

survivors, and disability insurance program is sound, and, based on the best estimates available, the contribution schedule now in the law makes adequate provision for meeting both short-range and long-range costs."

The Advisory Council appointed by Secretary Celebrezze in 1963, then, is the sixth major advisory group to consider social security. It is, however, the first since the Advisory Council on Social Security of 1947-48 to make a comprehensive review of the old-age, survivors, and disability insurance program.

Even though the statutory provision for future advisory councils does not call for another extensive review of the program, citizen groups will most likely be called upon again to make comprehensive studies of old-age, survivors, and disability insurance. Because of the importance of the program to virtually every American family and because of the outstanding contributions made by past councils, we can expect that the advisory-council technique will continue to play a prominent role in program appraisal and the making of program recommendations.

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## Notes and Brief Reports

### Old-Age, Survivors, and Disability Insurance: Administrative Expenses\*

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 only about  $\frac{1}{10}$  of 1 percent.<sup>1</sup> 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 is  $\frac{1}{2}$  of 1 percent of earnings; the self-employed contribute at a rate of  $\frac{3}{8}$  of 1 percent.

Contributions for the old-age and survivors insurance aspects 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  $\frac{7}{4}$  percent of

earnings up to \$4,800 a year, and for the self-employed the rate is 5.4 percent. These rates are scheduled to rise to  $8\frac{1}{4}$  percent and 6.2 percent, respectively, in 1966; they will be  $9\frac{1}{4}$  percent and 6.9 percent from 1968 on. The trust funds are also credited with receipts from the sale of miscellaneous services and supplies for which the initial outlays have been made from the trust funds—for example, preparation of statistical tabulations for other Government agencies.

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; they include (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.

Since January 1, 1940, administrative costs have also been paid from the trust funds.<sup>2</sup> They are clearly allocable in some instances 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 month by month 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. The program ex-

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<sup>1</sup> For earlier analyses of administrative costs, see the *Bulletin*, May-June 1960, pages 23-28, and March 1958, pages 13-16.

<sup>2</sup> 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.

penses incurred by the Department of Health, Education, and Welfare—primarily 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 1962, about 266 million separate earnings items were reported for approximately 75 million different persons. About 4.5 million new account numbers were issued in that year. This total was roughly 1 million more than that in earlier years, largely because of the use by the Internal Revenue Service of the numbers for income-tax control purposes. In addition, about 3.2 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 2.3 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 1962 about 3 million individuals were awarded monthly benefits, and about 892,000 lump-sum death payments, based on the earnings records of 865,000 deceased workers, were made. At the end of the year, monthly benefits were going to more than 18 million persons, including about 740,000 disabled-worker beneficiaries and 534,000 of their dependents. During the year, benefits were terminated for about 1.5 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 allowed 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. Costs related to child's benefits payable to disabled children aged 18 and over of retired or deceased workers are paid from the old-age and survivors insurance trust fund. In actual practice, these State agency costs are allocated between the two trust funds on about the same basis as the other operating costs of the disability program.

Construction costs for the central office building in Baltimore are another administrative expense item. Through the end of 1962 they amounted to about \$32.2 million; the total will amount to about \$36.3 million. These construction costs are charged as a current administrative expense although they are really a capital item. As a result, administrative expenses are somewhat overstated during the years in which these costs were charged. 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 the programs. Specifically, these are the Government's balancing cost for the civil-service retirement program<sup>3</sup> and the costs of the unemployment compensation program for Federal workers and the Federal employees' compensation program (workmen's compensation).

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 fund. They include space provided in Government buildings (rent is paid for other office space), personnel administration work by the Civil Service Commission, and costs for storage of records by the General Services Administration.

In old-age, survivors, and disability insurance as in private pension plans and group insurance programs, 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 cur-

<sup>3</sup> Before the middle of 1957, none of the cost to the Government for this program was met from the trust funds. 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 8¼ percent of payroll according to the valuation made in 1958).

rently, 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 1957-62.

[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

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 based on 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 \$253 million by 1962 (table 1). The 1962 total includes expenses of \$42.6 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 1951-62. 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 1951-62 rise in costs resulted to some degree from these factors but perhaps 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.<sup>4</sup>

Other factors in this great increase in costs were (1) the introduction of the disability freeze (maintaining the benefit rights of permanently and totally disabled insured workers); (2) the liberalization of the retirement 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 mini-

imum 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 1962 resulted principally from the 1960 and 1961 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 more than 2.5 million a year in 1961 and 1962.

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

TABLE 1.—Administrative expenses of the old-age and survivors insurance program in relation to contribution income, benefit payments, and taxable payroll, 1940-62

Calendar year	Total amount <sup>1</sup> (in millions)	As percent of—		
		Contributions	Benefit payments	Taxable payroll
1940-62.....	\$2,225	2.2	2.6	0.08
1940.....	26	4.1	74.3	.08
1941.....	26	3.3	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 <sup>2</sup> .....	253	2.1	1.9	.12

<sup>1</sup> Adjusted to reflect the deferred transfers relative 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.

<sup>2</sup> Preliminary estimates.

TABLE 2.—Administrative expenses of the disability insurance program in relation to contribution income, benefit payments, and taxable payroll, 1957–62

Calendar year	Total amount <sup>1</sup> (in millions)	As percent of—		
		Contributions	Benefit payments	Taxable payroll
1957–62.....	\$265.1	4.7	8.0	0.022
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 <sup>2</sup> .....	69.0	6.6	6.2	.032

<sup>1</sup> See footnote 1, table 1.

<sup>2</sup> Preliminary estimates.

been reduced in terms of dollars of constant purchasing 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 1940–62 has—with few exceptions—fluctuated between 2 percent and 3 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 1957–62.

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 5 years. This figure indicates 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 1940–62 amounted to \$2,225 million and the interest earnings of the trust fund to \$7,391 million, or more than three times as much. In 1962 the \$253 million spent for administration represented less than 50 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 the year, and benefit disbursements were made only during the last 5 months. Accordingly, the administrative expenses represented a relatively high proportion of benefit payments (37 percent) but a low proportion of contributions (3 percent) (table 2). As a proportion of total taxable payroll, administrative expenses for the disability insurance program amounted to only 0.01 percent. In 1962, administrative costs represented 6.2 percent of benefit payments, 6.6 percent of contributions, and 0.03 percent of payroll. Expenses (in dollars) 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.

The growth in the cost of administering the disability insurance program during the first 6 years of experience can be assigned primarily to liberalizations made by Congress. 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 the 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 1957–62, 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 2½ percent of contribution income and 2¼ percent of benefit outgo, with relatively little trend apparent. The rates of administrative expenses to total taxable payroll rose steadily, however, from 0.09 percent in 1957 to 0.15 percent in 1962. This trend resulted in part from the growth of the disability insurance pro-

TABLE 3.—Administrative expenses of the combined old-age, survivors, and disability insurance program in relation to contribution income, benefit payments, and taxable payroll, 1940-62

Calendar year	Total amount <sup>1</sup> (in millions)	As percent of—		
		Contributions	Benefit payments	Taxable payroll
1940-62.....	\$2,490	2.4	2.8	0.09
1957.....	164	2.2	2.2	.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 <sup>1</sup> .....	322	2.5	2.2	.15

<sup>1</sup> Preliminary estimates.

gram, which costs relatively more to administer than old-age and survivors insurance.

For the entire period (1940-62) that monthly benefits have been payable, administrative expenses have represented 2.4 percent of contributions, 2.8 percent of benefit payments, and 0.09 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 relatively low. By far the greatest part of such contributions is thus available for benefit payments.

## Independent Health Insurance Plans, 1962\*

“Independent” group health insurance plans in the United States had an estimated enrollment at the end of 1962 of 7 million persons for hospital care, about 8 million for surgical-obstetrical service and for in-hospital medical service, and somewhat more than 7 million for in-hospital medical service and office, clinic, and home visits. The plans had a total income of \$475 million in 1962 and expended \$430 million for benefits and \$32 million for administrative expenses.

The “independent” health insurance plans are all private organizations that are not Blue Cross plans, Blue Shield plans, or insurance companies and that provide specified health services and/or supplies or make benefit payments for them on a group prepayment, risk-spreading basis. If the plan does not itself provide the services, it may make payment directly to the supplier of the

\* Prepared by Louis S. Reed, Division of Research and Statistics.

services or it may reimburse the covered individual for his expenditures for them.

The plans are of five main types: (1) community plans, serving the general community or a consumer group and controlled by persons selected to represent the community or consumer group; (2) employer-employee-union plans, set up to serve a particular group of employees or union members (and usually their dependents) and operated by a jointly managed (employer-union) welfare fund or less frequently, by an employer, an employee association, or a union; (3) medical-society plans, serving the general community and sponsored by State or local medical societies but not affiliated with the National Association of Blue Shield Plans; (4) dental-society plans, serving the general community and sponsored by State or local dental societies; and (5) private group clinic plans, operated and owned by private physicians and/or dentists functioning as a group.

The Division of Research and Statistics makes annual surveys (in some years on an all-inclusive basis, in others on a sample basis) of independent health insurance plans in order to obtain information on their enrollment and finances. The data are then combined with similar data from the Blue Cross-Blue Shield plans and insurance companies to develop national estimates of the number and proportion of the population having health insurance coverage and of the total income and benefit expenditures of all health insurance organizations.<sup>1</sup>

The survey made in 1963 was on a sample basis. Questionnaires were sent to a few (32) of the larger plans of each type, and replies were received from 27. These responding plans in 1961 had more than half the enrollment in all independent plans; they had 80 percent of the total enrollment in community plans, about 40 percent of the enrollment in employer-employee-union plans, 52 percent of that in private group clinic plans, and 97 percent of the enrollment in medical-

<sup>1</sup> For summary findings of the latest comprehensive survey of all independent health insurance plans, see Donald G. Hay, “Independent Health Insurance Plans, 1961 Survey,” *Social Security Bulletin*, February 1963. More detailed findings are presented in Research Report No. 2, *Independent Health Insurance Plans, 1961*, by Donald G. Hay, Louis S. Reed, and Robert E. Mella, which is about to be released by the Division of Research and Statistics.