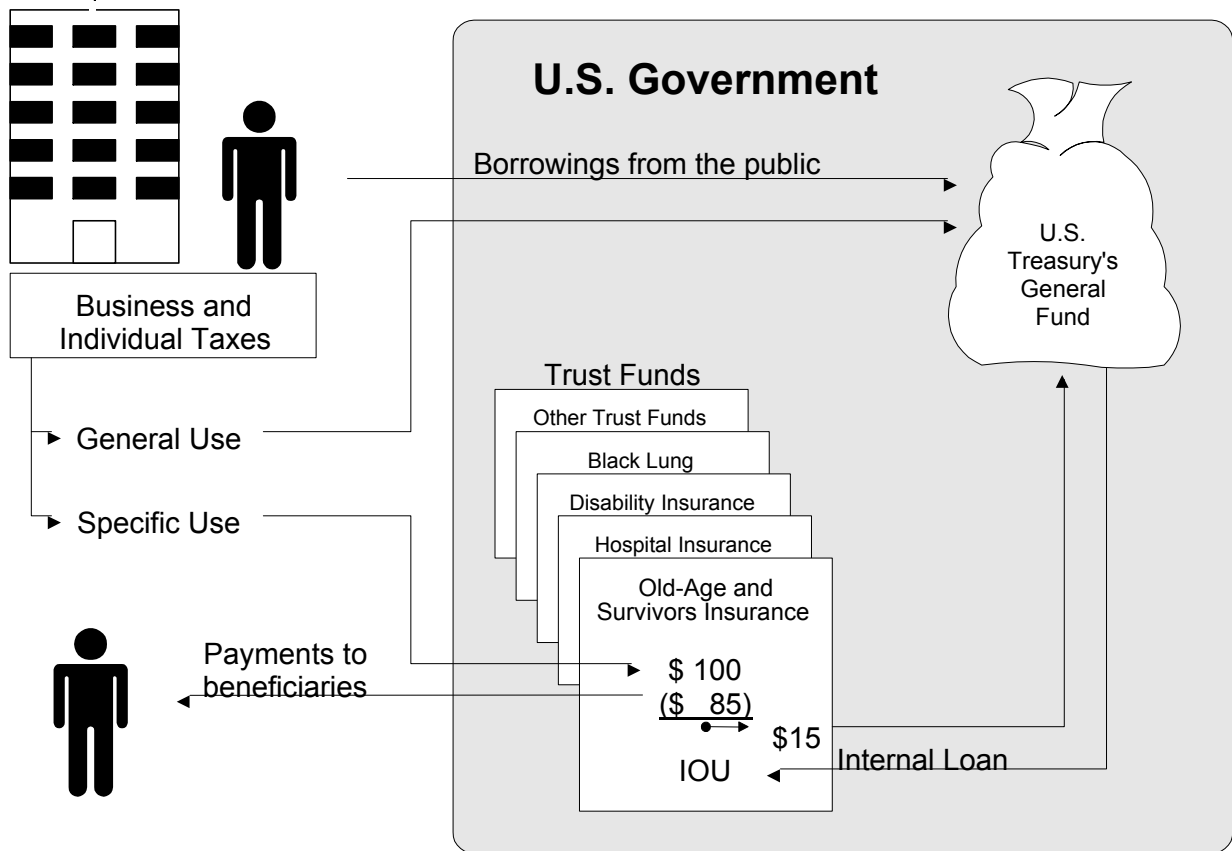
Benefits of the RRSIA of 2001 include:

- Increases the widow(er)s benefits by providing a guaranteed minimum amount of benefits.
- Restores full annuities to employees and their spouses who retire at age 60, instead of 62, with 30 years of railroad service.
- The vesting period is also reduced from 10 to 5 years.
- Creates a new National Railroad Retirement Investment Trust (Trust) to administer a new Railroad Retirement Investment Trust Fund (RRIT Fund).
- A new nongovernmental financial institution ("Disbursing Agent") will serve as a disbursing agent for all benefits payable under the Railroad Retirement Act.

Black Lung

The Black Lung Part C disability program’s net present value of future benefit payments for the 39-year period ending September 30, 2040 is \$3.5 billion. The net present value of future excise taxes for the 39-year period is \$7.9 billion, which results in a \$4.4 billion excess of excise taxes over benefit payments. However, the net present value of total cash outflows, including interest payments and administrative costs, is \$20.8 billion resulting in an excess of cash outflows over excise taxes of \$12.8 billion.

Trust Fund Financing



The Government collects taxes from business and individuals. Each type of tax collected is classified for “General use” or for “Specific use.” The taxes collected for general use are included in the general fund and are used to fund the Government’s general operations.

The taxes collected for specific use are credited to the corresponding trust fund that will use these funds to meet a particular Government purpose. The beneficiaries from these earmarked trust funds are paid directly from the balance of each of the corresponding trust funds. If the collections from taxes and other sources exceed outlays to the beneficiaries, the excess collections are invested, normally in Treasury securities, which means that the excess collections are “loaned” to the Treasury’s general fund. The reason for this is that the trust funds generally are not permitted to hold the excess cash collected. Usually, all excess collections as well as interest earnings must be invested by the trust funds in Treasury securities or Government-guaranteed securities. Therefore, the trust fund balances do not represent cash. These balances are the sum of all specific use collections plus interest and other receipts, less payments to beneficiaries over the life of the fund.

When payments to beneficiaries exceed receipts, the trust funds redeem a commensurate amount of their Federal debt securities holdings.

In addition to earmarked taxes, trust funds receive income from the interest earned on investments in Federal debt securities and, in some cases, from other sources as well.

Social Security

Congress passed the Social Security Act in 1935. The Act, as subsequently amended, includes programs that provide retirement and disability benefits. Congress established two trust funds for Social Security: The Federal Old-Age and Survivors Insurance (OASI) and the Federal Disability Insurance (DI) Trust Funds (combined as OASDI). OASI pays retirement and survivors' benefits and DI pays benefits to disabled workers and their dependents. At the end of calendar year 2000, OASDI benefits were paid to approximately 45 million beneficiaries. Revenue to the combined OASDI funds consists primarily of taxes on earnings paid by employees, their employers, and the self-employed. OASDI also receives revenue from the income taxes on some Social Security benefits and interest on its investments in Treasury securities. Social Security revenues not needed to pay current benefits or administrative expenses are invested in special-issue Treasury securities. Eligibility and benefit amounts are determined under the laws applicable for the period. Current law bases the amount of the monthly benefit payments for workers, or their eligible dependents or survivors, on the workers' lifetime taxable earnings histories.

The Board of Trustees of the OASI and DI Trust Funds provides in its annual report to the President and Congress short-range (10 year) and long-range (75 year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Board of Trustees uses three alternative sets of economic and demographic assumptions to show a range of possibilities. Assumptions are made about many economic and demographic factors, including gross domestic product, earnings, the Consumer Price Index (CPI), the unemployment rate, the fertility rate, immigration, mortality, and disability incidence and terminations. The assumptions used in the accompanying tables, generally referred to as the "intermediate assumption," reflect the best estimate of expected future experience, under current law.

Cashflow Projections

The present values of actuarial estimates as shown in the following sections were computed as of January 1, 2001, the beginning of the valuation period. The actuarial estimated income equals the sum of the present value of all estimated non-interest income during the period. The actuarial estimated expenditures equal the sum of the present value of all estimated payments during the valuation period. These estimates were prepared using the financing method deemed the most appropriate by Congress and the Board of Trustees. Estimates assume the program will cover future workers as they enter the labor force.

The primary receipts of OASDI are funds appropriated under permanent authority based on contributions payable by workers, their employers, and individuals with self-employment income. Revenue derived from subjecting a portion of OASDI benefits to Federal personal income taxation is dedicated to the OASDI and Hospital Insurance (HI) programs. All contributions, or taxes, are collected by the Internal Revenue Service (IRS) and deposited to the trust fund. Another source of income is interest received on the investments held by the trust funds, which is implicit in the present values presented in this report. The primary expenditures are for OASDI benefit payments and for expenses related to administration of the OASDI programs.

Under current legislation and using intermediate assumptions, the OASI and DI Trust Funds are projected to be exhausted in 2040 and 2026, respectively. Combined OASDI expenditures will exceed annual tax income beginning in 2016 and will exceed total annual income (including interest income) for calendar years 2025 and later. Thus, tax income plus a portion of interest income will be needed to meet expenditures for the years 2016 through 2024. Thereafter, in addition to tax income and interest income, a portion of the principal (combined OASDI assets) will be needed each year until the trust fund assets are totally exhausted in 2038. At that point, annual program tax income will be sufficient to pay only approximately 73 percent of the benefits due.

Chart 1 shows actuarial estimates of combined OASDI annual income (excluding interest) and expenditures for 1960-2075 in nominal dollars. The estimates are for the open group population, all persons projected to participate in the OASDI program as covered workers or beneficiaries, or both, during that period. Thus, the estimates include payments from, and on behalf of, workers who will enter covered employment during the period, as well as those already in covered employment at the beginning of that period. These estimates also include expenditures made to, and on behalf of, such workers during that period.

Currently, Social Security tax revenues exceed benefit payments, and the system is building large trust fund reserves to help finance the retirement of the baby boom generation. Under current estimates, benefit payments will begin to exceed taxes in 2016, and Social Security will start using annual trust fund interest to help pay benefits. Starting around 2025, Social Security will need to use the trust fund reserves themselves to help pay benefits; by about 2038, the trust fund reserves will be exhausted. The trust fund interest and reserves are in the form of Treasury securities that must be redeemed. The Government will need to raise taxes (other than OASDI payroll taxes),

increase borrowing from the public, cut spending for other programs, change the laws under which the Social Security program provides benefits, or some combination thereof, to redeem the securities.

Chart 1—Estimated OASDI Income (Excluding Interest) and Expenditures 1960-2075

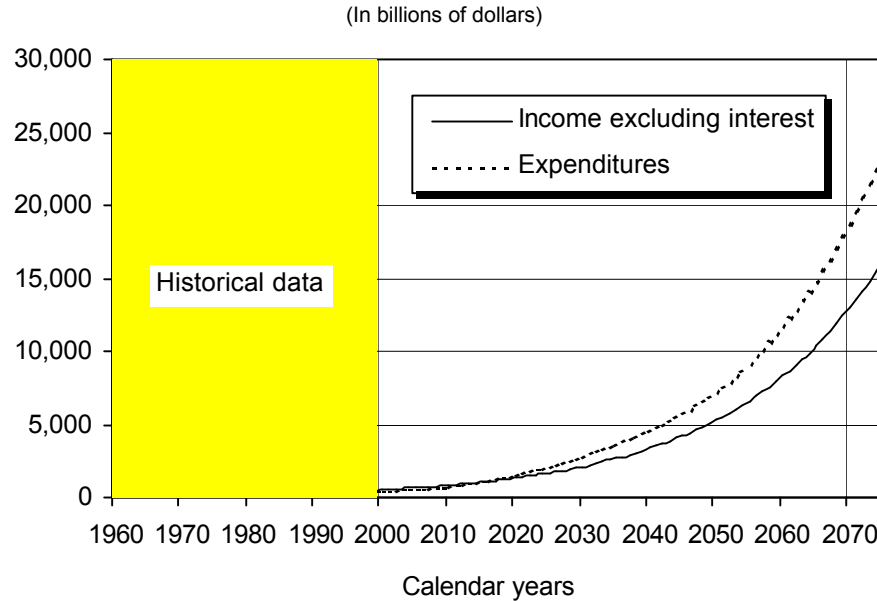


Chart 2 shows estimated annual income excluding interest and expenditures expressed as percentages of taxable payroll. As presently constructed, the program receives most of its income from the 6.2 percent payroll tax that employees and employers each pay on taxable wages and salaries (for a combined payroll tax rate of 12.4 percent of taxable payroll), and the 12.4 percent that is paid on taxable self-employment income. Because estimated annual income excluding interest consists primarily of payroll taxes, when expressed as a percentage of taxable payroll, it is close in magnitude to the OASDI payroll tax rate. The amount by which the income exceeds the tax rate reflects revenue transferred to the trust funds based on Federal income-taxation of OASDI benefits. When estimated expenditures are compared to income as percentages of taxable payroll, they necessarily reflect a similar pattern as when compared in nominal dollars. Whether expressed as percentages of taxable payroll or in nominal dollars, prior to 2016, estimated annual expenditures are less than estimated annual income, excluding interest, whereas in 2016 and thereafter expenditures are more.

The statement of social insurance on page 58 shows that the present value of the excess of income (excluding interest) over expenditures for the 75-year period is -\$4,207 billion. If augmented by the trust fund assets at the start of the period (January 1, 2001), it is -\$3,157 billion. This excess does not equate to the actuarial balance in the Trustees' Report. To reconcile these values, it should be considered that the excess (including the starting trust fund assets) would need to take into account the cost of attaining a target trust fund balance by the end of the period. The present value of this cost is \$237 billion, which reduces the excess to -\$3,394 billion. This reduced (more negative) excess, when expressed as a percent of taxable payroll, is defined by the Trustees in their annual reports to be the actuarial balance. Thus, the excess of -\$3,394 billion equates to the actuarial balance of -1.86 percent of taxable payroll reported in the 2001 Trustees' Report.

One interpretation of this negative actuarial balance (-1.86 percent of the taxable payroll) is that it represents the magnitude of the increase in the combined payroll tax rate for the 75-year period that would result in an actuarial balance of zero. The combined payroll tax rate is 12.4 percent today and is currently scheduled to remain at that level. An increase of 1.86 percentage points in this rate in each year of the 75-year projection period—about 0.93 percentage points for employees and employers each, resulting in a total rate for each of 7.13 percent—is estimated to produce enough income to pay all benefits due under current law for that period. Equivalent benefit reductions, or combinations of both tax increases and benefit reductions, could be made to achieve the same effect. Any accumulation and subsequent redemption of substantial trust fund assets may have economic and public policy implications that go beyond the operation of the OASDI program itself. Discussion of these broader issues is not within the scope of this report.

Chart 2—Estimated OASDI Income (Excluding Interest) and Expenditures as a Percentage of Taxable Payroll 1960-2075

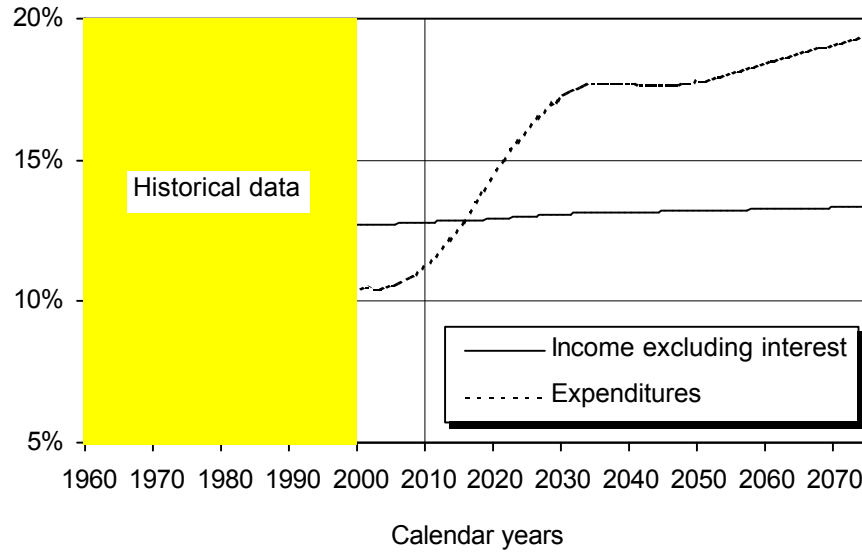
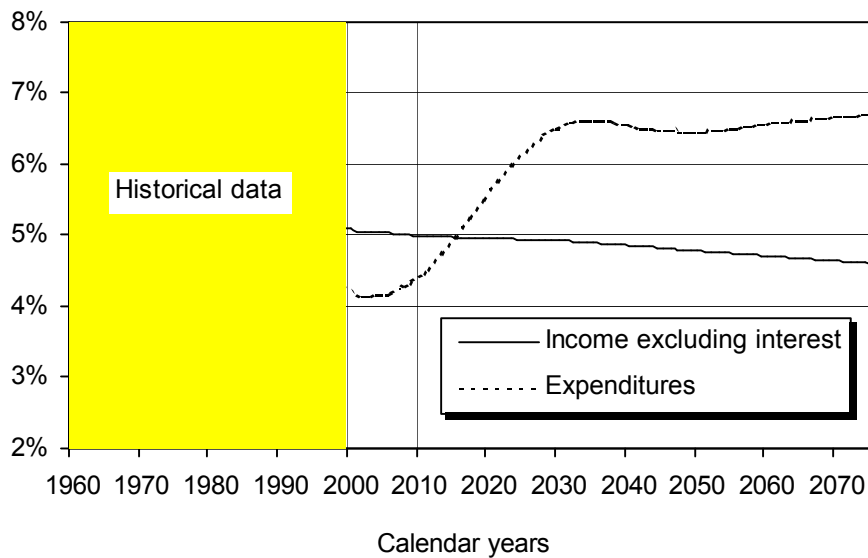


Chart 3 shows estimated annual income, excluding interest, and expenditures, expressed as percentages of GDP. Analyzing these cashflows in terms of percentage of the GDP, which represents the total value of goods and services produced in the United States, provides a measure of the size of the OASDI program in relation to the capacity of the national economy to sustain it.

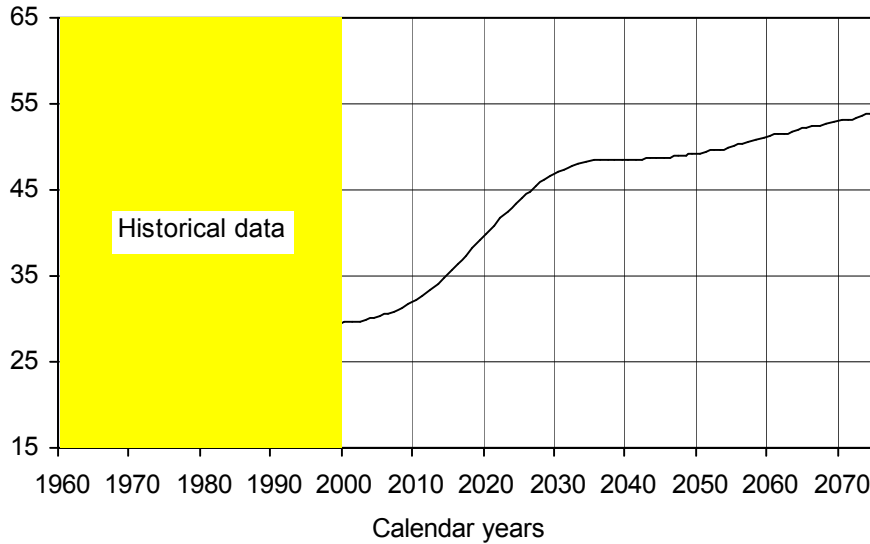
Chart 3—Estimated OASDI Income (Excluding Interest) and Expenditures as a Percentage of GDP 1960-2075



As shown in Chart 4, there were about 30 OASDI beneficiaries for every 100 covered workers in 2000. As indicated, this ratio is expected to increase substantially in the future. The most rapid increase will occur as the relatively large number of persons born during the baby boom (from the end of World War II through the mid-1960s) reaches retirement age and begins to receive benefits. At the same time, the relatively small number of persons born during the subsequent period of low fertility rates will comprise the labor force. Between 2030 and 2050, the number of workers per beneficiary is estimated to remain relatively stable as the baby-boom generation diminishes in size. After 2050, this ratio is expected to continue to increase at a slower pace, reflecting the

increasing numbers of beneficiaries due to projected increases in life expectancy. Under the intermediate assumption, by the end of the 75-year projection period, the number of OASDI beneficiaries per 100 covered workers is projected to increase to 54.

**Chart 4—Number of OASDI Beneficiaries per 100 Covered Workers
1960-2075**



Actuarial Assumptions and Sensitivity Analysis

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 that is receiving benefits, the level of monthly benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers’ earnings. 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 factors.

While it is reasonable to assume that actual trust fund experience will fall within the range defined by the three alternative sets of assumptions used in the Trustees’ report, no definite assurance can be given that this will occur because of the uncertainty inherent in projections of this type and length. In general, a greater degree of confidence can be placed in the assumptions and estimates 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 potential range of future program experience.

The assumptions fluctuate in the earlier years of the projection period before reaching their ultimate values for the remainder of the 75-year projection period. The following table summarizes the ultimate values assumed for the key economic and demographic factors underlying the actuarial estimates shown in this report.

The estimates used in this presentation are based on the assumption that the programs will continue as presently constructed. They are also based on various economic and demographic assumptions, including those in the following table:

Social Security Intermediate Assumptions

Year	Total Fertility Rate ¹	Age-Sex-Adjusted Death Rate ² (per 100,000)	Period Life Expectancy at Birth ³		Net Annual Immigration (Persons per Year)	Real-Wage Differential ⁴ (Percentage Points)	Average Annual Percentage Change In:			
			Male	Female			Average Annual Wage in Covered Employment	CPI ⁵	Real GDP ⁶	Average Annual Interest Rate ⁷
2001	2.06	796.5	74.0	79.6	840,000	1.9	4.9	3.0	3.1	5.6%
2005	2.04	773.7	74.6	80.0	900,000	1.2	4.4	3.2	2.3	6.2%
2010	2.02	751.1	75.3	80.3	900,000	1.0	4.3	3.3	2.0	6.3%
2020	1.97	701.7	76.4	81.1	900,000	1.0	4.3	3.3	1.7	6.3%
2030	1.95	649.4	77.3	81.9	900,000	1.0	4.3	3.3	1.7	6.3%
2040	1.95	603.3	78.2	82.6	900,000	1.0	4.3	3.3	1.7	6.3%
2050	1.95	562.6	79.0	83.3	900,000	1.0	4.3	3.3	1.6	6.3%
2060	1.95	526.6	79.8	84.0	900,000	1.0	4.3	3.3	1.6	6.3%
2070	1.95	494.5	80.5	84.7	900,000	1.0	4.3	3.3	1.6	6.3%

¹The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The ultimate total fertility rate is assumed to be reached in 2025.

²The age-sex-adjusted death rate is the crude rate that would occur in the enumerated total population as of April 1, 1990, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

³The period life expectancy for a group of persons born in a given year is the average that would be attained by such persons if the group were to experience in succeeding years the death rates by age observed in, or assumed for, the given year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

⁴The real-wage differential is the difference between the percentage increases, before rounding, in the average annual wage in covered employment, and the average annual CPI.

⁵The CPI is the annual average value for the calendar year of the CPI for Urban Wage Earners and Clerical Workers (CPI-W).

⁶The real GDP is the value of total output of goods and services, expressed in 1996 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

⁷The average annual interest rate is the average of the nominal interest rates, which, in practice, are compounded semiannually, for special-issue Treasury obligations sold only to the trust funds in each of the 12 months of the year.

Present value amounts attempt to demonstrate what future cashflow amounts would be if shown in interest discounted dollars. This is done by discounting, or removing, the increase in these cashflows that is caused by interest. Even small changes in the estimated amount of future interest over the next 75 years have dramatic impact on present value calculations. Given the cashflow estimates between the high and low interest-rate assumptions, the present value of OASDI expenditures over income ranges from \$6,125 billion to \$3,025 billion using ultimate annual real interest rates of 2.2 percent to 3.7 percent, respectively, compared to \$4,207 billion using the intermediate ultimate annual real interest rate of 3.0 percent. These interest rate assumptions do not influence the future cashflow in the OASDI program. If these charts were presented in nominal dollars, they would reflect a pattern similar to the present value charts shown here.

Charts of cashflows with varying assumptions that have not been adjusted for interest, as well as other assumptions that are not expected to have a material impact on OASDI, can be found in Social Security's Performance and Accountability Report and on the web at www.ssa.gov/finance.

These assumptions and the other values on which these displays are based reflect the intermediate assumptions of the 2001 Trustees' Report. Estimates made in certain prior years have changed substantially because of revisions to the assumptions based on changed conditions or experience, and to changes in actuarial methodology. It is reasonable to expect more changes for similar reasons in future reports.

Death Rates

The assumptions regarding future death rates have a substantial impact on estimated future cashflows in the OASDI program. The following table shows the present values of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about future reductions in death rates. The analysis was developed by varying the percentage decrease assumed to occur during 2000-2075 in death rates by age, sex, and cause of death. The decreases assumed for this period, summarized as average annual reductions in the age-sex-adjusted death rate, are 0.26, 0.68, and 1.23 percent per year, where 0.68 percent is the intermediate assumption in the 2001 Trustees' Report. (The resulting cumulative decreases in the age-sex-adjusted death rate during the same period are 17, 40 and 60 percent, respectively.) These assumptions do not apply uniformly to all ages. Some variation by age was assumed in recognition of historical patterns and to ensure that, in terms of the financial status of the OASDI program, estimates based on the summarized 0.26 percent and 1.23 percent reduction assumptions would be more optimistic and more pessimistic, respectively, than those based on the intermediate assumption.

As the following table demonstrates, if the reduction in death rate is changed from 0.68 percent, the Trustees' intermediate assumption, to 0.26 percent, meaning that people die younger, then the shortfall for the period of estimated OASDI income relative to expenditures would decrease to \$2,980 billion from \$4,207 billion; if the reduction is changed to 1.23 percent, meaning that people live longer, then the shortfall would increase to \$5,574 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Death Rate Assumptions Valuation Period: 2001-2075			
Average Annual Reduction in Death Rates	0.26%	0.68%	1.23%
Expenditures in excess of income (In billions of present-value dollars)	\$2,980	\$4,207	\$5,574

Real-Wage Differential

The following table shows the present value of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about the ultimate real-wage differential. These assumptions are that the ultimate real-wage differential will be 0.5, 1.0, and 1.5 percentage points, where 1.0 percentage point is the intermediate assumption in the 2001 Trustees' Report. The real-wage differential is the difference between the percentage increases in (1) the average annual wage in OASDI covered employment and (2) the average annual CPI. In each case, the ultimate annual increase in the CPI is assumed to be 3.3 percent (as used in the intermediate assumptions), yielding ultimate percentage increases in the average annual wage in covered employment of 3.8, 4.3, and 4.8 percent, respectively.

As the following table demonstrates, if the ultimate real-wage differential is changed from 1.0 percentage point, the Trustees' intermediate assumption, to 0.5 percentage point, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to \$4,660 billion from \$4,207 billion; if the ultimate real-wage differential was changed from 1.0 to 1.5 percentage points, then the shortfall would decrease to \$3,559 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate Real-Wage Assumptions Valuation Period: 2001-2075			
Ultimate percentage change in wages, CPI	3.8% - 3.3%	4.3% - 3.3%	4.8% - 3.3%
Expenditures in excess of income (In billions of present-value dollars)	\$4,660	\$4,207	\$3,559

Differences among the estimates of annual net cashflow based on the three assumptions about the ultimate real-wage differential become apparent early in the projection period. Higher real-wage differentials increase both wages and initial benefit levels. Because the effects on wages and, therefore, on payroll taxes are immediate, while the effects on benefits occur with a substantial lag, annual net cashflow is higher (less negative in later years) for higher assumed real-wage differentials. In the early years, when the effects on benefits are quite small and while the effects on wages are compounding, the patterns of the estimates of annual net cashflow based on the three assumptions diverge fairly rapidly.

Total Fertility Rate

The following table shows the present value of the estimated excess of OASDI expenditures over income for the 75-year period, using various assumptions about the ultimate total fertility rate. These assumptions are 1.7, 1.95, and 2.2 children per woman, where 1.95 is the intermediate assumption in the 2001 Trustees' Report. The total fertility rate is assumed to change gradually from its current level and to reach the selected ultimate value in 2025.

As the following table demonstrates, if the ultimate total fertility rate is changed from 1.95 children per woman, the Trustees' intermediate assumption, to 1.7, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to \$4,636 billion from \$4,207 billion; if the ultimate total fertility rate was changed to 2.2, then the shortfall would decrease to \$3,737 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate Total Fertility Rate Assumptions Valuation Period: 2001-2075			
Ultimate total fertility rate (children per woman)	1.7	1.95	2.2
Expenditures in excess of income (In billions of present-value dollars)	\$4,636	\$4,207	\$3,737

Consumer Price Index

The following table shows the present value of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about the ultimate rate of change in the CPI. These assumptions are that the ultimate annual increase in the CPI will be 2.3, 3.3, and 4.3 percent, where 3.3 percent is the intermediate assumption in the 2001 Trustees' Report. In each case, the ultimate real-wage differential is assumed to be 1.0 percentage point (as used in the intermediate assumptions), yielding ultimate percentage increases in average annual wages in covered employment of 3.3, 4.3, and 5.3 percent, respectively.

As the following table demonstrates, if the ultimate annual increase in the CPI is changed from 3.3 percent, the Trustees' intermediate assumption, to 2.3 percent, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to \$4,537 billion from \$4,207 billion; if the ultimate annual increase in the CPI was changed to 4.3 percent, then the shortfall would decrease to \$3,863 billion. This seemingly counter-intuitive result—that higher CPI increases result in decreased shortfalls, and vice versa—occurs because varying CPI increases while retaining the same annual real-wage differentials affect earnings (and, therefore, taxes) sooner than benefits (and, therefore, expenditures).

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate CPI-Increase Assumptions Valuation Period: 2001-2075			
Ultimate percentage change in wages, CPI	3.3% - 2.3%	4.3% - 3.3%	5.3% - 4.3%
Expenditures in excess of income (In billions of present-value dollars)	\$4,537	\$4,207	\$3,863

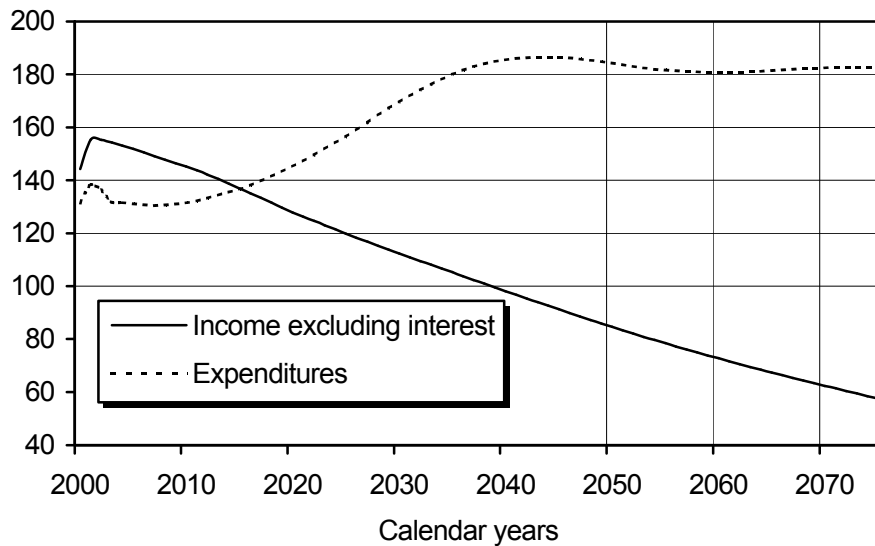
Hospital Insurance Medicare Part A

Federal Hospital Insurance (Medicare Part A) Trust Fund revenue consists primarily of taxes on earnings paid by employees, their employers, and the self-employed. The fund also receives revenue from part of the taxation of Social Security benefits and from interest on its investments in Treasury securities. Revenues not needed to pay current benefits of the Medicare Part A program or administrative expenses are invested in special issue Treasury securities.

The present values of actuarial estimates were computed as of the beginning of the valuation period, January 1, 2001. The contributions consist of the sum of the present value of various program income items expected to be received through fiscal 2075. The expenditure consists of the sum of the present value of estimated payments through fiscal 2075, claims incurred through September 30, 2001 that were unpaid as of that date, and administrative expenses related to those claims. Under intermediate assumptions from the 2001 Trustees' Report, and based on current legislation in place, the fund is projected to be exhausted in calendar year 2029.

Chart 5—Present Value of Estimated Medicare Part A Income (Excluding Interest) and Expenditures 2000-2075

(In billions of dollars)

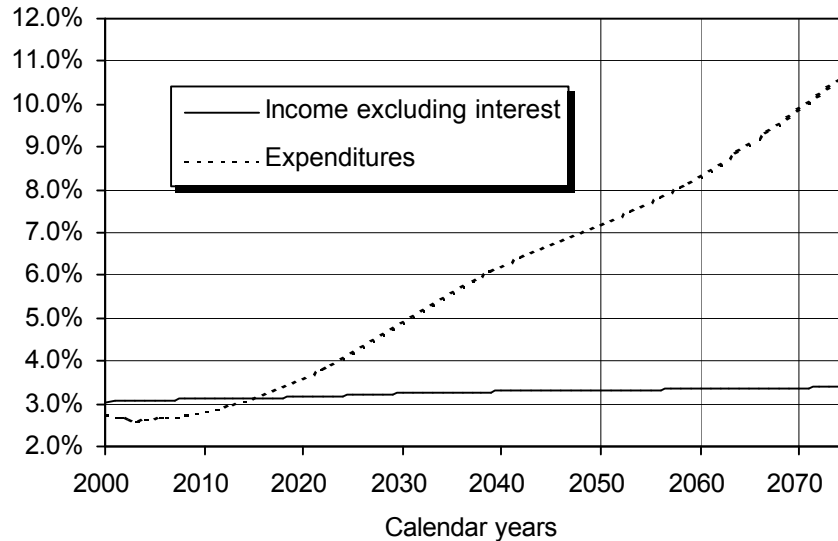


Medicare Part A Cashflow as a Percent of Taxable Payroll

Each year, estimates of the financial and actuarial status of the Medicare Part A program are prepared for the next 75 years. Because of the difficulty in comparing dollar values for different periods without some type of relative scale, income and expenditure amounts are shown relative to the earnings in covered employment that are taxable under the Medicare Part A program (referred to as “taxable payroll”).

Chart 6 illustrates income excluding interest and expenditures as a percent of taxable payroll over the next 75 years. Although the long-range financial outlook for the Medicare Part A program has improved substantially in recent years because of the Balanced Budget Act of 1997, favorable economic conditions, and efforts to curb fraud and abuse, the program remains seriously underfunded through 2075. This is due in part to health care cost increases that exceed wage growth; a more significant cause, however, is the impending retirement of those born during the 1945-1965 baby boom.

Chart 6—Estimated Medicare Part A Income (Excluding Interest) and Expenditures as a Percentage of Taxable Payroll 2000-2075

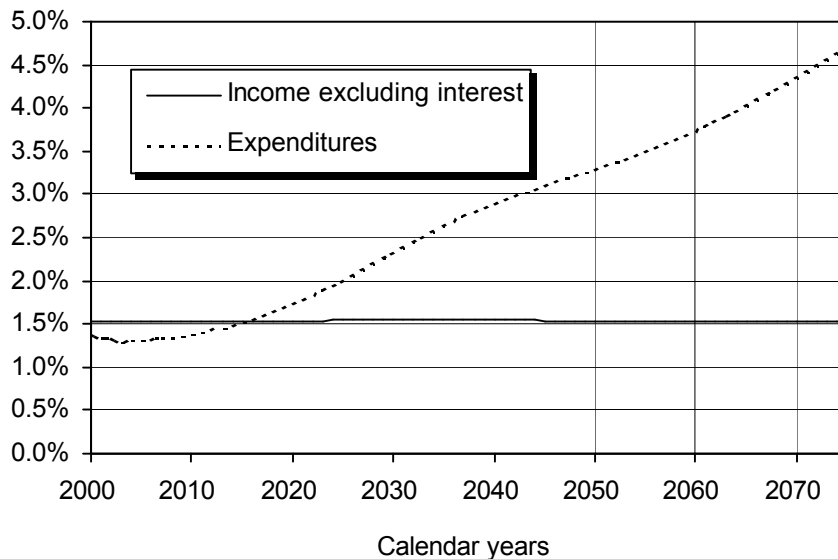


Medicare Part A Cashflow as a Percent of Gross Domestic Product (GDP)

Expressing Medicare-incurred disbursements as a percentage of GDP gives a relative measure of the size of the Medicare program compared to the general economy. GDP represents the total value of goods and services produced in the United States. This measure provides an idea of the relative financial resources that will be necessary to pay for Medicare services.

Chart 7 shows income excluding interest and expenditures for the Medicare Part A program over the next 75 years expressed as a percentage of GDP. In 2000, the expenditures were \$131.1 billion, which was 1.32 percent of GDP. This percentage increases steadily throughout the entire 75-year period.

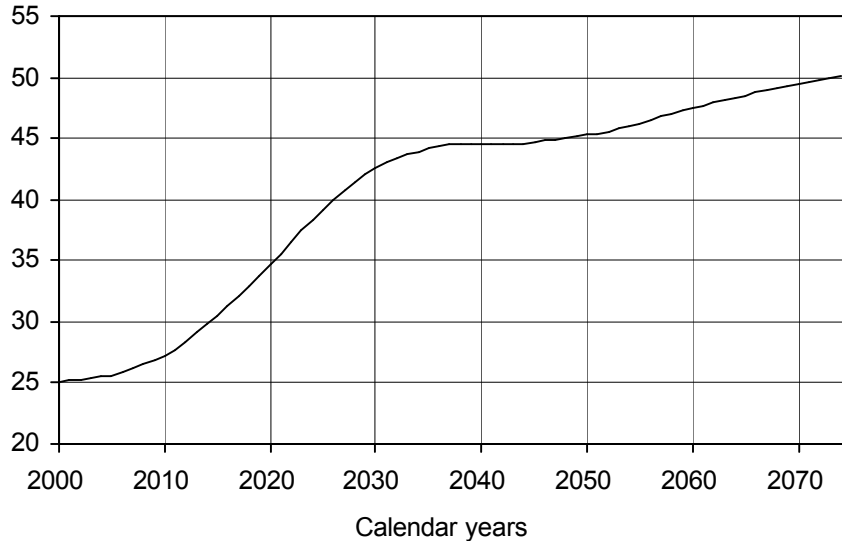
Chart 7—Estimated Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 2000-2075



Worker-to-Beneficiary Ratio

Another way to evaluate the long-range outlook of the Medicare Part A program is to examine the projected number of Medicare Part A beneficiaries per 100 covered workers. Chart 8 illustrates this ratio over the next 75 years. For the most part, current benefits are paid for by current workers. The retirement of the baby boom generation will therefore be financed by the relatively smaller number of persons born after the baby boom. In 2000, a group of 100 workers provided benefits for 25 beneficiaries. In 2030, however, after the last baby boomer turns 65, a group of 100 workers will provide benefits to 43 beneficiaries. The projected ratio continues to increase until there will be 50 beneficiaries per 100 workers in 2075.

**Chart 8—Number of Medicare Part A Beneficiaries per 100 Covered Workers
2000-2075**



Actuarial Assumptions and Sensitivity Analysis

In order to make projections regarding the future financial status of the Medicare Part A and Medicare Part B programs, various assumptions have to be made. First and foremost, the estimates presented here are based on the assumption that the programs will continue under present law. In addition, the estimates depend on many economic and demographic assumptions, including changes in wages and the CPI, fertility rates, immigration rates, and interest rates. In most cases, these assumptions vary from year to year during the first 5 to 30 years before reaching their ultimate values for the remainder of the 75-year projection period.

The following chart and amounts are presented for analysis of the major assumptions impacting estimates in Medicare’s future cashflows. Present value amounts attempt to demonstrate what future cashflow amounts would be if shown in today’s dollars. This is done by discounting, or removing, the increase in these cashflows that is caused by interest, sometimes referred to as inflation. Even small changes in the estimated amount of future interest over the next 75 years have dramatic impact on present value calculations. Given the cashflow assumptions between the highest and lowest expected interest assumptions, the present value of Medicare Part A expenditures over income ranges from \$7,003 billion to \$3,372 billion using interest rates of 2.2 percent to 3.7 percent, respectively.

Charts of cashflows with varying assumptions that have not been adjusted for interest, as well as other assumptions that are not expected to have a material impact on Medicare, can be found in the Centers for Medicare & Medicaid Services’ (CMS) Performance and Accountability Report and on the web at www.cms.gov.

The following table shows some of the underlying assumptions used in the projections of Medicare spending displayed in this report. Further details on these assumptions are available in the OASDI, Medicare Part A, and Medicare Part B Trustees’ Reports for 2001.

Medicare Intermediate Assumptions

Year	Fertility Rate ¹	Net Immigration	Real Wage Differential ²	Annual Percentage Change in:			Real Interest Rate ³
				Wages	CPI	Real GDP	
2001	2.05	900,000	1.9	4.9	3.0	3.1	2.6
2005	2.04	900,000	1.2	4.4	3.2	2.3	2.9
2010	2.02	900,000	1.0	4.3	3.3	2.0	3.0
2020	1.97	900,000	1.0	4.3	3.3	1.7	3.0
2030	1.95	900,000	1.0	4.3	3.3	1.7	3.0
2040	1.95	900,000	1.0	4.3	3.3	1.7	3.0
2050	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2060	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2070	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2075	1.95	900,000	1.0	4.3	3.3	1.6	3.0

¹ Average number of children per woman.

² Difference between percentage increase in wages and the CPI.

³ Average rate of interest earned on new trust fund securities, above and beyond rate of inflation.

Estimates made in prior years have changed substantially sometimes because of revisions to the assumptions, which are due either to changed conditions or to more recent experience. Furthermore, it is important to recognize that actual conditions are very likely to differ from the projections presented here, since the future cannot be anticipated with certainty. In order to illustrate the magnitude of the sensitivity of the long-range projections, three of the key assumptions were varied individually to determine the impact on the Medicare Part A actuarial present values and net cashflow. The assumptions varied were health care cost factors, the fertility rate, and real-wage differential.

The sensitivity of the projected Medicare Part A net cashflow to variations in future mortality rates is also of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per-beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Medicare Part A mortality sensitivity. CMS is sponsoring a current research effort that is expected to provide the information necessary to produce such estimates.

For this analysis, the intermediate economic and demographic assumptions in the *2001 Annual Report of the Board of Trustees of the Federal Hospital Insurance Trust Fund* are used as the reference point. Each selected assumption is varied individually to produce three scenarios. All present values are calculated as of January 1, 2001, and are based on estimates of income and expenditures during the 75-year projection period.

Health Care Costs

The following table shows the net present value of cashflow during the 75-year projection period under three alternative assumptions of the annual growth rate in the aggregate cost of providing covered health care services to beneficiaries. These assumptions are that the ultimate annual growth rate in such costs, relative to taxable payroll, will be 1 percent slower than the intermediate assumptions, the same as the intermediate assumptions, and 1 percent faster than the intermediate assumptions. In each case, the taxable payroll will be the same as that which was assumed for the intermediate assumptions.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Health Care Cost Assumptions			
Annual cost/payroll relative growth rate	-1 percentage point	Intermediate assumptions	+1 percentage point
Expenditures in excess of income (In billions of present-value dollars)	\$811	\$4,730	\$11,155

Under the low cost assumption, the annual absolute change in aggregate cost is equal to the intermediate assumption less 1 percent of the contemporaneous increase in taxable payroll. The above table demonstrates that if the ultimate growth rate assumption is 1 percentage point lower than the intermediate assumptions, the deficit of income over expenditures decreases from \$4,730 to \$811. Under the high cost assumption, the annual absolute change in aggregate cost is equal to the intermediate assumption plus 1 percent of the contemporaneous increase in taxable payroll. If the ultimate growth rate assumption is 1 percentage point higher than the intermediate assumptions, the deficit increases substantially to \$11,155 billion.

Fertility Rate

The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The table below shows the net present value of cashflow during the 75-year projection period under three alternative ultimate fertility rate assumptions: 1.7, 1.95, and 2.2 children per woman.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Fertility Rate Assumptions			
Ultimate fertility rate	1.7	1.95	2.2
Expenditures in excess of income (In billions of present-value dollars)	\$4,878	\$4,730	\$4,569

The table above demonstrates that if the assumed ultimate fertility rate is decreased from 1.95 to 1.7, the projected deficit of income over expenditures increases from \$4,730 billion to \$4,878 billion. On the other hand, if the ultimate fertility rate is increased from 1.95 to 2.2 children per woman, the deficit decreases to \$4,569 billion.

Real-Wage Differential

The following table shows the net present value of cashflow during the 75-year projection period under three alternative ultimate real-wage differential assumptions: 0.5, 1.0, and 1.5 percentage points. In each case, the CPI is assumed to be 3.3 percent, yielding ultimate percentage increases in average annual wages in covered employment of 3.8, 4.3, and 4.8 percent, respectively.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Real-Wage Assumptions			
Ultimate percentage increase in wages – CPI	3.8% - 3.3%	4.3% - 3.3%	4.8% - 3.3%
Ultimate percentage increase in real-wage differential	0.5%	1.0%	1.5%
Expenditures in excess of income (In billions of present-value dollars)	\$4,988	\$4,730	\$4,539

The above table demonstrates that if the ultimate real-wage differential assumption is decreased from 1.0 percentage point to 0.5 percentage point, the deficit of income over expenditures increases from \$4,730 billion to \$4,988 billion. On the other hand, if the ultimate real-wage differential assumption is increased from 1.0 percentage point to 1.5 percentage points, the deficit decreases to \$4,539 billion.

Federal Supplementary Medical Insurance Medicare Part B

The Medicare Part B program differs fundamentally from the Medicare Part A program by the way it is financed. In particular, Medicare Part B financing is not based on payroll taxes; instead, it is based on monthly premiums and income from the general fund of the U.S. Treasury. General fund transfers account for approximately 75 percent of the Medicare Part B Trust Fund's income.

Since the income to the Medicare Part B Trust Fund from beneficiary premiums and the general fund is adjusted annually to match expected costs, the trust fund is always in actuarial balance. By law, Medicare Part B income and expenditures will continue to be virtually the same. However, as shown in the trust fund illustration on page 61, transfers from the general fund of the U.S. Treasury draw from the same resources as any other social insurance program that is experiencing a negative cashflow. Moreover, the general fund transfers occur from one account of the Government to another and do not represent an external, earmarked source of tax or other revenue. Therefore, for the purposes of this report, with the objective of presenting the financial operations of these programs from a Governmentwide consolidated perspective, transfers from the general fund of the Treasury are excluded. This is the same reason that interest earned on Treasury securities is eliminated for this and all other social insurance programs—again, because such payments represent intragovernmental transfers.

The elimination of this major revenue source to the Medicare Part B Trust Fund produces information that appears to be significantly different from that presented in CMS's Annual Performance and Accountability Report, as well as the annual Trustees' Report on the Medicare Part B Trust Fund. From the perspective of the financial status of the Medicare Part B Trust Fund (as shown in the CMS financial statement and the Trustees' report), it is appropriate to consider all sources of income to the fund. Thus, the accounting treatment of Medicare Part B general revenues (and trust fund interest earnings) varies appropriately depending on whether an overall consolidated or trust fund perspective is shown.

Chart 9 shows the actuarial estimates of Medicare Part B premiums and disbursements for each of the next 75 years, in nominal dollars. Income includes monthly premiums paid by, or on behalf of, beneficiaries. Disbursements include benefit payments as well as administrative expenses.

Estimated Medicare Part B Premiums and Expenditures

**Chart 9—Medicare Part B Income, Premiums, and Expenditures
2000-2075**

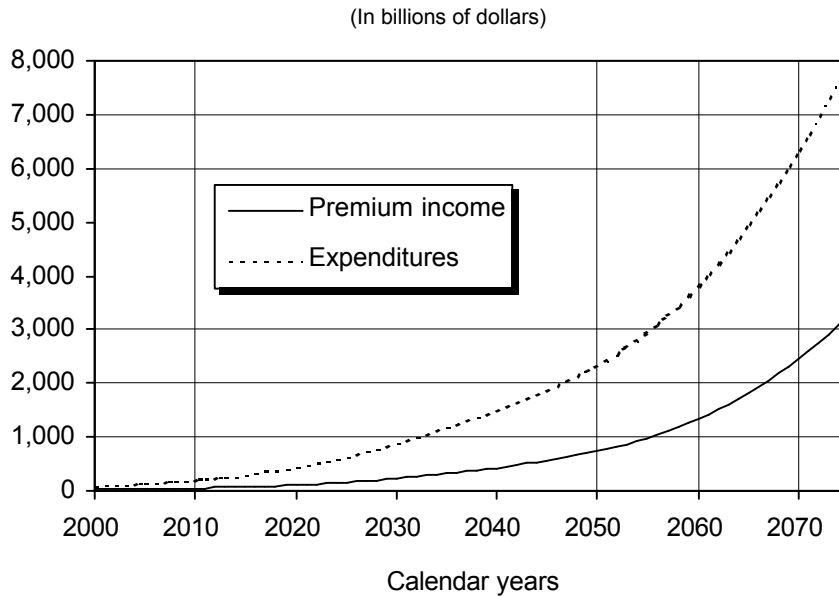
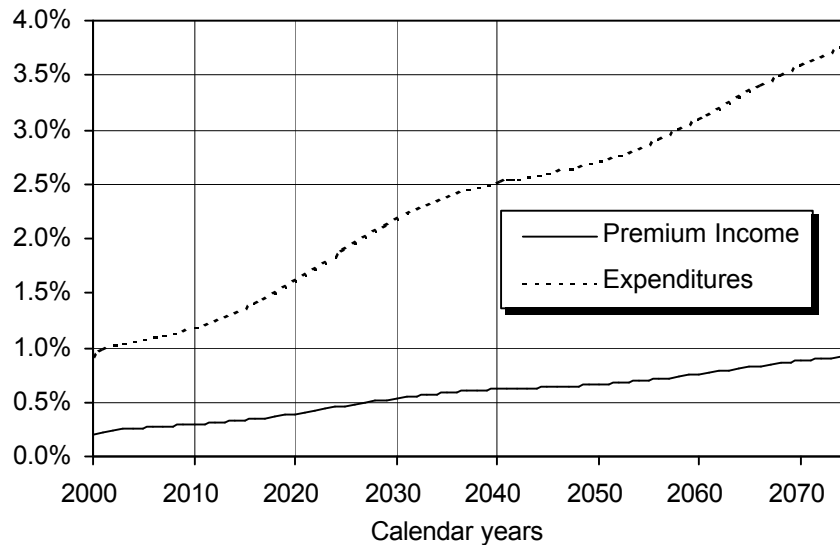


Chart 10 shows expenditures for the Medicare Part B program over the next 75 years expressed as a percentage of GDP. In 1999, Medicare Part B expenditures were \$90.7 billion, which was 0.92 percent of GDP. This percentage is projected to increase steadily through 2035, reflecting growth in the price, use, and intensity of Medicare Part B services that is expected to exceed GDP growth for many years, together with the effects of the baby boom retirement. After 2035, it levels off because Medicare Part B projections by assumption are tied directly to GDP plus 1 percentage point, and because relatively fewer number of persons born after the baby boom will be eligible for Medicare Part B benefits. Medicare Part B premium increases during the initial 25-year period are assumed to decline gradually in the last 12 years to the same rate as GDP per capita plus 1 percentage point and then to continue at the same rate as GDP per capita plus one percentage point in the last 50 years.

**Chart 10—Estimated Medicare Part B Premiums and Expenditures
as a Percent of GDP
2000-2075**



Estimated Medicare Part B Premiums and Expenditures

The Medicare Part B program's actuarial assumptions are the same as those used in Medicare Part A, presented on pages 71-72. Since the unique funding mechanism of Medicare Part B allows its trust fund to remain in actuarial balance, the data on various sensitivity analyses are not routinely compiled. It is planned that future editions of the *Financial Report* will regularly contain this information.

Railroad Retirement

Railroad retirement pays full annuities when eligible persons reach full retirement age with 10 years of service or age 62 with 30 years of service. It pays reduced annuities to eligible beneficiaries who are age 62 with 10 to 29 years of service, or age 60 with 30 years of service (See subsequent event, last paragraph). The Railroad Retirement program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as Social Security beneficiaries.

The Railroad Retirement Board (RRB) and Social Security Administration (SSA) share jurisdiction over the payment of retirement and survivor benefits. RRB has jurisdiction over the payment of retirement benefits if the employee had at least 10 years of railroad service. Additionally, for survivor benefits, RRB requires that the employee's last regular employment before retirement or death was in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee's railroad retirement credits to SSA. SSA treats them as Social Security credits.

Payroll taxes paid by railroad employers and their employees provide the primary source of income for the Railroad Retirement Survivor Benefit program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

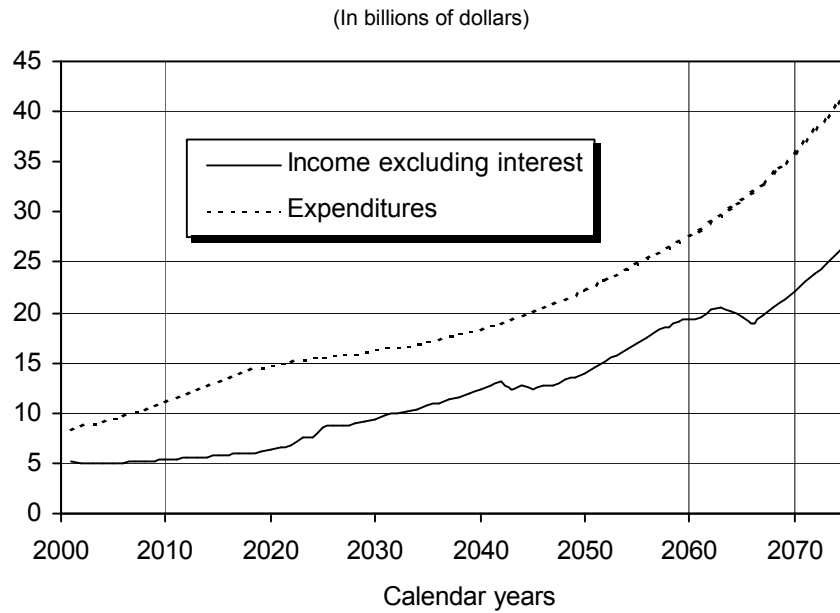
Other sources of program income include: financial interchanges with the Social Security trust funds; interest on investments; Federal income taxes on railroad retirement benefits; and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits).

Subsequent event: On December 21, 2001, President Bush signed the "The Railroad Retirement and Survivors' Improvement Act of 2001" (RRSIA) into law. The new law enhances benefits and changes the funding of the retirement program.

Benefits of the RRSIA of 2001 include:

- Increases the widow(er)s benefits by providing a guaranteed minimum amount of benefits.
- Restores full annuities to employees and their spouses who retire at age 60, instead of 62, with 30 years of railroad service.
- The vesting period is also reduced from 10 to 5 years.
- Creates a new National Railroad Retirement Investment Trust (Trust) to administer a new Railroad Retirement Investment Trust Fund (RRIT Fund).
- A new nongovernmental financial institution (“Disbursing Agent”) will serve as a disbursing agent for all benefits payable under the Railroad Retirement Act.

Chart 11—Estimated Railroad Retirement Income (Excluding Interest) and Expenditures 2000–2075



Railroad Retirement Program Actuarial Surplus or (Deficiency) ^{1,2} Under Employment Assumption 2 75-Year Projection as of January 1, 2001

(In billions of present-value dollars)

Estimated future income ³ received from or on behalf of:

Former employees and dependents.....	56.7
Current employees and dependents.....	57.0
Future employees and dependents.....	28.6
All participants.....	<u>142.3</u>

Estimated future expenditures: ⁴

Former employees and dependents.....	80.6
Current employees and dependents.....	67.3
Future employees and dependents.....	12.9
All participants.....	<u>160.8</u>

Estimated future excess of income over expenditures..... (18.5)

¹ Represents combined values for the Railroad Retirement Account, Social Security Equivalent Benefit Account and Railroad Retirement Supplemental Account.

² The data used reflect the provisions of the Railroad Retirement and Survivors' Improvement Act (RRSIA) of 2001. Comparable data for prior years is not available and would not be meaningful.

³ Future income includes tier I taxes, tier II taxes, supplemental annuity taxes, income taxes on benefits, financial interchange income, advances from general revenues and repayments of advances from general revenues. The calculations assume that all future transfers required by current law under the financial interchange will be met.

⁴ Future expenditures include benefit and administrative costs.

Note: Detail may not add to totals due to rounding. Employee and beneficiary status are determined as of 1/1/2000, whereas present values are as of 1/1/2001.

Estimated Expenditures in Excess of Income with Intermediate Employment Assumption Valuation Period 2001-2075

Average yearly employment at end of valuation period	111,000
Expenditures in excess of income (In billions of nominal dollars)	18.5

The average railroad employment is assumed to be 246,000 in 2000. The employment assumption, which is based on a model developed by the Association of American Railroads, assumes that (1) passenger employment will remain at the level of 46,000, and (2) the employment base, excluding passenger employment, will decline at a constant 3.0 percent annual rate for 25 years, at a reducing rate over the next 25 years, and remain level thereafter.

Black Lung (Part C)

The Black Lung Disability program compensates eligible coal miners who are disabled because of employment-related pneumoconiosis (black lung disease). The program provides both medical and survivor benefits. Under Part C, the Black Lung Disability Trust Fund (BLDTF) provides benefit payments to eligible

disabled miners when no responsible mine operator can be assigned the liability. The Department of Labor (DOL) administers Part C of the Black Lung Disability Benefits program.

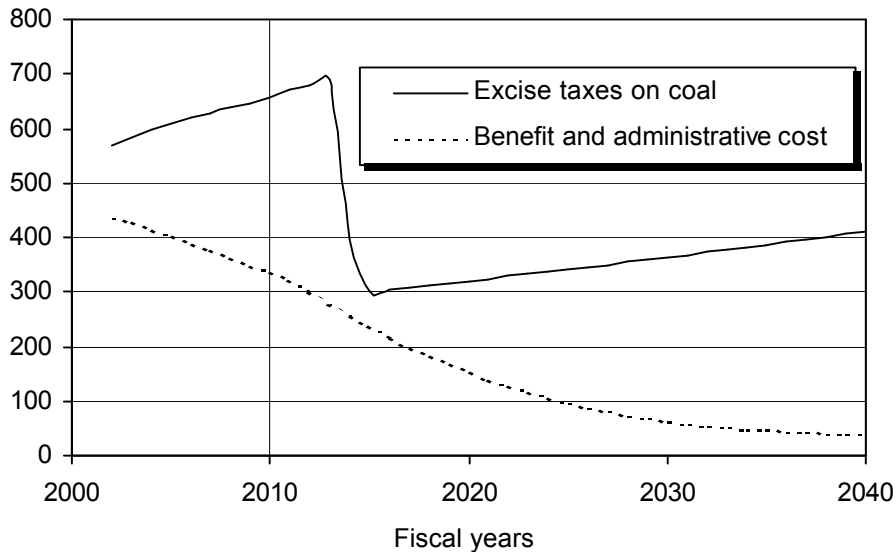
Excise taxes on coal mine operators, based on the sale of coal, partially fund the black lung disability payments and the related administrative and interest costs. Intragovernmental advances to the BLDTF, which must be repaid with interest, fund the shortfall.

Under current conditions, analysts project that scheduled reduction in taxes on coal sales will decrease cash inflows for the year 2014 and beyond. Between the years 2013 and 2015, projections estimate a 54 percent decrease in excise tax collections. By the year 2040, the rate reduction is expected to decrease cash inflows by a total of more than \$12.9 billion.

Chart 12 shows the estimated Black Lung expenditures (excluding interest payments) and excise tax collections for the period 2002 through 2040. Under the intermediate assumptions for the next 39 years, the Black Lung Trust Fund will collect \$17.2 billion in excise taxes on coal and pay \$7.3 billion for benefits and administrative costs. However, this favorable cashflow will not be sufficient to repay the intragovernmental debt that resulted from previous deficits. Currently this debt is \$7.2 billion. Cumulative net cash outflows including interest payments on the debt are projected to reach \$43.1 billion by the year 2040, increasing the debt to \$50.3 billion on September 30, 2040.

**Chart 12—Estimated Black Lung Expenditures and Excise Tax Collections
2002-2040**

(In millions of dollars)



Unemployment Insurance

The Unemployment Insurance program was created in 1935 to provide temporary, partial wage replacement to unemployed workers who lost their jobs. The program is administered through a unique system of Federal and State partnerships, established in Federal law, but executed through conforming State laws by State officials. The Department of Labor provides broad policy guidance and program direction, while program details such as benefit eligibility, duration and amount of benefits are established through individual State unemployment insurance statutes and administered through State unemployment insurance agencies.

The program is financed through the collection of Federal and State unemployment taxes that are deposited in the Unemployment Trust Fund and reported as Federal tax revenue. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for Federal and State administration of the unemployment insurance program, veterans' employment services, State employment services, and the Federal share of extended unemployment insurance benefits. Federal unemployment

taxes also are used to maintain a loan account within the Unemployment Trust Fund, from which insolvent States may borrow funds to pay benefits.

**Estimated Unemployment Trust Fund Contributions
and Expenditures
September 30, 2002 – September 30, 2011
(Expected Economic Conditions)**

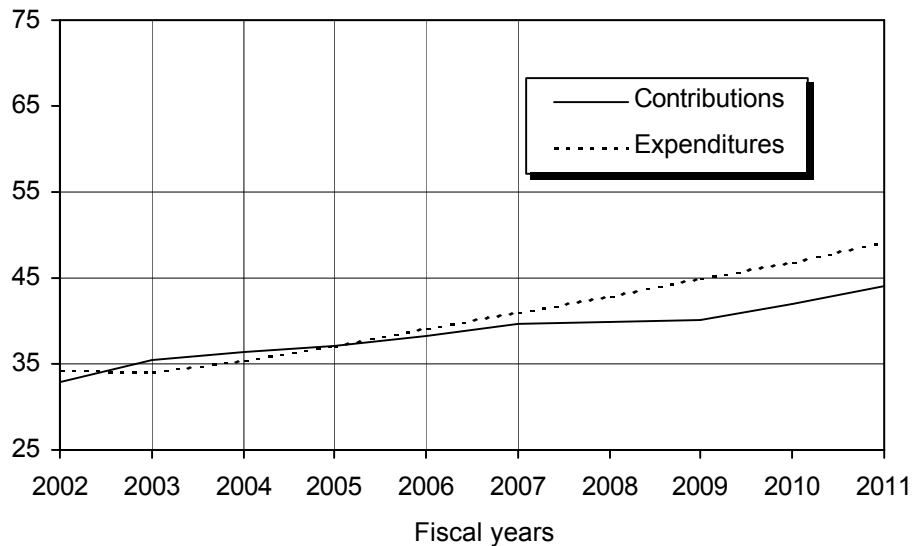
Contributions to September 30, 2011	386.1
Expenditures to September 30, 2011	<u>405.0</u>
Expenditures in excess of contributions (In billions of nominal dollars).....	<u>18.9</u>

Charts 13 through 15 demonstrate the effect on accumulated Unemployment Trust Fund assets of projected total cash inflows and cash outflows over a 10-year period ending September 30, 2011, under expected economic conditions, and mild recessionary and deep recessionary unemployment scenarios. Each scenario uses an open group that includes current and future participants of the Unemployment Insurance programs.

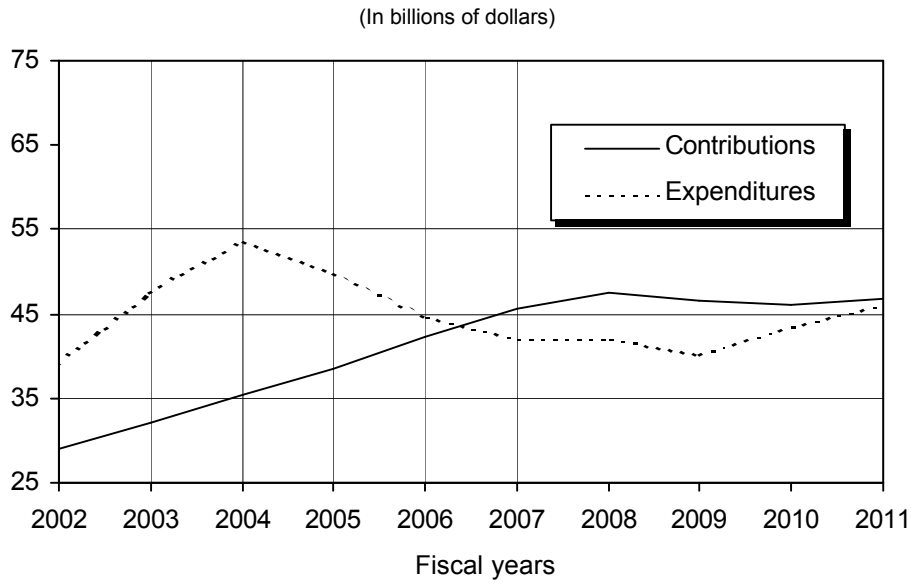
For expected economic conditions, the estimates are based on an expected unemployment rate of 4.78 percent during fiscal 2002, decreasing to 4.60 percent in fiscal 2005 and thereafter. Under the mild recessionary scenario, the expected unemployment rate will peak at 7.43 percent in fiscal 2004, and for the deep recession scenario the expected unemployment rate will rise to 10.15 percent in fiscal 2005.

**Chart 13—Estimated Unemployment Fund Cashflow
Using Expected Economic Conditions
2002-2011**

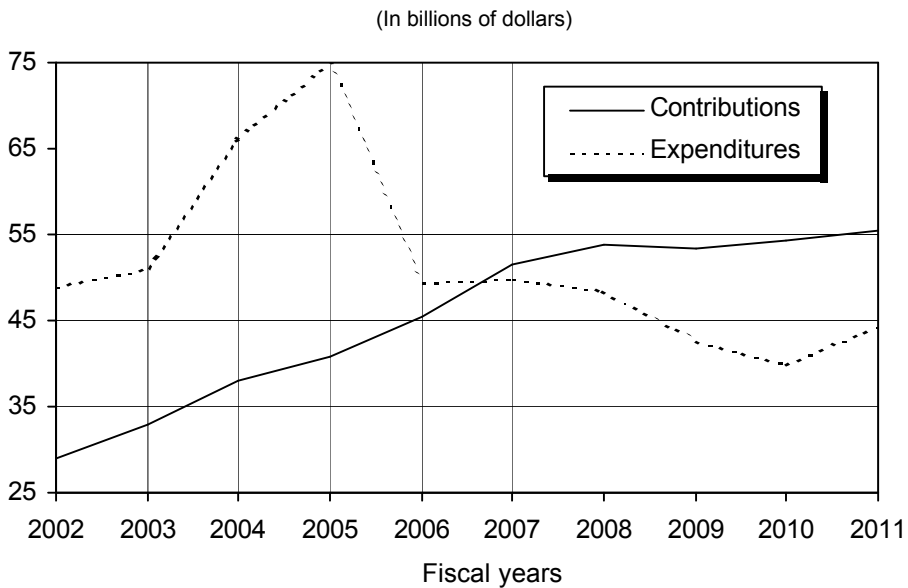
(In billions of dollars)



**Chart 14—Estimated Unemployment Fund Cashflow
Using a Mild Recessionary Unemployment Rate
2002-2011**



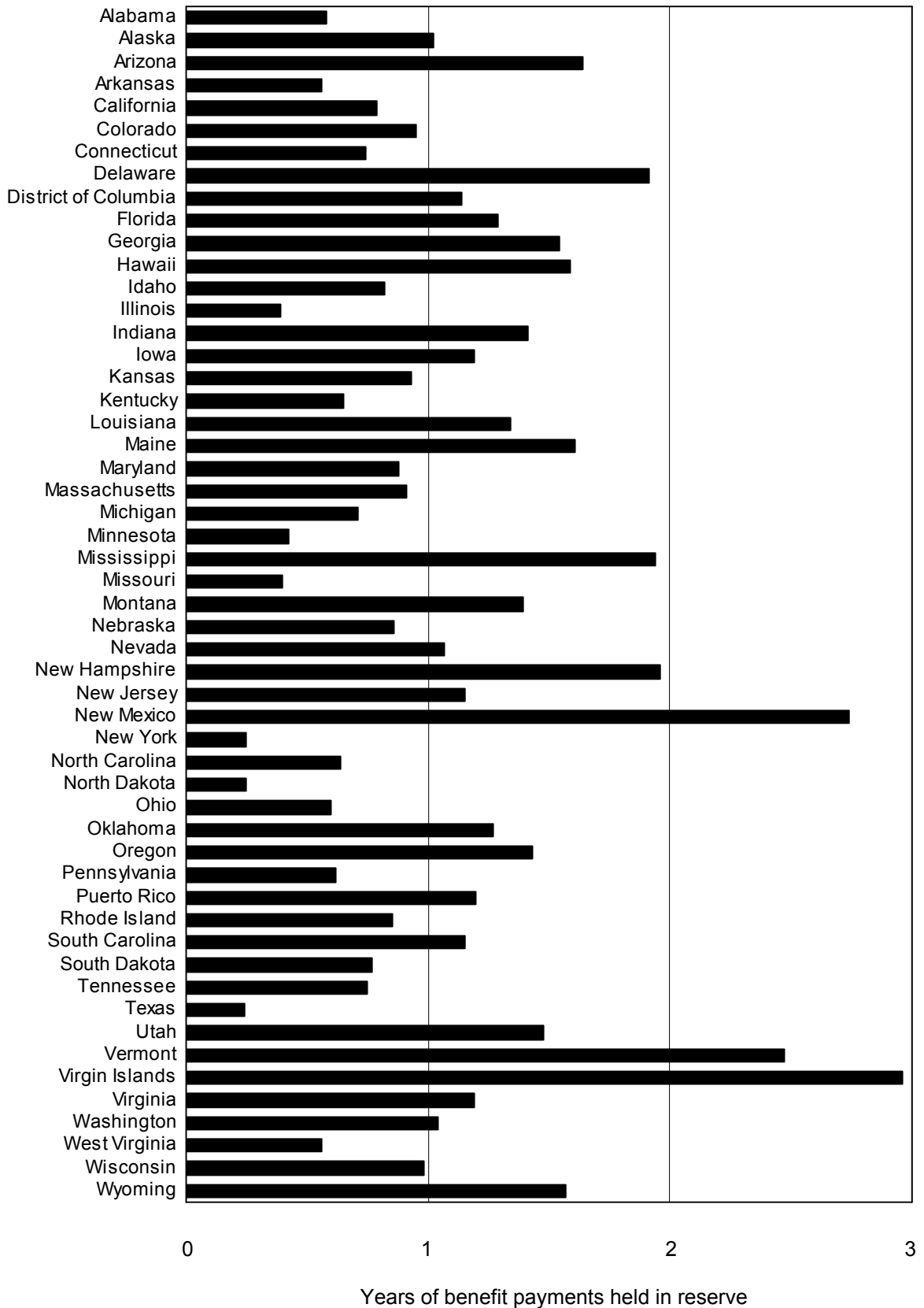
**Chart 15—Estimated Unemployment Fund Cashflow
Using a Deep Recessionary Unemployment Rate
2002-2011**



Unemployment Trust Fund Solvency

Chart 16 shows the adequacy of each State’s accumulated Unemployment Trust Fund assets to provide for future unemployment benefits. To be considered minimally solvent, a State’s reserve balance should provide for one year’s projected benefit payment needs based on the highest level of benefit payments experienced by the State.

Chart 16—Unemployment Trust Fund Solvency



Stewardship Investments

“Stewardship Investments” focus on Government programs aimed at providing long-term benefits by improving the Nation’s productivity and enhancing economic growth. These investments can be provided through direct Federal spending or grants to State and local governments for certain education and training programs, research and development, and federally financed but not federally owned property, such as bridges and roads. When incurred, these investments are included as expenses in determining the net cost of operations.

Stewardship Investments for the Years Ended September 30			
(In billions of dollars)	Fiscal 2001	Restated Fiscal 2000	Restated Fiscal 1999
Investments in non-Federal physical property.....	45.3	44.5	38.4
Investments in human capital	50.8	42.8	46.3
Research and development:			
Investments in basic research	19.9	18.6	17.2
Investments in applied research	18.9	16.7	16.5
Investments in development	40.7	39.0	41.3
Total investments	<u>175.6</u>	<u>161.6</u>	<u>159.7</u>

Non-Federal Physical Property

The Government makes grants and provides funds for the purchase, construction, and/or major renovation of State and local government physical properties. Cost for non-Federal physical property programs are included as expenses in the Statements of Net Cost and are reported as investments in the table above. They are measured on the same accrual basis of accounting used in the *Financial Report* statements.

Human Capital

The Government runs several programs that invest in human capital. Those investments go toward increasing and maintaining a healthy economy by educating and training the general public. Costs do not include training expenses for Federal workers.

Research and Development

Federal investments in research and development comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other future benefits.

- Investments in basic research are for systematic studies to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind.
- Investments in applied research are for systematic studies to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met.

- Investments in development are the systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems, or methods, including the design and development of prototypes and processes.

Current Services Assessment

The Current Services Assessment table shows the Office of Management and Budget's (OMB's) estimate of budget receipts, outlays, and surplus or deficit if no changes were made to laws that are already enacted. Receipts and mandatory outlays, such as Social Security benefits and net interest, involve ongoing activities that generally operate under permanent legal authority authorized by legislation. The current services estimates of receipts and mandatory spending assume that receipts and mandatory spending continue in the future as specified by current laws. The current services estimates for discretionary spending assume discretionary funding for fiscal 2002 equals appropriations enacted by Congress. It also assumes that discretionary funding for subsequent years holds constant in real terms. Because laws already enacted provide the bases for current services estimates, they do not constitute a proposed budget, nor do they predict the most likely budget outcomes.

The current services estimates may be used to help assess the sustainability of programs under current law. That is, they may be used to project whether future resources can sustain public services and meet obligations as they come due. In this way, they can warn of future problems inherent in current law. They also can provide a benchmark against which tax and spending proposals can be compared and the magnitude of proposed changes can be assessed. Moreover, they can provide an analytical perspective of Government by showing the short- and medium-term direction of current programs.

The following schedule presents the actual budget results for fiscal 2002 and the current services estimates for all Federal taxes and spending programs for the subsequent 6 years. It shows receipts by source and outlays by function. The estimates for these years are the same as the current services estimates published in the President's budget for fiscal 2003. They are, therefore, based on the same underlying economic, programmatic, and other technical assumptions as the current services estimates in that document.

Current Services Assessment Receipt and Outlay Estimates as Presented in the President's Budget

(In billions of dollars)	Base Year 2001	Fiscal Year					
		2002	2003	2004	2005	2006	2007
Receipts by Source:							
Individual income taxes.....	994	950	1,009	1,064	1,120	1,167	1,233
Corporation income taxes.....	151	203	208	215	242	248	259
Social insurance and retirement receipts.....	694	708	750	792	839	872	914
Excise taxes.....	66	67	69	71	74	75	78
Other receipts.....	86	83	84	93	91	98	98
Total receipts.....	<u>1,991</u>	<u>2,011</u>	<u>2,121</u>	<u>2,234</u>	<u>2,366</u>	<u>2,461</u>	<u>2,581</u>
Outlays by Function:							
National defense.....	309	348	354	364	375	381	387
Social Security.....	433	460	476	495	519	546	575
Medicare.....	217	226	233	241	257	265	284
Income security.....	270	311	320	324	333	344	351
Health.....	173	195	231	253	270	290	311
Veteran benefits and services.....	46	52	56	58	63	63	62
Education, training, employment, and social services.....	57	72	79	81	82	83	85
Transportation.....	55	62	60	61	63	64	66
Other programmatic functions.....	153	173	175	182	179	180	184
Net interest.....	206	177	175	178	174	168	160
Undistributed offsetting receipts ..	(55)	(55)	(78)	(94)	(98)	(94)	(99)
Total outlays.....	<u>1,864</u>	<u>2,020</u>	<u>2,080</u>	<u>2,142</u>	<u>2,218</u>	<u>2,289</u>	<u>2,366</u>
Surplus or deficit (-).....	<u>127</u>	<u>(9)</u>	<u>41</u>	<u>92</u>	<u>148</u>	<u>172</u>	<u>215</u>

Note: Details may not add to totals due to rounding.

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