

Highlights of Financial Position

Overview of Financial Data

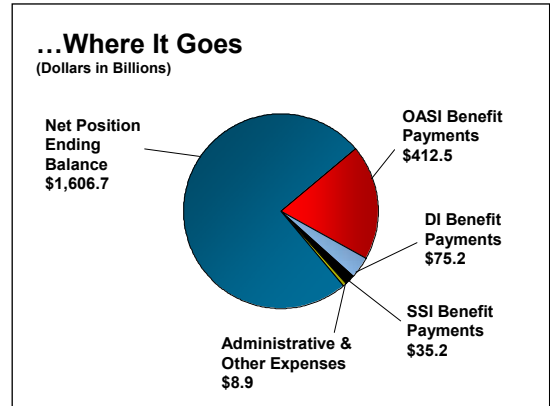
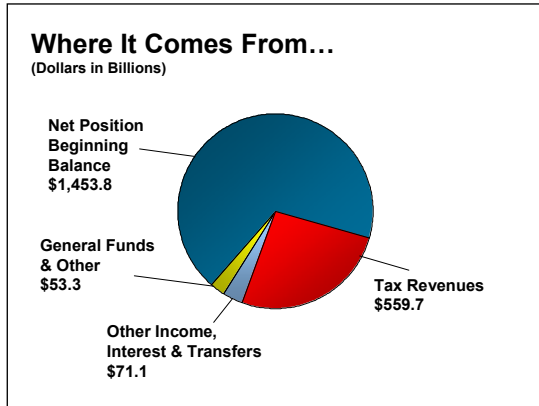
SSA's financial statements and footnotes appear on pages 145 through 192. The financial statements presented in this report can be considered complete and reliable as evidenced by the unqualified opinion the financial statements received from the independent audit firm of PricewaterhouseCoopers LLP. These statements combined the results from the programs administered by SSA. These programs include the Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI) programs (referred to as OASDI when discussing them in combination) and the Supplemental Security Income (SSI) program. OASI and DI have separate trust funds which are financed by payroll taxes, interest on trust fund investments and income taxes on retiree benefits (OASI only). SSI is financed by general revenues from the U.S. Treasury.

Balance Sheet: The Balance Sheet displayed on page 146 reflects total assets of \$1,668.9 billion, a 10.2 percent increase over the previous year. Approximately 98 percent of assets are investments. These investments are commonly known as the Social Security Trust Funds. By statute, we invest those funds not needed to pay current benefits in interest bearing Treasury securities. The \$151.2 billion growth (10 percent) in investments from 2003 is primarily due to tax revenues of \$559.7 billion and interest on those investments of \$87.6 billion, exceeding cost of operations of \$531.4 billion. The majority of our liabilities, 83 percent, consist of benefits that have accrued as of the end of the fiscal year but have not been paid. By statute, OASI and DI program benefits for the month of September are not paid until October. Liabilities grew in 2004 by \$1 billion (1.5 percent) primarily because of the growth in benefits due and payable. Reflecting the higher growth in assets than liabilities, the net position grew \$152.9 billion or 10.5 percent to \$1,606.7 billion. Interest on Investments, which is paid in the form of Treasury securities, represents 57.9 percent of the growth of the trust fund, up from 54.3 percent in 2003.

Statement of Net Cost: Net cost of operations increased \$22 billion or 4.3 percent from \$509.4 billion in 2003 to \$531.4 billion in 2004. Of this increase, \$21.8 billion (4.4 percent growth) resulted from increased benefit payments and \$0.3 billion (3.5 percent growth) resulted from operating expenses. The net cost and benefit payments of the OASI program both grew 3.7 percent while operating expenses grew by 2.3 percent. The number of OASI beneficiaries grew 1 percent to 39.6 million while average benefit payments grew by 3 percent to \$869 per month. The net cost and benefit payments of the DI program both grew by 7.7 percent. Operating expenses grew by 8.6 percent. The number of DI beneficiaries grew by 0.5 percent while average benefits increased 0.4 percent to \$733 per month. The SSI benefit payments increased 6.0 percent which was higher than the 5.8 percent increase in net costs because operating expenses were constant. The number of SSI beneficiaries grew by 1.5 percent while average benefits increased by 2.1 percent to \$564 per month.

Statement of Changes in Net Position: The Statement of Changes in Net Position reflects an increase of \$152.9 billion. This increase is primarily attributable to a \$151.2 billion increase in trust fund reserves. The following charts summarize the activity on SSA's Statement of Net Cost and Statement of Changes in Net Position by showing the funds SSA was provided in FY 2004 and how these funds were used. These statements are displayed on pages 147 and 148, respectively. Most resources available to SSA were used to finance current OASDI benefits and to accumulate reserves to pay future benefits. When funds are needed to pay administrative

expenses or benefit entitlements, investments are redeemed to supply cash to cover the outlays. Administrative expenses shown, as a percent of benefit expenses, is 1.7 percent. Total financing sources grew by \$19.5 billion or 2.9 percent from \$664.8 billion in 2003 to \$684.4 billion in 2004. The primary sources for this growth were a payroll and income tax revenue increase of \$12.9 billion (2.4 percent) from 2003 and investment income of \$3.4 billion (4.0 percent) from 2003. The growth in investment income was due to the 10.2 percent growth in investment which was partially offset by the drop of average interest yield from 6.52 percent to 6.25 percent.

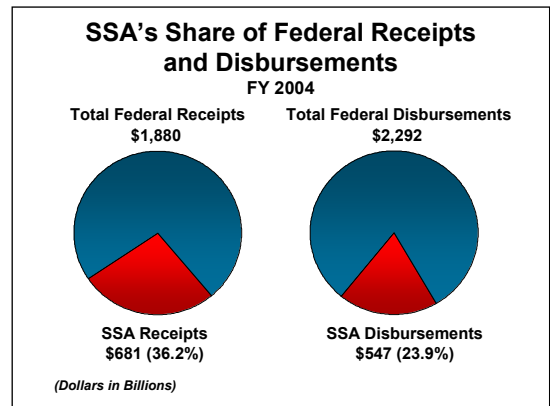


Statement of Budgetary Resources: This statement displayed on page 149 shows that SSA had \$562.9 billion in budgetary resources of which \$2.1 billion remained unobligated at year-end. SSA recorded total outlays of \$530.3 billion by the end of the year. Budgetary resources grew \$24.3 billion, or 4.5 percent from 2003, while outlays increased \$22.3 billion, or 4.4 percent.

Statement of Financing: This statement reconciles “Total resources used to finance activities,” an expression of budgetary spending, with the “Net cost of operations,” the proprietary expenses of the Agency. The statement displayed on page 150 identifies \$530.6 billion in budgetary spending for FY 2004, an increase of \$20.7 billion or 4.1 percent over last year. This total is offset by \$0.5 billion in resources not part of the net cost of operations, and is increased by \$0.4 billion in components of net cost of operations that will not require or generate resources in the current period. The resulting balance reflects a \$531.5 billion net cost of operations for the year, an increase of \$22 billion or 4.3 percent over FY 2003.

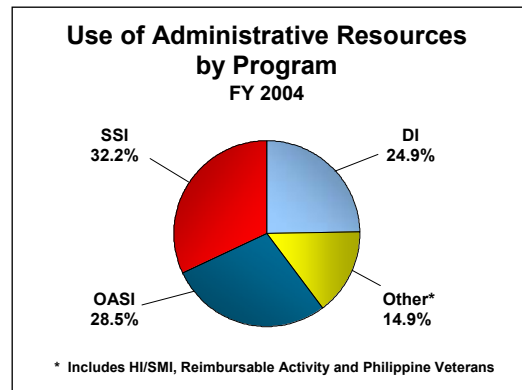
SSA’s Share of Federal Operations

The programs administered by SSA constitute a large share of the total receipts and disbursements of the Federal Government as shown in the chart to the right. Receipts for our programs represented 36.2 percent of the \$1.9 trillion in total Federal receipts, a decrease of 1.7 percent over last year. Disbursements stayed the same at 23.9 percent of Federal disbursements.



Use of Administrative Resources

The chart to the right displays the use of administrative resources for FY 2004 in terms of the programs SSA administers or supports. Although the DI and SSI programs comprise only 21.1 percent of the total benefit payments made by SSA, they consume over 57.2 percent of annual administrative resources. Claims for DI and SSI disability benefits are processed through State Disability Determination Services where a decision is rendered on whether the claimant is disabled. In addition, the Agency is required to perform continuing disability reviews on many individuals receiving DI and SSI disability payments to ensure continued entitlement to benefits. The FY 2003 use of administrative resources by program was 28.8 percent for the OASI program, 23.8 percent for the DI program, 32.4 percent for the SSI program and 15.0 percent for Other.



Trust Fund Solvency

Pay-as-you-go-Financing

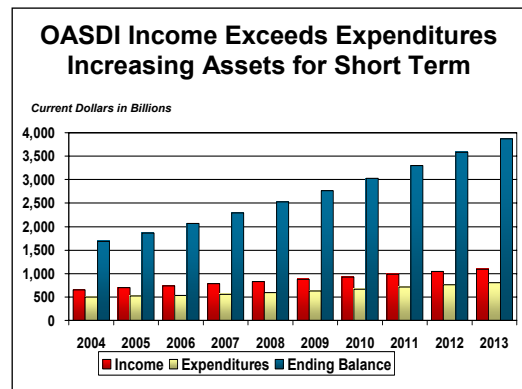
The Social Security Trust Funds are deemed to be adequately financed on a pay-as-you-go basis as long as assets (including current income and Trust Fund holdings) are sufficient to finance program obligations. Such adequacy is reflected in the maintenance of a positive Trust Fund balance. In recent years, current income has exceeded program obligations, and thus the Trust Fund holdings have been growing. The following table shows that Trust Fund holdings, expressed in terms of the number of months of program obligations that these holdings could finance has grown from 27.9 months at the end of FY 2000 to 38.2 months at the end of FY 2004, an increase of 37 percent.

Number of Months of Expenditures Year End Assets Can Pay (End of FY)					
	2000	2001	2002	2003	2004 ¹
OASI	28.7	31.8	35.0	37.7	40.4
DI	22.8	24.6	25.9	26.6	26.7
Combined	27.9	30.8	33.6	36.0	38.2

1. Estimates are based on 2004 Trustees Report intermediate assumptions.

Short Term Financing

The Social Security Trust Funds are deemed adequately financed for the short term when actuarial estimates of Trust Fund holdings for the beginning of each year are at least as large as program obligations for the year. Estimates in the 2004 Trustees Report indicate that the Social Security Trust Fund is adequately financed over the next 10 years. The graph shows that while combined OASDI expenditures and income are expected to increase by 69 and 73 percent, respectively, over the 10-year period, Trust Fund assets are expected to grow by 153 percent to \$3.9 trillion.



Long Term Financing

Social Security's financing is not projected to be sustainable over the long term with the tax rates and benefit levels scheduled in current law. In 2018, benefit payments will exceed tax revenues, and, in 2042, the Trust Fund will be exhausted according to the projections by Social Security's Chief Actuary. The primary reasons for the projected long-term inadequacy of financing under current law relate to changes in the demographics of the United States: baby boomers approaching retirement, retirees living longer, and birth below population replacement rates. In present value terms, the 75 year shortfall is \$3.7 trillion, which is a \$200 billion increase from the 2003 estimate. Possible reform alternatives being discussed -- singularly or in combination with each other -- are (1) increasing payroll taxes, (2) slowing the growth in benefits, (3) using general revenues or (4) increasing returns through either personal savings accounts or direct investments of the trust funds.

Page 38 provides additional discussion of the long term solvency of the OASDI Trust Fund. Pages 174 through 192 include the disclosures required by Federal Accounting Standards Advisory Board Statement 17, Accounting for Social Insurance.

Improper Payments Information Act of 2002

Narrative Summary of Implementation Efforts for FY 2004 and Agency Plans for FY 2005-FY 2007

Background

A key component of the President's Management Agenda is the initiative to reduce improper payments. The Improper Payments Information Act of 2002 (IPIA), Public Law 107-300, requires Federal agencies to report annually on the extent of the improper payments in those programs that are susceptible to significant improper payment and the actions they are taking to reduce such payments. IPIA has extended the improper payments reporting requirements beyond those programs and activities listed in the former Section 57 of Office of Management and Budget (OMB) Circular A-11.

On August 28, 2003, OMB issued their decision that only avoidable overpayments are to be included in the amount of improper payments reported under IPIA. Under this decision, payments resulting from legal or policy requirements are considered unavoidable and are not improper. OMB guidance on implementation of IPIA calls for SSA to continue to report on improper payments information for the OASI and DI programs, in addition to the SSI program, as was required by Section 57 of OMB Circular A-11. SSA is to continue to report on the improper payments found in the OASI and DI programs even though the level of such payments in these programs have continually been well below the threshold cited in IPIA. The OMB guidance also calls for the FY 2004 Performance and Accountability Report to include the most recently available data in reducing improper payments. Due to timing of the payment accuracy analysis, SSA's FY 2004 report includes results for FY 2003. Please refer to the Appendix for a detailed report of the FY 2003 results and plans to reduce improper payments.

OMB guidance on IPIA requires the evaluation of all payment outlays beyond the OASI, DI and SSI programs that SSA administers. SSA has performed a review of the Agency's administrative payments; e.g., payroll disbursements, vendor payments, etc. These payments were found not to be susceptible to significant improper payments. More information on the evaluation of improper payments is provided in the Appendix of the report.

Recovery Auditing

In FY 2004, SSA initiated recovery auditing of contractor payments in accordance with Section 831 of the Defense Authorization Act for Fiscal Year 2002 which requires agencies that enter into contracts with a total value in excess of \$500 million in a FY initiate a program to identify and recover payment errors. SSA hired auditing firm PRG Shultz and the recovery auditing effort began in January 2004. Preliminary management reports from the contractor do not indicate any significant recovery activity. Only .0006 percent, or about \$20,000, of the \$3.3 billion payments reviewed has been deemed improper and has been collected. The vendor will conclude their review in December 2004. Please refer to the Appendix for a detailed report on SSA's recovery auditing initiative.

Agency Efforts and Future Plans

SSA's OASI, DI and SSI quality assurance (QA) payment accuracy (Stewardship) reviews provide the data to measure the payment outlays in these programs each fiscal year. The OASDI accuracy rate continues to exceed 99.8 percent for both overpayments and underpayments. Even though we have achieved this high accuracy rate, we still strive to make additional achievements in payment accuracy. The detailed report on SSA's efforts to reduce improper payments identifies the major causes of improper payments over the past several years in the OASI and DI programs and the actions the Agency has taken to address these causes.

In the SSI program, SSA has established a 5-year goal to achieve 96 percent overpayment accuracy by FY 2008. Success in achieving the SSI goal is dependent on the effectiveness of the activities outlined in SSA's SSI Corrective Action Plan. In FY 2003, SSI payment accuracy results were 93.9 percent for overpayments and 98.8 percent for underpayments. The major causes of SSI overpayments in FY 2003 were wages and financial accounts (such as savings and checking accounts). The major causes of SSI underpayments in FY 2003 were wages, in kind support and maintenance and living arrangements.

OASI Improper Payment Initiatives

- Beginning in FY 2000, the Annual Earnings Test (AET) no longer applied to beneficiaries who are at the full retirement age or older.
- For the past several years, SSA implemented initiatives to correct computation errors in benefit payments. These efforts affected more than 1 million beneficiaries and \$4 billion in past and future benefits.
- In the relationship/dependency area, SSA redesigned its student eligibility process.
- Improvements were made to wage and self-employment earnings reports by modifying the Social Security Statement and increasing electronic filing of W-2's.
- SSA is developing software processes to identify missing military service (MS) wage credits and to remove MS credits that were incorrectly granted. The processes involve reviewing the military employer identification numbers used in SSA's earnings records, verifying SSA's MS information against other government databases and developing MS profiles using SSA's data stores. Subsequently, SSA will pay any underpayments that are due beneficiaries and collect overpayments identified by the new processes.

DI Improper Payment Initiatives

- A Substantial Gainful Activity (SGA) software tool is available in every field office to ensure proper handling of SGA cases.
- Correction of workers compensation (WC) errors, the leading cause of DI underpayments for FY's 1999 through 2003, continues through dedication of SSA's Operations staff to rework affected cases. In addition, a major OASDI software release in June 2004 provides more automated tools to assist in the cleanup effort.
- The Agency is working with State governments to improve the current paper-based process to report death data. Electronic Death Reporting (EDR), a web-based automation of the death registration process, would provide timely and accurate death data. Currently, three States are providing EDR online to SSA and two more States are scheduled to be added by the end of September 2004.

SSI Improper Payments Initiatives

- In FY 2004, SSA completed a test to determine the feasibility of implementing monthly wage reporting using touch-tone and telephone technology. Results of the test are pending which will be the basis to decide whether to proceed with this technology that offers the opportunity to prevent SSI wage overpayments estimated at \$487 million in FY 2003.
- To further improve SSI payment accuracy, the Foster Care and Independence Act of 1999 gives the Commissioner the authority to require SSI recipients to provide authorization for SSA to obtain any and all financial institution records. Refusal to provide, or revocation of, an authorization may result in ineligibility for SSI. In an effort to reduce the amount of overpayments caused by financial accounts, SSA promulgated final regulations in FY 2004 that allow the Agency to query financial institutions electronically. In February 2004, SSA began a proof of concept to test the feasibility of financial institutions accepting electronic bank account verification requests. Thus far, the proof of concept is demonstrating the financial community's support of this process. In addition, verification requests are being returned quickly to the Agency which allows immediate continuation of the SSI application or redetermination. Upon Agency review of the proof of concept final report, it will be determined whether to proceed with systems development to automate the bank account verification process in future fiscal years. SSI financial account issues accounted for a projected \$453 million in overpayment deficiencies for FY 2003.
- Effective January 2001, SSA began using online queries to access the Office of Child Support Enforcement's (OCSE) quarterly wage data and "new hires" OCSE file as tools to assist in detecting improper payments due to wages. In an effort to learn quickly about unreported work, SSA is exploring the usefulness of a quarterly match with the "new hires" OCSE file. Improper SSI payments due to living arrangements and in-kind support and maintenance result from recipients not reporting changes in their household living situations or changes in the recipient's contributions to household expenses. This is a complex area where recipient understanding of reporting requirements is very difficult to address. For this reason a portion of the annual SSI redetermination workload is targeted to addressing improper payments due to living arrangement changes. The redetermination process is the most powerful tool available to SSA for preventing and detecting all types of SSI improper payments, including those due to living arrangements and in-kind support and maintenance. To detect improper SSI payments, SSA regularly reviews cases that statistical profiles indicate are most likely to be in error.

Limitation on Financial Statements

The principal financial statements beginning on page 146 have been prepared to report the financial position and results of operations of SSA, pursuant to the requirements of 31 U.S.C. 3515 (b).

While the statements have been prepared from the books and records of SSA in accordance with generally accepted accounting principles (GAAP) for Federal entities and the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.