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1978 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND

COMMUNICATION

FROM

THE BOARD OF TRUSTEES, FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND

TRANSMITTING

THE 1978 ANNUAL REPORT OF THE BOARD, PURSUANT TO SECTION 1841(b) OF THE SOCIAL SECURITY ACT, AS AMENDED

MAY 16, 1978.—Referred to the Committees on Ways and Means and Interstate and Foreign Commerce and ordered to be printed

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LETTER OF TRANSMITTAL

BOARD OF TRUSTEES OF THE
FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND,
Washington, D.C., May 15, 1978.

The SPEAKER OF THE HOUSE OF REPRESENTATIVES,
Washington, D.C.

SIR: We have the honor to transmit to you the 1978 Annual Report of the Board of Trustees of the Federal Supplementary Medical Insurance Trust Fund (the 13th such report), in compliance with the provisions of section 1841(b) of the Social Security Act.

Respectfully,

W. MICHAEL BLUMENTHAL,
Secretary of the Treasury and Managing Trustee of the Trust Fund.

RAY MARSHALL,
Secretary of Labor.

JOSEPH A. CALIFANO, Jr.,
Secretary of Health, Education, and Welfare.

DON I. WORTMAN,
Acting Commissioner of Social Security and Secretary, Board of Trustees.

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The PRESIDENT OF THE SENATE,
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1978 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND

THE BOARD OF TRUSTEES

The Federal Supplementary Medical Insurance Trust Fund, established on July 30, 1965, is held by the Board of Trustees under the authority of section 1841(b) of the Social Security Act, as amended. The Board is comprised of three members who serve in an ex officio capacity. The members of the Board are the Secretary of the Treasury, the Secretary of Labor, and the Secretary of Health, Education, and Welfare. The Secretary of the Treasury is designated by law as the Managing Trustee. The Commissioner of Social Security is Secretary of the Board. The Board of Trustees reports to the Congress once each year in compliance with section 1841(b)(2) of the Social Security Act. This is the 1978 annual report, the thirteenth such report.

ADVISORY COUNCIL ON SOCIAL SECURITY

The Secretary of Health, Education, and Welfare, on February 26, 1978, announced the appointment of an Advisory Council on Social Security under the provisions of section 706 of the Social Security Act. The Council consists of a Chairman and 12 members representing organizations of employers and of employees, self-employed persons, and the public.

Under the law, the Social Security Advisory Council is charged with making a comprehensive study of the status of the social security cash benefit and Medicare programs. This study is to include an examination of the financial status of the trust funds in relation to the long-term commitments of the programs, benefit levels, the scope of coverage, and other aspects of the programs, including their impact on public assistance.

The Council is required to submit its final reports to the Secretary of Health, Education, and Welfare no later than October 1, 1979. After the Council's reports are transmitted by the Secretary to the Congress and to the Board of Trustees of each of the trust funds, the Council will cease to exist. The Council's report and recommendations with respect to the supplementary medical insurance program will be included in the 1980 annual report of the Board of Trustees.

HIGHLIGHTS

(a) Disbursements of the supplementary medical insurance trust fund increased 22 percent in fiscal year 1977 (October 1 through September 30 basis) over 1976 (July 1 through June 30 basis). Most

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of this increase resulted from higher physician fees recognized by the program and the use of more physician services by program enrollees. Other major factors in the increased outlays include greater use of outpatient hospital services and home health services and increased enrollment.

(b) Income to the trust fund increased 48 percent in fiscal year 1977 over 1976. This resulted from increased adequate actuarial rates which determine the general revenue contribution and from increased enrollment in the program. The adequate actuarial rates promulgated included margins to restore the losses to the program during fiscal year 1976.

(c) The trust fund increased $1,040 million to $2,279 million during 1977. This resulted from increased income to the program and cost increases below the level anticipated.

(d) In December of 1977, the Secretary of the Health, Education, and Welfare promulgated a standard monthly premium rate of $8.20 and adequate actuarial rates of $13.40 for the aged enrollees and $25.00 for the disabled enrollees for the 12-month period ending June 30, 1979.

(e) An average of 22.7 million persons aged 65 and over were enrolled in the program in fiscal year 1977. This is about 94 percent of the aged population. An additional 2.3 million disabled beneficiaries were enrolled in the same period.

Social Security Amendments Since the 1977 Report

During 1977 the following public laws affecting the operation of the Federal Supplementary Medical Insurance Trust Fund were enacted:

(a) Public Law 95–142, enacted October 25, 1977, is intended to strengthen the Government's capability to detect, prosecute, and punish fraudulent activities in Federal health care programs. Specifically, the law strengthens program penalty sanctions, requires increased disclosure of information by providers of services and suppliers, and makes improvements in the Professional Standards Review Organization program.

(b) Public Law 95–210, enacted December 13, 1977, provides for reimbursement under the supplementary medical insurance program for medical services provided in rural health clinics by nonphysicians. Prior to this legislation, rural health clinics which did not have a full-time physician were ineligible for Medicare reimbursement.

Nature of the Trust Fund

The Federal Supplementary Medical Insurance Trust Fund was established on July 30, 1965, as a separate account in the United States Treasury. All the financial operations of the supplementary medical insurance program are handled through this fund.

The major sources of receipts of the trust fund are (1) premiums paid by eligible persons who are voluntarily enrolled in the program and (2) contributions of the Federal Government that are authorized to be appropriated and transferred from the general fund of the Treasury. Eligible persons aged 65 and over have been able to enroll in the program since its inception in July 1966. Since July 1973, disabled persons under age 65, who meet certain eligibility requirements, have also been able to enroll in the program.

The premiums paid by participants are based on the standard monthly premium rate, which is the same for participants aged 65 and over and for disabled participants under age 65. Premiums paid for fiscal years 1967 through 1973 were matched by an equal amount of Government contributions. Beginning July 1973, the amount of Government contributions corresponding to premiums paid by each of the two groups of participants is determined by applying a ratio, prescribed in the law for each group, to the amount of premiums received from that group of participants. The ratio is equal to (1) twice the amount of the adequate actuarial rate applicable to the particular group of participants, minus the amount of the standard monthly premium rate, divided by (2) the amount of the standard monthly premium rate.

Standard monthly premium rates and adequate actuarial rates are promulgated each year by the Secretary of Health, Education, and Welfare. The standard monthly premium rates in effect from the beginning of the program, July 1966 through June 1978, and the rate promulgated for July 1978 through June 1979, are shown in table 1. Adequate actuarial rates in effect from July 1973 through June 1978, and the rates promulgated for July 1978 through June 1979, are also shown.

Another source from which receipts of the trust fund are derived is interest received on investments held by the fund. The investment procedures of the fund are described later in this section.

Section 201(i) of the Social Security Act authorizes the Managing Trustee to accept and deposit in the trust fund unconditional money gifts or bequests made for the benefit of the fund or for any activity financed through the fund.

Expenditures for benefit payments and administrative expenses under the program are paid out of the trust fund. All expenses incurred by the Department of Health, Education, and Welfare and by the Department of the Treasury in carrying out the supplementary medical insurance provisions of title XVIII of the Social Security Act are charged to the trust fund. The Secretary of Health, Education, and Welfare certifies benefit payments to the Managing Trustee, who makes the payments from the trust fund in accordance therewith.

Hospitals, at their option, are permitted to combine their billing for both hospital costs and physician components of radiology and pathology services rendered hospital inpatients by hospital-based physicians. Where hospitals elect this billing procedure, payments are made initially from the hospital insurance trust fund, with reimbursement later to it from the supplementary medical insurance trust fund. The reimbursements so made are on a provisional basis and are subject to adjustment, with appropriate interest allowances, as the actual experience develops and is analyzed.

The Social Security Amendments of 1967 and 1972 authorize the Secretary of Health, Education, and Welfare to develop and conduct a broad range of experiments and demonstration projects designed to determine various methods of increasing efficiency and economy in providing health care services, while maintaining the quality of such services, under the hospital insurance and supplementary medical insurance programs. The costs of such experiments and demonstration projects are paid out of the hospital insurance and supplementary medical insurance trust funds.

Congress has authorized expenditures from the trust funds for constructions, rental, and lease or purchase contract of office buildings and related facilities for use in connection with the supplementary medical insurance program. Both the capital costs of construction financed directly from the trust fund and the rental, lease, or purchase contract costs of acquiring facilities are included in trust fund expenditures. In 1972–75, construction of several large facilities was authorized under purchase contract authority, wherein initial capital costs are borne by the private sector. Under this method of facilities acquisition, trust fund expenditures for use and ultimate Government ownership of a facility are made over periods of from 10 to 30 years. Whatever the manner of acquisition, the net worth of facilities and other fixed capital assets is not carried in the statements of the operations of the trust fund presented in this report. This is because the value of fixed capital assets does not represent funds available for benefit or administrative expenditures and, therefore, is not viewed as being a consideration in assessing the actuarial status of the funds.

That portion of the trust fund which, in the judgment of the Managing Trustee, is not required to meet current expenditures for benefits and administration is invested in interest-bearing obligations of the U.S. Government (including special public-debt obligations described below), in obligations guaranteed as to both principal and interest by the United States, or in certain federally sponsored agency obligations that are designated in the laws authorizing their issuance as lawful investments for fiduciary and trust funds under the control and authority of the United States or any officer of the United States. Obligations of these types may be acquired on original issue at the issue price or by purchase of outstanding obligations at their market price.

The Social Security Act authorizes the issuance of special public-debt obligations for purchase exclusively by the trust fund. The law requires that such special public-debt obligations shall bear interest at a rate based on the average market yield (computed on the basis of market quotations as of the end of the calendar month next preceding the date of such issue) on all marketable interesting-bearing obligations of the United States forming a part of the public debt which are not due or callable until after the expiration of 4 years from the end of such calendar month.

TABLE 1.—STANDARD MONTHLY PREMIUM RATES AND ADEQUATE ACTUARIAL RATES

	Standard monthly premium rate	Adequate actuarial rate	
		Participants aged 65 and over	Disabled participants under age 65
July 1966—March 1968	$3.00		
April 1968—June 1970	4.00		
12-mo period ending June 30 of—			
1971	5.30		
1972	5.60		
1973	5.80		
1974 [1]	6.30	$6.30	$14.50
1975	6.70	6.70	18.00
1976	6.70	7.50	18.50
1977	7.20	10.70	19.00
1978	7.70	12.30	25.00
1979	8.20	13.40	25.00

[1] In accordance with limitations on the costs of health care imposed under Phase III of the Economic Stabilization Program, the standard premium rate for July and August 1973 was set at $5.80 and $6.10, respectively. Effective September 1973, the rate increased to $6.30.

SUMMARY OF THE OPERATIONS OF THE TRUST FUND, FISCAL YEAR 1977

Beginning with fiscal year 1977, the period of the time covered by the fiscal year of the U.S. Government was changed from the 12 months beginning on July 1 of each year and ending on June 30 of the following year to the 12 months beginning on October 1 of each year and ending on September 30 of the following year, in accordance with the Congressional Budget Act of 1974 (Public Law 93–344). This Act further provided that the calendar quarter July-September 1976 be a period of transition from fiscal year 1976, which ended on June 30, 1976, to fiscal year 1977, which began on October 1, 1976.

A statement of the income and disbursements of the Federal Supplementary Medical Insurance Trust Fund in fiscal year 1977, and of the assets of the fund at the beginning and end of the fiscal year, is presented in table 2. Corresponding amounts for the interim period, July-September 1976 (which were not presented in last year's annual report), are also shown in the table.

The total assets of the trust fund amounted to $1,239 million on September 30, 1976. During fiscal year 1977, total receipts amounted to $7,383 million, and total disbursements were $6,342 million. Total assets thus increased $1,041 million during the year to a total of $2,279 million on September 30, 1977.

TABLE 2.—STATEMENT OF OPERATIONS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND DURING THE INTERIM PERIOD[1] AND FISCAL YEAR 1977

[In thousands]

	Interim [1]	Fiscal year 1977
Total assets of the trust fund, beginning of period	$1, 218, 555	$1, 238, 508
Receipts:		
Premium from participants:		
Participants aged 65 and over	492, 298	1, 986, 937
Disabled participants under age 65	46, 350	205, 966
Total premiums	538, 648	2, 192, 903
Transfers from general fund of the Treasury:		
Government contributions:		
For premiums received from participants aged 65 and over	734, 092	4, 025, 935
For premiums received from disabled participants under age 65	143, 908	1, 009, 469
Total Government contributions	878, 000	5, 035, 405
Interest on delayed transfers of Government contributions		17, 539
Total transfers from general fund of the Treasury	878, 000	5, 052, 944
Interest:		
Interest on investments	4, 420	132, 259
Interest on amounts of interfund transfers due to adjustment in allocation of administrative expenses and construction costs [2]		4, 451
Total interest	4, 420	136, 710
Total receipts	1, 421, 068	7, 382, 557
Disbursements:		
Benefit payments:		
Paid directly from the trust fund for costs of health services	1, 267, 063	5, 858, 559
Transfers to the hospital insurance trust fund for reimbursement of interest loss related to transfer payments made in conjunction with the costs of radiology and pathology services [3]	1, 500	6, 000
Total benefit payments	1, 268, 563	5, 864, 559
Costs of experiments and demonstration projects [3]	475	2, 363

See footnotes at end of table.

TABLE 2.—STATEMENT OF OPERATIONS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND DURING THE INTERIM PERIOD[1] AND FISCAL YEAR 1977—Continued

[In thousands]

	Interim[1]	Fiscal year 1977
Total assets of the trust fund—Continued		
Disbursements—Continued		
Administrative expenses:		
Department of Health, Education, and Welfare[4]	130,636	515,076
Treasury Department	38	115
Railroad Retirement Board	286	960
Civil Service Commission		103
Construction of facilities for Social Security Administration	1,117	184
Interfund transfers due to adjustment in allocation of—		
Administrative expenses[5]		−41,920
Construction costs[5]		226
Gross administrative expenses	132,077	474,744
Less receipts from sale of surplus supplies, materials, etc.		27
Net administrative expenses	132,077	474,717
Total disbursements	1,401,115	6,341,639
Net addition to the trust fund	19,953	1,040,918
Total assets of the trust fund, end of year	1,238,508	2,279,426

[1] The interim period is the period from July 1, to Sept. 30, 1976.
[2] A positive figure represents a transfer of interest to the supplementary medical insurance trust fund from the other social security trust funds. A negative figure represents a transfer of interest from the supplementary medical insurance trust fund to the other social security trust funds.
[3] For explanation, see text.
[4] Includes administrative expenses of the carriers and intermediaries.
[5] A positive figure represents a transfer from the supplementary medical insurance trust fund to the other social security trust funds. A negative figure represents a transfer to the supplementary medical insurance trust fund from the other social security trust funds.

Note: Totals do not necessarily equal the sum of rounded components.

Of the total receipts, $1,987 million represented premium payments by (or on behalf of) participants aged 65 and over, and $206 million represented premium payments by (or on behalf of) disabled participants under age 65. Total premium payments amounted to $2,193 million, an increase of 9.3 percent over the amount of $2,007 million for the preceding 12-month period. This increase in premiums from participants resulted primarily from (1) the expected growth in the number of persons enrolled in the supplementary medical insurance program, and (2) the increase from $6.70 to $7.20 per month in the standard premium rate that became effective on July 1, 1976, and the increase from $7.20 to $7.70 per month in the standard premium rate that became effective on July 1, 1977.

Contributions received from the general fund of the Treasury amounted to $5,053 million. This amount consisted of $4,026 million representing contributions relating to premiums paid by participants aged 65 and over, $1,009 million representing contributions relating to the premiums paid by disabled participants under age 65, and $18 million in interest on delayed transfers of Government contributions.

The remaining $137 million of receipts consisted almost entirely of interest on the investments of the trust fund.

Of the $6,342 million in total disbursements, $5,859 million represented benefits paid directly from the trust fund for health services covered under Title XVIII of the Social Security Act. In addition, transfers were made to the hospital insurance trust fund consisting of $6 million to adjust for the loss of interest caused by the delay in transferring payments for the costs of radiology and pathology services that were paid initially from the hospital insurance trust fund but that were liabilities of the supplementary medical insurance trust fund.

Total benefit payments from the trust fund in fiscal year 1977, therefore, amounted to $5,865 million, an increase of 20.2 percent over the corresponding amount of $4,879 million paid in the preceding 12-month period.

Reference has been made in an earlier section to provisions which authorize payment from the trust fund for costs of experiments and demonstration projects in providing health care services. In fiscal year 1977, payments for such costs amounted to about $2 million.

The remaining $475 million of disbursements was for net administrative expenses. Administrative expenses are allocated and charged directly to each of the four trust funds—old-age and survivors insurance, disability insurance, hospital insurance, and supplementary medical insurance—on the basis of provisional estimates. Periodically, as actual experience develops and is analyzed, adjustments to the allocations of administrative expenses and costs of construction for prior periods are affected by interfund transfers, with appropriate interest allowances.

In table 3, the experience with respect to actual amounts of participants' premiums, Government contributions, and benefit payments in fiscal year 1977 is compared with the estimates for fiscal year 1977 which appeared in the 1976 and 1977 annual reports. The actual experience was relatively close to the estimates for premiums, Government contributions, and benefit payments.

TABLE 3.—COMPARISON OF ACTUAL AND ESTIMATED OPERATIONS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND, FISCAL YEAR 1977

[Dollar amounts in millions]

Item	Actual amount	Comparison of actual experience with estimates for fiscal year 1977 published in— 1977 report: Estimated amount	1977 report: Actual as percentage of estimate	1976 report: Estimated amount	1976 report: Actual as percentage of estimate
Premiums from participants	$2,193	$2,180	101	$2,162	101
Government contributions	5,053	5,053	100	5,053	100
Benefit payments	5,867	5,999	98	5,905	99

The assets of the trust fund at the end of the interim period totaled $1,239 million, consisting of $1,244 million in the form of obligations of the U.S. Government and, as an offset, an extension of credit of $5 million against securities to be redeemed. This was covered by the redemption of securities on October 1, 1976. The net increase in the par value of the investments owned by the fund during the interim period amounted to $14 million. New securities at a total par value of $1,417 million were acquired during the interim period through the investment of receipts. All of these new securities were certificates of indebtedness. The par value of securities redeemed during the interim period was $1,403 million, including $1,348 million in certificates of indebtedness. The assets of the trust fund at the end of fiscal year 1977 totaled $2,279 million, consisting of $2,232 million in the form of obligations of the U.S. Government and an undisbursed balance of $47 million. Table 4 shows a comparison of the total assets of the fund and their distribution at the end of the interim period and at the end of fiscal year 1977. A comparison of the assets of the trust fund with liabilities for incurred but unpaid benefits (and related administrative expenses) is shown in a later section.

TABLE 4.—ASSETS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND, AT THE END OF THE INTERIM PERIOD[1] AND AT THE END OF FISCAL YEAR 1977

	Sept. 30, 1976		Sept. 30, 1977	
	Par value	Book value[2]	Par value	Book value[2]
Investments in public-debt obligations sold only to this fund (special issues):				
Certificates of indebtedness:				
7⅛ percent, 1977	$51,533,000	$51,533,000.00		
7⅛ percent, 1978			$41,235,000	$41,235,000.00
7⅜ percent, 1977	17,311,000	17,311,000.00		
Notes: 6⅝ percent, 1980	277,822,000	277,822,000.00	277,822,000	277,822,000.00
Bonds:				
7⅛ percent, 1978			121,411,000	121,411,000.00
7⅛ percent, 1979			137,817,000	137,817,000.00
7⅛ percent, 1981			56,246,000	56,246,000.00
7⅛ percent, 1982			56,245,000	56,245,000.00
7⅛ percent, 1983			56,245,000	56,245,000.00
7⅛ percent, 1984			56,245,000	56,245,000.00
7⅛ percent, 1985			56,245,000	56,245,000.00
7⅛ percent, 1986			56,245,000	56,245,000.00
7⅛ percent, 1987			56,245,000	56,245,000.00
7⅛ percent, 1988			56,245,000	56,245,000.00
7⅛ percent, 1989			56,245,000	56,245,000.00
7⅛ percent, 1990			56,246,000	56,246,000.00
7⅛ percent, 1991			56,246,000	56,246,000.00
7⅛ percent, 1992			137,816,000	137,816,000.00
7⅜ percent, 1981	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1982	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1983	11,546,000	11,546,000.00	11,546,000	11,546,000.00
7⅜ percent, 1984	11,546,000	11,546,000.00	11,546,000	11,546,000.00
7⅜ percent, 1985	11,546,000	11,546,000.00	11,546,000	11,546,000.00
7⅜ percent, 1986	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1987	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1988	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1989	11,547,000	11,547,000.00	11,547,000	11,547,000.00
7⅜ percent, 1990	73,510,000	73,510,000.00	73,510,000	73,510,000.00
7½ percent, 1981	8,060,000	8,060,000.00	8,060,000	8,060,000.00
7½ percent, 1982	8,060,000	8,060,000.00	8,060,000	8,060,000.00
7½ percent, 1983	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1984	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1985	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1986	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1987	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1988	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1989	8,061,000	8,061,000.00	8,061,000	8,061,000.00
7½ percent, 1990	8,060,000	8,060,000.00	8,060,000	8,060,000.00
7½ percent, 1991	81,570,000	81,570,000.00	81,570,000	81,570,000.00
7⅝ percent, 1981	61,964,000	61,964,000.00	61,964,000	61,964,000.00
7⅝ percent, 1982	61,964,000	61,964,000.00	61,964,000	61,964,000.00
7⅝ percent, 1983	61,964,000	61,964,000.00	61,964,000	61,964,000.00
7⅝ percent, 1984	61,964,000	61,964,000.00	61,964,000	61,964,000.00
7⅝ percent, 1985	61,964,000	61,964,000.00	61,964,000	61,964,000.00
7⅝ percent, 1986	61,963,000	61,963,000.00	61,963,000	61,963,000.00
7⅝ percent, 1987	61,963,000	61,963,000.00	61,963,000	61,963,000.00
7⅝ percent, 1988	61,963,000	61,963,000.00	61,963,000	61,963,000.00
7⅝ percent, 1989	61,963,000	61,963,000.00	61,963,000	61,963,000.00
Total investments in public-debt obligations	1,243,945,000	1,243,945,000.00	2,232,078,000	2,232,078,000.00
Undisbursed balance		[3] −5,436,542.07		47,348,202.11
Total assets		1,238,508,457.93		2,279,426,202.11

[1] The interim period is the period from July 1 to Sept. 30, 1976.
[2] Par value, plus unamortized premium, less discount outstanding.
[3] The negative figure represented an extension of credit which was covered by the redemption of securities on the 1st day of the following month.

The new increase in the par value of the investments held by the fund during fiscal year 1977 amounted to $988 million. New securities at a total par value of $8,387 million were acquired during the fiscal year, through the investment of receipts and reinvestment of funds made available from the redemption of securities. The par value of securities redeemed during the year was $7,399 million. Included in these amounts is $7,355 million in certificates of indebtedness that were acquired, and $7,383 million in certificates of indebtedness that were redeemed, within the fiscal year.

The effective annual rate of interest earned by the assets of the supplementary medical insurance trust fund during the 12 months ending on June 30, 1977 was 7.4 percent. (This period is used because interest on special issues is paid semiannually on June 30 and December 31.) The interest rate on special issues purchased by the trust fund in June 1977 was 7⅛ percent, payable semiannually.

Expected Operations and Status of the Trust Fund During the Period October 1, 1977 to December 31, 1980

Financing for the supplementary medical insurance program is established annually on the basis of standard monthly premium rates (paid by or on behalf of the participants) and adequate actuarial rates (on which general revenue contributions are based) which are applicable to a period of July 1 through the following June 30. In recent years, allowable fee limits for physician services have also been established to apply to the same July 1 to June 30 period.

Standard premium rates and adequate actuarial rates have been promulgated for periods through June 30, 1979. It has been assumed in this report that financing after that time will be established to cover the incurred expenses of the program.

The projections assume that allowable fees for physician services will increase an average of 8.8 percent for the 12-month period ending June 30, 1978 and will increase an average of 7.9 percent for the 12-month period ending June 30, 1979. The costs per enrollee for institutional services under Part B are projected to increase 25 percent for the 12-month period ending June 30, 1978 over the previous 12 months and an additional 25 percent for the 12-month period ending June 30, 1979.

Table 5 shows the projected operations of the trust fund on a fiscal year basis through fiscal year 1980. Table 5A shows the corresponding development on a calendar year basis. The trust fund increased substantially in fiscal year 1977 due primarily to financing measures intended to improve the status of the trust fund. The adequate rates for the 12-month periods ending June 30, 1978, and June 30, 1979, were promulgated with specific margins to maintain an adequate level of the trust fund. As a result the fund is projected to increase to $3,588 million by the end of fiscal year 1978 and $4,273 million by the end of fiscal year 1979.

TABLE 5.—ESTIMATED PROGRESS OF SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND (CASH BASIS), FISCAL YEARS 1978-80 AND ACTUAL DATA FOR 1967-77

[In millions]

Fiscal year	Income				Disbursements			Balance in fund at end of year [2]
	Premiums from participants	Government contributions [1]	Interest on fund	Total income	Benefit payments	Administrative expenses	Total disbursements	
Historical:								
1967	$647	$623	$15	$1,285	$664	[3] $134	$799	$486
1968	698	634	21	1,353	1,390	143	1,532	307
1969	903	984	23	1,911	1,645	195	1,840	378
1970	936	928	12	1,876	1,979	217	2,196	57
1971	1,253	1,245	17	2,516	2,035	248	2,283	290
1972	1,340	1,365	29	2,734	2,255	288	2,544	481
1973	1,427	1,430	45	2,902	2,391	246	2,637	746
1974	1,704	2,029	76	3,809	2,874	409	3,283	1,272
1975	1,887	2,330	106	4,322	3,765	404	4,170	1,424
1976	1,951	2,939	104	4,994	4,671	529	5,200	1,219
Interim [4]	539	878	4	1,421	1,268	133	1,401	1,239
1977	2,193	5,053	137	7,383	5,867	475	6,342	2,279
Projected:								
1978 [5]	2,408	6,383	204	8,995	7,075	611	7,686	3,588
1979 [5]	2,631	6,853	267	9,751	8,411	655	9,066	4,273
1980 [5]	2,860	7,857	305	11,022	9,847	704	10,551	4,744

[1] The payments shown as being from the general fund of the Treasury include certain interest-adjustment items.
[2] The financial status of the program depends on both the total net assets and the liabilities of the program. (See table 7).
[3] Administrative expenses shown include those paid in fiscal 1966 and 1967.
[4] Interim period is the period from July 1 to Sept. 30, 1976.
[5] Beginning with fiscal year 1977 the fiscal year is the 12-mo period ending with Sept. 30 of the year indicated.

TABLE 5A.—ESTIMATED PROGRESS OF SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND (CASH BASIS), CALENDAR YEARS 1978-80 AND ACTUAL DATA FOR 1966-77

[In millions]

Calendar year	Income				Disbursements			Balance in fund at end of years [2]
	Premiums from participants	Government contributions [1]	Interest on funds	Total income	Benefit payments	Administration expenses	Total disbursements	
Historical:								
1966	$322	0	$3	$324	$128	$75	$203	$122
1967	640	$933	24	1,597	1,197	110	1,307	412
1968	832	858	21	1,711	1,518	183	1,702	421
1969	914	907	18	1,839	1,865	196	2,061	199
1970	1,096	1,093	12	2,201	1,975	238	2,212	188
1971	1,302	1,313	24	2,639	2,117	260	2,377	450
1972	1,382	1,389	37	2,808	2,325	290	2,614	643
1973	1,550	1,705	57	3,311	2,526	318	2,844	1,111
1974	1,804	2,225	95	4,124	3,318	410	3,728	1,506
1975	1,918	2,648	106	4,673	4,273	462	4,735	1,444
1976	2,060	3,810	106	5,977	5,080	542	5,622	1,799
1977	2,247	5,386	172	7,805	6,038	467	6,505	3,099
Projected:								
1978	2,463	6,234	240	8,937	7,406	622	8,028	4,008
1979	2,688	7,039	291	10,018	8,763	667	9,430	4,596
1980	2,919	8,202	328	11,449	10,237	717	10,954	5,091

[1] The payments shown as being from the general fund of the Treasury include certain interest-adjustment items.
[2] The financial status of the program depends on both the total net assets and the liabilities of the program. (See table 7.)

ACTUARIAL STATUS OF THE TRUST FUND

1. ACTUARIAL SOUNDNESS OF THE SUPPLEMENTARY MEDICAL INSURANCE PROGRAM

The concept of actuarial soundness, as it applies to the supplementary medical insurance program, is closely related to the concept as it applies to private group insurance. The supplementary medical insurance program essentially is yearly renewable term insurance intended to be self-supporting from premium income paid by the enrollees and from income contributed from general revenue in proportion to premium payments. The law requires the Secretary of Health, Education, and Welfare to establish income on the basis of incurred costs. That is, the income to the program during a 12-month period for which financing is being established must be sufficient to pay for services (including associated administrative costs) expected to be rendered during that period even though payment for some of these services will not be made until after the close of the period. The portion of income required to cover those benefits not paid until after the close of the year is added to the trust fund until needed. Thus, the amount of assets in the trust fund at any time should be no less than the costs of the benefits and administration incurred but not yet paid. Since the income per enrollee (premium plus government contribution rate) is established prospectively, it is subject to projection error. As a result, the income to the program may not be equal to incurred costs; therefore trust fund assets should be maintained at a level which is adequate to cover the impact of a moderate degree of projection error as well as the value of incurred but unpaid expenses.

In testing the actuarial soundness of the supplementary medical insurance program, it is not appropriate to look beyond the period for which the enrollee premium rate and level of general revenue financing have been established. The primary tests of actuarial soundness, then, are that (1) income for years for which financing has been established be sufficient to meet the projected benefits and associated administrative expenses incurred for that period, (2) assets be sufficient to cover projected liabilities which will have been incurred by the end of that time but will not have been paid yet, and (3) assets be sufficient further to protect against the possibility that cost increases under the program will be somewhat higher than assumed in the projection. Even if these tests of actuarial soundness are not met, the program can continue to operate if the trust fund remains at a level adequate to permit the payment of claims as presented.

2. INCURRED EXPERIENCE OF THE SUPPLEMENTARY MEDICAL INSURANCE PROGRAM

The tests of actuarial soundness of the supplementary medical insurance program noted above rely on the incurred experience of the program. Cash disbursements for benefits and administrative expenses by themselves are misleading, due to the relatively large liabilities outstanding at any time for benefits and processing costs that must be paid for services already performed. These liabilities result from the lag between the time that services are performed and the time that payments for them are made.

The experience of the program is substantially more difficult to determine on an incurred basis than on a cash basis. In the early months of program operations, it appears that some bills containing errors were never resubmitted following correction. Payment for some services is reported only on a cash basis, and the incurred experience must be inferred from the cash payment information. For recent time periods, the tabulations of bills are incomplete due to normal processing delays. Finally, since bills are tabulated only for a sample of beneficiaries, the data is subject to bias and random fluctuation inherent in the sampling process.

Table 6 shows the estimated transactions of the trust fund on an incurred basis. For the reasons stated above, the incurred experience must be viewed as an estimate even for historical years. Various checks, such as cash outlay data, assure that the estimates are reasonably close, however.

TABLE 6.—ESTIMATED INCOME AND DISBURSEMENTS INCURRED UNDER SUPPLEMENTARY MEDICAL INSURANCE PROGRAM, 12-MO PERIODS ENDING JUNE 30, 1967–79

[In millions]

12-mo period ending June 30—	Premiums from participants	Government contributions	Interest on fund	Benefit payments	Administrative expenses	Net operations in year
Historical:						
1967	$647	$647	$15	$1,121	[1] $190	−$2
1968	698	698	21	1,446	149	−178
1969	903	903	23	1,769	210	−150
1970	936	936	12	1,930	212	−258
1971	1,253	1,253	17	2,089	255	179
1972	1,340	1,340	29	2,286	292	131
1973	1,427	1,426	45	2,501	257	140
1974	1,704	2,031	76	3,148	443	215
1975	1,887	2,396	108	3,922	421	48
1976	1,951	2,972	109	4,856	550	−374
1977	2,156	4,695	159	5,884	508	618
Projected:						
1978	2,353	5,904	208	7,081	611	773
1979	2,573	6,564	251	8,434	674	280

[1] Includes administrative expenses incurred prior to the beginning of the program.

3. ACCUMULATED EXCESS OF ASSETS OVER LIABILITIES

The liability outstanding at any time for the cost of services performed for which no payment has been made is referred to as "benefits incurred but unpaid". Estimates of the amount of benefits incurred but unpaid as of June 30 of each year, and of the administrative expenses related to processing these benefits, appear in table 7. For most years of the program, assets have not been as large as outstanding liabilities. Nonetheless, the fund has remained positive, allowing claims to be paid.

TABLE 7.—SUMMARY OF ESTIMATED ASSETS AND LIABILITIES OF THE SUPPLEMENTARY MEDICAL INSURANCE PROGRAM, ON JUNE 30, 1967–79

[Dollar amounts in millions]

	Past experience as of June 30—											Projected as of June 30—	
	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Assets:													
Balance in trust fund	$486	$307	$378	$57	$290	$481	$746	$1,272	$1,424	$1,219	$2,170	$3,353	$4,078
Government contributions due and unpaid	24	88	7	15	22	−3	−7	−5	67	105	88	38	0
Total assets	510	395	385	72	312	478	739	1,267	1,491	1,324	2,258	3,391	4,078
Liabilities:													
Benefits incurred but unpaid	457	513	637	588	642	673	783	1,057	1,214	1,399	1,694	2,026	2,402
Administrative cost thereon	56	62	77	72	79	83	94	133	150	171	196	225	255
Total liabilities	513	575	714	660	721	756	877	1,190	1,364	1,570	1,890	2,251	2,657
Excess of assets over liabilities	−3	−180	−329	−588	−409	−278	−138	77	127	−246	368	1,140	1,421
Ratio [1]	.00	−.09	−.15	−.25	−.16	−.10	−.04	.02	.02	−.04	.05	.13	.13

[1] Ratio of the excess of assets over liabilities to the following year's total incurred expenditures.

Program financing has been established through June 1979. On the basis of this financing, the status of the trust fund is expected to improve significantly, from an estimated excess of assets over liabilities of approximately $368 million at the end of June 1977 to a projected $1,421 million at the end of June 1979. This amounts to 13 percent of incurred expenditures for the following 12-month period, a level which is sufficient to cover the impact of a moderate degree of projection error.

4. SENSITIVITY TESTING

Some of the assumptions underlying the projection presented in this report are highly uncertain, and variations in these assumptions would have a substantial impact on expenditures. In order to test the future status of the program under varying assumptions, a low cost projection and a high cost projection were prepared by varying these key assumptions. The low and high cost alternative sets of assumptions are intended to reflect growth rates for the various components of program costs which are more favorable and adverse, respectively, than those of the intermediate projection and which are not unreasonable themselves in light of the nature and historical experience of the program. As such, they provide a range of financial outcomes, within which the actual experience of the program might reasonably be expected to fall.

Table 8 indicates that, under the low cost assumptions, trust fund assets would exceed liabilities significantly by the end of June 1979 (the period through which financing has been established), reaching a level of 25 percent of the following year's incurred expenditures. If these low growth rates were actually to materialize, then subsequent financing rates could be adjusted downward in order to lower the excess of assets over liabilities to more appropriate levels. Under the high cost assumptions, trust fund assets would be approximately equal to liabilities by the end of June 1979. If these high growth rates were to occur, the program would remain just solvent and subsequent financing rates would have to be adjusted upward in order to generate more appropriate levels for the excess of assets over liabilities.

TABLE 8.—ACTUARIAL STATUS OF THE SMI TRUST FUND UNDER 3 SETS OF ASSUMPTIONS FOR THE 12-MONTH PERIOD ENDING WITH JUNE OF THE YEAR SHOWN

	Intermediate projection (this report)		Low cost projection		High cost projection	
	1978	1979	1978	1979	1978	1979
Per enrollee increases over prior year in:						
Physician fees (percent)	8.8	7.9	7.3	6.4	10.3	9.4
Physician utilization (percent)	2.0	3.0	.5	1.0	5.0	5.0
Outpatient hospital and home health agency (percent)	25.0	25.0	15.0	15.0	40.0	40.0
Assets as of June 30 (in millions)	$3,391	$4,078	$3,585	$4,830	$3,092	$2,972
Liabilities as of June 30 (in millions)	2 251	2,657	2,179	2,474	2,363	2,926
Excess of assets over liabilities (in millions)	1,140	1,421	1,406	2,356	729	46
Ratio[1]	0.13	0.13	0.17	0.25	0.07	0.00

[1] Ratio of excess of assets over liabilities to the following year's total incurred expenditures.

Conclusion

The financing of the supplementary medical insurance program has been established through June 1979, by the promulgation of standard monthly premium rates (paid by or on behalf of each enrollee) of $7.70 for the year ending June 1978 and $8.20 for the year ending June 1979 and of adequate actuarial rates which determine the amount to be contributed from general revenue on behalf of each enrollee.

Under the intermediate assumptions used in this report, income to the trust fund is projected to exceed disbursements during both fiscal years 1978 and 1979. The assets in the trust fund, on a cash basis, are projected to increase from $2,279 million at the end of fiscal year 1977 to an estimated $4,273 million at the end of 1979. About two-thirds of this year-end balance, however, is attributable to liabilities for benefits and associated administrative costs which will have been incurred but not yet paid.

The actuarial status of the trust fund is expected to improve significantly, from an estimated excess of assets over liabilities of approximately $368 million at the end of June 1977 to a projected $1,421 million at the end of June 1979 (representing 13 percent of projected incurred expenditures for the following 12-month period). Even under more pessimistic assumptions as to cost increases, income produced on the basis of financing already established plus assets held in the trust fund will be sufficient for the trust fund to remain solvent through that period of time. Hence, the financing established through June 1979 is sufficient to cover projected benefit and administrative costs incurred through that time period and to build a level of trust fund assets which is adequate to cover the impact of a moderate degree of projection error.