BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND FEDERAL DISABILITY INSURANCE TRUST FUNDS WASHINGTON, D.C., MAY 31, 2013

HON. JOSEPH R. BIDEN, JR.,
President of the Senate.

DEAR MR. PRESIDENT:

In accordance with the requirements of section 709 of the Social Security Act, we are writing to notify you that we project that the asset reserves held in the Federal Disability Insurance (DI) Trust Fund will become inadequate within the next 10 years. As shown in the 2013 OASDI Trustees Report, which we are issuing today and a copy of which is attached, the projected asset reserves of the DI Trust Fund fall below 20 percent of annual cost during 2015 based on our intermediate set of economic, demographic, and programmatic assumptions. Moreover, we project that the reserves of the DI Trust Fund will be depleted one year later, in 2016, and only about 80 percent of benefits scheduled in current law will be payable at that time if no legislative action is taken.

Background—Section 709 of the Social Security Act requires the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds (the Board) to submit a report to each House of the Congress when it determines that the balance ratio of a trust fund for any calendar year may become less than 20 percent. The balance ratio is the ratio of asset reserves at the beginning of a year to the cost for that year.[1] Section 709 further requires that the report include:

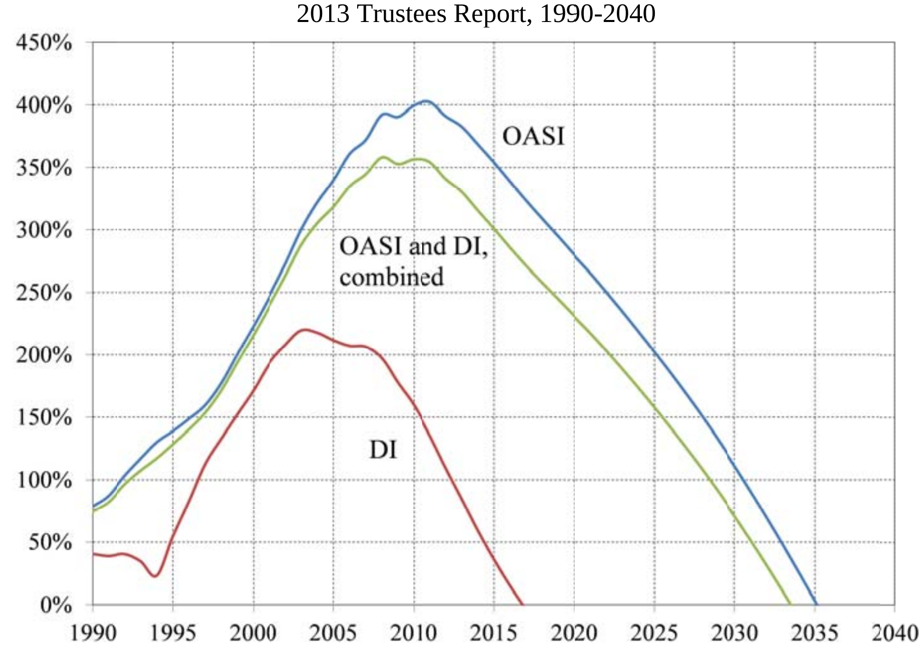
> *. . . recommendations for statutory adjustments affecting the receipts and disbursements of such Trust Fund necessary to maintain the balance ratio of such Trust Fund at not less than 20 percent, with due regard to the economic conditions which created such inadequacy in the balance ratio and the amount of time necessary to alleviate such inadequacy in a prudent manner. The report shall set forth specifically the extent to which benefits would have to be reduced, taxes . . . would have to be increased, or a combination thereof, in order to obtain the objectives referred to in the preceding sentence.*

The Disability Insurance Trust Fund—Each year, the Board prepares a report, commonly referred to as the Trustees Report, on the financial outlook for the Social Security trust funds. Estimates in the 2013 Trustees Report show that although the Old-Age and Survivors Insurance (OASI) Trust Fund and the theoretical combined OASI and Disability Insurance (DI) Trust Funds are adequately financed through the 10-year short-range projection period under intermediate assumptions, the DI fund alone is not.

[1] This ratio is also called a *trust fund ratio* in the 2013 OASDI Trustees Report.

Under the intermediate assumptions of the 2013 Trustees Report (those representing the Trustees' best estimate of future economic and demographic trends), the asset reserves of the DI Trust Fund steadily decline, falling below 20 percent of annual cost during 2015 and becoming depleted in 2016. The figure below shows the estimated balance ratios for the combined OASI and DI Trust Funds and for each fund separately up to the date of trust fund reserve depletion.

Balance ratios for the OASI and DI Trust Funds, separately and combined, based on present law under the Intermediate Assumptions of the 2013 Trustees Report, 1990-2040



The Board believes that reporting the expected future decrease in the balance ratio for the DI Trust Fund in this and previous letters fulfills the statutory requirement to give due regard to the amount of time necessary to alleviate the inadequacy in a prudent manner.

Maintaining a Balance Ratio of at Least 20 Percent—The following table shows the minimum annual amounts of change necessary to keep the DI balance ratio from falling below 20 percent over the next 10 years. For each year through 2022, the table shows the amounts of: (1) additional payroll tax revenue; (2) cost reductions; and (3) a combination of equal amounts of payroll tax revenue increases and cost reductions needed to meet this goal. We chose this period because it coincides with the short-range projection period in the 2013 Trustees Report and because nominal dollar amounts become increasingly less meaningful for years farther in the future. Maintaining a balance ratio of at least 20 percent for the DI Trust Fund would require larger changes after 2022.

The additional payroll tax revenue amounts required to meet the 20-percent minimum DI balance ratio differ somewhat from the required reductions in cost. Payroll tax revenue changes affect asset reserves (the numerator of the balance ratio) but have little if any immediate effect on cost (the denominator); benefit changes needed to reduce program cost affect both asset reserves and cost directly and simultaneously. Under the combined approach, roughly one-half of the amounts shown would be raised through additional payroll tax revenue and one-half would be implemented through cost reductions.

Amounts required to prevent DI balance ratio from declining below 20 percent under the Intermediate Assumptions of the 2013 Trustees Report
(In billions)

Calendar year	Additional payroll tax revenue only	Cost reductions[a] only	Total amounts of additional payroll tax revenue and cost reductions[a] under a combined approach
2015	$8.1	$1.6	$4.9
2016	31.2	32.0	31.6
2017	28.3	29.1	28.7
2018	25.7	26.3	26.0
2019	24.4	24.8	24.6
2020	24.0	24.0	24.0
2021	25.0	25.0	25.0
2022	26.4	26.2	26.3
Total, 2015-2022	193.2	189.1	191.1

[a]Amounts shown for cost reductions through changes in benefits are net of partially offsetting estimated reductions that would occur automatically due to income taxes on Social Security benefits.

A projected trust fund level of 20 percent of annual cost may be sufficient to enable the timely payment of benefits but does not provide an adequate reserve against adverse contingencies. A more stringent measure of trust fund strength is the test of short-range financial adequacy. As described in the 2013 Trustees Report, meeting this test requires that the estimated balance ratio remain at or above 100 percent if the current ratio is at least 100 percent. If the current balance ratio is under 100 percent, then the projected ratio must reach 100 percent by the beginning of the sixth year and remain at or over 100 percent throughout the remainder of the 10-year short-range period. In addition, projected financial resources must be sufficient to pay all estimated costs over the entire 10-year period. We apply this test based on our intermediate assumptions. Compliance with this test should be an important goal for any statutory adjustments designed to strengthen the financial condition of the DI Trust Fund.

Recommendation—Based on the intermediate estimates in the 2013 Trustees Report, the asset reserves of the DI Trust Fund would fall below 20 percent of annual cost during 2015 and would be depleted in 2016 in the absence of corrective legislation. Lawmakers should take prompt action to strengthen the short-term finances of the DI Trust Fund.

As described above, lawmakers could choose to increase revenues to the DI Trust Fund independent of any effect on the OASI program, to reduce cost through modification of the DI program, or to use a combination of methods to strengthen the financial condition of the DI Trust Fund. Such actions would improve the finances of the DI Trust Fund without a corresponding diminution in OASI Trust Fund asset reserves.

Alternatively, lawmakers could strengthen the finances of the DI Trust Fund by reallocating part of the existing payroll tax rate from the OASI Trust Fund to the DI Trust Fund. This reallocation would provide additional revenue for the DI Trust Fund without requiring an increase in overall tax rates. Although reallocation would improve the finances of the DI Trust Fund, it would worsen the finances of the OASI Trust Fund and produce no net improvement for the combined OASI and DI Trust Funds. Lawmakers reallocated tax rates most recently in 1994, when the DI Trust Fund was projected to become exhausted within 10 years, but the OASI Trust Fund and the combined OASI and DI Trust Funds were not.

The Board recommends that lawmakers enact appropriate legislation as soon as possible after careful consideration of the status of the DI program.

Respectfully,

JACOB J. LEW,
Secretary of the Treasury, and Managing Trustee of the Trust Funds.

SETH D. HARRIS,
Acting Secretary of Labor, and Trustee.

KATHLEEN SEBELIUS,
Secretary of Health and Human Services, and Trustee.

CAROLYN W. COLVIN,
Acting Commissioner of Social Security, and Trustee.

CHARLES P. BLAHOUS III,
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ROBERT D. REISCHAUER,
Trustee.

DAVID A. WEAVER,
Associate Commissioner, Office of Program Development and Research, Social Security Administration, and Acting Secretary, Board of Trustees.