

Old-Age, Survivors, and Disability Insurance: Administrative Expenses

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THE ADMINISTRATION of the old-age, survivors, and disability insurance program has never cost more than a small proportion of contribution income—2–3 percent in most years. Administrative costs are also small by another measure; as a proportion of the total taxable payroll on which contributions are based, they are less than $\frac{1}{2}$ of 1 percent. The costs are met from two funds—the old-age and survivors insurance trust fund and the disability insurance trust fund. These funds, though similar, are operated separately.

Into the disability insurance trust fund established by the 1956 amendments to the Social Security Act are paid the proceeds from the additional contributions required under that legislation to meet the cost of the disability benefits. The combined employer-employee contribution rate for this purpose was initially set at 0.50 percent of earnings, but it was increased in the 1965 amendments to 0.70 percent. The self-employed contribution rate has always been 25 percent lower than the combined employer-employee rate. The maximum annual earnings to which these rates are applicable was increased in 1959 from \$4,200 to \$4,800 and in 1966 to \$6,600.

Contributions for the old-age and survivors insurance portion of the program are paid into the old-age and survivors insurance trust fund. The combined employer-employee rate for old-age and survivors insurance and disability insurance purposes at the present time is 7.7 percent of earnings up to \$6,600 a year, and for the self-employed the rate is 5.8 percent. These rates are scheduled to rise in 1967, in 1969, and 1973, reaching an ultimate level of 9.7 percent and 7.0 percent respectively. Contributions for the old-age and survivors insurance program represent the difference between the contributions from these rates and those that go into the disability insurance trust fund.

The trust funds are credited with receipts from

the sale of surplus materials and supplies. Such receipts are here considered as offsets to gross administrative expenses in the calculation of the net administrative expenses. Charges are made to other government agencies and to private organizations and individuals who are provided research or informational services not directly related to the program. Receipts derived from such charges are used as an offset to administrative expenses paid from the appropriations of Congress; such offset administrative expenses do not appear in the statements of the trust fund operations, and correspondingly these receipts are not shown as being credited to the trust funds.

Monthly benefits to disabled workers and their eligible dependents are paid from the disability insurance trust fund. All other benefits are paid from the old-age and survivors insurance trust fund—including (a) child's benefits to disabled persons aged 18 or over who are the children of retired or deceased insured workers and (b) any additional old-age and survivors insurance benefit amounts payable as a result of the disability freeze (maintaining the benefit rights of disabled insured workers).

Since January 1, 1940, administrative costs have also been paid from the trust funds.¹ In some instances they are clearly allocable to only one fund, but usually an estimated allocation between the two funds is necessary.

The allocations for Treasury Department expenses in connection with the program are made monthly for each trust fund, but for other expenses the appropriate adjustment between the trust funds is not made until after the end of the fiscal year, when a full analysis can be made. During the period considered here the program expenses incurred by the Department of Health,

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¹ Before 1940, administrative costs were paid from the General Treasury, which was effectively reimbursed since the appropriations made to the old-age reserve account (predecessor of the old-age and survivors insurance trust fund) closely approximated the tax receipts less these administrative costs.

Education, and Welfare—primarily those of the Social Security Administration—are paid, as they arise, out of the old-age and survivors insurance trust fund. Full adjustment by transfer of money from the disability insurance trust fund to the old-age and survivors insurance trust fund is made for each fiscal year after the year has ended, and at the same time the latter fund is compensated for its loss of interest.

ADMINISTRATIVE WORKLOAD

The administration of the program presents a recordkeeping job that is probably without parallel. For the calendar year 1965, about 280 million separate earnings items were reported for approximately 79.5 million different persons. About 6 million new account numbers were issued in that year. This total includes about 800,000 that were issued in connection with the health insurance program enacted in the 1965 amendments. In addition, about 4.2 million duplicate account-number cards were issued because the original had been lost or worn out or because of a change in name—usually for women who had recently married. Date-of-birth changes, name changes, and cross-referrals were involved in about 3.2 million revisions in account-number records.

Claims development and adjudication represent the most costly phase of the administrative workload, and the continuing payment of monthly benefits also involves a considerable amount of administrative work. During 1965, over 3 million individuals were awarded monthly benefits, and over 1 million lump-sum death payments were made. At the end of the year, monthly benefits were going to more than 21 million persons, including about 1¾ million disabled-worker beneficiaries and their dependents. During the year, benefits were terminated for about 2 million persons—in most cases because the beneficiary died or was a child beneficiary who attained age 18.

EXPENDITURES

The administrative costs met from the trust funds include such direct expenses of the Social

Security Administration as salaries, rentals of machinery and property, and purchase of supplies. Similar expenses incurred by the Treasury Department in collecting contributions and issuing benefit checks and certain expenses that the Department of Health, Education, and Welfare incurs in operating the old-age, survivors, and disability insurance program are also paid from the trust funds.

The indirect expenses paid from the trust funds include those incurred by various State agencies in connection with the determination of disability. The general principle is that the cost of processing the claims from disabled workers should be distributed between the two trust funds on the basis of the actuarially estimated liability to each fund of an average disability award. (The liability to the old-age and survivors insurance trust fund represents benefits to be paid after the worker reaches age 65 and to dependents if the disabled worker dies before he reaches age 65.) Costs incurred in investigating a beneficiary's continuing eligibility for disability benefits and in processing denied initial claims are charged to the disability insurance trust fund.

Construction cost for district offices and for

TABLE 1.—Administrative expenses of the old-age and survivors insurance program in relation to contribution income, benefit payments, and taxable payroll, 1940-65

Calendar year	Total amount ¹ (in millions)	As percent of—		
		Contributions	Benefit payments	Taxable payroll
1940-65.....	\$3.120	2.1	2.4	0.09
1940.....	26	4.1	74.3	.08
1941.....	26	4.3	29.5	.06
1942.....	28	2.8	21.4	.05
1943.....	29	2.3	17.5	.05
1944.....	29	2.2	13.9	.04
1945.....	30	2.3	10.9	.05
1946.....	40	3.1	10.6	.06
1947.....	46	3.0	9.9	.06
1948.....	51	3.0	9.2	.06
1949.....	54	3.2	8.1	.07
1950.....	61	2.3	6.5	.07
1951.....	81	2.4	4.3	.07
1952.....	88	2.3	4.0	.07
1953.....	88	2.2	2.9	.06
1954.....	92	1.8	2.5	.07
1955.....	119	2.1	2.4	.08
1956.....	132	2.1	2.3	.08
1957.....	144	2.1	2.0	.08
1958.....	181	2.4	2.1	.10
1959.....	200	2.5	2.0	.10
1960.....	191	1.8	1.8	.09
1961.....	236	2.1	2.0	.11
1962.....	255	2.1	1.9	.12
1963.....	275	1.9	1.9	.12
1964.....	291	1.9	2.0	.12
1965 ²	327	2.0	2.0	.13

¹ Adjusted to reflect the deferred transfers relating to administrative expense allocation between the old-age and survivors insurance and the disability insurance trust funds, as prescribed by law; the figures are thus on an "actually incurred" basis.

² Preliminary estimates.

the central office building in Baltimore is another administrative expense item. Through the end of 1965 these expenditures amounted to about \$36.5 million. This type of cost is charged as a current administrative expense, although it is really a capital item. As a result, administrative expenses are somewhat overstated during the years in which such costs were charged. The amount of the overstatement will be counterbalanced by lower reported expenses later, when the only charges will be for maintenance; there will be no charges for rent or for interest on or amortization of the capital cost of the building.

A few indirect expenses that may be properly chargeable to the program are not paid out of the trust funds. The principal expenses of this type are the costs of benefits under certain employee programs for those employees whose salaries are paid out of the trust funds and who are covered by such programs. Specifically, these are the Government's balancing cost for the civil-service retirement program² and the costs of the unemployment compensation program for Federal workers. Also, under the Federal employees' compensation program (workmen's compensation) the trust funds were not charged for costs due to deaths or injuries occurring before December 1, 1960.

The costs of certain other employee benefits are met directly from the trust funds. They are the employer contributions for the Federal employee group life insurance program, the Federal employee health benefits program, and the old-age, survivors, and disability insurance program for employees not under the civil service retirement program and the matching employer cost (6½ percent of payroll) of the civil service retirement system for employees covered by that program.

The costs of some relatively small items are not met from the trust funds, including space provided in some Government buildings, personnel administration work by the Civil Service Commis-

² Before the middle of 1957, none of the cost to the Government for this program was met from the trust funds, since then Government agencies did not match employee contributions. Currently, each agency matches the employee contribution of 6½ percent, which meets almost all the cost for current service. The remainder of the current-service cost and all the accrued liability cost (for past service) is to be met from general funds (a total of about 9½ percent of payroll on a level-cost basis according to the valuation made as of 1963).

sion, and costs for storage of records by the General Services Administration.

In the old-age, survivors, and disability insurance program as in private pension plans and group insurance programs, the covered employers meet some of the indirect cost of administration. The chief item of this kind arises in connection with the employers' maintenance of individual wage records for the quarterly reports, from which individuals' earnings histories are developed. The employer would do part of this work, in any event, in connection with income-tax withholding.

COST ALLOCATION BETWEEN FUNDS

There is no requirement in the law that the program's administrative expenses be allocated between the two trust funds on a current basis. All expenses can be met from one trust fund currently, and the appropriate allocation and transfer can be made after the fiscal year has ended. For an adequate analysis of the administrative expenses of the two parts of the program, however, the data must first be adjusted to allocate the costs as "actually incurred." Otherwise, they would be misleading, as shown by the following figures on a "cash" basis for calendar years 1957-65.

[In millions]

Calendar year	Old-age and survivors insurance trust fund	Disability insurance trust fund
1957.....	\$162	\$3
1958.....	194	12
1959.....	184	50
1960.....	203	36
1961.....	239	64
1962.....	256	66
1963.....	281	68
1964.....	296	79
1965.....	328	90

The 1959 figures are especially deceptive. In that year, two cost allocations were paid from the disability insurance trust fund to the old-age and survivors insurance trust fund; in 1957 no such allocation was paid.

MEASURING COSTS

To permit proper analysis, administrative costs should be related to an appropriate base. Three

bases are possible—contribution income, benefit disbursements, and taxable payroll—each with certain advantages and certain disadvantages.

When administrative costs are related to contribution income, there is the disadvantage that, as the tax rate is changed, the ratio fluctuates widely and therefore has limited significance. Changes in the maximum earnings base that is subject to taxes also affect the ratio significantly but generally less than changes in the tax rates.

The ratio of administrative costs to benefit disbursements can be misleading, particularly during the early years of operation, when such disbursements were relatively low and when most of the administrative expenses were incurred in handling the wage records that would produce future benefits.

The ratio of administrative costs to taxable payroll seems most meaningful, since it indicates the percentage of the taxable payroll needed to pay for the operation of the system. This ratio too can be misleading if wage levels rise and if the maximum earnings base is not kept up-to-date, since then administrative expenses—all other things being equal—will rise more rapidly than taxable payroll. The general public probably finds this concept the hardest of the three to understand.

Old-Age and Survivors Insurance

As the coverage of the program was expanded and the beneficiary rolls grew, the cost of administering old-age and survivors insurance rose from \$26 million in 1940 to about \$90 million a year in 1952, 1953, and 1954 and to \$327 million by 1965 (table 1). The 1965 total includes expenses of \$44.5 million incurred by the Treasury Department in connection with the program and reimbursed from the trust fund.

The various factors bringing about the large rise in administrative costs can best be examined by considering separately the two periods 1940–50 and 1951–65. In the earlier period the growth in costs was primarily related to advances in the general level of employment, growth in the number of claims as more persons attained insured status, and a rise in the number of beneficiaries. The 1951–65 rise in costs resulted to some degree from these factors but primarily from program

changes. In both periods, operating costs were affected by the continuing rise in general wage and price levels.

Among the reasons for the sharp rise from 1954 to 1959 (more than 100 percent) were the extension of coverage by the 1954 amendments to certain groups—self-employed farmers, for example—and the fact that individuals in other groups, such as domestic workers and farm workers, for whom coverage was not available until the 1950 amendments, started to become eligible for benefits.³

Other factors in this increase in administrative costs were (1) the introduction of the disability freeze; (2) the liberalization of the earnings test, which, although far more equitable than the former test, is more complex to administer; (3) the relatively large number of claims processed after the minimum retirement age for women had been lowered from 65 to 62; (4) the complexities inherent in the 1954, 1956, and 1958 amendments covering new groups and providing new types of benefit protection; (5) the legislation providing for general pay raises for Federal employees and for charging part of the employee-benefit costs for the civil service retirement system and the Federal employee group life insurance system directly to the employing agency; and (6) the one-time construction costs of the new central office building in Baltimore.

The increase from 1960 to 1965 resulted principally from the effect of the 1960, 1961 and 1965 amendments. These changes significantly liberalized the requirements for entitlement to benefits and brought a sizable increase in the number of applications for benefits and in the number of awards. Another important factor was the reduction of the minimum retirement age for men from 65 to 62, which also increased the number of claims processed. The total number of awards increased from less than 2.0 million in 1960 to an average of 2.4 million per year in 1961–65.

Despite the rise in administrative costs in terms of dollars, unit costs—the cost, for example, of establishing and maintaining an earnings record account or the cost of adjudicating a claim—have been reduced in terms of dollars of constant pur-

³ The administrative costs incurred in handling the earnings reports and in adjudicating claims are relatively larger for these groups than for others.

chasing power. Improved administrative operating techniques, including the greater use of electronic data-processing equipment, have brought about this reduction.

The ratio of administrative expenses to contribution income during 1940-65 has, with few exceptions, fluctuated between 2 percent and 3 percent. Since calendar year 1960, it has remained at about 2 percent.

The ratio of administrative expenses to benefit payments was almost 75 percent in 1940, the first year that monthly benefits were paid. It then dropped sharply, to 30 percent in 1941, and subsequently has declined continuously, falling to about 2 percent in 1957-65.

For the first 18 years the ratio of administrative expenses to taxable payroll was 0.08 percent or less; it was somewhat higher in the most recent years (1959-65) because of changes in the law that have considerably liberalized the program, thus adding to the work loads, without any increase in the amount of earnings subject to tax, which has remained at \$4,800. (This figure was increased to \$6,600 in the 1965 act, to be effective in 1966.) The ratios indicate clearly the relatively low cost of administering the old-age and survivors insurance program.

Administrative expenses for old-age and survivors insurance may also be compared with interest earned by the trust fund. Administrative expenses during 1940-65 amounted to \$3,120 million and the interest earnings of the trust fund to \$9,080 million, or about three times as much. In 1965, the \$327 million spent for administration represented about 55 percent of the interest earned by the trust fund.

Disability Insurance

The administrative expenses in the first few years of operation of any social insurance program are not typical of the long-run situation. The disability insurance trust fund began operations in 1957, but contributions were deposited in the fund only during the last 11 months of that year, and benefit disbursements were made only during the last 5 months. Accordingly, the administrative expenses in 1957 represented a relatively high proportion (37 percent) of benefit payments, but a low proportion (3 percent) of

contributions (table 2). As a proportion of total taxable payroll, administrative expenses for the disability insurance program amounted to only 0.011 percent.

TABLE 2.—Administrative expenses of the disability insurance program in relation to contribution income, benefit payments, and taxable payroll, 1957-65

Calendar year	Total amount ¹ (in millions)	As percent of—		
		Contributions	Benefit payments	Taxable payroll
1957-65.....	\$511.4	5.6	6.9	0.027
1957.....	20.8	3.0	36.7	.011
1958.....	26.3	2.7	10.6	.015
1959.....	33.9	3.7	7.4	.017
1960.....	48.3	4.8	8.5	.023
1961.....	66.8	6.4	7.5	.032
1962.....	66.9	6.4	6.1	.031
1963.....	72.8	6.6	6.0	.032
1964.....	84.5	7.3	6.5	.036
1965.....	91.1	7.7	5.8	.037

¹ See footnote 1, table 1.

² Preliminary estimates.

For the 9-year period, administrative expenses in relation to contributions have increased steadily—from a ratio of about 3 percent in the early years to 7.7 percent in 1965. This ratio will decrease in 1966, as a result of the increase in the contribution rate allocated to this program under the 1965 amendments. For the same period, the ratio of administrative expenses to benefit payments decreased and was at a level of about 6 percent in 1962-65. The ratio of administrative expenses to taxable payroll rose during the period and was at a level of about 0.035 percent in the last 5 years; it will decrease somewhat for 1966, because of the increase in the earnings base under the 1965 amendments.

The dollar amount of the administrative expenses of the disability insurance program will probably continue to grow as the number of persons becoming insured for benefits rises and the number on the rolls increases. It is likely, however, that the rate of growth will be slower than it has been in the past.

The growth in the cost of administering the disability insurance program can be attributed primarily to legislative liberalizations. The first significant liberalization occurred in 1958, when benefits to dependents of disabled workers were first paid. The second was enacted in 1960, when the age-50 limitation for entitlement to monthly disability benefits was eliminated. The full effect of this change was felt in 1961, when 433,000

determinations of workers' disability were made. This total represented an increase of 48 percent from that of the preceding year. Another factor in the growth of administrative expenses is, of course, the normal maturing of the disability beneficiary rolls.

The Combined Program

Table 3 presents an analysis of the combined administrative expenses for old-age and survivors insurance and for disability insurance in the calendar years 1957-65, when both programs were in operation. Throughout this period—when, on the whole, benefit disbursements were slightly higher than contribution income—administrative expenses represented about 2.3 percent of either contributions or benefit outgo, with relatively little trend apparent. The ratio of administrative expenses to total taxable payroll rose steadily, however, from 0.09 percent in 1957 to 0.17 percent in 1965. This trend resulted in part from the growth of the disability insurance program, which costs relatively more to administer than old-age and survivors insurance, and from liber-

TABLE 3.—Administrative expenses of the combined old-age, survivors, and disability insurance program in relation to contribution income, benefit payments, and taxable payroll, 1957-65.

Calendar year	Total amount (in millions)	As percent of—		
		Contri- butions	Benefit payments	Taxable payroll
1957.....	\$164	2.2	2.2	0.09
1958.....	207	2.4	2.4	.11
1959.....	234	2.6	2.3	.12
1960.....	240	2.0	2.1	.12
1961.....	303	2.5	2.4	.14
1962.....	322	2.5	2.2	.15
1963.....	348	2.2	2.3	.15
1964.....	375	2.2	2.3	.16
1965.....	418	2.4	2.3	.17

alizations in the old-age and survivors insurance program enacted without a corresponding increase in the earnings base.

For the entire period (1940-65) that monthly benefits have been payable, administrative expenses have represented 2.3 percent of contributions, 2.6 percent of benefit payments, and 0.10 percent of taxable payroll. It is clear that, whatever base is used, administrative expenses paid out of the trust funds—in other words, out of the contributions of workers and employers—are low. By far the greatest part of such contributions is thus available for benefit payments.