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THE 1968 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND

LETTER

FROM

THE BOARD OF TRUSTEES
FEDERAL SUPPLEMENTARY INSURANCE TRUST FUND

TRANSMITTING

THE 1968 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND

MARCH 27, 1968.—Referred to the Committee on Ways and Means, 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., March 25, 1968.

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

SIR: We have the honor to transmit to you the 1968 Annual Report of the Board of Trustees of the Federal Supplementary Medical Insurance Trust Fund (the 3d such report), in compliance with the provisions of section 201(c) of the Social Security Act, as amended.

Respectfully,

HENRY H. FOWLER,
Secretary of the Treasury, and
Managing Trustee of the Trust Fund.
W. WILLARD WIRTZ,
Secretary of Labor.
WILBUR J. COHEN,
Acting Secretary of
Health, Education, and Welfare.
ROBERT M. BALL,
Commissioner of Social Security, and
Secretary, Board of Trustees.

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THE 1968 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.

Fiscal Year Highlights

The fiscal year 1967 was the first full year of operation of the supplementary medical insurance program insofar as both premiums and benefit payments are concerned (since benefits were first available on July 1, 1966, premium collections started then).

Premiums collected in fiscal year 1967 amounted to $647 million, while the matching contributions from the general fund of the Treasury amounted to $623 million. The deficiency of $24 million in Government matching funds will be made up in fiscal year 1968.

Total receipts of the trust fund amounted to $1,284 million in fiscal year 1967. In addition to contributions, receipts consisted of $14 million in interest on investments.

Total disbursements from the trust fund in fiscal year 1967 amounted to $798 million. Of this amount, $664 million was paid out for benefits (this amount is based on Treasury statements; an additional $5 million has been identified by carriers as benefit withdrawals in fiscal year 1967 that did not clear through the Treasury before July 1, 1967). The remaining $134 million was for administrative expenses, which were relatively high as compared with benefit disbursements because the former were relatively high due to the initial expenses in establishing the program and because the latter were relatively low due to the inherent lags in making the benefit payments. The actual outgo for benefits in this first year of operation was 13 percent lower than the original estimate, which was contained in the 1966 trustees report; this difference resulted primarily from the lag in the actual benefit disbursements being significantly greater than had been originally estimated.

The excess of total income over total outgo, amounting to $486 million, represented the total assets of the trust fund on June 30, 1967.

After the close of fiscal year 1967, Congress made extensive amendments to the Social Security Act directly affecting the supplementary medical insurance program. These amendments made significant changes in the benefit provisions, insofar as costs are concerned. These provisions are described more fully in another section of this report,

and their effects are taken into account in the actuarial cost estimates presented in this report.

The promulgation of the premium rate for the period April 1968 through June 1969; namely, a standard premium rate of $4 per month—also took into account the changes made by the 1967 amendments. Appendix I gives a statement of the actuarial assumptions and bases employed in arriving at the new premium rate.

Legislation in 1967

Public Law No. 90–97, approved September 30, 1967, extended the general enrollment period for the supplementary medical insurance program that had been scheduled for October through December 1967, so that it would run through March 1968. The initial $3 monthly premium rate was continued through March 1968, instead of through December 1967, and the promulgation by the Secretary of Health, Education, and Welfare of the new standard premium rate (for persons enrolling in the earliest possible enrollment period) was delayed so that it could occur any time before January 1, 1968—to be applicable for the period April 1968 through December 1969 (which period was changed by subsequent legislation).

The Social Security Amendments of 1967 (Public Law 90–248, approved January 2, 1968) affect significantly the future levels of income and disbursements under the supplementary medical insurance program. Benefit protection was expanded. Eligibility requirements for the payment of benefits were liberalized. Some modifications in the coverage provisions were made.

The more important changes, significant from an actuarial standpoint, are presented below:

1. Effective April 1, 1968, the outpatient diagnostic services which were previously covered under hospital insurance will be covered for benefit purposes under the supplementary medical insurance program.
2. Effective April 1, 1968, the deductible and coinsurance provisions formerly applicable to the professional component of pathology and radiology services furnished to inpatients in hospitals will no longer be applicable.
3. Effective July 1, 1968, broader coverage of outpatient physical therapy services is provided, primarily in instances where the individual is not homebound.
4. Effective April 1, 1968, the supplementary medical insurance program will cover the costs of ancillary services furnished in hospitals that are not covered under the hospital insurance program (e.g., because the individual had exhausted his hospital benefits under that program or was not covered thereunder).
5. Claims will now have to be filed no later than the end of the calendar year following the year when the services were rendered except that the limit for services furnished in October through December of any year is the end of the second calendar year following such year.
6. The standard premium rate is to be determined on an annual basis for periods beginning with each July (instead of a biennial calendar year basis), except that the premium rate promulgated for the period beginning April 1968 is to be applicable through June 1969.

7. The general enrollment periods will be January through March of each year (instead of October through December of odd-numbered years). Enrollees will be permitted to disenroll at any time (effective at the end of the following quarter), instead of only during general enrollment periods.

8. Whenever the transfer of matching funds from the general fund of the Treasury is not made simultaneously with the enrollee contributions, an appropriate interest adjustment is to be made (applicable only to transactions after June 30, 1967).

9. The availability of the contingency reserve based on appropriations from the general fund of the Treasury, with any amounts used being repayable, was extended for 2 years (i.e., until December 31, 1969).

The effect of the foregoing benefit changes is to increase the cost of the program by about 6 percent relatively.

Appendix II gives a summary of the provisions of the supplementary medical insurance program as it is constituted following the enactment of the 1967 amendments.

Summary of the Operations of the Trust Fund, Fiscal Year 1967

A statement of the income and disbursements of the Federal supplementary medical insurance trust fund during fiscal year 1967 and of the assets of the fund at the beginning and end of the fiscal year is presented in table 1.

TABLE 1.—STATEMENT OF OPERATIONS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND DURING THE FISCAL YEAR 1967

Receipts, fiscal year 1967:		
Premiums from participants:		
Deducted from benefits [1]	$527,901,607.14	
Deposited by States	32,135,900.00	
Collected by Social Security Administration [2]	86,644,135.41	
Total premiums		$646,681,642.55
Contributions from general fund of the Treasury		623,000,000.00
Interest:		
On investments	$15,041,275.05	
Less interest on amounts transferred to the old-age and survivors insurance trust fund for administrative expenses	989,000.00	
Net interest		14,052,275.05
Total receipts		1,283,733,917.60
Disbursements, fiscal year 1967:		
Benefit payments		664,260,684.06
Administrative expenses:		
Department of Health, Education, and Welfare [3]	$107,969,999.30	
Treasury Department	9,745.00	
Civil Service Commission	41,830.00	
Reimbursement to old-age and survivors insurance trust fund—		
For expenses in fiscal year 1966 [4]	24,136,504.00	
For expenses in fiscal year 1967 [5]	1,405,000.00	
For construction of facilities for Social Security Administration	129,889.00	
Gross administrative expenses	133,692,967.30	
Less receipts for sale of surplus supplies, materials, etc	10,879.22	
Net administrative expenses		133,682,088.08
Total disbursements		797,942,772.14
Net addition to the trust fund		485,791,145.46
Total assets of the trust fund, June 30, 1967		485,791,145.46

[1] Transferred from the old-age and survivors insurance and disability insurance trust funds, the railroad retirement account, and the civil service retirement and disability fund.

[2] With respect to uninsured persons and insured persons not receiving monthly benefits.

[3] Including administrative expenses of the carriers.

[4] $24,095,779 for expenses of the Department of Health, Education, and Welfare and $40,725 for expenses of the Civil Service Commission.

[5] For expenses of the Public Health Service.

The total assets of the trust fund amounted to $486 million on June 30, 1967. Since the operations of the trust fund began on July 1, 1966, it had no assets at the beginning of the fiscal year 1967.

Net receipts of the fund amounted to $1,284 million. Of this total, $647 million represented premium payments by the enrollees, and $623 million represented the matching contributions from the general fund of the Treasury (the deficiency of $24 million will be made up, along with appropriate interest after June 30, 1967, in fiscal year 1968). The remaining $14 million of receipts consisted of net interest on the investments of the fund.

Disbursements from the fund during the fiscal year 1967 totaled $798 million. Of this total, $664 million was for benefit payments.

The remaining disbursements amounted to $134 million for net administrative expenses.

The assets of this fund at the end of fiscal year 1967 totaled $486 million, consisting of $479 million in the form of obligations of the U.S. Government and $7 million in undisbursed balances. Table 2a shows the distribution of the total assets of the fund at the end of fiscal year 1967

TABLE 2-a.—ASSETS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND BY TYPE, AT END OF FISCAL YEAR 1967

	Par value	Book value [1]
Investments in public debt obligations sold only to this fund (special issues):		
Certificates of indebtedness, 4¾ percent, 1968	$31,923,000	$31,923,000.00
Notes:		
4¾ percent, 1969	31,923,000	31,923,000.00
4¾ percent, 1970	31,923,000	31,923,000.00
4¾ percent, 1971	31,923,000	31,923,000.00
4¾ percent, 1972	31,923,000	31,923,000.00
4¾ percent, 1973	31,923,000	31,923,000.00
4¾ percent, 1974	287,311,000	287,311,000.00
Total, investments in public debt obligations	478,849,000	478,849,000.00
Undisbursed balances		6,942,145.46
Total assets		485,791,145.46

[1] Par value, plus unamortized premium, less discount outstanding.

The 1965 amendments provided that the public-debt obligations issued for purchase by the supplementary medical insurance trust fund shall have maturities fixed with due regard for the needs of the trust fund. In implementing the similar provision for the old-age and survivors insurance and disability insurance trust funds, the maturity dates for the holdings of special issues are spread as nearly as practicable in equal amounts over a 15-year period.

On June 30, 1967, special issues held by the supplementary medical insurance trust fund were distributed in equal amounts of $31,923,000 maturing in each of the 7 years, 1968–74. In addition, $255,388,000 (representing 8 years' annual amounts at the foregoing $31,923,000 rate) was invested in 7-year notes bearing 4¾-percent interest and maturing on June 30, 1974.

The 7-year notes amounting to $255,388,000 were acquired on June 30, 1967, under the following circumstances: If, on June 30, 1967, the trust fund holdings of special issues had been spread equally over a 15-year period, it would have been necessary for the Treasury to

issue, for purchase by the trust fund, approximately $31,923,000 of bonds maturing in each of the 8 years, 1975–82. Such bonds—with more than 7 years of maturity—would have been required, under present law (31 U.S.C. 753(a)), to bear an interest rate no higher than 4¼ percent. On the other hand, the application of section 1841(c) of the Social Security Act resulted in a rate of 4¾ percent. Accordingly, the sum of $255,388,000 that would have been invested in bonds maturing during the period 1975–82 was, instead, invested in notes that had the longest possible duration to maturity—that is, in 4¾-percent notes maturing June 30, 1974 (which were in addition to the $31,923,000 of notes that had the same maturity date, which were issued as part of the normal 15-year spread, as mentioned previously).

New securities at a total par value of $1,739 million were acquired during the fiscal year through the investment of receipts of the fund and the reinvestment of funds made available from the maturity of securities. The par value of securities redeemed during the year was $1,260 million. A summary of transactions for the fiscal year, by type of security, is presented in table 2b.

TABLE 2-b.—STATEMENT OF TRANSACTIONS IN PUBLIC-DEBT SECURITIES FOR THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND DURING THE FISCAL YEAR 1967

[All amounts represent par values]

	Acquisitions	Dispositions
Obligations sold only to this fund (special issues):		
Certificates of indebtedness:		
4⅜ percent, 1967	$58,919,000	$58,919,000
4½ percent, 1967	110,218,000	110,218,000
4⅝ percent, 1967	424,476,000	424,476,000
4¾ percent, 1967	354,380,000	354,380,000
4¾ percent, 1967	31,923,000	0
5 percent, 1967	145,966,000	145,966,000
5⅛ percent, 1967	104,665,000	104,665,000
5⅜ percent, 1967	61,210,000	61,210,000
Notes:		
4¾ percent, 1969	31,923,000	0
4¾ percent, 1970	31,923,000	0
4¾ percent, 1971	31,923,000	0
4¾ percent, 1972	31,923,000	0
4¾ percent, 1973	31,923,000	0
4¾ percent, 1974	287,311,000	0
Total transactions	1,738,683,000	1,259,834,000

Table 3 compares the actual experience in the fiscal year with the estimates presented in the previous two reports. The actual premium collections have been somewhat higher than the estimates, due to greater participation than had been estimated (the estimates in the 1966 report, based on the data contained in the Budget Document of the United States for the fiscal year 1967, assumed only 80-percent participation—although the original actuarial cost estimates assumed a range of 80 to 95 percent, averaging 87½ percent—whereas the actual participation has been about 92 percent). The actual benefit payments were significantly lower than estimated; this was caused by the fact that the timelag involved in the payment of benefits was much longer than had been estimated. On an incurred basis, rather than on a cash basis, it is estimated that benefit payments in the period July 1966 through December 1967 were about 7 percent higher than the allowance therefor in the premium-rate determination. Since the actual benefit payments were so much lower than in the estimates, the

actual balance in the trust fund at the end of the year considerably exceeded the estimated amount.

TABLE 3.—COMPARISON OF ACTUAL AND ESTIMATED OPERATIONS OF THE SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND, FISCAL YEAR 1967

[Dollar amounts in millions]

	Actual amount	1966 report		1967 report	
		Estimated amount	Estimate as percentage of actual	Estimated amount	Estimate as percentage of actual
Premiums from enrollees	$647	$550	85	$623	96
Government contribution	623	550	88	623	100
Benefit payments	664	765	115	861	130
Assets, end of year	486	205	42	260	53

Note: In interpreting the figures in the above table, reference should be made to the accompanying text.

Actuarial Status of the Trust Fund

In discussing the actuarial status of the supplementary medical insurance program, it is first necessary to consider the experience on an accrual basis and the limitations on the accuracy of the estimates before presenting and discussing the results of these estimates.

(1) Actuarial status of program dependent on accrued experience

The actuarial status of the program, and of the trust fund, can appropriately be measured only on an accrual basis; that is, the solvency of the trust fund depends on the services performed, on the basis of which benefits must be paid. 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 timelag between the time that services are performed and the time that benefits for them are paid. This lag is due to the $50 deductible which must be accumulated before any benefits are payable, the tendency of enrollees to accumulate bills and submit them together (especially at the end of the year), and the time required by carriers to process and adjudicate the bills received.

This liability outstanding at any time for benefits for services performed for which no payment has been made may be referred to as "benefits incurred but unpaid." Estimates of the amount of such benefits incurred but unpaid as of the end of each calendar year according to the "expected" estimates, and of the administrative expenses related to processing these benefits, appear in table 4. Also included in table 4 are estimates of the excess of premiums collected in advance over premiums due and uncollected, and of Government matching contributions due but not yet transferred to the trust fund.

The actuarial status of the program and the financial status of the trust fund at any time can be found by adjusting the balance in the trust fund account by the net of these asset and liability items on that date (as in item C of table 4). The actuarial experience of the program during any period can be obtained by adjusting the cash flow of premiums, matching Government contributions, benefit payments, and administrative expenses to an accrual basis by adding the net increase in each asset or liability item during the period to the corresponding item on a "cash" basis for that period.

TABLE 4.—SUMMARY OF PROJECTED ASSETS AND LIABILITIES OF THE SUPPLEMENTARY MEDICAL INSURANCE PROGRAM, ACCORDING TO "EXPECTED" ESTIMATE, AT END OF CALENDAR YEARS 1966–68

[In millions of dollars]

	As of Dec. 31—		
	1966	1967	1968
A. Assets:			
Premiums due and uncollected, less premiums collected in advance	−$7	−$11	−$11
Government matching contributions due and unpaid, less such contributions with respect to premiums paid in advance	315	18	−7
Actual balance in trust fund	122	412	337
Total assets	430	419	319
B. Liabilities outstanding:			
Benefits incurred but unpaid	363	439	339
Administrative cost for processing that are unrelated to benefits incurred but unpaid	32	43	31
Total liabilities	395	482	370
C. Net actuarial surplus	35	−63	−51

The dependence of the actuarial status of the program on the accrued experience is recognized in section 1839(b)(2), in which it is stated that the premium rate "shall be such amount as the Secretary estimates to be necessary so that the aggregate premiums for such 12-month period will equal one-half of the total for the benefits and administrative costs which he estimates will be *payable* from the Federal supplementary medical insurance trust fund *for* such 12-month period." [Italic supplied.] Similarly, an assessment of the actuarial status of the program and of the financial status of the trust fund for any period must be made on the basis of estimates of the benefits and administrative expenses "payable * * * for" (i.e., accrued in such period).

(2) *Necessary limitations on accuracy of estimates of past and future experience*

There are many difficulties in projecting the cost of a service benefit program that are not encountered in projecting the cost of cash benefit programs, due to the many economic and social factors involved. This is especially so as to the rate at which physicians may increase their fees and as to the increase in utilization of services that will gradually result from placing physician services within the financial means of over 92 percent of those aged 65 or older. Further difficulties result from the absence of firm estimates of the present and immediate past experience of the program, on which projections of future experience can be based (as discussed in appendix IV); and any errors in the former are necessarily incorporated into the latter. The "expected" estimates of the 1966 experience could vary as much as 10 percent from the actual experience, and estimates for later years could vary further from the actual experience.

Final conclusions as to the accrued experience of the program for 1966–67 will not be possible until the deadline for filing claims based on services performed during 1966–67 has passed, all claims have been adjudicated and decided by carriers, payment records covering all benefit payments have been prepared by carriers and forwarded to Social Security Administration, and the payment records pertaining to benefits paid through the deadline for filing claims based on services received during 1967 have been reconciled with the benefits actually paid from the trust fund for this period.

(3) Expected estimates

The financing of this program is essentially different from that for the cash benefit programs in that the premium is only set for a 1-year period (except for the period from April 1968 through June 1969); consequently, estimates are needed only for 1½ years into the future. Thus, there is not the same need for estimates of the highest cost and lowest cost experience that might be reasonably expected over many years into the future, so that the financing of the system can be set at the middle of the range between what would be necessary to finance the highest cost experience thought reasonably possible and the lowest cost experience thought reasonably possible. Further, the premium rate is required by law to be based on the best estimate possible of the benefits and administrative expenses that can be expected to accrue for services performed during the period to which such rate is to be applicable. Such an estimate can be referred to as an "expected" estimate.

The "expected" estimates of the cost per capita of benefits and administrative expenses that was accrued during calendar years 1966–67, and that anticipated for calendar years 1968–70, appear in table A in appendix IV. Since the $50 deductible applies to each calendar year, these costs can be developed only for calendar year periods; however, the premium rate is to be determined for fiscal year periods (except for the initial period July 1966 through March 1968 and the period from April 1968 through June 1969). The prorated average monthly rate of these costs for the periods to which a particular premium rate is applicable are as follows:

Period	Applicable premium rate	Benefit payments	Administrative costs	Total disbursements
July 1966–March 1968	$3	$5.00	$0.72	$6.42
April 1968–June 1969	4	7.22	.66	7.88

The premium rate for the period from July 1966 through March 1968 was about 7 percent lower than the combined benefits and administrative expenses accrued during this period. The slightly unfavorable experience during this period resulted primarily from an increase of approximately 15 percent in the average fees charged by physicians between July 1965 (when the premium rate was determined) and July 1967 (the approximate mid-point of the period in which the benefits were paid), as compared with the 6-percent increase assumed for this period. Further, the administrative expenses were higher than originally estimated (on a continuing basis)—the actual ratio of administrative expenses to benefit payments on an accrual basis was 10 percent in 1967, as against the estimate of 8½ percent.

(4) Expected estimates of the accrued experience

The expected estimates for the accrued experience of the supplemental medical insurance program for calendar years 1966-68 appear in table 5. Premiums and Government matching contributions were assumed to be paid for the estimated actual enrollment during 1966–67; in later years, 92 percent participation was assumed. As of July 1967, it is estimated that approximately 92 percent of persons aged 65 or over in the United States were enrolled.

The standard premium rate for periods after June 1969 will be determined for each fiscal year before the beginning of the calendar year in which such fiscal year begins.

TABLE 5.—ESTIMATED INCOME AND DISBURSEMENTS PAYABLE (ACCRUAL BASIS) UNDER SUPPLEMENTARY MEDICAL INSURANCE PROGRAM, CALENDAR YEARS 1966-68

[In millions of dollars]

Calendar year	Premiums from participants	Government contributions	Benefit payments	Administrative expenses	Interest on fund	Net of operations in year	Accumulated surplus at end of year
1966	$315	$315	$491	[1] $107	$3	$35	$35
1967	636	636	1,272	121	23	−98	−63
1968	832	832	1,525	147	20	+12	−51

[1] Administrative expenses shown include those incurred in 1965 and 1966.

Note.—Experience on accrued basis for period from Apr. 1, 1968 through June 30, 1969, is estimated to be as follows (in millions of dollars):

Premiums	Government contribution	Benefits	Administrative expenses	Interest	Net in period	Accumulated surplus at end of period
1,117	1,117	2,002	199	30	63	−60

Benefit payments have been projected from the expected estimates of per capita costs that are shown in table A of appendix IV assuming the same average enrollment as for premium income. Administrative expenses as projected on a cash basis, and adjusted to an accrual basis by assuming that processing costs relating to benefits incurred but unpaid at the end of any calendar year are 9 percent of such benefit payments.

The trust fund balances shown in the various tables presented in this report do not include the contingency reserve that is authorized to be available until December 31, 1969. The size of this reserve is to be $18 times the estimated number of persons who were eligible to participate in the program on July 1, 1966, if they had so elected. Any amount appropriated and drawn would be repayable without interest from future income of the program.

As can be seen by examination of table 4, the program netted an estimated surplus of $35 million on an accrual basis during calendar year 1966, an abnormal period due to the application of the full $50 deductible in a 6-month period and due to considerable nonrecurring startup expenses. Due to the inadequacy of the $3 premium rate (by about 7 percent), benefit payments and administrative expenses incurred exceeded accrued income during calendar year 1967 by an estimated $98 million, leaving an estimated deficit of $63 million on an accrual basis for the initial 1½-year period. The estimated accrued deficit increased during the first quarter of 1968 by $60 million to reach approximately $123 million by March 31, 1968.

The increased premium rate for April 1968 through June 1969 results in an estimated net accrued surplus for the last 9 months of 1968 amounting to $72 million, which reduces the estimated net accrued deficit to $51 million as of December 31, 1968.

Interest earnings of $30 million are estimated to be earned during this 18-month period at an interest rate of 5 percent per year on the

average balance in the trust fund. As explained previously, the large positive balance in the trust fund is a result of the natural delay between the date that services are performed and benefits accrued and the date on which benefit payments made on the basis of the services are paid. The balance in the fund during 1966–67, and in the beginning of 1968, was unusually large due to the newness of the program and the lack of familiarity of many enrollees with reimbursement insurance. The interest earned on these unusually large balances will contribute about half of the decrease expected in the net accrued deficit during the period from April 1968 through March 1969. Thus, income derived from those enrolled during 1966–67 will contribute substantially toward reducing the deficit incurred in that period.

(5) Expected estimates of the experience on a cash basis

The income and disbursements of the trust fund on a cash basis for calendar years 1966–67 and projected for calendar years 1968–69 according to the expected estimates appear in table 6. Cash income exceeded cash disbursements during 1966–67 by a large margin, resulting in a large cash balance in the trust fund at the end of 1967 of $412 million, although the program actually had an estimated net deficit of $63 million on that date, due to the large liabilities outstanding on account of incurred but unpaid claims. Cash disbursements are expected to exceed cash income during calendar year 1968 due to the inadequacy of the $3 premium rate during the first quarter of the year and due to an assumed reduction of $112 million in the liabilities for incurred but unpaid benefits and for the cost of processing such benefits.

TABLE 6.—ESTIMATED PROGRESS OF SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND, CALENDAR YEARS 1968–69, AND ACTUAL DATA FOR 1966–67

[In millions of dollars]

Calendar year	Premiums from participants	Government contributions	Benefit payments	Administrative expenses	Interest on fund	Balance in fund at end of year
Actual experience:						
1966	$322	----------	$128	[1] $75	$3	$122
1967	640	$933	1,196	110	23	412
Expected estimate:						
1968	832	857	1,625	159	20	337
1969 [2]	903	903	1,707	173	17	280
High-cost estimate:						
1968	832	857	1,780	163	14	172
1969 [2]	903	903	2,081	187	[3] 2	(3)

[1] Administrative expenses shown include those incurred in 1965 and 1966.
[2] Experience that would result if the premium rate remained at $4 after June 1969.
[3] Would require use of contingency fund that is authorized to be available from the general fund of the Treasury (maximum of $342,000,000).

(6) High-cost estimates

Although the premium is set, and the actuarial status of the program and the trust fund is determined, by the "expected" estimate of the future experience of the program, there is the question of the adequacy of cash resources should the developing experience follow the highest cost assumptions that appear reasonable in the immediate future. Accordingly, it seems desirable to test out this matter using such high-cost assumptions, as contrasted with those that are expected.

Such estimates were prepared using the high portion of the range thought reasonably likely for each assumption that is required in estimating the current and future experience. These estimates are appropriate only for measuring the adequacy of the cash balance in the trust fund if the experience turns out to be as high as can reasonably be anticipated.

Comparisons of the cash resources of the trust fund with the disbursements that would result if the experience that developed produced as high a cost as might reasonably be expected appear in tables 6 and 7. As can be seen from table 7, under these conditions, there would be a slight cash deficit in the trust fund by the end of fiscal 1968, a circumstance that would require a transfer from the authorized contingency reserve. Under these adverse conditions (which are not anticipated based on current information available), the premium rate would presumably be increased, effective July 1969, which would solve the cash problem of the program. An additional margin would, however, have to be incorporated into future premium rates—both to insure adequate cash to pay benefits and to rebuild the balance in the trust fund to a reasonable level.

The very small cash deficit that would result if the experience followed the highest cost assumptions that appear reasonable provides assurance that there will be enough funds to pay benefits—in effect, by borrowing from the reserves for incurred but unpaid claims.

(7) Summary of actuarial status of program

The actuarial status of the program and the financial status of the trust fund depend on the determination and measurement of the accrued income and benefit payments and administrative expenses accrued under the program. Due to the small inadequacy of the initial $3 rate, there was an estimated net deficit in the operations of the program from July 1966 through March 1967 of about 7 percent and hence in the estimated accrued balance at the end of this period. However, due to the normal delay between the time that services were furnished and the time at which benefits were claimed on the basis of these services, there was an adequate cash balance in the trust fund, and the cash balance will continue to be adequate through fiscal year 1969, considering the availability of the contingency fund, even if the experience follows high-cost assumptions.

The premium rate of $4 that is set for the period April 1968 through June 1969 will, according to the expected estimate, result in an estimated net surplus to the program that will reduce the estimated net deficit to about $60 million, about half of the estimated net deficit at the beginning of this period.

Expected Operations and Status of the Trust Fund During the Period July 1, 1967, to June 30, 1970

The estimated progress of the supplementary medical insurance trust fund on a cash basis during fiscal years 1968–70 according to the expected estimates appears in table 7. Cash income during fiscal year 1967 exceeded cash disbursements by $486 million, leaving a balance in the trust fund of this amount as of June 30, 1967. This amount exceeded by a small margin the benefit payments and process-

ing costs related thereto based on services furnished prior to June 30, 1967, that would subsequently be claimed, adjudicated, and paid. Such liabilities outstanding as of June 30, 1967, for benefit payments and administrative expenses incurred but unpaid were unusually large due to the newness of the program and the lack of familiarity of many enrollees with reimbursement insurance.

According to the expected estimate of the benefits that will be paid during fiscal year 1968, benefit payments will exceed benefits accrued, thus reducing the liability outstanding at the end of the period for benefits incurred but unreported. This is equivalent to the assumption that the average delay from the time that services are performed and the time at which benefits based on these services are paid will decrease, as the enrollees become familiar with the program and claim benefits more promptly, as the administrative system becomes routine, and as a result of provision in the 1967 amendments for payment on the basis of an itemized bill when there is no assignment, rather than requiring a receipted bill. Consequently, cash disbursements during fiscal year 1968 are estimated to exceed cash income by a relatively large amount as compared to the estimated net deficit on an accrued basis, due to this reduction anticipated in liabilities outstanding. As a result, the balance in the trust fund is estimated to be reduced to $348 million at the end of fiscal year 1968.

TABLE 7.—ESTIMATED PROGRESS OF SUPPLEMENTARY MEDICAL INSURANCE TRUST FUND, FISCAL YEARS 1968–70, AND ACTUAL DATA FOR 1967

[In millions of dollars]

Fiscal year	Premiums from participants	Government contributions	Benefit payments	Administrative expenses	Interest on fund	Balance in fund at end of year
Actual experience:						
1967	$647	$623	$664	[1] $134	$14	$486
Expected estimate:						
1968	714	739	1,473	139	21	348
1969	895	895	1,656	167	19	334
1970 [2]	909	909	1,766	179	14	221
High-cost estimate:						
1968	714	739	1,502	139	20	318
1969	895	895	1,947	176	8	−7

[1] Administrative expenses shown include those incurred in fiscal 1966 and 1967.
[2] Experience that would result if the premium rate remained at $4 after June 1969.

For fiscal years 1969 and 1970, the liability outstanding for benefits incurred but unreported are assumed to remain a constant amount. This assumption implies that the delay between the accrued date and the payment date of benefits will be reduced slightly (the benefit payments accrued that are assumed to be incurred but unpaid are then a lower percentage of the total benefit payments, which gradually increase). As a result, cash benefit payments in fiscal years 1969–70 are assumed to be equal to those accrued.

According to the "expected" estimates—that is, the best estimates that can be made based on information currently available of the experience most likely to occur—there will be an estimated net gain (that is, an excess of accrued income over benefit payments and administrative expenses accrued) during fiscal year 1968. This results from the fact that the $4 premium rate for this period is estimated to

be adequate to finance the program on an accrual basis. Due to the assumed reduction during this period in the liabilities outstanding for benefits and administrative expenses incurred but unpaid, however, cash disbursements are expected to exceed cash income in this period, with the result that the balance in the trust fund is estimated to decrease slightly, to $334 million at the end of fiscal year 1969.

If the experience that develops should follow the highest cost assumptions that appear reasonable—that is, substantially more adverse than expected—the balance in the trust fund would decline to $318 million at the end of fiscal year 1968 and would be exhausted at the end of fiscal year 1969, a situation that would require the appropriation and use of some of the contingency fund that is authorized for use through the end of calendar year 1969. The fact that there would be adequate assets in the trust fund to pay benefits throughout the period for which the $4 premium rate has been set (and considering the availability of the $342 million contingency reserve) shows that this premium rate will provide adequate revenue to meet benefit obligations until the premium rate can be increased, even under very unfavorable experience—substantially more adverse than expected.

Conclusion

According to the best estimates that can be made based on information currently available as to the actual experience that will develop in the immediate future, the premium rate promulgated for the period April 1968 through June 1969 is slightly more than sufficient to finance the cost of benefit payments and administrative expenses that will accrue in this period. Further, the estimated net deficit of the program, as measured on an accrual basis, that resulted from the slight inadequacy of the initial premium rate (applicable for July 1966 through March 1968), amounted to $123 million on March 31, 1968, but will be reduced to $60 million on June 30, 1969.

Due to the absence of conclusive data as to the accrued cost of the program during 1966–67 upon which to base projections of future experience, a variation of more than 10 percent from the best, or "expected," estimate of future experience is quite possible. But there will be an adequate cash flow under the program from which to pay benefits and administrative expenses throughout this period, even if experience should produce the highest cost that appears reasonably possible based on information currently available. The availability of sufficient funds to pay benefits is further guaranteed by the availability of the authorized contingency reserve of $342 million until the end of 1969. Thus, the financing of the supplementary medical insurance program can be considered to be on a financially sound basis throughout the period from April 1968 through June 1969.