

# United States Government Supplemental Information (Unaudited) for the Years Ended September 30, 2010, and 2009

## Fiscal Projections for the U.S. Government— Fiscal Year 2010

This section is prepared pursuant to Statement of Federal Financial Accounting Standard (SFFAS) 36, *Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government*. It is intended to help readers of the Financial Report of the U.S. Government (FR) assess whether future budgetary resources will be sufficient to sustain public services and to meet future obligations as they come due, assuming that the Federal Government's current policies for spending and taxation are continued.<sup>1</sup> Such an assessment requires prospective information about receipts and spending, the resulting debt, and how these amounts relate to the economy. The assessment is also referred to as reporting on "fiscal sustainability."

The information in this section is important not only for its financial, but also its social and political, implications. Financial reports should provide information that can help readers assess the likelihood that the Government will be able to continue providing the equivalent level of public services and to assess whether financial burdens without related benefits will be shifted to future taxpayers. Fiscal sustainability reporting should assist the reader in understanding these financial, social, and political implications.<sup>2</sup>

The projections and analysis presented here are mathematical extensions and extrapolations based on an array of assumptions as described below, including the assumption that current Federal policy does not change. These projections cannot be interpreted as forecasts or predictions of the future, in part because they encompass hypothetical future trends or events that are improbable. This is the first year in which this information is included with the other Supplemental Information, and the methods and assumptions used in producing this section are still under development.

### Statement of Long Term Fiscal Projections

Table 1, on the following page, presents projections of the Federal Government's receipts and non-interest spending.<sup>3</sup> Receipt categories include individual income taxes, Social Security and Medicare payroll taxes, and all other receipts. On the spending side, the projections include both mandatory (entitlement) programs, such as Social Security and Medicare, which provide benefits under standing law, and discretionary programs, such as defense spending, which are funded through annual appropriations. The data in Table 1 are presented as in the Federal budget, which differs in some respects from the presentation of these data in the trustees' reports for Social Security and Medicare (these differences are explained below). The key assumptions used in preparing these projections are summarized in the next section. The projections for Social Security and Medicare are based on the same economic and demographic assumptions as are used for the 2010 trustees' reports for these programs. Projections for the other categories are also consistent with the assumptions used for the trustees' reports. The Federal budget provides the framework used for the projections. In order to produce a more realistic projection of the fiscal outlook under current policy, the projections assume several likely departures from current law, noted below.

<sup>1</sup> Statement of Federal Financial Accounting Standard 36, Fiscal Projections for the U.S. Government, par. 7.

<sup>2</sup> SFFAS 36, par. 8.

<sup>3</sup> For the purposes of this analysis, spending is defined in terms of outlays. In the context of Federal budgeting, spending can either refer to budget authority – the authority to commit the government to spend an amount – or to outlays, which reflect actual payments made.

<b>Table 1: Long Range Projections of Federal Receipts and Spending</b>		
75-Year Present Values: FY 2011-2085 as of 9/30/2010		
	Dollars in Trillions	% GDP
<b>Receipts:</b>		
Social Security Payroll Taxes	37.8	4.4
Medicare Payroll Taxes	12.4	1.4
Individual Income Taxes	90.6	10.5
All Other Receipts	34.4	4.0
<b>Total Receipts</b>	<b>175.2</b>	<b>20.2</b>
<b>Non-interest Spending:</b>		
Defense Discretionary	31.0	3.6
Nondefense Discretionary	30.7	3.6
Social Security	49.1	5.7
Medicare Part A (supported by payroll taxes)	17.3	2.0
Medicare Parts B & D (net of premiums; supported by general revenues)	20.4	2.4
Medicaid	24.2	2.8
Other Mandatory	18.8	2.2
<b>Total Non-interest Spending</b>	<b>191.6</b>	<b>22.1</b>
<b>Non-interest Spending less Receipts</b>	<b>16.3</b>	<b>1.9</b>

Note: The 75-year present value of nominal GDP, which drives the calculations above, is \$865.6 trillion.

The projections in Table 1 are expressed in present value dollars as of October 1, 2010, and as a percentage of the present value of Gross Domestic Product (GDP).<sup>4</sup> The present value of a future amount, say \$1 billion in March 2020, is the amount of money that if invested on October 1, 2010 in an account earning the government borrowing rate would have a balance of \$1 billion in March 2020. The present value of a receipt or expenditure category over 75 years is simply the sum of the annual present value amounts. GDP measures the total value of all final goods and services produced in the U.S. and is thus a good measure of the overall size of the economy. When expressing a receipt or expenditure category over 75 years as a percent of GDP, the present value dollar amount is divided by the present value of GDP over 75 years. Measuring budget quantities as a percentage of GDP is a useful indicator of the economy's capacity to sustain Government programs. The interest rates used to compute present values (the rates of interest earned in the hypothetical account) are the rates that underlie the projections in the 2010 Social Security trustees' report.

The projections shown in Table 1<sup>5</sup> are made over a 75-year time frame, consistent with the time frame featured in the Social Security and Medicare trustees' reports. As discussed later, one notable difference introduced in broadening the fiscal perspective to the Government as a whole is that the projections are based on fiscal years starting on October 1, 2010, whereas the trustees' reports feature projections made on a calendar-year basis. This change allows the projections to start from more current numbers, including the actual results from fiscal year 2010.

<sup>4</sup> GDP is the total market value of all final goods and services produced domestically during a given period of time. The components of GDP are: private sector consumption and investment, government consumption and investment, and net exports (exports less imports). Equivalently, GDP is a measure of the gross income generated domestically over the same time period.

<sup>5</sup> Of the \$16.3 trillion 75-year present value net excess of non-interest spending over receipts (1.9 percent of the 75-year present value of GDP) expressed in Table 1, \$5.3 trillion or 0.6 percent of GDP relates to programs funded by the government's general revenues and \$11.1 or 1.3 percent of GDP relates to Social Security (OASDI) and Medicare Part A, which are funded by payroll taxes and which are not funded in any material respects by the government's general revenues. If payroll and self-employment taxes and related assets in the OASDI Trust Funds or Medicare Part A become insufficient to cover related benefits, as indicated by projections, additional funding for each of these two programs would be necessary or scheduled benefits would need to be reduced. If the government's general revenues are insufficient to cover both mandated transfers to Medicare Parts B and D and spending for other general government programs funded by the government's general revenues, as indicated by the projections, either Medicare Parts B and D revenues (premiums and state transfers), or the government's general revenues would need to be increased, spending for Medicare Parts B and D and/or other general government spending would need to be reduced, and/or additional amounts would need to be borrowed from the public.

The discussion below also considers the period of time beyond the 75-year window, noting most importantly that the assumptions become more uncertain the further in time the projections are extended.

This analysis and discussion of long-term fiscal projections for the U.S. Government does not include activities of State and local governments.

## Assumptions Used and Relationship to Other Financial Statements

A fundamental assumption underlying the projections in Table 1 is that current Federal policy – as defined below – does not change. **It is important to note that the projection of receipts and expenditures under current policy is not a forecast or prediction of the most likely outcome.** Indeed, the primary reason to project current policy amounts is to help inform the question of whether policy should change. If policy does change, the projections will of course prove to be untrue.

In addition, actual expenditures and receipts could be materially different than those projected even if policy does not change. This is because the long-range projections are inherently uncertain and because simplifying assumptions are made. One key simplifying assumption is that interest rates paid on public debt are assumed to be similar to those paid in the past, regardless of the amount of debt outstanding.

The projections in Table 1 focus on future cash flows, and do not reflect either the accrual basis or the modified-cash basis of accounting. The differences among the bases are largely based on timing. Cash-based projections reflect receipt or spending at the time cash is received or when a payment is made by the Government. In contrast, accrual-based projections reflect amounts in the time period in which income is earned (even if not yet received) or when an expense or obligation is incurred (even if cash has not yet been disbursed). The cash basis is consistent with methods used to prepare the Statement of Social Insurance (SOSI) and the generally cash-based Federal budget.

The following summarizes the assumptions used for the key categories of receipts and spending presented in Table 1 and in the related analysis:

- **Social Security:** Social Security (OASDI) spending in the Financial Report projections is based on the projected expenditures in the Social Security trustees' report for benefits (as indicated in the more detailed discussion of Social Insurance on page 150, plus the Railroad Retirement interchange, but excluding administrative expenses. The projections of Social Security payroll taxes and future Social Security spending are based on budget historical data for FY 2010. The projected growth rates for future spending and payroll taxes are drawn from the spending and tax growth rate projections underlying the latest trustees' report.
- **Medicare:** Current law Medicare spending is based on incurred expenditures from the 2010 Medicare trustees' report, which reflects the changes in Medicare that resulted from passage of the Affordable Care Act (ACA), and, therefore, projects lower costs than in previous reports. However, some adjustments are required to convert these amounts to Medicare spending as measured in the budget. Medicare Part B and D premiums, as well as State contributions to Part D, are subtracted from gross spending in measuring Part B and Part D outlays in the budget.<sup>6</sup> The budget treats these premiums as "negative spending" rather than receipts, since they represent payment for a service and are in that sense "business like." Government receipts are defined as payments obtained through the Government's sovereign power to tax. With these adjustments, Medicare spending net of administrative costs corresponds to Medicare spending in the budget. The long-term fiscal projection uses historical budget data from FY 2010 for Medicare spending and Part A payroll tax revenues, with both growing at growth rates presented in the trustees' report. Also, as discussed in Note 26, there is uncertainty about whether the projected reductions in health care cost growth will be fully achieved. Note 26 includes an alternative projection to illustrate the uncertainty of projected Medicare costs.

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<sup>6</sup> Medicare Part B and D premiums and State contributions to Part D are subtracted from the Part B and D spending displayed in Table 1. The total 75-year present value of these subtractions is \$7.7 trillion, or 0.9 percent of GDP.

- Medicaid:** The Medicaid program was also affected by the changes legislated in the ACA. Medicaid enrollment will be larger because of health reform, and many newly insured Americans will be covered through Medicaid. To reflect these changes, certain adjustments were made in the model that has been used to project Medicaid in past years for the Financial Report. The model starts with the projections from the *2008 Actuarial Report* prepared by the Office of the Actuary, Centers for Medicare and Medicaid Services (CMS).<sup>7</sup> As projections in that report only extend until 2018, the model assumes that Medicaid benefits in 2019 and later years grow at the same rate per beneficiary as Medicare benefits grow. Effects of the ACA, as calculated by CMS, were added to the base projections, as were other adjustments, to align base projections with the latest budget data. The Medicaid projections reflect the temporary increase in Medicaid spending due to the American Recovery and Reinvestment Act of 2009 (ARRA) as well as the phase-out of the Medicaid spending authorized by ARRA.
- Other Spending:** Other spending components are assumed to increase by the rate of growth in nominal GDP, implying that such spending will remain constant as a percentage of GDP. In these projections, aside from the expected reductions in Overseas Contingency Operations (OCO) spending, defense spending grows at the same rate as nominal GDP. Adjustments are also made for other components of temporary spending that are not expected to persist in the long run: the discretionary and mandatory spending authorized by ARRA and other notable stabilization measures including temporary expansions in unemployment insurance benefits, the implementation of the Troubled Asset Relief Program (TARP), the purchase of government-sponsored enterprise (GSE) preferred stock, as well as higher net spending for the Federal Deposit Insurance Corporation (FDIC).
- Receipts (Other than Social Security and Medicare):** Instead of attempting a projection of the entire income distribution, the Financial Report projections link individual income taxes to wages and salaries, and all other receipts to GDP. Individual income taxes are projected to return to their historical ratio to wages and salaries over the next four years, and from that point on to increase gradually to reflect the progressive nature of the Federal income tax, which implies that as real wages rise over time, the average taxpayer will move into higher tax brackets. The levels of individual income taxes are also adjusted over the next several years for the phase-out of the temporary tax cuts enacted by ARRA.
- Interest Spending:** Interest spending is determined by projected interest rates and the level of outstanding debt held by the public. The long-run interest rate assumptions match those of the 2010 Social Security Trustees Report. These same rates are used to convert future cash flows to present values as of the start of fiscal year 2011. The specific interest rates used are the same as those used to discount future payroll taxes in the Social Security trustees' report. The trustees' reports rates are converted to a fiscal year basis from a calendar year basis.

## Departures from Current Law and Policy

It was noted earlier that the long-term fiscal projections are made on the basis of current Federal policy, even where current Federal policy would not be continued under provisions of current law. For example, the projections presented in Table 1 and throughout this analysis are made without regard to the statutory limit on outstanding Federal debt. The projection also assumes several other departures from current law: continued discretionary appropriations in the projection period, the continued payment of Social Security and Medicare benefits beyond the projected point of trust fund exhaustion, extension of some of the 2001/2003 tax cuts and the indexing of the alternative minimum tax (AMT), and the reauthorization of many mandatory programs with future expiration dates. The projections do not assume continued action to override the scheduled reductions in Medicare physician fees. These physician reductions are reflected in the projections incorporated here, just as they are reflected in the Medicare trustees' report and in the Statement of Social Insurance.

## The Sustainability of Fiscal Policy

An important purpose of the Financial Report is to help citizens and policymakers assess whether current fiscal policy is sustainable and, if it is not, the urgency and magnitude of policy reforms necessary to make it sustainable. A sustainable policy is one where the ratio of debt held by the public to GDP (debt to GDP) is stable over time. The

<sup>7</sup> Christopher J. Truffer, John D. Klemm, E. Dirk Hoffman, and Christian J. Wolfe, *2008 Actuarial Report on the Financial Condition for Medicaid*, Office of the Actuary, Centers for Medicare and Medicaid Services, United States Department of Health and Human Services.

discussion below focuses on balancing revenues and expenditures over time, and does not consider fairness or efficiency implications of the reforms necessary to achieve sustainability.

It is shown below that, under current policy, the ratio of debt to GDP is projected to rise continuously over the next 75 years, eventually exceeding 350 percent in 2085. If these projections were extended beyond 2085, the deficit excluding interest would continue as the population continues to age and if the other assumptions made for the 75-year horizon continue to hold. The persistence of the deficit excluding interest beyond the 75-year horizon implies that the ratio of debt to GDP would continue to grow beyond the 75-year horizon. The continuing rise in this ratio means that current policy is unsustainable.

### **Current Policy Projections for Primary Deficits**

A key determinant of growth in the debt-to-GDP ratio and hence fiscal sustainability is the primary deficit-to-GDP ratio. The primary deficit is the difference between non-interest spending and receipts, and the primary deficit-to-GDP ratio is simply the primary deficit expressed as a percent of GDP. As shown in Chart 1, the primary deficit-to-GDP ratio grew rapidly in 2008 and 2009 due to the financial crisis and the recession and the policies pursued to combat both, and is projected to fall rapidly to near zero as the economy recovers. The projection period begins in 2011. After 2020, the primary deficit-to-GDP ratio is projected to increase, reaching 2 percent in 2030 and remaining at or above 1.8 percent through the end of the 75-year projection period and beyond.

The level of revenues as a percentage of GDP has been depressed by the recession and tax reductions enacted as part of the ARRA. As the economy recovers and the tax cuts expire, it is projected that the revenue share of GDP will return to near its long-run average. Beyond that point individual income taxes are projected to grow gradually as increases in real incomes cause more taxpayers and a larger share of total income to fall into higher tax brackets.<sup>8</sup> This projection assumes that Congress and the President will continue to enact legislation that prevents the share of income subject to the Alternative Minimum Tax from rising. On the spending side, the projected increase in non-interest spending as a percentage of GDP is principally due to growth in Medicare, Medicaid, and Social Security spending, as is shown in Chart 2. The Social Security spending share of GDP is projected to increase about 1.2 percentage points over the next 25 years as the baby boom generation retires. The same demographic patterns will affect Medicare spending. After 2035, the Social Security spending share of GDP is relatively steady, while the Medicare spending share of GDP continues to increase, albeit at a slower rate, due to projected increases in health care costs. For the same reason, Medicaid spending is also projected to rise over time.

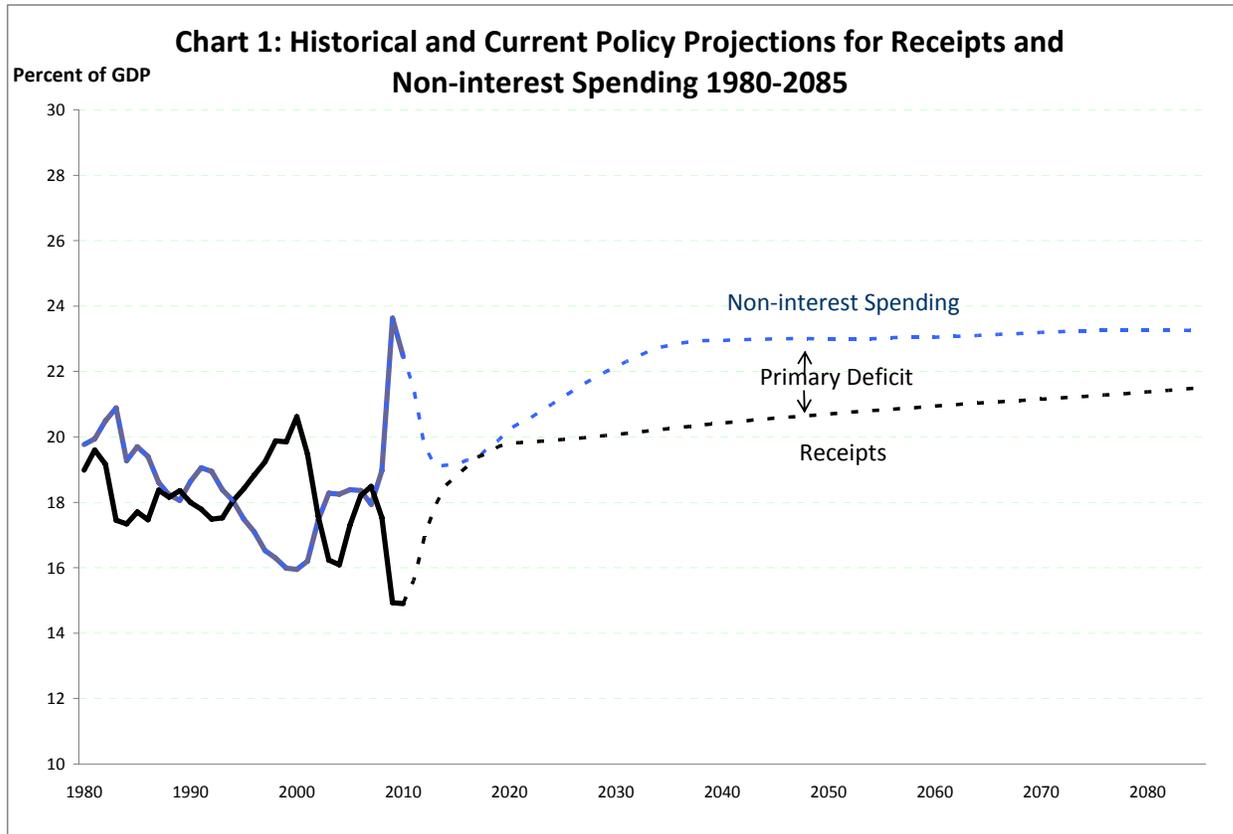
Both Medicare and Medicaid have been significantly affected by the recently passed health reform legislation, the Affordable Care Act (ACA). An effect of the reform is to expand health coverage. The long-term budgetary effect will depend on the effectiveness of provisions designed to reduce health care cost growth. The 2010 Medicare trustees' report projects that the new law could hold down future Medicare cost growth substantially compared with previous projections if fully implemented. The Medicare spending projections in this Report are based on the projections in the 2010 Medicare Trustees Report. If the trustees' report projections hold true, there will be a substantial slowdown in future Medicare and Medicaid spending growth. That assumption is reflected in these long-run fiscal projections. However, even with this reduced Medicare and Medicaid spending, there is still a persistent gap between projected receipts and projected total Federal non-interest spending.

### **Current Policy Projections for Debt and Interest Payments**

The primary deficit projections in Chart 1, along with projections for interest rates and GDP, determine the projections for the ratio of debt held by the public to GDP that are shown in Chart 3. That ratio was 62 percent at the end of fiscal year 2010, and under current policy, it is projected to exceed 70 percent in 2020, 130 percent in 2040, and 350 percent in 2085. Continued upward pressure on spending for the elderly after 75 years because of increasing longevity implies that the debt-to-GDP ratio would continue to rise beyond that point if there is no change in policy. The continuing rise of the debt-to-GDP ratio suggests that current policy is unsustainable.

Chart 3 also displays the projection of debt held by the public as a percent of GDP as published in the 2009 Financial Report. The 2010 projection is lower than the 2009 projection in every year of the projection period, with the size of the gap increasing rapidly over time. The reduction in projected debt has decreased the size of the fiscal gap dramatically since 2009. The improved outlook this year is almost entirely attributable to lower projected spending for Medicare and Medicaid and increased projected receipts that result from the ACA. The lower level of projected publicly held debt relative to last year's projection reflects lower projected primary deficits. As reported in Table 1, primary deficits over the 75-year projection average 1.9 percent of GDP. For comparison, the projections in last year's report implied that the average primary deficit would be 5.5 percent of GDP. As noted, this improvement in projected primary deficits is largely attributable to the enactment of the ACA.

<sup>8</sup> Projected revenues also account for increases (as a share of GDP) in employer-sponsored health insurance costs, which are tax exempt.



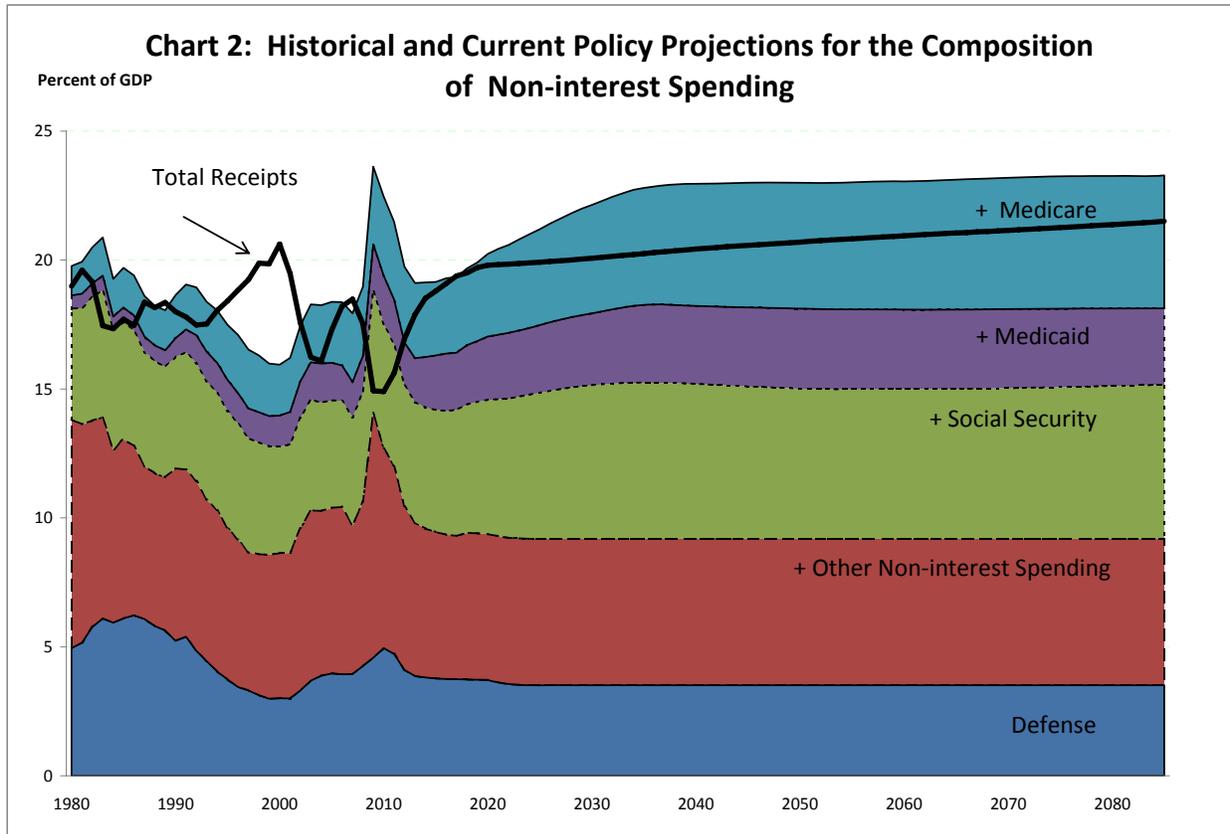
The change in debt held by the public from one year to the next is equal to the unified budget deficit, the difference between total spending and total receipts.<sup>9</sup> Total spending consists of non-interest spending plus interest spending. Chart 4 reveals clearly that the rapid rise in total spending and the unified deficit is almost entirely due to projected interest payments on the debt. As a percent of GDP, interest spending was 1.4 percent in 2010, and under current policies it is projected to reach 5 percent by 2030 and 19 percent by 2085.

### The Fiscal Gap

The fiscal gap measures how much the primary surplus (receipts less non-interest spending) must increase in order for fiscal policy to achieve a target debt-to-GDP ratio in a particular future year. In these projections, the fiscal gap is estimated over a 75-year period, from 2011 to 2085, and the target debt-to-GDP ratio is equal to the ratio at beginning of the projection period, in this case the end of fiscal year 2010 debt-to-GDP ratio of 62 percent of GDP.

The 75-year fiscal gap under current policy is estimated at 2.4 percent of GDP, as reflected in Table 2. As noted in Table 1, the difference between projected programmatic (non-interest) spending and receipts is 1.9 percent of GDP (reflecting the deficit condition of excess spending over receipts). However, eliminating this primary deficit of 1.9 percent of GDP is not sufficient to stabilize the debt-to-GDP ratio. Because interest rates are assumed to exceed the growth rate of GDP, reaching primary balance will still leave debt rising relative to GDP. The average primary surplus needed to return the debt-to-GDP ratio to its initial level and fully close the fiscal gap is 0.5 percent of GDP per year.

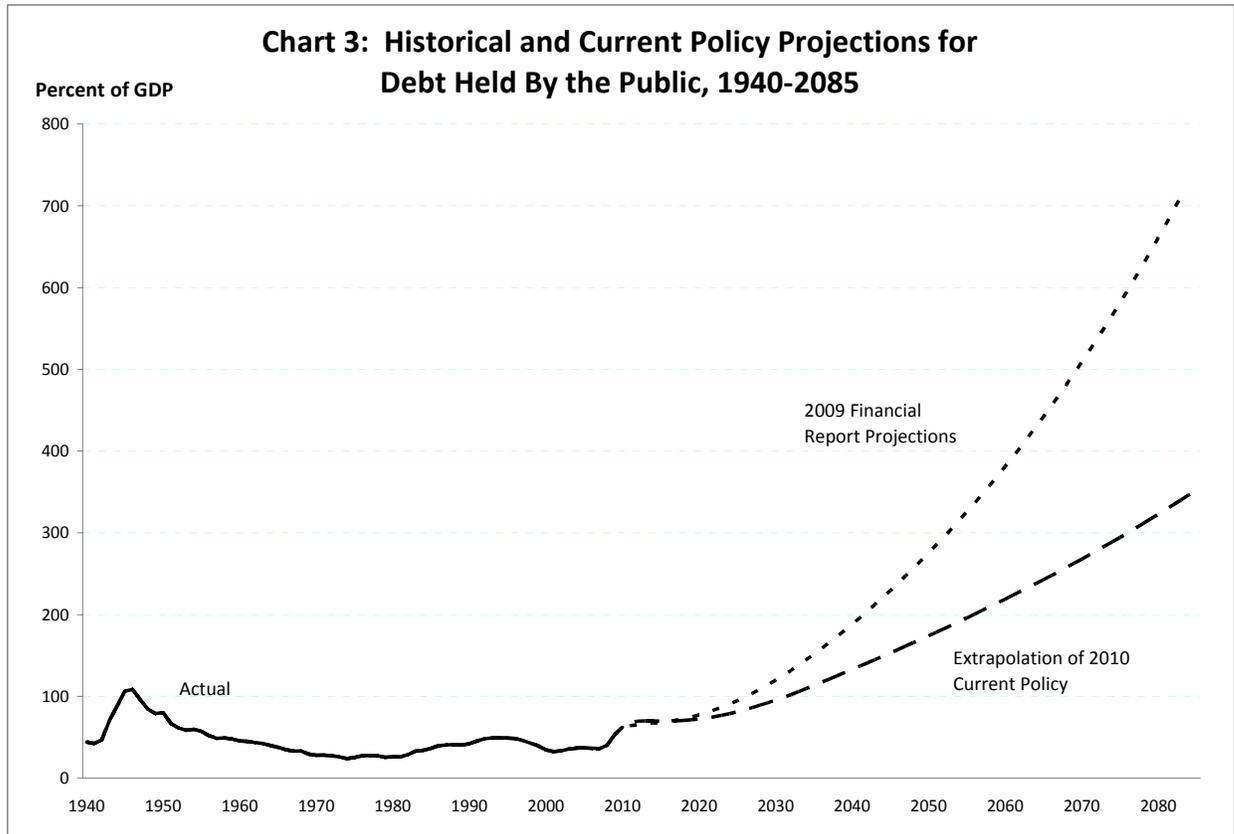
<sup>9</sup> Debt held by the public is also affected by certain transactions not included in the unified budget deficit, such as changes in Treasury's cash balances and the nonbudgetary activity of Federal credit financing accounts. These transactions are assumed to net to zero in the long-range projections.



### The Cost of Closing the 75-Year Fiscal Gap

The longer policy action to close the fiscal gap is delayed, the larger the post-reform primary surplus must be to stabilize the debt-to-GDP ratio by the end of the 75 year period. Varying the years in which reforms are introduced while holding constant the ultimate target ratio of debt to GDP helps to illustrate the cost of delaying policy changes that close the fiscal gap. The reforms considered here increase the primary surplus relative to current policy by a fixed percent of GDP starting in the reform year. Three such policies are considered, each beginning in a different year. The analysis shows that the longer policy action is delayed, the larger the post-reform primary surplus must be to stabilize the debt-to-GDP ratio in 2085. Future generations are harmed by policy delay because higher primary surpluses imply lower spending and/or higher taxes than would be needed with earlier deficit reduction.

As previously shown in Chart 1, under current policy, primary deficits occur in virtually every year of the projection period. Table 2 shows primary surplus changes necessary to make the debt-to-GDP ratio in 2085 equal to its level in 2010 under each of the three policies. If reform begins in 2011, then it is sufficient to raise the primary surplus share of GDP by 2.4 percentage points in every year between 2011 and 2085 in order to have a debt-to-GDP ratio in 2085 equal to the level in 2010. This raises the average 2011-2085 primary surplus-to-GDP ratio from -1.9 percent to 0.5 percent. In contrast, if reform is begun in 2021 or 2031, the primary surplus must be raised by 2.9 percent and 3.7 percent of GDP, respectively, in order to reach a debt-to-GDP ratio in 2085 equal to the level in 2010. The difference between the primary surplus boost starting in 2021 and 2031 (2.9 and 3.7 percent of GDP, respectively) and the primary surplus boost starting in 2011 (2.4 percent of GDP) is a measure of the additional burden policy delay would impose on future generations. This policy change could take the form of a reduction in spending, an increase in taxes, or some combination of both that produced the same improvement in the budget surplus. The costs of delay are due to the debt-to-GDP ratio rising during the interim period, which increases the future amount of interest that must be covered with the primary surplus. Delaying reform increases the cost of reaching the target debt-to-GDP ratio even if the target year is extended beyond 2085, since the starting debt-to-GDP ratio will be higher.

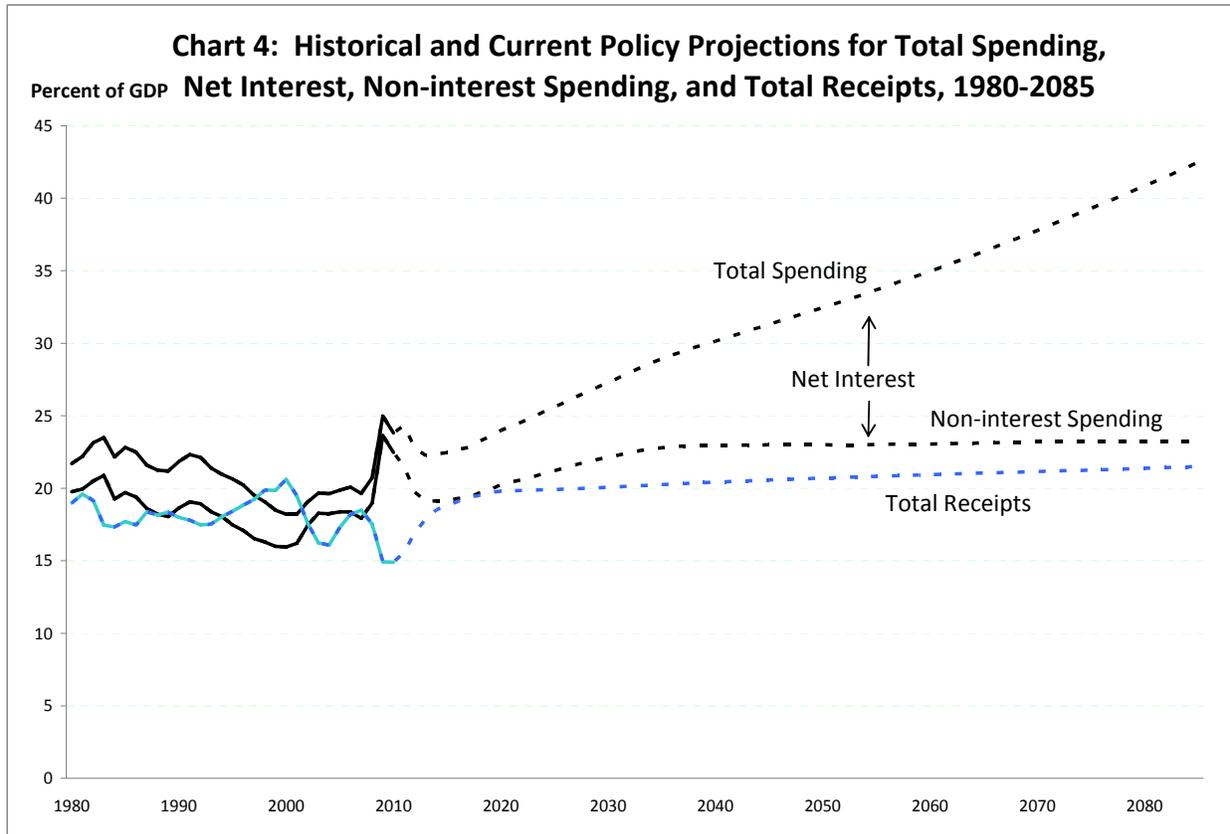


These estimates likely understate the cost of delay because they do not assume interest rates will rise as the debt-to-GDP ratio grows. If a higher debt-to-GDP ratio increases the interest rate, making it more costly for the government to service its debt and simultaneously slowing private investment, the primary surplus required to return the debt-to-GDP ratio to its 2010 level will also increase. This dynamic may accelerate with higher ratios of debt to GDP, potentially leading to the point where there may be no feasible level of taxes and spending that would reduce the debt-to-GDP ratio to its 2010 level.

<b>Table 2</b>	
<b>Costs of Delaying Fiscal Consolidation</b>	
<b>Period of Delay</b>	<b>Change in Average Primary Surplus</b>
No Delay: Reform in 2011	2.4 percent of GDP between 2011 and 2085
Ten Years: Reform in 2021	2.9 percent of GDP between 2021 and 2085
Thirty Years: Reform in 2031	3.7 percent of GDP between 2031 and 2085

## Alternative Scenarios

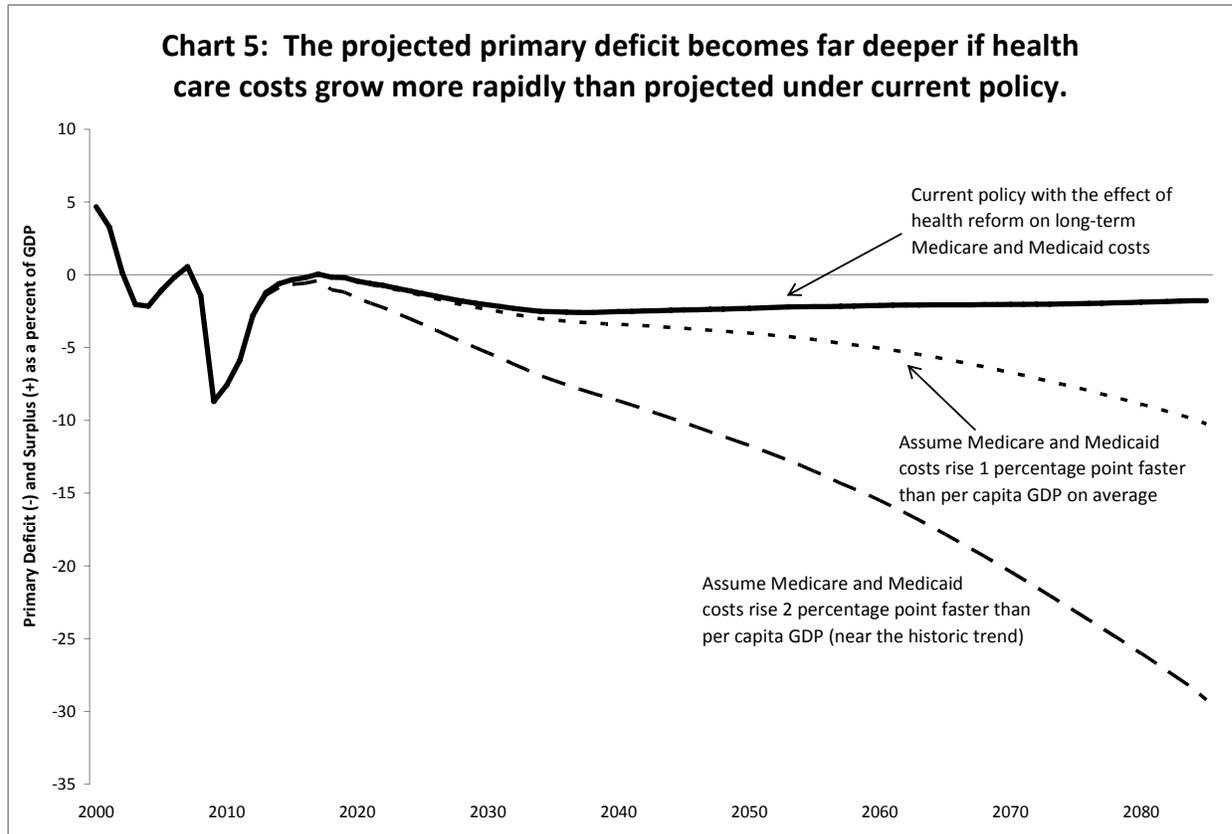
The long-run outlook for the budget is extremely uncertain and therefore it makes sense to consider possible alternative projections to indicate the range of uncertainty. There are many dimensions to the projections for which reasonable variations could be considered. Some of the key issues concern long-run economic and demographic assumptions. The long-run fiscal gap is partly the result of demographic patterns that have emerged over the last 50 years with lower birth rates and reduced mortality. The population is aging rapidly and will continue to do so over the next several decades, which puts pressure on programs such as Social Security, Medicare, and Medicaid nursing



care. A shift in expected fertility could have important long-run effects on the budget outlook. The current assumption is that U.S. fertility will remain close to the replacement rate of approximately 2 children per woman. If the fertility rate were to increase significantly, there would be more workers in the future to support the elderly and to help service existing debt. Conversely, if the fertility rate were to fall below replacement, the strains on the budget would become even more severe. Improvements in mortality operate like a decline in fertility. Increases in immigration operate like an increase in fertility.

One of the most important assumptions underlying the projections is the expected growth of health care costs. Enactment of the ACA reduced the expected long-run growth rates of health care costs, but these growth rates are still highly uncertain. As an illustration of the dramatic effect of variations in health care growth rates, Chart 5 shows the effect on future primary deficits of growth rates that are one percent higher or two percent higher than the growth rates in the base projection. The one percent higher health care cost growth scenario raises the average of non-interest spending less receipts over 75 years to 3.8 percent of GDP, compared to 1.9 percent of GDP assumed in the base projection and displayed in Table 1. The two percent higher health cost growth scenario raises the average of non-interest spending less receipts over 75 years even further, to 10.5 percent of GDP. The dramatic deterioration caused by higher health care cost growth shows the critical importance that effective implementation of the ACA has on the long-run fiscal outlook.

Other key economic assumptions in this report include the future growth rate of real GDP, which itself depends on assumptions such as future growth in the labor force and labor productivity. Historically, U.S. labor productivity has increased at a rate of about 2 percent or more per year, but there have been periods when productivity grew less rapidly and other periods in which it grew faster. Productivity growth has averaged 2.5 percent per year over the last 15 years, which is above its long-run trend. In these budget projections, the rate of productivity growth is assumed to be somewhat below its long-run trend, which is a conservative assumption. It is unlikely that higher productivity growth will be sufficient to resolve the long-run budget problem. Faster growth will lead to higher wages, which will lead to more tax revenue in the near term, but these gains will be partly offset by higher payments for Social Security and other benefit programs in the long term, because benefits are tied to wages. Also, medical costs show a positive relationship with GDP, so higher GDP growth may be matched by higher Medicare and Medicaid spending. Real interest rates are another factor that affects the calculations. The higher are real interest rates, the more costly it is to sustain debt. Inflation is not a major factor in these calculations. Changes in the trend



rate of inflation have offsetting effects on future revenues and future spending, so the budget effect is more nearly neutral in the long run.

## Fiscal Projections in Context

As indicated earlier, the projections discussed here are neither forecasts nor predictions. Their purpose is to help readers assess whether current fiscal policy is sustainable and, if it is not sustainable, the magnitude of needed reforms to make it sustainable. If policy changes, perhaps in response to projections like those presented here, then the projections will of course prove to be untrue.

In addition, projections of how Federal finances will evolve over several decades under current policies are extremely uncertain. However, the conclusion that current policies are unsustainable is almost certainly robust to reasonable alternative assumptions.

One way to place these long-range fiscal projections in context is in comparison to projections for other developed nations. Several countries have begun to produce long-range fiscal projections in the last two decades. However, comparisons are difficult because the coverage of the reports and the time horizon projected vary across countries. The horizon for most of these reports is less than 75 years, and the projections are not always updated annually. Some of the countries that have produced long-range projections have shown sustainable policies in the long run, although the recent financial crisis will have worsened the near-term budget outlook in almost every country. Early developers of such fiscal projections include Australia, New Zealand, Canada, the United Kingdom, Denmark, Sweden, Norway, and the Netherlands.<sup>10</sup>

<sup>10</sup> The Organization for Economic Cooperation and Development (OECD) released a policy brief in October 2009 (available at <http://www.oecd.org/dataoecd/40/26/43836144.pdf>) describing the efforts of different member countries to produce long-term fiscal projections.

## Conclusion

The United States took a potentially significant step towards fiscal sustainability in 2010 by reforming its system of health insurance. The legislated changes for Medicare, Medicaid, and other health coverage hold the prospect of lowering the long-term growth trend for future health care costs and significantly reducing the long-term fiscal gap. But even with the new law, the projections discussed above indicate that, under current policies and the assumptions used in this report, the debt-to-GDP ratio will continually increase over the next 75 years and beyond, which means current policies are not sustainable. As indicated earlier, the longer policy action to avert these trends is delayed, the larger are the projected revenue increases and/or spending decreases necessary to reach a target debt-to-GDP ratio. These projections, however, are neither forecasts nor predictions. They are presented here to provide a foundation upon which readers can form their own conclusions about fiscal sustainability.

## Social Insurance

The social insurance programs consisting of Social Security, Medicare, Railroad Retirement, and Black Lung were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the Government. Because taxpayers rely on these programs in their long-term planning, social insurance program information should indicate whether the current law provisions of the programs can be sustained, and more generally what effect they will likely have on the Government's financial condition. The resources needed to run these programs are raised through taxes and fees. Eligibility for benefits rests in part on earnings and time worked by the individuals. Social Security benefits are generally redistributed intentionally toward lower-wage workers (i.e., benefits are progressive). In addition, each social insurance program has a uniform set of entitling events and schedules that apply to all participants.

### Social Security and Medicare

#### Social Security

The OASI Trust Fund was established on January 1, 1940, as a separate account in the Treasury. The DI Trust Fund, another separate account in the Treasury, was established on August 1, 1956. OASI pays cash retirement benefits to eligible retirees and their eligible dependents and survivors, and the much smaller DI fund pays cash benefits to eligible individuals who are unable to work because of medical conditions and certain family members of such eligible individuals. Though the events that trigger benefit payments are quite different, both trust funds have the same earmarked financing structure: primarily payroll taxes and income taxes on benefits. All financial operations of the OASI and DI Programs are handled through these respective funds. The two funds are often referred to as simply the combined OASDI Trust Funds. At the end of calendar year 2009, OASDI benefits were paid to approximately 53 million beneficiaries.

The primary financing of these two funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Since 1990, employers and employees have each paid 6.2 percent of taxable earnings. The self-employed pay 12.4 percent of taxable earnings. Payroll taxes are computed on wages and net earnings from self-employment up to a specified maximum annual amount, referred to as maximum taxable earnings (\$106,800 in 2010), that increases each year with economy-wide average wages.

Legislation passed in 1984 subjected up to half of OASDI benefits to tax and allocated the revenue to the OASDI Trust Funds, and in 1993 legislation upped the potentially taxed portion of benefits to 85 percent and allocated the additional revenue to the Hospital Insurance Trust Fund.

#### Medicare

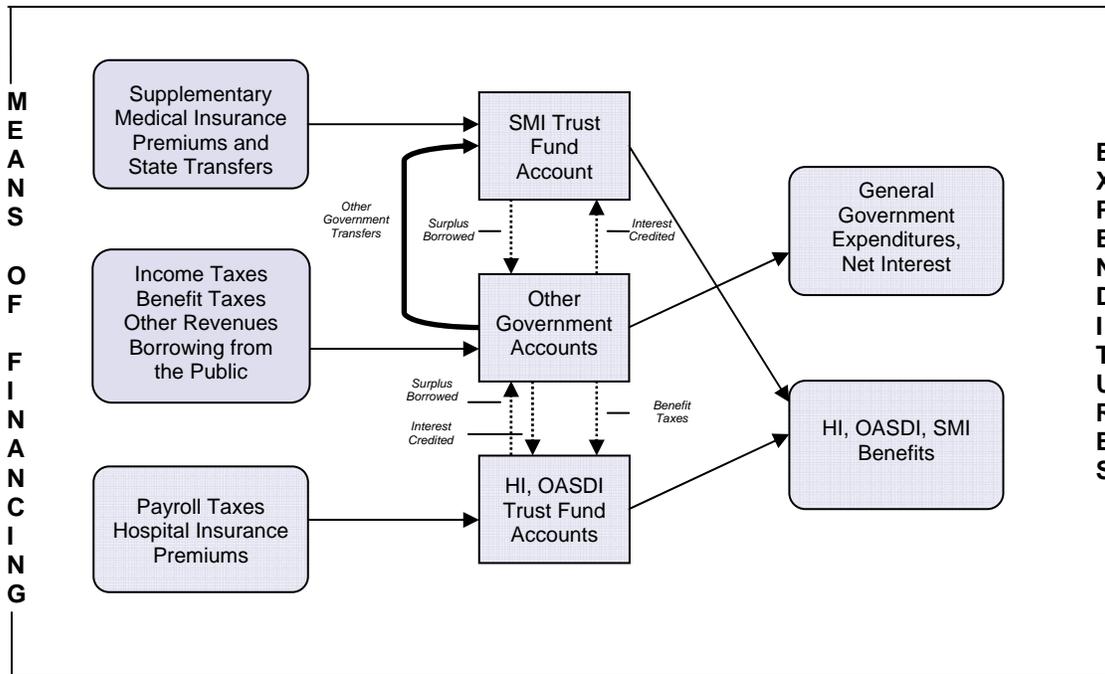
The Medicare Program, created in 1965, also has two separate trust funds: the Hospital Insurance (HI, Medicare Part A) and Supplementary Medical Insurance (SMI, Medicare Parts B and D) Trust Funds.<sup>1</sup> HI pays for inpatient acute hospital services and major alternatives to hospitals (skilled nursing services, for example) and SMI pays for hospital outpatient services, physician services, and assorted other services and products through the Part B account and pays for prescription drugs through the Part D account. Though the events that trigger benefit payments are similar, HI and SMI have different earmarked financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Currently, employers and employees each pay 1.45 percent of earnings, while self-employed workers pay 2.9 percent of their net earnings. Beginning 2013, employees and self-employed individuals with earnings above certain thresholds will pay an additional HI tax of 0.9 percent on earnings above those thresholds. Other income to the HI fund includes a small amount of premium income from voluntary enrollees, a portion of the Federal income taxes that beneficiaries pay on Social Security benefits (as explained above), and interest credited on Treasury securities held in the HI Trust Fund. As is explained in the next section, these Treasury securities and related interest have no effect on the consolidated statement of Governmentwide finances.

For SMI, transfers from the General Fund of the Treasury represent the largest source of income covering about 75 percent and 82 percent of program costs for Parts B and D, respectively. Beneficiaries pay monthly

<sup>1</sup> Medicare legislation in 2003 created the new Part D account in the SMI Trust Fund to track the finances of a new prescription drug benefit that began in 2006. As in the case of Medicare Part B, approximately three-quarters of revenues to the Part D account will come from future transfers from the General Fund of the Treasury. Consequently, the nature of the relationship between the SMI Trust Fund and the Federal budget described below is largely unaffected by the presence of the Part D account though the magnitude will be greater.

premiums that finance approximately 25 percent and 18 percent of costs for Parts B and D, respectively. With the introduction of Part D drug coverage, Medicaid is no longer the primary payer of drug benefits for beneficiaries dually eligible for Medicare and Medicaid. For those beneficiaries, States must pay the Part D account a portion of their estimated foregone drug costs for this population (referred to as State transfers). As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund. These Treasury securities and related interest have no effect on the consolidated statement of Governmentwide finances. See Note 26—Social Insurance, for additional information on Medicare program financing.

**Figure 1**  
**Social Security, Medicare, and Governmentwide Finances**



**Social Security, Medicare, and Governmentwide Finances**

The current and future financial status of the separate Social Security and Medicare Trust Funds is the focus of the trustees’ reports, a focus that may appropriately be referred to as the “trust fund perspective.” In contrast, the Government primarily uses the *unified budget* concept as the framework for budgetary analysis and presentation. It represents a comprehensive display of all Federal activities, regardless of fund type or on- and off-budget status, and has a broader focus than the trust fund perspective that may appropriately be referred to as the “budget perspective” or the “Governmentwide perspective.” Social Security and Medicare are among the largest expenditure categories of the U.S. Federal budget. Together, they now account for more than a third of all Federal spending and the percentage is projected to rise dramatically for the reasons discussed below. This section describes in detail the important relationship between the trust fund perspective and the Governmentwide perspective.

Figure 1 is a simplified graphical depiction of the interaction of the Social Security and Medicare Trust Funds with the rest of the Federal budget.<sup>2</sup> The boxes on the left show sources of funding, those in the middle represent the trust funds and other Government accounts (of which the General Fund is a part) into which that funding flows, and the boxes on the right show simplified expenditure categories. The figure is intended to illustrate how the various sources of program revenue flow through the budget to beneficiaries. The general approach is to group revenues and expenditures that are linked specifically to Social Security and/or Medicare separately from those for other government programs.

<sup>2</sup> The Federal unified budget encompasses all Government financing and is synonymous with a Governmentwide perspective.

Each of the trust funds has its own sources and types of revenue. With the exception of General Fund transfers to SMI, each of these revenue sources represents revenue from the public that are earmarked specifically for the respective trust fund, and cannot be used for other purposes. In contrast, personal and corporate income taxes and other revenue go into the General Fund of the Treasury and are drawn down for any Government program for which Congress has approved spending.<sup>3</sup> The arrows from the boxes on the left represent the flow of the revenues into the trust funds and other Government accounts.

The heavy line between the top two boxes in the middle of Figure 1 represents intragovernmental transfers to the SMI Trust Fund from other Government accounts. The Medicare SMI Trust Fund is shown separately from the two Social Security trust funds (OASI and DI) and the Medicare HI Trust Fund to highlight the unique financing of SMI. SMI is currently the only one of the programs that is funded through transfers from the General Fund of the Treasury, which is part of the other Government accounts (the Part D account receives transfers from the States). The transfers finance roughly three-fourths of SMI Program expenses. The transfers are automatic; their size depends on how much the program requires, not on how much revenue comes into the Treasury. If General Fund revenues become insufficient to cover both the mandated transfer to SMI and expenditures on other general Government programs, Treasury would have to borrow to make up the difference. In the longer run, if transfers to SMI increase beyond growth in general revenues as shown below, they are projected to increase significantly in coming years—then Congress must either raise taxes, cut other Government spending, reduce SMI benefits, or borrow even more.

The dotted lines between the middle boxes of Figure 1 also represent intragovernmental transfers but those transfers arise in the form of “borrowing/lending” between the Government accounts. Interest credited to the trust funds arises when the excess of program income over expenses is loaned to the General Fund. The vertical lines labeled *Surplus Borrowed* represent these flows from the trust funds to the other Government accounts. These loans reduce the amount the General Fund has to borrow from the public to finance a deficit (or likewise increase the amount of debt paid off if there is a surplus). However, the General Fund has to credit interest on the loans from the trust fund programs, just as if it borrowed the money from the public. The credits lead to future obligations for the General Fund (which is part of the other Government accounts). These transactions are indicated in Figure 1 by the vertical arrows labeled *Interest Credited*. The credits increase trust fund income exactly as much as they increase credits (future obligations) in the General Fund. From the standpoint of the Government as a whole, at least in an accounting sense, these interest credits are a wash.

It is important to understand the additional implications of these loans from the trust funds to the other Government accounts. When the trust funds get the receipts that they loan to the General Fund, these receipts provide additional authority to spend on benefits and other program expenses. The General Fund, in turn, has taken on the obligation of paying interest on these loans every year and repaying the principal when trust fund income from other sources falls below expenditures—the loans will be called in and the General Fund will have to finance the benefits paid by the trust fund through general revenues or borrowing, just as for any Governmental program.

Actual dollar amounts roughly corresponding to the flows presented in Figure 1 are shown in Table 1 for fiscal year 2010. In Table 1, revenues from the public (left side of Figure 1) and expenditures to the public (right side of Figure 1) are shown separately from transfers between Government accounts (middle of Figure 1). Note that the transfers (\$213.8 billion) and interest credits (\$101.0 billion) received by the trust funds appear as negative entries under “Other Government” and are thus offsetting when summed for the total budget column. These two intragovernmental transfers are the key to the differences between the trust fund and budget perspectives.

<sup>3</sup> Other programs also have dedicated revenues in the form of taxes and fees (and other forms of receipt) and there are a large number of earmarked trust funds in the Federal budget. Total trust fund receipts account for about 40 percent of total Government receipts with the Social Security and Medicare Trust Funds accounting for about two-thirds of trust fund receipts. For further discussion, see the report issued by the Government Accountability Office, *Federal Trust and Other Earmarked Funds*, GAO-01-199SP, January 2001. In the figure and the discussion that follows, all other programs, including these other earmarked trust fund programs, are grouped under “Other Government Accounts” to simplify the description and maintain the focus on Social Security and Medicare.

From the Governmentwide perspective, only revenues received from the public (and States in the case of Medicare, Part D) and expenditures made to the public are important for the final balance. Trust fund revenue from the public consists of payroll taxes, benefit taxes, and premiums. For HI, the difference between total expenditures made to the public (\$249.0 billion) and revenues (\$203.4 billion) was (\$45.6 billion) in 2010, indicating that HI had a relatively small negative effect on the overall budget outcome *in that year*. For the SMI account, revenues from the public (premiums) were relatively small, representing about a quarter of total expenditures made to the public in 2010. The difference (\$206.2 billion) resulted in a net draw on the overall budget balance in that year. For OASDI, the difference between total expenditures made to the public (\$706.2 billion) and revenues from the public (\$669.4 billion) was (\$36.8) billion in 2010, indicating that OASDI had a negative effect on the overall budget outcome *in that year*.

The trust fund perspective is captured in the bottom section of each of the three trust fund columns. For HI, total expenditures exceeded total revenues by \$31.0 billion in 2010, as shown at the bottom of the first column. This cash deficit was made up by calling in past loans made to the General Fund (i.e., by redeeming Trust Fund assets). For SMI, total revenues of \$278.5 billion (\$61.8 + \$216.7), including \$213.7 billion transferred from other Government accounts (the General Fund), exceeded total expenditures by \$10.5 billion. Transfers to the SMI Program from other Government accounts (the General Fund), amounting to about 80 percent of program costs, are obligated under current law and, therefore, appropriately viewed as revenue from the trust fund perspective. For OASDI, total revenues of \$787.9 billion (\$669.4 + \$118.5), including interest and a small amount of other Government transfers, exceeded total expenditures of \$706.2 billion by \$81.7 billion.

**Table 1**  
**Revenues and Expenditures for Medicare and Social Security**  
**Trust Funds and the Total Federal Budget**  
**for the Fiscal Year ended September 30, 2010**

(In billions of dollars)	Trust Funds					Total <sup>1</sup>
	HI	SMI	OASDI	Total	All Other	
<b>Revenues from the public and States:</b>						
Payroll and benefit taxes, State grants...	197.4		669.4	866.8		866.8
Premiums .....	6.0	57.3		63.3		63.3
Other taxes and fees .....		4.5		4.5	1,227.1	1,231.6
Total .....	203.4	61.8	669.4	934.6	1,227.1	2,161.7
Total expenditures to the public <sup>2</sup> .....	249.0	268.0	706.2	1,223.2	2,232.6	3,455.8
<b>Net results—budget perspective<sup>3</sup> .....</b>	<b>(45.6)</b>	<b>(206.2)</b>	<b>(36.8)</b>	<b>(288.6)</b>	<b>(1,005.5)</b>	<b>(1,294.1)</b>
<b>Revenues from other Government accounts:</b>						
Transfers .....	0.1	213.7		213.8	(213.8)	
Interest credits .....	14.5	3.0	118.5	136.0	(136.0)	
Total .....	14.6	216.7	118.5	349.8	(349.8)	
<b>Net results—trust fund perspective (change in Trust Fund balance)<sup>3</sup> .....</b>	<b>(31.0)</b>	<b>10.5</b>	<b>81.7</b>	<b>61.2</b>	<b>N/A</b>	<b>N/A</b>

<sup>1</sup> This column is the sum of the preceding two columns and shows data for the total Federal budget. The figure \$1,294.1 billion was the total Federal deficit in fiscal year 2010.

<sup>2</sup> The OASDI figure includes \$4.4 billion transferred to the Railroad Retirement Board for benefit payments and is, therefore, an expenditure to the public.

<sup>3</sup> Net results are computed as revenues less expenditures.

Notes: Amounts may not add due to rounding.  
 "N/A" indicates not applicable.

## Cashflow Projections

### Background

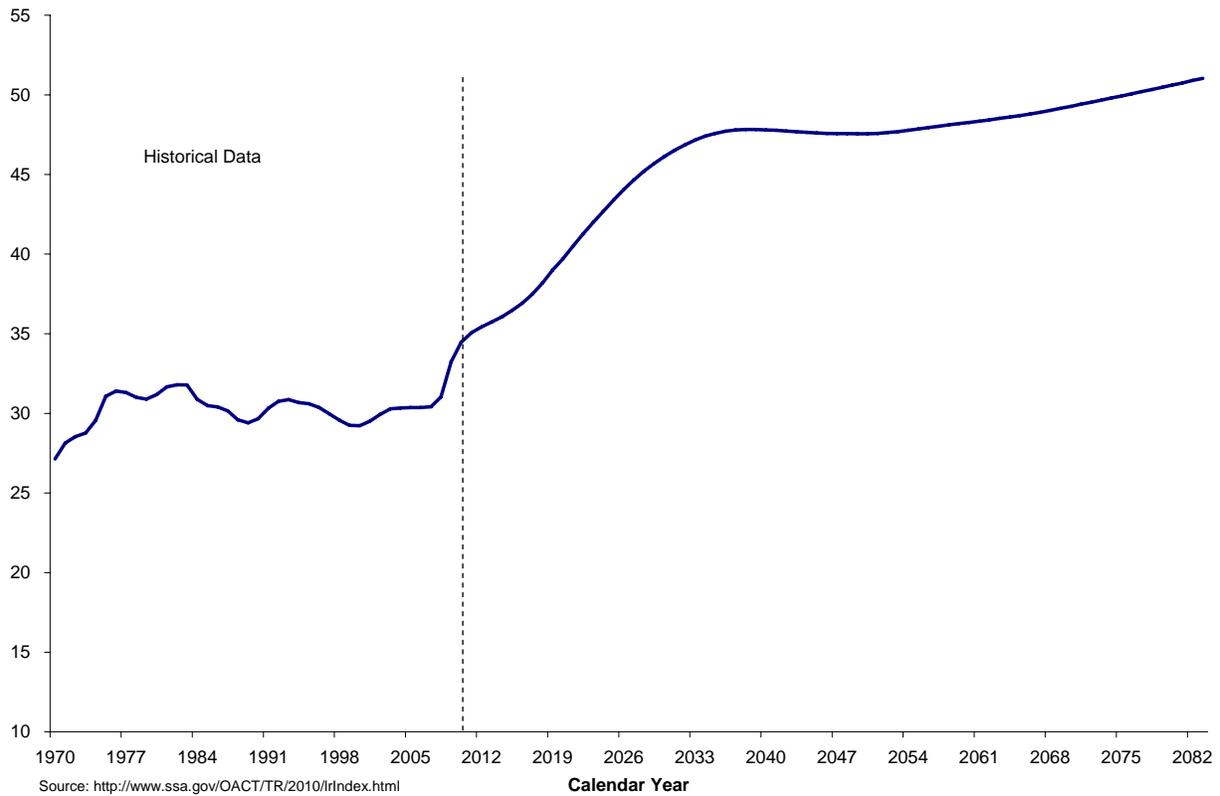
*Economic and Demographic Assumptions.* The Boards of Trustees<sup>4</sup> of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. The economic and demographic assumptions used for the most recent set of intermediate projections for Social Security and Medicare are shown in the "Social Security" and "Medicare" sections of Note 26—Social Insurance.

*Beneficiary-to-Worker Ratio.* Underlying the pattern of expenditure projections for both the OASDI and Medicare Programs is the impending demographic change that will occur as the large baby-boom generation, born in the years 1946 to 1964, retires or reaches eligibility age. The consequence is that the number of beneficiaries will increase much faster than the number of workers who pay taxes that are used to pay benefits. The pattern is

<sup>4</sup> There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor; the Commissioner of the Social Security Administration; and two public trustees who are appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees are members of two different political parties.

illustrated in Chart 1 which shows the ratio of OASDI beneficiaries to 100 covered workers for the historical period and estimated for the next 75 years. In 2010, there were about 34 beneficiaries for every 100 workers. By 2030, there will be about 46 beneficiaries for every 100 workers. A similar demographic pattern confronts the Medicare Program. For example, for the HI Program, there were about 30 beneficiaries for every 100 workers in 2010; by 2030, there are expected to be about 43 beneficiaries for every 100 workers. This ratio for both programs will continue to increase to about 49 beneficiaries for every 100 workers by the end of the projection period, after the baby-boom generation has moved through the Social Security system and as birth rates decline and longevity increase.

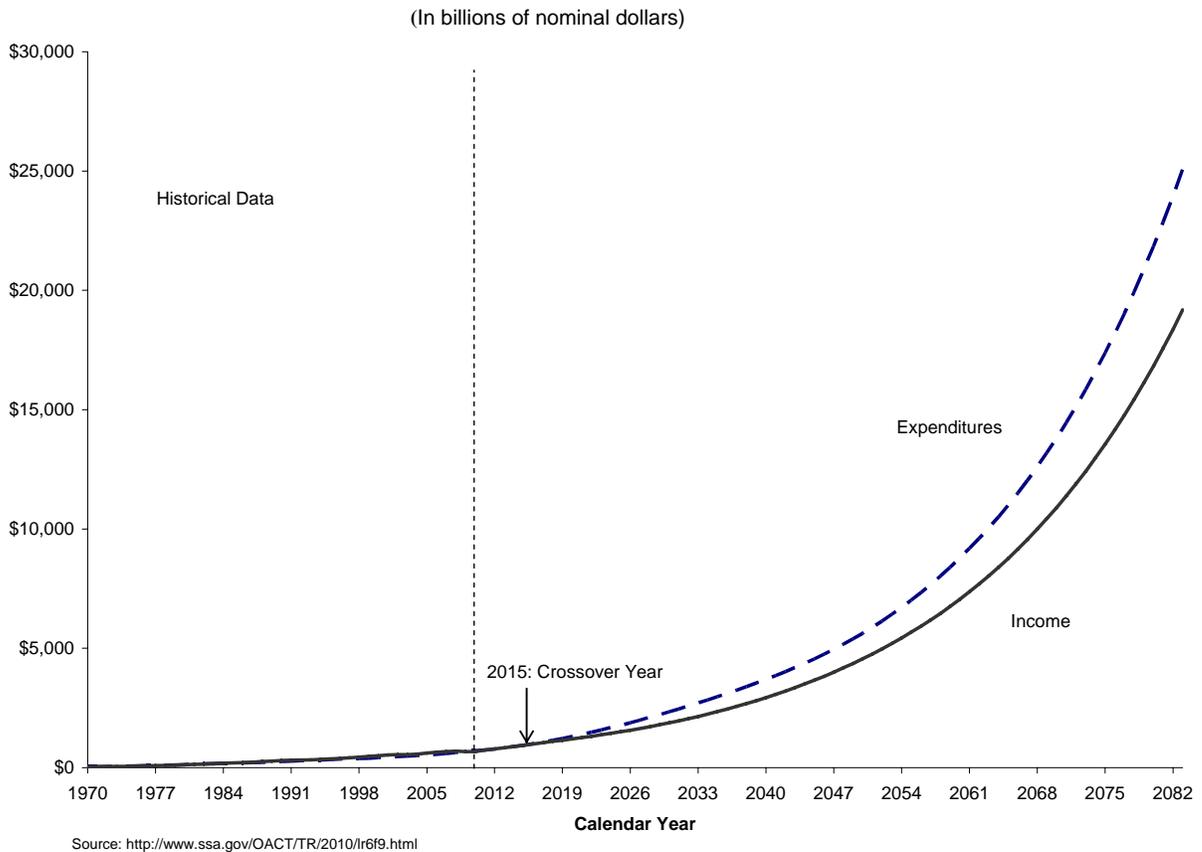
**Chart 1—OASDI Beneficiaries per 100 Covered Workers  
1970-2084**



### Social Security Projections

*Nominal Income and Expenditures.* Chart 2 shows historical values and actuarial estimates of combined OASDI annual income (excluding interest) and expenditures for 1970-2084 in nominal dollars. The estimates are for the open-group population. That is, the estimates include taxes paid from, and on behalf of, workers who will enter covered employment during the period, as well as those already in covered employment at the beginning of that period. These estimates also include scheduled benefit payments made to, and on behalf of, such workers during that period. Note that expenditure projections in Chart 2 and subsequent charts are based on current-law benefit formulas, regardless of whether the income and assets are available to finance them.

**Chart 2—OASDI Income (Excluding Interest) and Expenditures  
1970-2084**

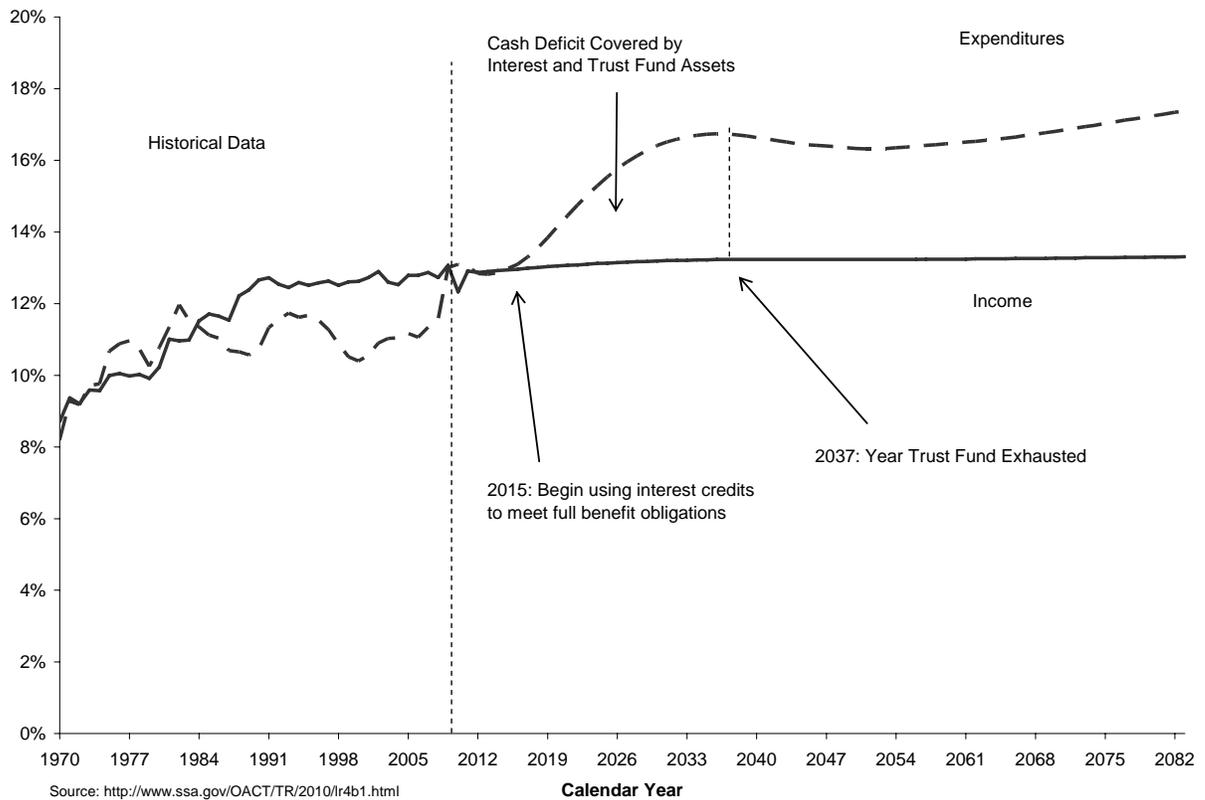


Currently, Social Security tax revenues exceed benefit payments and will continue to do so until 2015, when revenues are projected to fall below benefit payments, after which the gap between expenditures and revenues continues to widen.

*Income and Expenditures as a Percent of Taxable Payroll.* Chart 3 shows annual income (excluding interest but including both payroll and benefit taxes) and expenditures expressed as percentages of taxable payroll, commonly referred to as the income rate and cost rate, respectively.

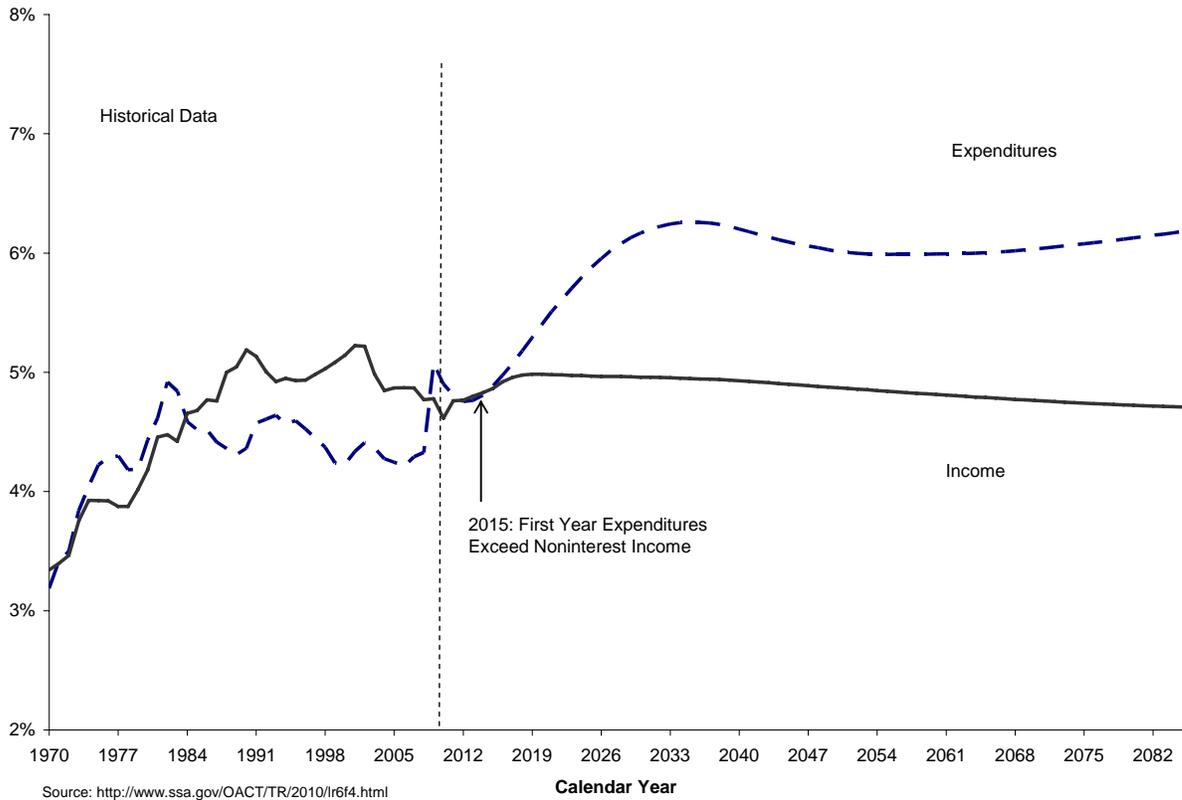
The OASDI cost rate is projected to increase rapidly and first exceeds the income rate in 2015, producing cashflow deficits thereafter. As described above, surpluses that occur prior to 2016 are “loaned” to the General Fund and accumulate, with interest, reserve spending authority for the trust fund. The reserve spending authority represents an obligation for the General Fund. Beginning in 2015, Social Security will start using interest credits to meet full benefit obligations. The Government will need to raise taxes, reduce benefits, increase borrowing from the public, and/or cut spending for other programs to meet its obligations to the trust fund. By 2037, the trust fund reserves (and thus reserve spending authority) are projected to be exhausted. Even if a trust fund's assets are exhausted, however, tax income will continue to flow into the fund. Present tax rates would be sufficient to pay 78 percent of scheduled benefits after trust fund exhaustion in 2037 and 75 percent of scheduled benefits in 2084.

**Chart 3—OASDI Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2084**



*Income and Expenditures as a Percent of GDP.* Chart 4 shows estimated annual income (excluding interest) and expenditures, expressed as percentages of GDP, the total value of goods and services produced in the United States. This alternative perspective shows the size of the OASDI Program in relation to the capacity of the national economy to sustain it. The gap between expenditures and income generally widens with expenditures generally growing as a share of GDP and income declining slightly relative to GDP. Social Security's expenditures are projected to grow from 4.8 percent of GDP in 2010 to 6.02 percent in 2084. In 2084, expenditures are projected to exceed income by 1.42 percent of GDP.

**Chart 4—OASDI Income (Excluding Interest) and Expenditures  
as a Percent of GDP  
1970-2084**



*Sensitivity Analysis.* Actual future income from OASDI payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors: the size and composition of the population that is receiving benefits, the level of monthly benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers' earnings. These factors will depend, in turn, upon future marriage and divorce rates, birth rates, death rates, migration rates, labor force participation and unemployment rates, disability incidence and termination rates, retirement age patterns, productivity gains, wage increases, cost-of-living increases, and many other economic and demographic factors.

This section presents estimates that illustrate the sensitivity of long-range expenditures and income for the OASDI Program to changes in *selected individual assumptions*. In this analysis, the intermediate assumption is used as the reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost (Alternative I) and high-cost (Alternative III) projections. For example, when analyzing sensitivity with respect to variation in real wages, income and expenditure projections using the intermediate assumptions are compared to the outcome when projections are done by changing only the real wage assumption to either low-cost or high-cost alternatives.

The low-cost alternative is characterized by assumptions that generally improve the financial status of the program (relative to the intermediate assumption) such as slower improvement in mortality (beneficiaries die younger). In contrast, assumptions under the high-cost alternative generally worsen the financial outlook. One exception occurs with the CPI assumption (see below).

Table 2 shows the effects of changing individual assumptions on the present value of estimated OASDI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. For example, the intermediate assumption for the annual rate of *reduction in age-sex-adjusted death rates* is 0.79 percent. For the low-cost alternative, a slower reduction rate (0.33 percent) is assumed as it means that beneficiaries die at a younger age relative to the intermediate assumption, resulting in lower expenditures. Under the low-cost assumption, the shortfall drops from \$7,947 billion to \$6,076 billion, a 24 percent smaller shortfall. The high-cost death rate assumption (1.32 percent) results in an increase in the shortfall, from \$7,947 billion to \$9,991 billion, a 26 percent increase in the shortfall. Clearly, alternative death rate assumptions have a substantial impact on estimated future cashflows in the OASDI Program.

A higher fertility rate means more workers relative to beneficiaries over the projection period, thereby lowering the shortfall relative to the intermediate assumption. An increase in the rate from 2.0 to 2.3 percent results in an 12 percent smaller shortfall (i.e., expenditures less income), from \$7,947 billion to \$6,978 billion.

Higher real wage growth results in faster income growth relative to expenditure growth. Table 2 shows that a real wage differential that is 0.6 greater than the intermediate assumption of 1.2 results in a drop in the shortfall from \$7,947 billion to \$5,893 billion, a 26 percent decline.

The CPI change assumption operates in a somewhat counterintuitive manner, as seen in Table 2. A lower rate of change results in a higher shortfall. This arises as a consequence of holding the real wage assumption constant while varying the CPI so that wages (the income base) are affected sooner than benefits. If the rate is assumed to be 1.8 percent rather than 2.8 percent, the shortfall rises about 6 percent, from \$7,947 billion to \$8,444 billion.

The effect of net immigration is similar to fertility in that, over the 75-year projection period, higher immigration results in proportionately more workers (taxpayers) than beneficiaries. The low-cost assumption for net immigration results in a 6 percent drop in the shortfall, from \$7,947 billion to \$7,475 billion, relative to the intermediate case; and the high-cost assumption results in a 6 percent higher shortfall.

Finally, Table 2 shows the sensitivity of the shortfall to variations in the real interest rate or, in present value terminology, the sensitivity to alternative discount rates assuming a higher discount rate results in a lower present value. The shortfall of \$6,303 billion is 21 percent lower when the real interest rate is 3.6 percent rather than 2.9 percent, and 33 percent higher shortfall when the real interest rate is 2.1 percent rather than 2.9 percent.

**Table 2**  
**Present Values of Estimated OASDI Expenditures in Excess of Income**  
**Under Various Assumptions, 2010-2084**

(Dollar values in billions; values of assumptions shown in parentheses)

Assumption	Financing Shortfall Range		
	Low	Intermediate	High
Average annual reduction in death rates.....	6,076 (0.33)	7,947 (0.79)	9,991 (1.32)
Total fertility rate .....	6,978 (2.3)	7,947 (2.0)	8,892 (1.7)
Real wage differential .....	5,893 (1.8)	7,947 (1.2)	9,312 (0.6)
CPI change .....	7,400 (3.8)	7,947 (2.8)	8,444 (1.8)
Net immigration.....	7,475 (1,370,000) <sup>1</sup>	7,947 (1,065,000) <sup>1</sup>	8,394 (780,000) <sup>1</sup>
Real interest rate.....	6,303 (3.6)	7,947 (2.9)	10,579 (2.1)

<sup>1</sup> Amounts represent the average annual net immigration over the 75-year projection period.

Source: 2010 OASDI Trustees Report and SSA.

## Medicare Projections

*Medicare Legislation.* The Affordable Care Act as amended by the Health Care and Education Reconciliation Act of 2010 (the “Affordable Care Act” or ACA) significantly improves projected Medicare finances. The most important cost saving provision in the ACA is a revision in payment rates for parts A and B services other than for physicians’ services. Relative to payment rates made under prior law that were based on the rate at which prices for inputs used to provide Medicare services increase, the ACA reduces those payment rates by the rate at which productive efficiency in the overall economy increases, which is projected to average 1.1 percent per year. The ACA also achieves substantial cost savings by reducing payment rates for private health plans providing Parts A and B services (Part C or Medicare Advantage) to more closely match per beneficiary costs. Partly offsetting these changes was an increase in prescription drug coverage. In addition, the ACA increases Part A revenues by: (a) taxing high-cost employer-provided health care plans and thereby giving employers incentives to increase the share of compensation paid as taxable earnings, and (b) imposing a new 0.9 percent surtax on earnings in excess of \$200,000 (individual tax return filers) or \$250,000 (joint tax return filers) starting in 2013.

The 2010 Medicare Trustees Report warns that the “actual future costs for Medicare are likely to exceed those shown by the current-law projections’ that underlie both the Trustees Report and this Financial Report. This warning is primarily due to the fact that productivity growth in the provisions of Medicare services have in the past been much smaller than productivity growth in the overall economy, which suggests that the new productivity-based downward adjustments to Medicare payment rates may not be sustainable. This concern is reinforced by the fact that similar adjustments to payment rates for Medicare physicians’ services mandated by a 1996 Medicare reform have been consistently overridden by new law.

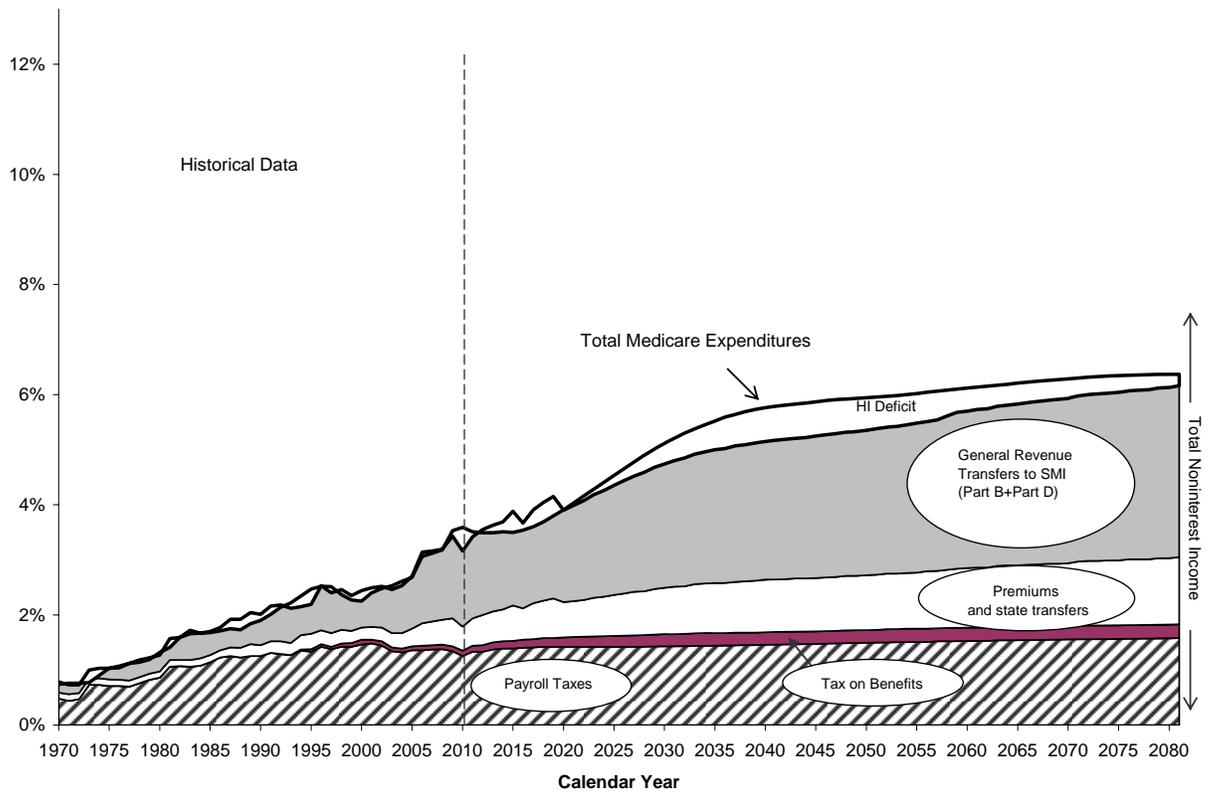
*Health Care Cost Growth.* In addition to the growth in the number of beneficiaries per worker, the Medicare Program has the added pressure of expected growth in the use and cost of health care per person that is driven in large part by new technology. Growth in Medicare cost per beneficiary in excess in growth in per capita GDP is referred to as “excess cost growth.” In last year’s Financial Report, excess cost growth was assumed to be about 1 percentage point—that is, Medicare expenditures per beneficiary were assumed to grow, on average, about one percentage point faster than per capita GDP over the long range. An assumption for excess cost growth was smaller than in recent history; excess cost growth averaged 1-1/2 percentage points between 1990 and 2007.<sup>5</sup> The combination of more beneficiaries per worker and 1 percent excess cost growth caused projected Medicare expenditures to grow substantially more rapidly than GDP in the 2009 Financial Report. In this year’s Report, however, long-term excess cost growth is essentially zero because of the productivity adjustments to payment rates called for by the ACA. As a result, the long term projected Medicare spending share of GDP in this Report is driven primarily by the same demographic trends that drive the OASDI spending share of GDP.

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<sup>5</sup> Congressional Budget Office, the Long-Term Budget Outlook, June 2009.

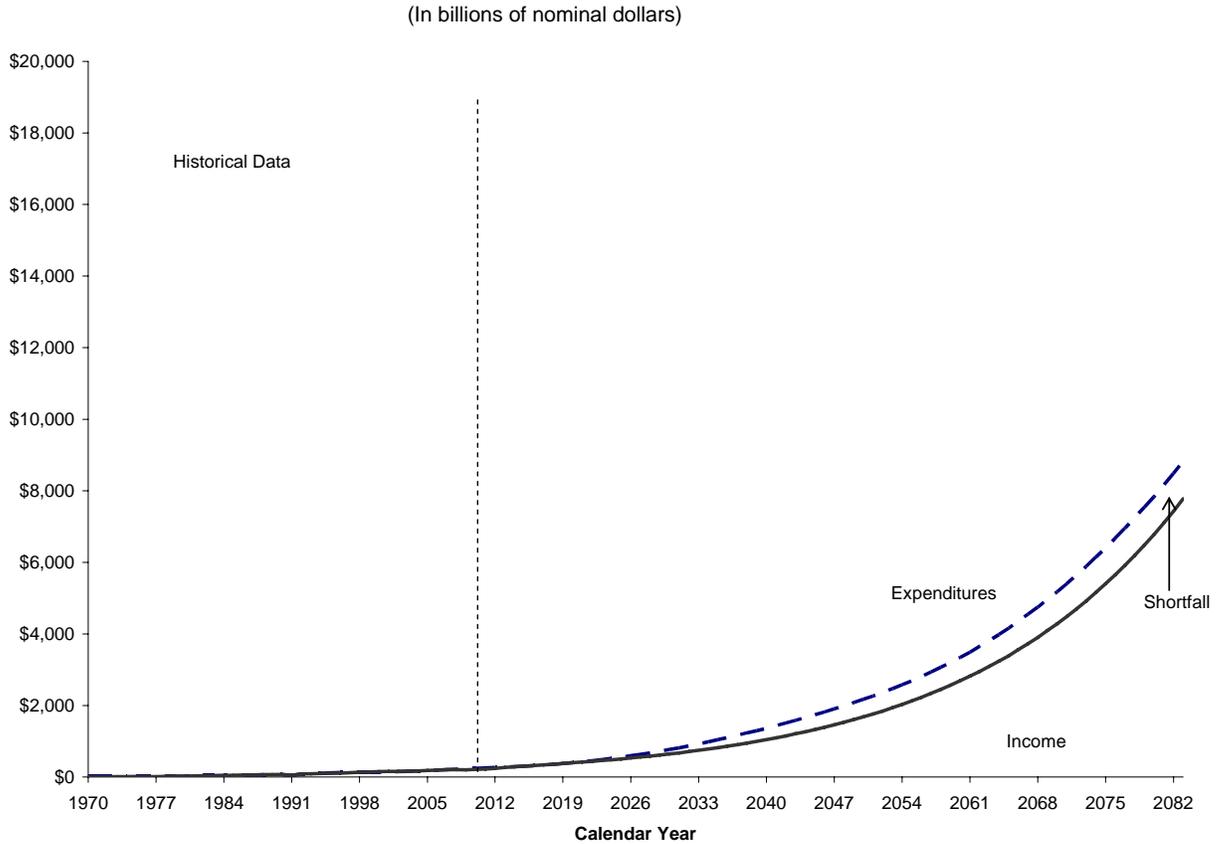
*Total Medicare.* Chart 5 shows expenditures and current-law noninterest revenue sources for HI and SMI combined as a percentage of GDP. The total expenditure line shows Medicare costs rising to 6.37 percent of GDP by 2084. Revenues from taxes and premiums (including State transfers under Part D) are expected to increase from 1.79 percent of GDP in 2010 to 3.06 percent of GDP in 2084. Payroll tax income increases gradually as a percent of GDP because the new tax on earnings in excess of \$250,000 for joint tax return filers and \$200,000 for individual tax return filers applies to an increasing share of earnings because the \$250,000 and \$200,000 thresholds are not indexed for price changes. Premiums combined for Parts B and D of SMI are approximately fixed as a share of Parts B and D costs, so they also increase as a percent of GDP. General revenue contributions for SMI, as determined by current law, are projected to rise as a percent of GDP from 1.37 percent to 3.13 percent over the same period. Thus, revenues from taxes and premiums (including State transfers) will fall substantially as a share of total noninterest Medicare income (from 57 percent in 2010 to 49 percent in 2084) while general revenues will rise (from 43 percent to 51 percent). The gap between total noninterest Medicare income (including general revenue contributions) and expenditures begins around 2010 and then steadily continues to widen, reaching 0.2 percent of GDP by 2081.

**Chart 5—Total Medicare (HI and SMI) Expenditures and Noninterest Income as a Percent of GDP 1970-2081**



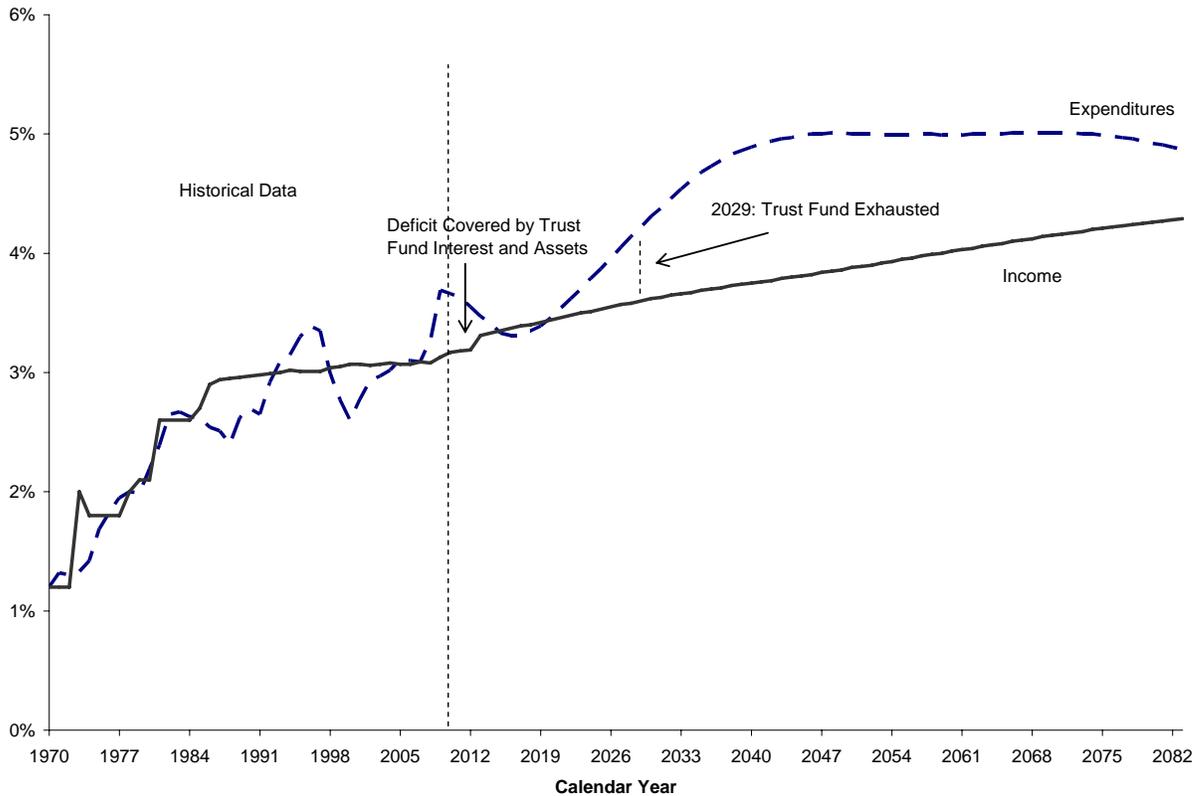
*Medicare, Part A (Hospital Insurance)—Nominal Income and Expenditures.* Chart 6 shows historical and actuarial estimates of HI annual income (excluding interest) and expenditures for 1970-2084 in nominal dollars. The estimates are for the open-group population.

**Chart 6—Medicare Part A Income (Excluding Interest) and Expenditures  
1970-2084**



*Medicare, Part A Income and Expenditures as a Percent of Taxable Payroll.* Chart 7 illustrates income (excluding interest) and expenditures as a percentage of taxable payroll over the next 75 years. The chart shows that the expenditure rate exceeds the income rate in 2008, and cash deficits continue thereafter. Trust fund interest earnings and assets provide enough resources to pay full benefit payments until 2029 with general revenues used to finance interest and loan repayments to make up the difference between cash income and expenditures during that period. Pressures on the Federal budget will thus emerge well before 2029. Present tax rates would be sufficient to pay 85 percent of scheduled benefits after trust fund exhaustion in 2029 and 89 percent of scheduled benefits in 2084.

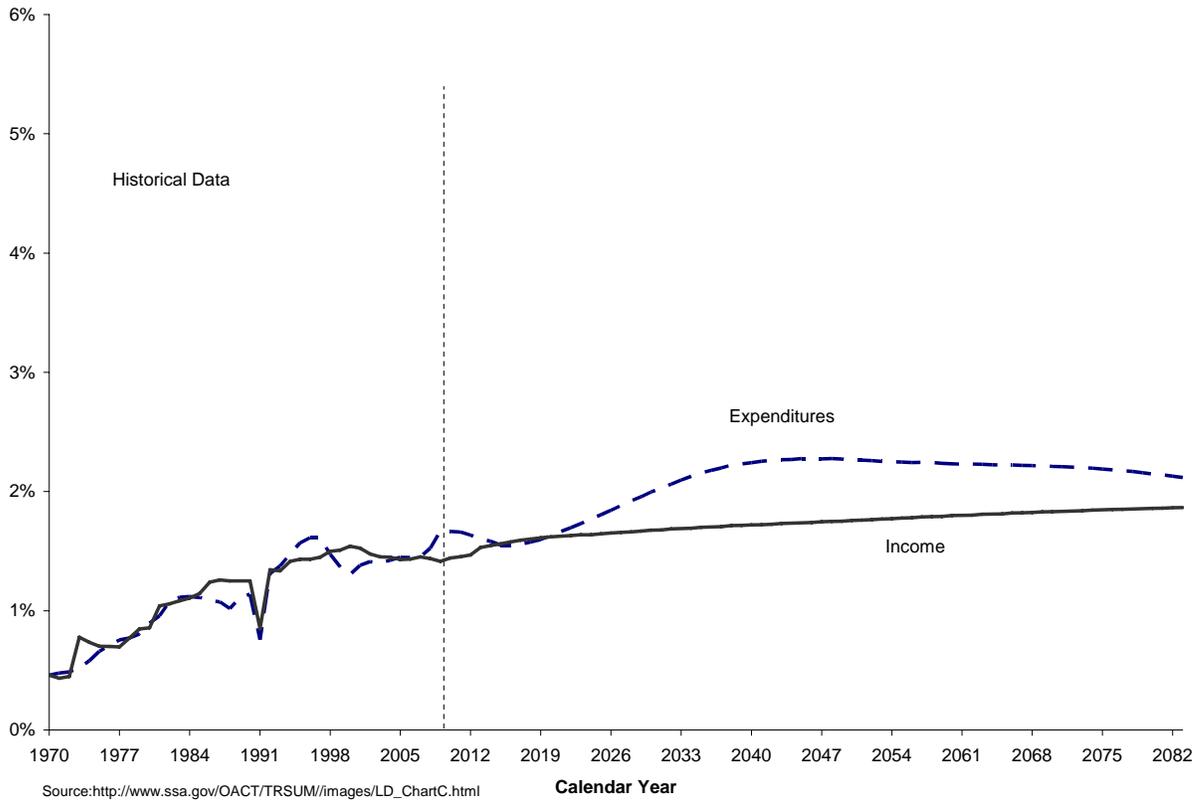
**Chart 7—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2084**



Source: [http://www.ssa.gov/OACT/TRSUM/images/LD\\_ChartC.html](http://www.ssa.gov/OACT/TRSUM/images/LD_ChartC.html)

*Medicare, Part A Income and Expenditures as a Percent of GDP.* Chart 8 shows estimated annual income (excluding interest) and expenditures, expressed as percentages of GDP, and the total value of goods and services produced in the United States. This alternative perspective shows the size of the HI Program in relation to the capacity of the national economy to sustain it. Medicare Part A’s expenditures are projected to grow from 1.7 percent of GDP in 2010, to 1.99 percent in 2030, and to 2.11 percent by 2084. The gap between expenditure and income shares of GDP widens and peaks at 0.53 percent in 2047 and then commences a steady decline, reaching 0.24 percent of GDP in 2084.

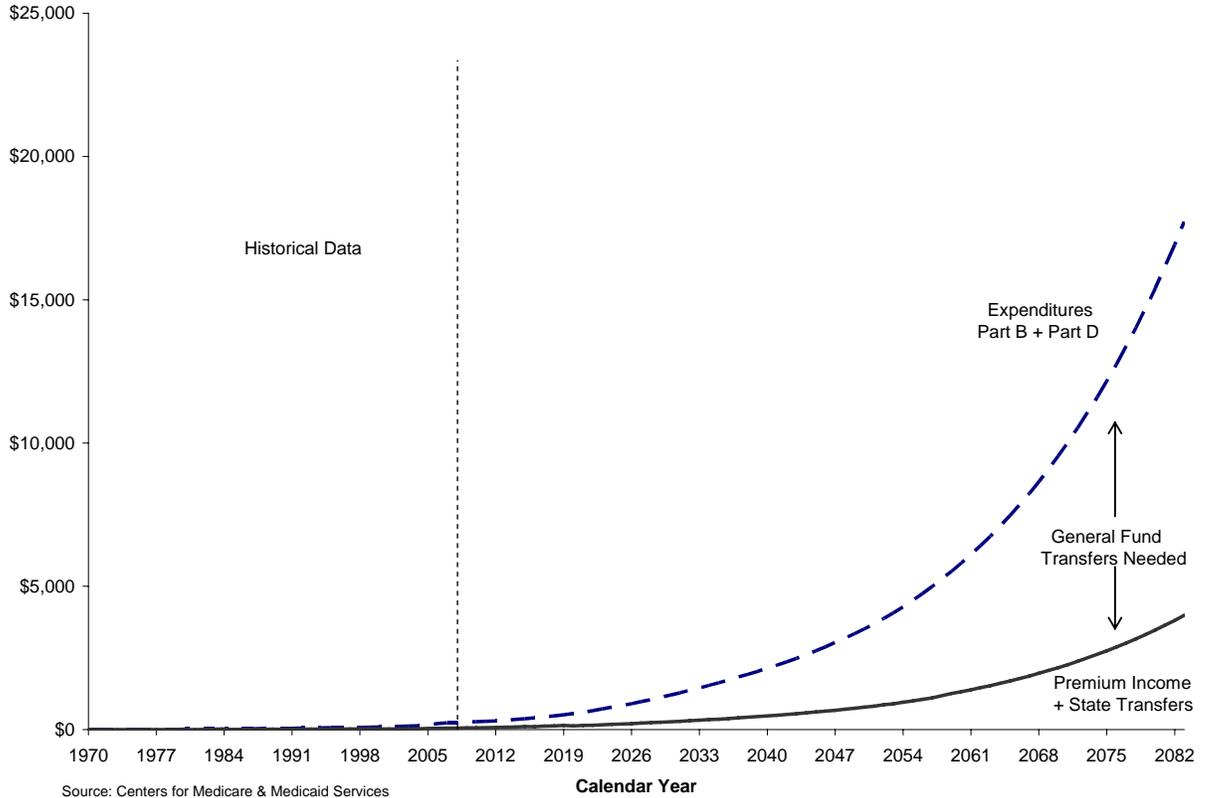
**Chart 8—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2084**



*Medicare, Parts B and D (Supplementary Medical Insurance).* Chart 9 shows historical and actuarial estimates of Medicare Part B and Part D premiums (and Part D State transfers) and expenditures for each of the next 75 years, in nominal dollars. The gap between premiums and State transfer revenues and program expenditures, a gap that will need to be filled with transfers from general revenues, grows throughout the projection period.

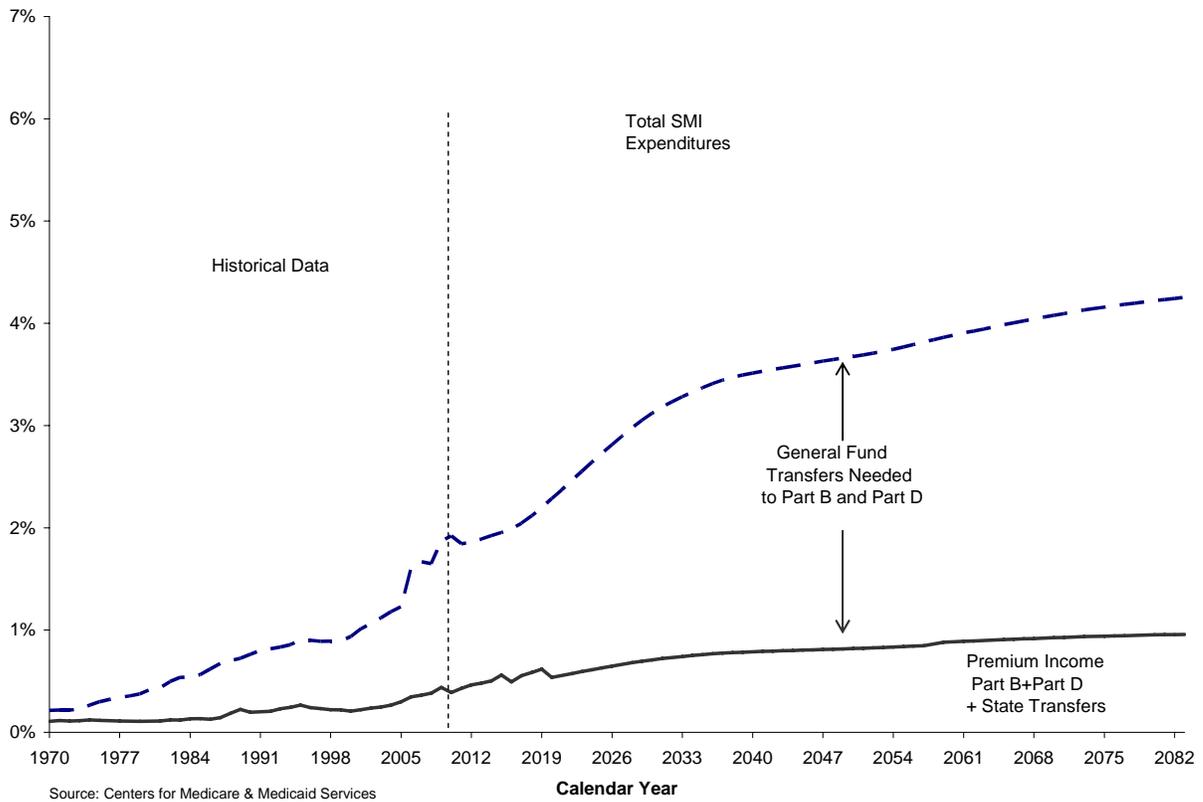
**Chart 9—Medicare Part B and Part D Premium and State Transfer Income and Expenditures  
1970-2084**

(In billions of nominal dollars)



*Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP.*  
 Chart 10 shows expenditures for the Supplementary Medical Insurance Program over the next 75 years expressed as a percentage of GDP, providing a perspective on the size of the SMI Program in relation to the capacity of the national economy to sustain it. SMI expenditures as a share of GDP are expected to grow rapidly from 1.92 percent in 2010 to 3.4 percent in 2035, and then grow more slowly reaching 4.26 in 2084. This growth pattern reflects growth in Medicare spending per beneficiary that is positive for the first half of the projection period before turning negative as a result of provisions in the ACA and to population ageing that is rapid through 2035 as the baby boom generation move into their advanced years and then slows to a modest pace consistent with increasing longevity. Premium and State transfer income grows from about 0.42 in 2010 to 1.14 percent in GDP in 2084, so the portion financed by General Fund transfers to SMI is projected to be about 76 percent throughout the projections period.

**Chart 10—Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP 1970-2084**



*Medicare Sensitivity Analysis.* This section illustrates the sensitivity of long-range cost and income estimates for the Medicare Program to changes in *selected individual assumptions*. As with the OASDI analysis, the intermediate assumption is used as the reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost and high-cost projections (see description of sensitivity analysis for OASDI).

Table 3 shows the effects of changing various assumptions on the present value of estimated HI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. Clearly, net HI expenditures are extremely sensitive to alternative assumptions about the growth in health care cost. For the low-cost alternative, the slower growth in health costs causes the shortfall to drop from \$2,683 billion to a surplus of \$2,146 billion, a 180 percent change from the \$2,683 billion shortfall to the \$2,146 billion surplus. The high-cost assumption results in a near quadrupling of the shortfall, from \$2,683 billion to \$10,346 billion.

Variations in the next four assumptions in Table 3 result in relatively minor changes in net HI expenditures. The higher or lower fertility assumptions cause an approximate 13 and 14 percent change in the shortfall relative to the intermediate case. The higher or lower real wage growth rate results in about a 22 and 44 percent change in the shortfall relative to the intermediate case. Wages are a key cost factor in the provision of health care. Higher wages also result in greater payroll tax income. HI expenditures exceed HI income by a wide and increasing margin in the future (Charts 6 to 8). CPI and net immigration changes have very little effect on net HI expenditures. Higher immigration increases the net shortfall modestly as higher payroll tax revenue is more than offset by higher medical care expenditures.

Table 3 also shows that the present value of net HI expenditures is 24 percent lower if the real interest rate is 3.6 percent rather than 2.9 percent and 34 percent higher if the real interest rate is 2.1 percent rather than 2.9 percent.

**Table 3**  
**Present Values of Estimated Medicare Part A Expenditures in Excess of**  
**Income Under Various Assumptions, 2010-2084**

(Dollar values in billions; values of assumptions shown in parentheses)

Assumption <sup>1</sup>	Financing Shortfall Range		
	Low	Intermediate	High
Average annual growth in health costs <sup>2</sup> .....	(2,146) (2.0)	2,683 (3.0)	10,346 (4.0)
Total fertility rate <sup>3</sup> .....	2,308 (2.3)	2,683 (2.0)	3,035 (1.7)
Real wage differential .....	1,507 (1.8)	2,683 (1.2)	3,284 (0.6)
CPI change .....	2,466 (3.8)	2,683 (2.8)	2,924 (1.8)
Net immigration.....	2,605 (1,370,000)	2,683 (1,065,000)	2,774 (780,000)
Real interest rate.....	2,107 (3.6)	2,683 (2.9)	3,603 (2.1)

<sup>1</sup> The sensitivity of the projected HI net cashflow to variations in future mortality rates is also of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Part A, mortality sensitivity.

<sup>2</sup> Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low-cost and high-cost alternatives assume that costs increase 1 percent slower or faster, respectively, than the intermediate assumption, *relative to growth in taxable payroll*.

<sup>3</sup> The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year and if she were to survive the entire childbearing period.

<sup>4</sup> Amount represents the average annual net immigration over the 75-year projection period.

Table 4 shows the effects of various assumptions about the growth in health care costs on the present value of estimated SMI (Medicare Parts B and D) expenditures in excess of income. As with HI, net SMI expenditures are very sensitive to changes in the health care cost growth assumption. For the low-cost alternative, the slower assumed growth in health costs reduces the Governmentwide resources needed for Part B from \$12,901 billion to \$9,288 billion and in Part D from \$7,229 billion to \$5,050 billion, about a 30 percent difference in each case. The high-cost assumption increases Governmentwide resources needed to \$18,546 billion for Part B and to \$10,695 billion for Part D, about a 44 percent and a 48 percent difference for Part B and Part D, respectively.

**Table 4**  
**Present Values of Estimated Medicare Parts B and D Future Expenditures**  
**Less Premium Income and State Transfers Under Three Health Care Cost**  
**Growth Assumptions, 2010-2084**

(In billions of dollars)

Medicare Program <sup>1</sup>	Governmentwide Resources Needed		
	Low (3.1)	Intermediate (4.1)	High (5.1)
Part B .....	9,288	12,901	18,546
Part D .....	5,050	7,229	10,695

<sup>1</sup> Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low and high scenarios assume that costs increase one percent slower or faster, respectively, than the intermediate assumption.

Source: Centers for Medicare & Medicaid Services.

## Sustainability of Social Security and Medicare

### 75-Year Horizon

According to the 2010 Medicare Trustees Report, the HI Trust Fund is projected to remain solvent until 2029 and, according to the 2010 Social Security Trustees Report, the OASDI Trust Funds are projected to remain solvent until 2037. In each case, some general revenues must be used to satisfy the authorization of full benefit payments until the year of exhaustion. This occurs when the trust fund balances accumulated during prior years are needed to pay benefits, which leads to a transfer from general revenues to the trust funds. Moreover, under current law, General Fund transfers to the SMI Trust Fund will occur into the indefinite future and will continue to grow with the growth in health care expenditures.

The potential magnitude of future financial obligations under these three social insurance programs is, therefore, important from a unified budget perspective as well as for understanding generally the growing resource demands of the programs on the economy. A common way to present future cashflows is in terms of their *present value*. This approach recognizes that a dollar paid or collected next year is worth less than a dollar today, because a dollar today could be saved and earn a year's worth of interest.

Table 5 shows the magnitudes of the primary expenditures and sources of financing for the three trust funds computed on an open-group basis for the next 75 years and expressed in present values. The data are consistent with the Statements of Social Insurance included in the principal financial statements. For HI, revenues from the public are projected to fall short of total expenditures by \$2,683 billion in present value terms which is the additional amount needed in order to pay scheduled benefits over the next 75 years.<sup>6</sup> From the trust fund perspective, the amount needed is \$2,379 billion in present value after subtracting the value of the existing trust fund balances (an asset to the trust fund account but an intragovernmental transfer to the overall budget). For SMI, revenues from the

<sup>6</sup> Interest income is not a factor in this table as dollar amounts are in present value terms.

public for Parts B and D combined are estimated to be \$20,130 billion<sup>7</sup> less than total expenditures for the two accounts, an amount that, from a budget perspective, will be needed to keep the SMI program solvent for the next 75 years. From the trust fund perspective, however, the present values of total revenues and total expenditures for the SMI Program are roughly equal due to the annual adjustment of revenue from other Government accounts to meet program costs.<sup>8</sup> For OASDI, projected revenues from the public fall short of total expenditures by \$7,947 billion<sup>9</sup> in present value dollars, and, from the trust fund perspective, by \$5,407 billion.

From the Governmentwide perspective, the present value of the total resources needed for the Social Security and Medicare Programs over and above current-law funding sources (payroll taxes, benefit taxes, and premium payments from the public) is \$30,760 billion. From the trust fund perspective, which counts the trust funds (\$2,921 billion in present value) and the general revenue transfers to the SMI Program (\$20,130 billion in present value) as dedicated funding sources, additional resources needed to fund the programs are \$7,709 billion in present value.

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<sup>7</sup> The actuarial present value of estimated 75-year future expenditures in excess of estimated 75-year future revenue for Medicare Parts A, B, and D decreased from \$38,107 billion in 2009 to \$22,813 billion in 2010, a reduction of \$15,294 billion. As explained at the beginning of this section, the decrease is primarily attributable to provisions of ACA as amended by the Health Care and Education Reconciliation Act of 2010 (the "Affordable Care Act" or ACA). The funding shortfall change by program is \$(11,088) billion for Part A, \$(4,264) billion for Part B, and \$57 billion for Part D.

<sup>8</sup> The SMI Trust Fund has \$77 billion of existing assets.

<sup>9</sup> For 2010, the actuarial present value of estimated future expenditures in excess of estimated future revenue, increased from \$7,677 billion in 2009 to \$7,947 billion in 2010. This increase is primarily attributable to the inclusion of an additional year for the Social Security Program in the projection period and valuing the shortfall in 2010 present value dollars rather than 2009 present value dollars, and the increase in taxable payroll that is expected to come about because of the new tax on high-cost health plans scheduled to go into effect starting in 2018 increase employer incentives for paying compensation as earnings subject to payroll tax rather than as untaxed health benefits. There were other changes to economic and demographic assumptions, and to projection methods, that were largely offsetting in their effect on the Social Security Program's projections.

**Table 5**  
**Present Values of Costs Less Revenues of 75-Year Open-Group Obligations**  
**HI, SMI, and OASDI**

(In billions of dollars, as of January 1, 2010)

	HI	SMI		OASDI	Total
		Part B	Part D		
<b>Revenues from the public:</b>					
Taxes.....	14,408	-	-	40,118	54,526
Premiums, State transfers.....		4,836	2,486		7,322
Total.....	14,408	4,836	2,486	40,118	61,848
<b>Total costs to the public.....</b>	<b>17,090</b>	<b>17,737</b>	<b>9,715</b>	<b>48,065</b>	<b>92,607</b>
<b>Net results — budget perspective*</b>					
.....	2,682	12,901	7,229	7,947	30,760
Revenues from other					
Government accounts.....	-	12,901	7,229	-	20,130
Trust fund balance as of					
1/1/2010.....	304	76	1	2,540	2,921
<b>Net results — trust fund perspective*</b>					
.....	<u>2,379</u>	<u>(76)</u>	<u>(1)</u>	<u>5,407</u>	<u>7,709</u>

\*Net results are computed as costs less revenues.

Note: Details may not add to totals due to rounding.

Source: 2010 OASDI and Medicare Trustees' Reports.

## Infinite Horizon

The 75-year horizon represented in Table 5 is consistent with the primary focus of the Social Security and Medicare Trustees' Reports. For the OASDI Program, for example, an additional \$7.9 trillion in present value will be needed above currently scheduled taxes to pay for scheduled benefits (\$5.4 trillion from the trust fund perspective). Yet, a 75-year projection is not a complete representation of all future financial flows through the infinite horizon. For example, when calculating unfunded obligations, a 75-year horizon includes revenue from some future workers but only a fraction of their future benefits. In order to provide a more complete estimate of the long-run unfunded obligations of the programs, estimates can be extended to the infinite horizon. The open-group infinite horizon net obligation is the present value of all expected future program outlays less the present value of all expected future program tax and premium revenues. Such a measure is provided in Table 6 for the three trust funds represented in Table 5.

From the budget or Governmentwide perspective, the values in line 1 plus the values in line 4 of Table 6 represent the value of resources needed to finance each of the programs into the infinite future. The sums are shown in the last line of the table (also equivalent to adding the values in the second and fifth lines). The total resources needed for all the programs sums to \$77.9 trillion in present value terms. This need can be satisfied only through increased borrowing, higher taxes, reduced program spending, or some combination.

The second line shows the value of the trust fund at the beginning of 2010. For the HI and OASDI Programs this represents, from the trust fund perspective, the extent to which the programs are funded. From that perspective, when the trust fund is subtracted, an additional \$6.3 trillion and \$16.2 trillion, respectively, are needed to sustain the programs into the infinite future. As described above, from the trust fund perspective, the SMI Program is fully funded, from a Governmentwide basis, the substantial gap that exists between premiums and State transfer revenue and program expenditures in the SMI Program (\$31.5 trillion and \$21 trillion) represents future general revenue obligations of the Federal budget.

In comparison to the analogous 75-year number in Table 5, extending the calculations beyond 2084, captures the full lifetime benefits, and taxes and premiums of all current and future participants. The shorter horizon understates financial needs by capturing relatively more of the revenues from current and future workers and not capturing all of the benefits that are scheduled to be paid to them.

**Table 6**  
**Present Values of Costs Less Tax, Premium and State Transfer Revenue**  
**through the Infinite Horizon, HI, SMI, OASDI**

(In trillions of dollars as of January 1, 2010)

	HI	SMI		OASDI	Total
		Part B	Part D		
Present value of future costs less future taxes, premiums, and State transfers for current participants .....	7.2	10.6	5.2	20.0	43.0
Less current trust fund balance .....	0.3	0.1	-	2.5	2.9
Equals net obligations for past and current participants .....	6.9	10.5	5.2	17.5	40.1
Plus net obligations for future participants .....	(0.6)	21.0	15.8	(1.3)	34.9
Equals net obligations through the infinite future for all participants .....	<u>6.3</u>	<u>31.5</u>	<u>21.0</u>	<u>16.2</u>	<u>75.0</u>
Present values of future costs less the present values of future income over the infinite horizon .....	<u>6.6</u>	<u>31.6</u>	<u>21.0</u>	<u>18.7</u>	<u>77.9</u>

Details may not add to totals due to rounding.

Source: 2010 OASDI and Medicare Trustees' Reports.

## Railroad Retirement, Black Lung, and Unemployment Insurance

### Railroad Retirement

The Railroad Retirement Board (RRB) was created in the 1930s to establish a retirement benefit program for the nation's railroad workers. As the Social Security Program legislated in 1935 would not give railroad workers credit for service performed prior to 1937, legislation was enacted in 1934, 1935, and 1937 (collectively the Railroad Retirement Acts of the 1930s) to establish a railroad retirement program separate from the Social Security Program.

Railroad retirement pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

Payroll taxes paid by railroad employers and their employees provide a primary source of income for the Railroad Retirement and Survivors' Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: financial interchanges with the Social Security and Medicare trust funds, earnings on investments, Federal income taxes on railroad retirement benefits, and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits). See Note 26—Social Insurance, for additional information on railroad retirement program financing.

The RRSIA liberalized benefits for 30-year service employees and their spouses, eliminated a cap on monthly benefits for retirement and disability benefits, lowered minimum service requirements from 10 to 5 years, and provided for increased benefits for widow(er)s. Per the RRSIA, amounts in the Railroad Retirement Account and the SSEB Account that are not needed to pay current benefits and administrative expenses are transferred to the NRRIT whose sole purpose is to manage and invest railroad retirement assets. NRRIT's Board of Trustees is empowered to invest trust assets in nongovernmental assets, such as equities and debt, as well as, in Government securities. Prior to RRSIA, all investments were limited to Government securities.

Since its inception, NRRIT has received \$21.3 billion from RRB (including \$19.2 billion in fiscal year 2003, pursuant to RRSIA) and returned \$9.9 billion. During fiscal year 2010, the NRRIT made net transfers of \$2.0 billion to the RRB to pay retirement benefits. Administrative expenses of the trust are paid out of trust assets. The balance as of September 30, 2010, and 2009, of non-Federal securities and investments of the NRRIT are disclosed in Note 9—Securities and Investments.

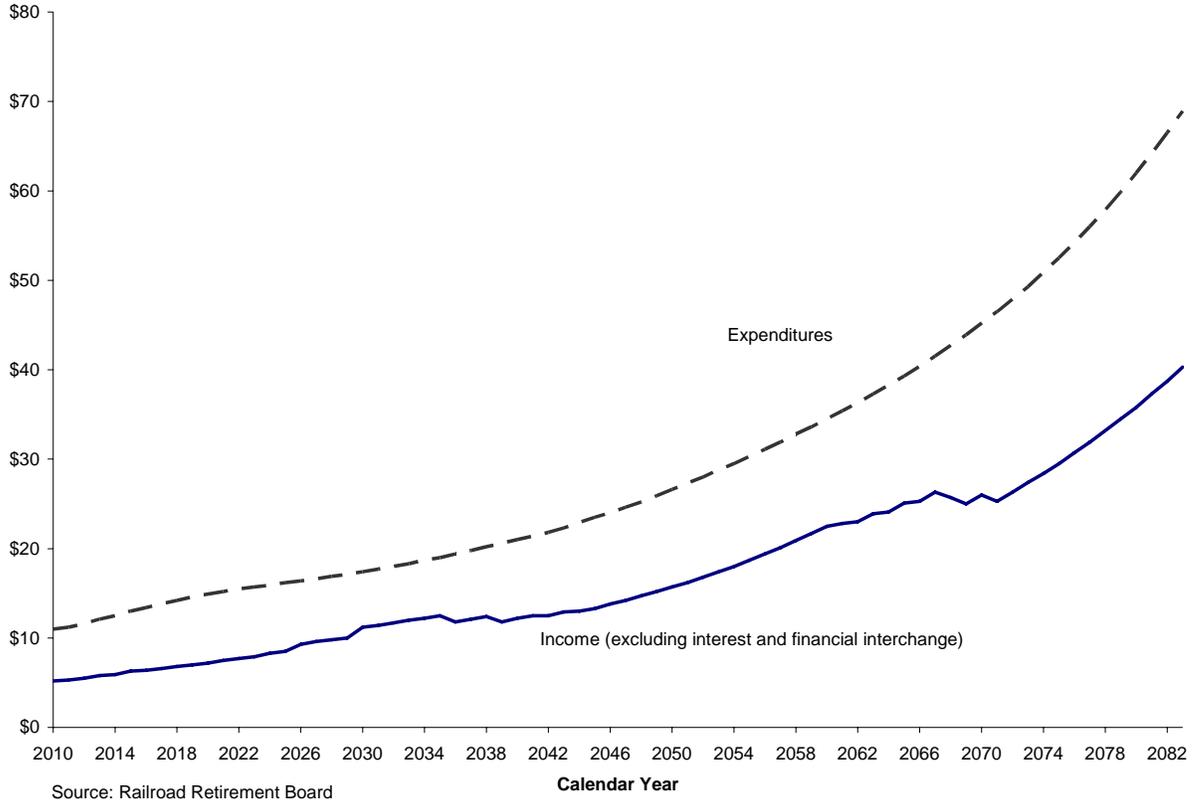
### Cashflow Projections

*Economic and Demographic Assumptions.* The economic and demographic assumptions used for the most recent set of projections are shown in the "Railroad Retirement" section of Note 26—Social Insurance.

*Nominal Income and Expenditures.* Chart 11 shows, in nominal dollars, estimated railroad retirement income (excluding interest and financial interchange income) and expenditures for the period 2010-2084 based on the intermediate set of assumptions used in the RRB's actuarial evaluation of the program. The estimates are for the open-group population, which includes all persons projected to participate in the Railroad Retirement Program as railroad workers or beneficiaries during the period. Thus, the estimates include payments from, and on behalf of, those who are projected to be employed by the railroads during the period as well as those already employed at the beginning of the period. They also include expenditures made to, and on behalf of, such workers during that period.

**Chart 11—Estimated Railroad Retirement Income  
(Excluding Interest and Financial Interchange Income) and Expenditures  
2010-2084**

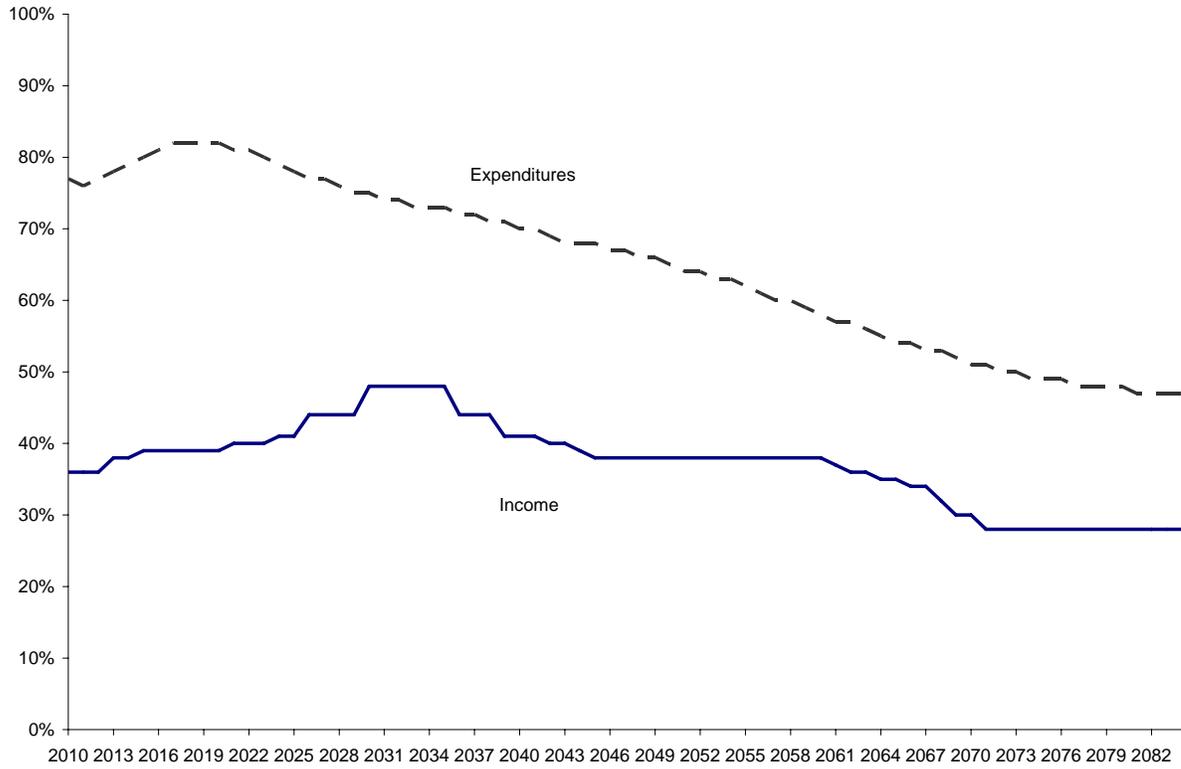
(In billions of nominal dollars)



As Chart 11 shows, expenditures are expected to exceed tax income for the entire projection period. The imbalances continue to widen until about 2023, decrease slightly for next 7 years, and then begin to grow steadily after 2030.

*Income and Expenditures as a Percent of Taxable Payroll.* Chart 12 shows estimated expenditures and income as a percent of tier II taxable payroll. The imbalances grow until 2020 but then begin to decrease somewhat steadily as expenditures fall. Tax rates begin to decline after 2035, stabilizing in 2071 and after. Compared to last year, projected tax rates are lower, on average. The tier II tax rate is determined from a tax rate table based on the average account benefit ratio.

**Chart 12—Estimated Railroad Retirement Income  
(Excluding Interest and Financial Interchange Income) and Expenditures  
as a Percent of Tier II Taxable Payroll  
2010-2084**



Source: Railroad Retirement Board

Calendar Year

*Sensitivity Analysis.* Actual future income from railroad payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors as mentioned above. Two crucial assumptions are employment growth and the interest rate. Table 7 shows the sensitivity of the shortfall in the Railroad Retirement Program to variations in these two assumptions. The low-cost employment scenario has a 5.2 percent smaller shortfall of income to expenditures, and the high-cost scenario has a 4.8 percent higher shortfall. A higher discount rate reduces future values relative to a lower rate. As seen in the table, the shortfall is 29.4 percent lower if the interest rate is 11 percent rather than 7.5 percent and 78.7 percent higher when the interest rate is 4 percent rather than 7.5 percent.

**Table 7**  
**Present Values of Railroad Retirement Expenditures in Excess of Income**  
**Under Various Employment and Interest Rate Assumptions, 2010-2084**

(Dollar values in billions; values of assumptions shown in parentheses)

<b>Assumption</b>	<b>Low</b>	<b>Middle</b>	<b>High</b>
Employment <sup>1</sup> .....	97.2 (-0.5%)	102.5 (-2.0%)	107.4 (-3.5%)
Interest rate.....	72.4 (11%)	102.5 (7.5%)	183.2 (4.0%)

<sup>1</sup> The low and middle employment scenarios have passenger service employment remaining at 43,000 workers per year and the remaining employment base declining at 0.5 percent and 2.0 percent, respectively, for the next 23 years. The high-cost scenario has passenger service employment declining by 500 per workers per year until a level of 35,000 is reached with the remaining employment base declining by 3.5 percent per year for 25 years, at a reducing rate over the next 25 years, and remaining level thereafter.

Source: Railroad Retirement Board.

## Sustainability of Railroad Retirement

Table 8 shows the magnitudes of the primary expenditures and sources of financing for the Railroad Retirement Program computed on an open-group basis for the next 75 years and expressed in present values as of January 1, 2010. The data are consistent with the Statements of Social Insurance.

From a Governmentwide perspective, revenues are expected to fall short of expenditures by approximately \$102.5 billion, which represents the present value of resources needed to sustain the Railroad Retirement Program. From a trust fund perspective, when the trust fund balance and the financial interchange and transfers are included, the combined balance of the NRRIT, the Railroad Retirement Account, and the SSEB Account show a slight surplus.

**Table 8**  
**Present Values of 75-Year Projections of Revenues and Expenditures for the Railroad Retirement Program**<sup>1, 2</sup>

(In billions of present-value dollars as of January 1, 2010)

<b>Estimated future income (excluding interest)</b> <sup>3</sup> received from or on behalf of:	
Current participants who have attained retirement age.....	5.4
Current participants not yet having attained retirement age.....	46.8
Those expected to become participants.....	65.5
All participants.....	<u>117.7</u>
<b>Estimated future expenditures:</b> <sup>4</sup>	
Current participants who have attained retirement age.....	104.8
Current participants not yet having attained retirement age.....	88.0
Those expected to become participants.....	27.4
All participants.....	<u>220.2</u>
<b>Net obligations from budget perspective (expenditures less income)</b> .....	102.5
Railroad retirement program assets (mostly investments stated at market) <sup>5</sup> .....	24.9
Financial interchange from Social Security Trust.....	<u>78.7</u>
<b>Net obligations from trust fund perspective</b> .....	<u><u>(1.1)</u></u>

<sup>1</sup> Represents combined values for the Railroad Retirement Account, SSEB Account, and NRRIT, based on middle employment assumption.

<sup>2</sup> The data used reflect the provisions of RRSIA of 2001.

<sup>3</sup> Future income (excluding interest) includes tier I taxes, tier II taxes, and income taxes on benefits.

<sup>4</sup> Future expenditures include benefits and administrative expenditures.

<sup>5</sup> The value of the fund reflects the 7.5 percent interest rate assumption. The RRB uses the relatively high rate due to investments in private securities.

Note: Detail may not add to totals due to rounding. Employee and beneficiary status are determined as of 1/1/2009 whereas present values are as of 1/1/2010.

## Black Lung

The Federal Coal Mine Health and Safety Act of 1969 created the Black Lung Disability Benefit Program to provide compensation, medical, and survivor benefits for eligible coal miners who are totally disabled due to pneumoconiosis (black lung disease) arising out of their coal mine employment. The survivor benefits are available only for eligible survivors of coal miners who died due to pneumoconiosis. DOL operates the Black Lung Disability Benefit Program. The BLDTF provides benefit payments to eligible coal miners totally disabled by pneumoconiosis and to eligible survivors when no responsible mine operator can be assigned the liability. The beneficiary population is a nearly closed universe in which attrition by death exceeds new entrants by a ratio of more than ten to one.

Excise taxes on coal mine operators, based on the sale of coal, are the primary source of financing black lung disability payments and related administrative costs. The Black Lung Benefits Revenue Act provided for repayable advances to the BLDTF from the General Fund of the Treasury, in the event that BLDTF resources were not adequate to meet program obligations. Prior to legislation enacted in 2008 that allowed for the restructuring of BLDTF debt, the trust fund had accumulated large liabilities from significant and growing shortfalls of excise taxes relative to benefit payments and interest expenses.

The Energy Improvement and Extension Act of 2008 (P.L. 110-343), enacted on October 3, 2008, contained several provisions that significantly improved the BLDTF's financial position, including:

- Continuation of a previously-enacted increase in coal excise tax rates for an additional 5 years, through December 2018;
- Provision for the restructuring of BLDTF debt by refinancing the outstanding repayable advances with proceeds from issuing new debt instruments with lower interest rates; and
- A one-time appropriation that significantly reduced the outstanding debt of the BLDTF.

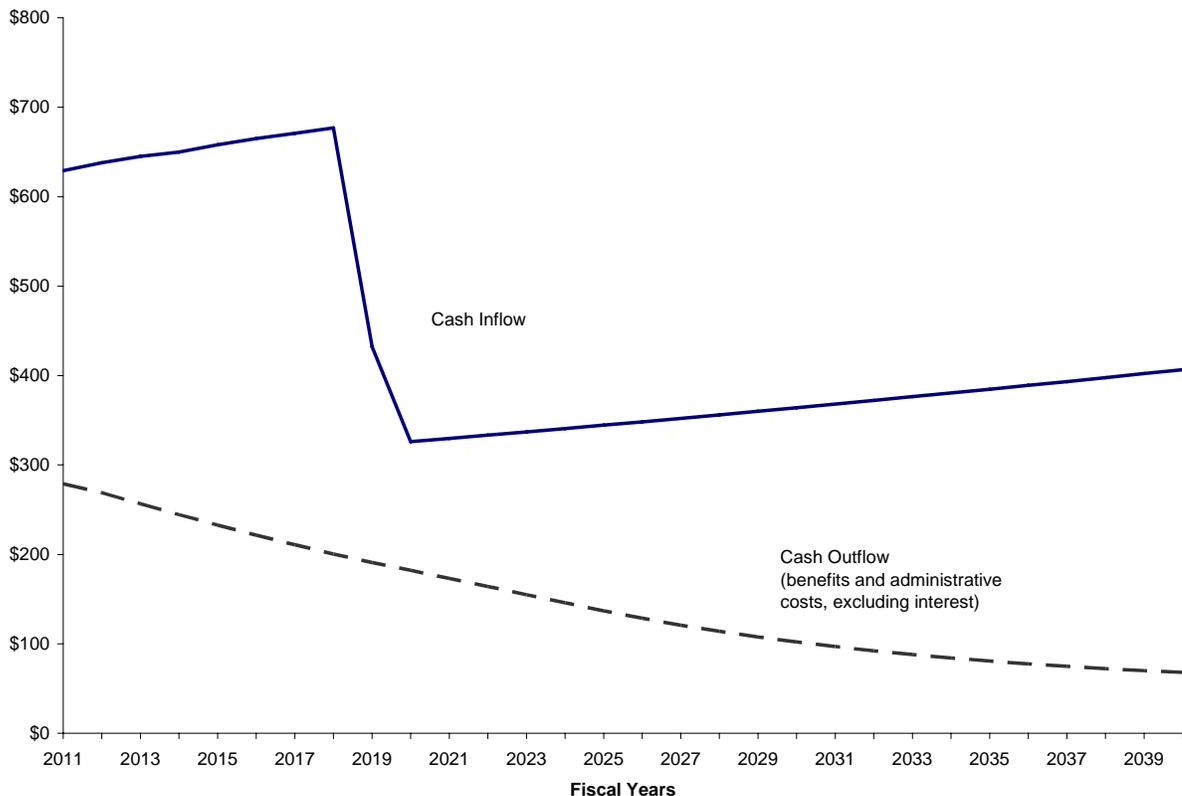
The Act also allowed that any debt issued by the BLDTF subsequent to the refinancing may be used to make benefit payments, other authorized expenditures, or to repay debt and interest from the initial refinancing. All debt issued by the BLDTF was effected as borrowing from the Treasury's Bureau of the Public Debt.

On September 30, 2010, total liabilities of the BLDTF exceeded assets by \$6.2 billion. Prior to the enactment of P.L. 110-343, this shortfall was funded by repayable advances to the BLDTF, which are repayable with interest. Pursuant to P.L. 110-343, any shortfall will be financed with debt instruments similar in form to zero-coupon bonds.

From the budget or consolidated financial perspective, Chart 13 shows projected black lung expenditures (excluding interest) and excise tax collections for the period 2011-2040. The significant assumptions used in the most recent set of projections are shown in the "Black Lung" section of Note 26—Social Insurance. The projected decrease in cash inflows in the year 2019 and, thereafter, is the result of a scheduled reduction in the tax rate on the sale of coal. This rate reduction is projected to result in a 36 percent decrease in the amount of excise taxes collected between the years 2018 and 2019.

**Chart 13—Estimated Black Lung Income and Expenditures (Excluding Interest)  
2011-2040**

(In millions of nominal dollars)



Source: Department of Labor

**Table 9**  
**Present Values of 30-Year Projections of Expenditures and Revenues**  
**for the Black Lung Disability Benefit Program**

(In billions of present value dollars, as of September 30, 2010)

Projected future expenditures .....	2.9
Projected future tax income .....	8.1
Net obligations from budget perspective (expenditures less income) .....	(5.2)
Accumulated balance due general fund .....	6.2
Net obligations from trust fund perspective .....	1.0

Note: Detail may not add to totals due to rounding.

Source: Department of Labor projections and Treasury Department calculations.

Table 9 shows present values of 30-year projections of expenditures and revenues for the Black Lung Disability Benefit Program computed as of September 30, 2010. Cashflows were discounted using the rates on the debt in the BLDTF. From a Governmentwide (budget) perspective, the present value of expenditures is expected to be less than the present value of income by \$5.2 billion (a surplus). From a trust fund perspective, a large balance (\$6.2 billion) is owed to the General Fund. From that perspective, when that accumulated balance is combined with the cashflow surplus, the program has a shortfall of \$1.0 billion in present value dollars. This compares to a shortfall of \$0.6 billion reported in last year's *Financial Report*.

**Unemployment Insurance**

The Unemployment Insurance Program was created in 1935 to provide temporary partial wage replacement to workers who lost their jobs. The program is administered through a unique system of Federal and State partnerships established in Federal law but administered through conforming State laws by State agencies. DOL interprets and enforces Federal law requirements and provides broad policy guidance and program direction, while program details such as benefit eligibility, duration, and amount of benefits are established through individual State unemployment insurance statutes and administered through State unemployment insurance agencies.

The program is financed through the collection of Federal and State unemployment taxes that are credited to the UTF and reported as Federal tax revenue. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for Federal and State administration of the Unemployment Insurance Program, veterans' employment services, State employment services, and the Federal share of extended unemployment insurance benefits. Federal unemployment taxes are also used to maintain a loan account within the UTF, from which insolvent State accounts may borrow funds to pay unemployment insurance benefits.

Chart 14 shows the projected cash contributions and expenditures over the next 10 years under expected economic conditions (described below). The significant assumptions used in the projections include total unemployment rates, civilian labor force levels, percent of unemployed receiving benefits, total wages, distribution of benefit payments by State, State tax rate structures, State taxable wage bases, and interest rates on UTF investments. These projections, excluding interest earnings, indicate a negative net cashflow until 2012 followed by positive net cashflow for the remainder of the projection period.

The Worker, Homeownership, and Business Assistance Act of 2009, was enacted on November 6, 2009. The Act extended unemployment benefits to eligible recipients up to 14 additional weeks in all States. It also extended a total of up to 20 additional weeks in States with unemployment of 8.5 percent or greater. The Act also amended section 3301 of the Internal Revenue Code of 1986 to extend the 0.2 percent Federal Unemployment Tax Act (FUTA) surtax on covered employers through June 30, 2011. No benefits are payable for weeks of unemployment commencing before the date of enactment of the Act.

P.L. 111-205 Unemployment Compensation Extension Act of 2010, enacted on July 22, 2010, amends the Supplemental Appropriation Act, 2008 with respect to the state-established individual emergency unemployment compensation account (EUCA) and to apply to claims for Emergency Unemployment Compensation (EUC) payments the terms and conditions of state unemployment compensation law relating to availability of work, active search for work, and refusal to accept work. The Act extends the final dates for entering a federal-state agreement under the EUC program through November 30, 2010. The Act also postpones the termination of the program until April 30, 2011, and amends the Assistance for Unemployed Workers and Struggling Families Act to extend until December 1, 2010, and requires Federal payments to states cover 100 percent of EUC.

**Chart 14—Estimated Unemployment Trust Fund Cashflow  
Using Expected Economic Conditions  
2011-2020**

(In billions of nominal dollars)

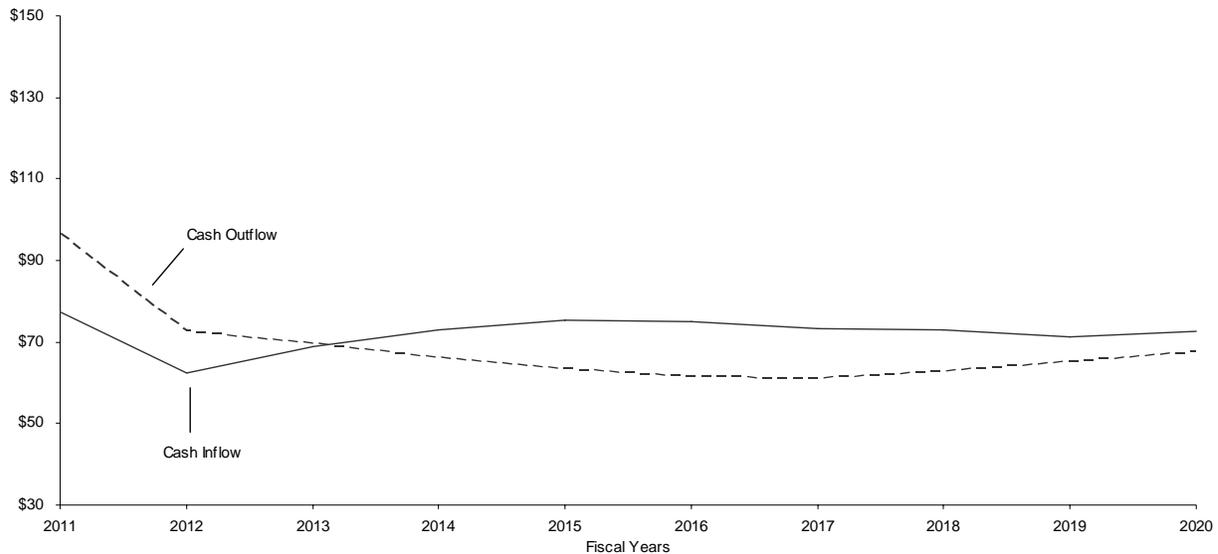


Table 10 shows present values of 10-year projections of revenues and expenditures for the Unemployment Insurance Program using a discount rate of 4.25 percent, the average of the interest rates underlying the 10-year projections. Three sets of numbers are presented in order to show the effects of varying economic conditions as reflected in different assumptions about the unemployment rate. For expected economic conditions, the estimates are based on an unemployment rate of 9.27 percent during fiscal year 2011, decreasing to below 6 percent in fiscal year

2015 and thereafter. Under Recovery Scenario One (decreasing unemployment rates), the unemployment rate decreases from 8.3 percent in fiscal year 2011 to 5.2 percent after fiscal year 2016. Under Recovery Scenario Two (higher than expected unemployment), the unemployment rate is assumed to reach 10.38 percent in fiscal year 2011 decreasing to below 6 percent in fiscal year 2016 and thereafter.

Each scenario uses an open-group that includes current and future participants of the Unemployment Insurance Program. Table 10 shows the impact on the UTF projections of varying projected unemployment rates. For example, in Recovery Scenario Two, while tax income is projected to increase as higher layoffs result in higher employer taxes, benefit outlays increase even more. From the Governmentwide (budget) perspective, under expected conditions, the present value of income exceeds the present value of expenditures by \$21.8 billion. From the same perspective, under Recovery Scenario Two, the present value of expenditures exceeds the present value of income by \$1.6 billion. From a trust fund perspective, the program has a (\$15.4) billion balance. When combined with the present value of net cash income under expected economic conditions, the program has a surplus of \$6.4 billion.

**Table 10**  
**Present Values of 10-Year Projections of Expenditures and Revenues for Unemployment Insurance Under Three Alternative Scenarios for Economic Conditions**

(In billions of present value dollars, as of September 30, 2010)

	<b>Economic Conditions</b>		
	<b>Expected</b>	<b>Recovery Scenario One</b>	<b>Recovery Scenario Two</b>
Projected future expenditures .....	556.1	534.9	602.5
Projected future cash income .....	577.9	568.9	600.9
Net obligations from budget perspective (expenditures less income) .....	(21.8)	(34.0)	1.6
Trust fund assets .....	(15.4)	(15.4)	(15.4)
Net obligations from trust fund perspective <sup>1</sup> .....	(6.4)	(18.5)	17.1

<sup>1</sup> Net obligations from the trust fund perspective equals net obligations from the budget perspective minus trust fund assets. The positive values in this line are indicative of deficits.

Note: Detail may not add to totals due to rounding.

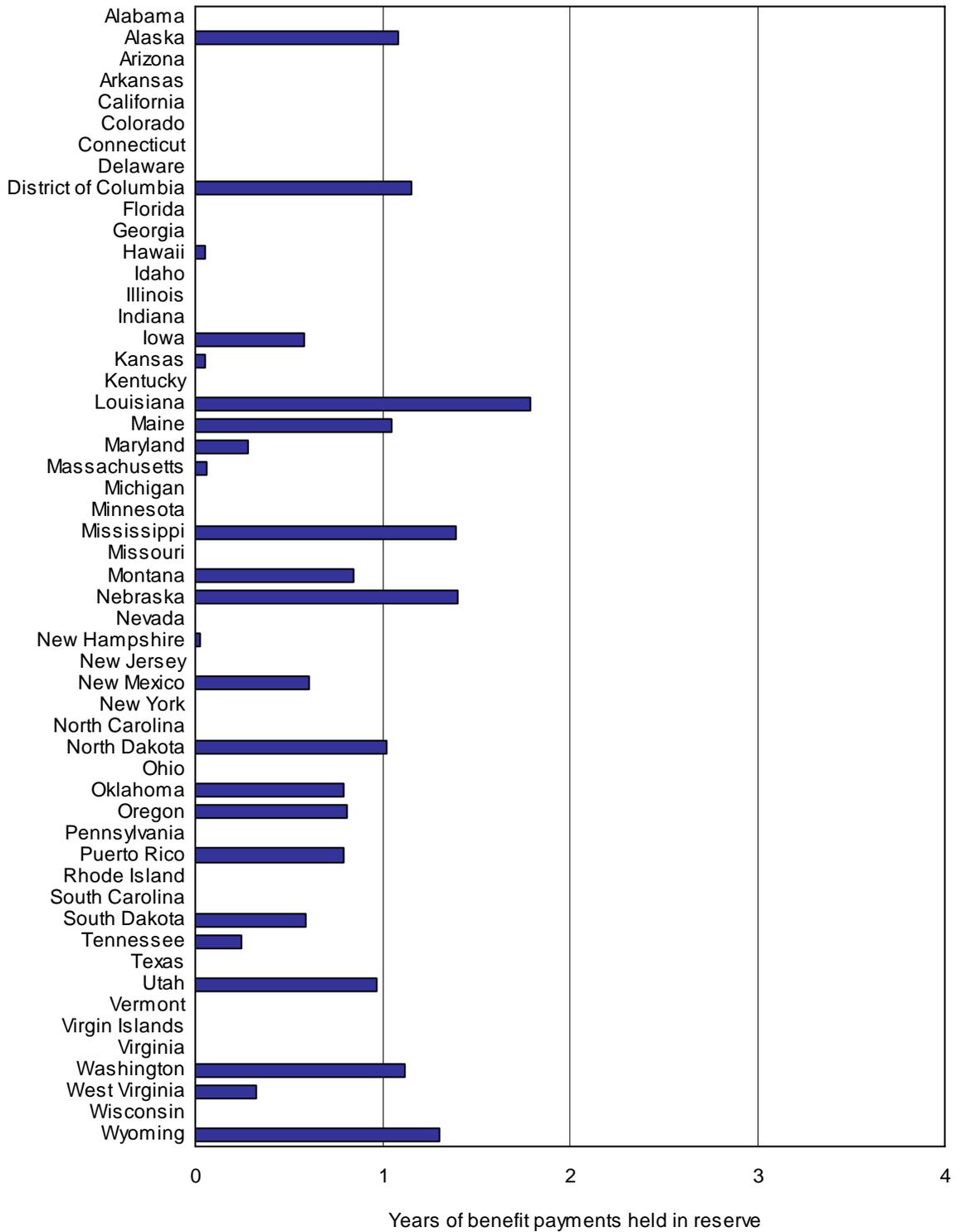
Source: Department of Labor.

**Unemployment Trust Fund Solvency**

Each State’s accumulated UTF net assets or reserve balance should provide a defined level of benefit payments over a defined period. To be minimally solvent, a State’s reserve balance should provide for one year’s projected benefit payment needs based on the highest levels of benefit payments experienced by the State over the last 20 years. A ratio of 1.0 or greater indicates a state is minimally solvent. States below this level are vulnerable to exhausting their funds in a recession. States exhausting their reserve balance borrow funds from the Federal Unemployment Account (FUA) to make benefit payments. During fiscal year 2010, the balances in the FUA were depleted and the FUA borrowed from the Treasury General Fund.

Chart 15 presents the State by State results of this analysis as of September 30, 2010. As the chart illustrates, 44 state funds were below the minimal solvency ratio of 1.0 at September 30, 2010.

**Chart 15—Unemployment Trust Fund Solvency as of September 30, 2010**



## Deferred Maintenance

Deferred maintenance is the estimated cost to bring Government-owned property, plant, and equipment to an acceptable condition, resulting from not performing maintenance on a timely basis. Deferred maintenance excludes the cost of expanding the capacity of assets or upgrading them to serve needs different from those originally intended. The consequences of not performing regular maintenance could include increased safety hazards, poor service to the public, higher costs in the future, and inefficient operations. Estimated deferred maintenance costs are not accrued in the Statements of Net Cost or recognized as a liability on the Balance Sheets.

The amounts disclosed for deferred maintenance are allowed to be measured using one of the following three methods:

- Condition assessment surveys are periodic inspections of the Government-owned property to determine the current condition and estimated cost to bring the property to an acceptable condition.
- Life-cycle cost forecast is an acquisition or procurement technique that considers operation, maintenance, and other costs in addition to the acquisition cost of assets.
- Management analysis method is founded on inflation-adjusted reductions in maintenance funding since the base year.

The amounts disclosed in the table below have all been measured using the condition assessment survey method. The standards for acceptable operating condition and the changes in these standards and changes in asset condition vary widely between the Federal entities.

Some deferred maintenance has been deemed critical. Such amounts and conditions are defined by the individual agencies with responsibility for the safekeeping of these assets. The critical maintenance amount is not included in the low or high estimates amounts and is reported separately. Low and high estimates are based on the materiality of the estimated cost of returning the asset to the acceptable condition versus the total value of the corresponding asset.

	<b>Deferred Maintenance as of September 30</b>					
	<b>Deferred Maintenance Cost Range</b>				<b>Critical Maintenance</b>	
	<b>Low Estimate</b>		<b>High Estimate</b>			
(In billions of dollars)	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
<b>Asset category:</b>						
Buildings, structures and facilities .....	129.7	93.5	134.8	98.7	95.0	2.4
Furniture, fixtures and equipment .....	4.7	0.3	4.7	0.3	4.5	0.2
Other general property, plant, and equipment .....	5.3	12.9	5.3	12.9	4.9	0.2
Heritage assets.....	1.9	10.0	1.9	10.0	1.6	0.1
Stewardship land .....	3.5	3.1	5.2	4.5		-
<b>Total deferred maintenance ....</b>	<b>145.1</b>	<b>119.8</b>	<b>151.9</b>	<b>126.4</b>	<b>106.0</b>	<b>2.9</b>

The agencies material to property, plant, and equipment are the DOD, DOE, DOI, DHS, GSA, TVA, and USPS. These agencies comprise 91 percent of the Government’s total reported property, plant, and equipment cost of \$1,640.5 billion as of September 30, 2010.

Please refer to the individual financial statements of DOD, DOE, DOI, and DHS for detailed significant information on deferred maintenance, including the standards used for acceptable operating condition and changes in asset condition. As of the end of fiscal year 2010, GSA, TVA, and USPS had no material amounts of deferred maintenance cost.

## Unexpended Budget Balances

The Federal budget and budget process largely use obligational accounting—a distinct administrative control through which Federal Agencies control, monitor, and report on the status of funds at their disposal. Unexpended budget balances consist of the unobligated and obligated, but unliquidated, budget balances.

Unobligated budget balances, including amounts for trust funds, are the cumulative amount of budget balances that are not obligated and that remain available for obligation. In 1-year accounts, the unobligated balance is not available for new obligations after the end of the fiscal year. In multiyear accounts, the unobligated balance may be carried forward and remains available for obligation for the period specified. In no-year accounts, the unobligated balance is carried forward until specifically rescinded by law or the head of the agency concerned determines that the purposes for which it was provided have been accomplished and disbursements have not been made against the appropriation for 2 consecutive years. The total unobligated budget balances as of September 30, 2009, and 2008, are \$1,012.7 billion and \$688.9 billion, respectively.

Obligated budget balances are the cumulative budget balances that have been obligated but not liquidated. The obligated balance can be carried forward for a maximum of 5 years after the appropriation has expired. The total obligated budget balances as of September 30, 2009, and 2008, are \$1,418.1 billion and \$1,104.4 billion, respectively.

The President's Budget is located at [www.whitehouse.gov/omb](http://www.whitehouse.gov/omb); unexpended budget balances are shown in the supporting documentation section under "Balances of Budget Authority." The President's Fiscal Year 2011 Budget (issued on February 1, 2010), includes the actual amounts unobligated and obligated amounts for fiscal year 2009. The President's Budget with fiscal year 2010 actual amounts is expected to be published in February 2011.

## Tax Burden

The Internal Revenue Code provides for progressive tax rates, whereby higher incomes are generally subject to higher tax rates. The following tables present the latest available information on income tax and related income, deductions, and credit for individuals by income level and for corporations by size of assets.

### Individual Income Tax Liability for Tax Year 2008

Adjusted Gross Income (AGI)	Number of Taxable Returns (In thousands)	AGI (In millions of dollars)	Total Income Tax (In millions of dollars)	Average AGI per Return (In whole dollars)	Average Income Tax per Return (In whole dollars)	Income Tax as a Percentage of AGI
Under \$15,000 .....	37,970	104,025	2,227	2,740	59	2.1%
\$15,000 under \$30,000 .....	29,687	655,035	18,958	22,065	639	2.9%
\$30,000 under \$50,000 .....	25,641	1,002,998	56,953	39,117	2,221	5.7%
\$50,000 under \$100,000 .....	30,926	2,193,691	184,554	70,934	5,968	8.4%
\$100,000 under \$200,000 .....	13,851	1,845,103	232,270	133,211	16,769	12.6%
\$200,000 under \$500,000 .....	3,477	993,427	193,700	285,714	55,709	19.5%
\$500,000 or more .....	899	1,468,581	342,919	1,663,572	381,445	23.4%
Total .....	<u>142,451</u>	<u>8,262,860</u>	<u>1,031,581</u>			

### Corporation Income Tax Liability for Tax Year 2007

Total Assets (In thousands of dollars)	Income Subject to Tax (In millions of dollars)	Total Income Tax after Credits (In millions of dollars)	Percentage of Income Tax after Credits to Taxable Income
Zero assets .....	26,280	8,593	32.7%
\$1 under \$500 .....	8,205	1,582	19.3%
\$500 under \$1,000 .....	4,292	1,017	23.7%
\$1,000 under \$5,000 .....	15,577	4,628	29.7%
\$5,000 under \$10,000 .....	10,008	3,299	33.0%
\$10,000 under \$25,000 .....	16,650	5,547	33.3%
\$25,000 under \$50,000 .....	13,139	4,347	33.1%
\$50,000 under \$100,000 .....	16,621	5,392	32.4%
\$100,000 under \$250,000 .....	27,977	9,100	32.5%
\$250,000 under \$500,000 .....	35,046	10,876	31.0%
\$500,000 under \$2,500,000 .....	145,944	44,586	30.6%
\$2,500,000 or more .....	928,546	232,408	25.0%
Total .....	<u>1,248,285</u>	<u>331,375</u>	<u>26.5%</u>

## Tax Gap

The tax gap is the difference between what taxpayers should pay and what they actually pay due to not filing tax returns, not paying their reported tax liability on time, or failing to report their correct tax liability. The tax gap, about \$345.0 billion based on updated fiscal year 2001 estimates, represents the amount of noncompliance with the tax laws. Underreporting of income tax, employment taxes, and other taxes represents 82 percent of the tax gap. The IRS remains committed to finding ways to increase compliance and reduce the tax gap, while minimizing the burden on the vast majority of taxpayers who pay their taxes accurately and on time.

The tax gap is the aggregate amount of tax (i.e., excluding interest and penalties) that is imposed by the tax laws for any given tax year but is not paid voluntarily and timely. The tax gap arises from three types of noncompliance: not filing required tax returns on time or at all (the nonfiling gap), underreporting the correct amount of tax on timely-filed returns (the underreporting gap), and not paying on time the full amount reported on timely-filed returns (the underpayment gap). Of these three components, only the underpayment gap is observed; the nonfiling gap and the underreporting gap must be estimated. Each instance of noncompliance by a taxpayer contributes to the tax gap, whether or not the IRS detects it, and whether or not the taxpayer is even aware of the noncompliance. Obviously, some of the tax gap arises from intentional (willful) noncompliance, and some of it arises from unintentional mistakes.

The collection gap is the cumulative amount of assessed tax, penalties, and interest that has been assessed over many years, but has not been paid by a certain point in time and which the IRS expects to remain uncollectible. In essence, it represents the difference between the total balance of unpaid assessments and the net taxes receivable reported on the IRS' balance sheet. The tax gap and the collection gap are related and overlapping concepts, but they have significant differences. The collection gap is a cumulative balance sheet concept for a particular point in time, while the tax gap is like an income statement item for a single year. Moreover, the tax gap estimates include all noncompliance, while the collection gap includes only amounts that have been assessed (a small portion of all noncompliance).

## Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest) that may be paid for claims pending judicial review by the Federal courts or, internally, by appeals. The total estimated payout (including principal and interest) for claims pending judicial review by the Federal courts is \$8.8 billion and \$4.7 billion for fiscal years 2010 and 2009, respectively. For those under appeal, the estimated payout is \$8.0 billion and \$6.3 billion for fiscal years 2010 and 2009, respectively. There are also unasserted claims for refunds of certain excise taxes. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5 for reporting the amounts in the balance sheets or for disclosure in the Notes to the Financial Statements. However, they meet the criteria in SFFAS No. 7 for inclusion as supplemental information. To the extent judgments against the Government for these claims prompt other similarly situated taxpayers to file similar refund claims; these amounts could become significantly greater.

## Tax Assessments

The Government is authorized and required to make inquiries, determinations, and assessments of all taxes which have not been duly paid. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as enforcement programs such as examination, under-reporter, substitute for return and combined annual wage reporting. Assessments with little or no future collection potential are called write-offs. Although compliance assessments and write-offs are not considered receivables under Federal accounting standards, they represent legally enforceable claims of the Government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

Compliance assessments and pre-assessment work in process are \$95.4 billion and \$77.2 billion for fiscal years 2010 and 2009, respectively. The amount of allowance for uncollectible amounts pertaining to compliance assessments cannot be reasonably estimated, and thus the net realizable value of the value of the pre-assessment work-in-process cannot be determined. The amount of assessments that agencies have statutory authority to collect at the end of the period, but have been written off and excluded from accounts receivable are \$99.0 billion and \$105.4 billion for fiscal years 2010 and 2009, respectively.

## Risk Assumed

Risk assumed information is important for all Federal insurance and guarantee programs, except social insurance, life insurance and loan guarantee programs. Risk assumed is generally measured by the present value of unpaid expected losses net of associated premiums, based on the risk inherent in the insurance or guarantee coverage in force. In addition to the liability for unpaid insurance claims included in Note 18—Insurance and Guarantee Program Liabilities, for events that have already occurred, the Government is also required to report as supplementary information risk assumed amounts and the periodic changes in those amounts.

The assessments of losses expected based on the risk assumed are based on actuarial or financial methods that include information and assumptions applicable to the economic, legal and policy environment in force at the time the assessments are made. Management has estimated the loss amounts based on the risk assumed as well as the periodic changes.

Please refer to the individual financial statements of the PBGC, USDA and NCUA for further detailed information, including information as to the indicators of the range of uncertainty around expected estimates, including indicators of the sensitivity of the estimates to changes in major assumptions.

### Risk Assumed Information as of September 30

(In billions of dollars)

	2010	2009
<b>Present value of unpaid expected losses, net of associated premiums:</b>		
Pension Benefit Guaranty Corporation .....	190.0	168.2
National Credit Union Administration .....	7.5	5.9
Department of Agriculture .....	7.5	8.9
All other .....	2.0	1.6
Total .....	<u>207.0</u>	<u>184.6</u>
<b>Periodic changes in risk assumed amounts:</b>		
Pension Benefit Guaranty Corporation .....	21.8	121.4
National Credit Union Administration .....	1.6	5.7
Department of Agriculture .....	(1.4)	(1.0)
All other .....	0.4	0.4
Total .....	<u>22.4</u>	<u>126.5</u>

## Unmatched Transactions and Balances

(In millions of dollars)	Fiscal Year 2010	Fiscal Year 2009
<b>Change in intra-Governmental unmatched balances:</b>		
Debt/investment .....	1,369.9	(1,202.7)
Interest payable/receivable .....	3.6	13.6
Loans payable/receivable .....	6,399.2	(6,396.5)
Benefit program contributions payable/receivable .....	110.2	(25.7)
Accounts payable/receivable .....	(4,111.7)	4,380.6
Advances from/to others and deferred credits/prepayments .....	(953.8)	1,121.7
Transfers payable/receivable .....	80.6	(61.2)
	2,898.0	(2,170.2)
<b>Unmatched intra-Governmental transactions:</b>		
Federal securities interest revenue/expense—investment exchange .....	1.3	40.1
Borrowings interest revenue/expense—exchange .....	(26.3)	55.9
Borrowings gains/losses .....	(1.7)	125.3
Nonexpenditure transfers-in/out .....	1,683.5	234.0
Expenditure transfers-in/out .....	649.9	20,357.0
Transfers-in/out without reimbursement .....	(752.8)	10,221.6
Imputed financing source/cost .....	(15.4)	(15.0)
Benefit program revenue/cost .....	(1,448.3)	(1,240.2)
	90.2	29,778.7
<b>General fund transactions:</b>		
Fund balance with Treasury .....	(4,697.6)	98,104.3
Appropriations of unavailable special or trust fund receipts— transfers out/in .....	(976.7)	94.4
Appropriations received/warrants .....	22,060.4	(5,454.1)
Other taxes and receipts/trust fund warrants .....	2,235.1	3,753.3
Custodial and non-entity collections transferred out/in .....	(713,283.8)	(2,528,596.1)
Other general fund transactions .....	693,163.0	2,424,135.8
	(1,499.6)	(7,962.4)
Net intra-agency reporting errors and restatements .....	(719.2)	(2,229.2)
Unmatched transactions and balances, net .....	769.4	17,416.9

( ) Parentheses indicate a decrease to Net Position.

The Statement of Operations and Changes in Net Position includes an amount for unmatched transactions and balances that result from the consolidation of Federal reporting entities. Transactions between Federal entities must be eliminated in consolidation to calculate the financial position of the U.S. Government. Many of the amounts included in the table represent intragovernmental activity and balances that differed between Federal agency trading partners and often totaled significantly more in the absolute than the net amounts shown. In addition, included in the “General Fund Transactions” section are certain intragovernmental accounts, primarily related to agency unreconciled transactions with the General Fund, totaling hundreds of billions of dollars. The table also reflects other consolidating adjustments and other adjustments that contributed to the unmatched transactions and balances amount.

Unmatched transactions and balances between Federal entities impact not only in the period in which differences originate but also in the periods where differences are reconciled. As a result, it would not be proper to conclude that increases or decreases in the unmatched amounts shown in the “Unmatched Transactions and Balances” table reflect improvements or deteriorations in the Government’s ability to reconcile intragovernmental transactions. The Federal community considers the identification and accurate reporting of intragovernmental activity a priority.

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