



CRS Report for Congress

Social Security: The Windfall Elimination Provision (WEP)

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Summary

The windfall elimination provision (WEP) reduces the Social Security benefits of workers who also have pension benefits from employment not covered by Social Security. Its purpose is to remove an advantage these workers would otherwise receive because of Social Security's benefit formula that favors workers with smaller amounts of Social Security-covered career earnings. Opponents contend that the provision is basically inaccurate and often unfair. In the 110th Congress, three bills (H.R. 82, H.R. 726 and S. 206) have been introduced to modify or repeal the WEP. In the 109th Congress, five bills (H.R. 147, H.R. 1690, H.R. 1714, S. 619, and S. 866) were introduced that would have modified or repealed the WEP. This report will be updated annually or upon legislative activity.

Background

Social Security monthly benefits are computed by applying a formula to an average of a person's earnings from work subject to the Social Security tax. The formula applies three progressive factors — 90%, 32%, and 15% — to three different levels, or brackets, of average monthly covered earnings (these earnings brackets change each year to reflect changes in national wage levels). The result is known as the “primary insurance amount,” or PIA, and is rounded down to the nearest 10 cents. The formula is designed so that workers with low average career earnings receive a PIA that is a larger proportion of their earnings than do workers with high average earnings. For persons who reach age 62, die or become disabled in 2007, the PIA is determined thus:

| Factor | Average Career Monthly Earnings |
|--------|---------------------------------|
| 90% | first \$680, plus |
| 32% | \$680 through \$4,100, plus |
| 15% | over \$4,100 |

A different Social Security benefit formula, referred to as the “windfall elimination provision” (WEP), applies to many workers who also are entitled to a pension from work not covered by Social Security (e.g., work under the Federal Civil Service Retirement System).¹ Under these rules, the 90% factor in the first band of the formula is replaced by a factor of 40%. The effect is to lower the proportion of their earnings in the first bracket that are converted to benefits. The following table illustrates how the provision works in 2007.

Table 1. Monthly PIA for a Worker With Average Monthly Earnings of \$1,000

| Regular Formula | | Windfall Elimination Formula | |
|------------------------------|--------|------------------------------|--------|
| 90% of first \$680 | \$612 | 40% of first \$680 | \$272 |
| 32% of \$680 through \$4,100 | 102.40 | 32% of \$680 through \$4,100 | 102.40 |
| 15% over \$4,100 | 00.00 | 15% over \$4,100 | 00.00 |
| Total | 714.40 | Total | 374.40 |

Thus, under the windfall elimination formula the benefit for the worker is \$340 (\$714.40-\$374.40) less per month than under the regular formula. Note that once average monthly earnings exceed the first level in the formula of \$680, the amount of the reduction remains at \$340 per month because the lower replacement factor of the first level no longer applies. For example, if the worker had \$2,000 of average monthly earnings instead of \$1,000, the windfall reduction still would be \$340 per month. However, because the dollar reduction is limited to the first bracket of the PIA formula, the percent reduction in benefits relative to the regular PIA formula varies by AIME. For example, if we applied the WEP formula to a worker with an AIME of \$4,000, this worker would still see a dollar reduction of \$340 per month. However, this worker would experience a 20% reduction in benefits under the WEP compared to the regular PIA formula, while the worker with a \$1,000 AIME would experience a 48% reduction in benefits under the WEP compared to the regular PIA formula.

The provision includes a guarantee (designed to help protect workers with low pensions) that the reduction in benefits caused by the windfall elimination formula can never exceed more than one-half of the pension based on noncovered work. The provision also exempts workers who have 30 or more years of “substantial” employment covered under Social Security (i.e., having earned at least one-quarter of the “old-law” Social Security maximum taxable wage base for each year in question).² Also, lesser

¹ Social Security Act §215(a)(7).

² For determining years of coverage after 1978 for individuals with pensions from noncovered employment, the amount is 25% of what the contribution and benefit base otherwise would have been if the 1977 Social Security Amendments had not been enacted. In 2007, the “old-law” taxable wage base is equal to \$72,600, and, thus, to earn credit for one year of “substantial” employment under the WEP, a worker would have to earn at least \$18,150 in Social Security covered-employment.

reductions apply to workers with 21 through 30 years of substantial covered employment, as follows:

| | Years of Social Security Coverage | | | | | | | | | | |
|-------------------------|-----------------------------------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| | 20 | 21 | 22 | 23 | 24 | 25 | 26 | 27 | 28 | 29 | 30 |
| First factor in formula | 40% | 45% | 50% | 55% | 60% | 65% | 70% | 75% | 80% | 85% | 90% |

The provision does not apply (1) to employees of governments or nonprofit organizations who were mandatorily covered by Social Security on January 1, 1984, because of the 1983 amendments (e.g., the President, Members of Congress); (2) to workers who reached age 62, became disabled, or were first eligible for a pension from noncovered employment, before 1986; (3) in computing survivor benefits; (4) to benefits from foreign Social Security systems that are based on a “totalization” agreement with the United States; and (5) to people whose only noncovered employment that resulted in a pension was in military service before 1957 or is based on railroad employment.

According to the Social Security Administration (SSA), as of December 2002, 635,000 recipients were affected by the WEP. Of these 66% were men. SSA estimates that in 2000, 3.5% of recipients affected by the WEP had incomes below the poverty line. For comparison purposes, at that time 8.5% of all Social Security beneficiaries age 65 and older had incomes below the poverty line and 11.3% of the general population had incomes below the poverty line.³

Legislative History and Rationale

This provision was enacted in 1983 as part of major amendments designed to shore up the financing of the Social Security program. Its purpose was to remove an unintended advantage that the regular Social Security benefit formula provided to persons who also had pensions from non Social Security-covered employment. The regular formula was intended to help workers who spent their work careers in low paying jobs, by providing them with a benefit that replaces a higher proportion of their earnings than the benefit that is provided for workers with high earnings. However, the formula could not differentiate between those who worked in low-paid jobs throughout their careers and other workers who appeared to have been low paid because they worked many years in jobs not covered by Social Security (these years are shown as zeros for Social Security benefit purposes). Thus, under the old law, workers who were employed for only a portion of their careers in jobs covered by Social Security — even highly paid ones — also received the advantage of the “weighted” formula, because their few years of covered earnings were averaged over their entire working career to determine the average covered earnings on

³ Poverty rates were calculated by David Weaver of the Social Security Administration’s Office of Retirement Policy using the March 2001 Current Population Survey (CPS). Poverty status is taken directly from the CPS and is thus subject to errors in the reporting of income. The sample for the WEP poverty rate only includes persons for whom SSA administrative records could be matched. The sample size for the WEP poverty rate is relatively small (230 cases). The poverty rates for the Social Security beneficiary population age 65 and over and for the general population do not require matched data and are based completely on CPS data.

which their Social Security benefits were based. The new formula is intended to remove this advantage for these workers.

Arguments for the Windfall Elimination Provision. Proponents of the measure say that it is a reasonable means to prevent payment of overgenerous and unintended benefits to certain workers who otherwise would profit from happenstance (i.e., the mechanics of the Social Security benefit formula). Furthermore, they maintain that the provision rarely causes hardship because by and large the people affected are reasonably well off as most of them also receive government pensions.

Arguments Against the Windfall Elimination Provision. Some opponents believe the provision is unfair because it substantially reduces a benefit that workers had included in their retirement plans. Others criticize how the provision works. They say the arbitrary 40% factor in the windfall elimination formula is an inaccurate way to determine the actual windfall when applied to individual cases. For example, they say it over-penalizes lower paid workers with short careers, or with full careers that are fairly evenly split. They also say it is regressive, because the reduction is confined to the first bracket of the benefit formula and causes a relatively larger reduction in benefits for low-paid workers.

Recent Legislation

In the 110th Congress, three bills have been introduced to repeal or alter the WEP. H.R. 82, was introduced by Representative Berman, and S. 206, the companion bill to H.R. 82 in the Senate, was introduced by Senator Feinstein. Under this bill, all Social Security benefits paid after December 2007 would no longer be reduced by the WEP. The Congressional Budget Office has estimated that full repeal of the WEP would cost approximately \$32.7 billion between 2006 and 2015. According to the Office of the Actuary of the SSA, elimination of the WEP would cost 0.06% of taxable payroll (causing an increase in Social Security's long-range deficit of about 3%).⁴

H.R. 726, introduced by Representative Barney Frank, would eliminate the WEP for those whose combined monthly income from Social Security and the noncovered pension was less than \$2,500 in 2007 and indexed annually to the national average wage. The bill would gradually phase in the provision for those who have a combined monthly income between \$2,500 and \$3,334. For those with combined monthly incomes exceeding \$3,335, the WEP would remain fully applicable.

In the 109th Congress, five bills were introduced that would have altered the windfall provision. H.R. 147, introduced by Representative McKeon, and S. 619, introduced by Senator Feinstein, would have repealed the windfall elimination provision for Social Security benefits payable after December 2005. H.R. 1690, introduced by Representative Barney Frank, was identical to H.R. 726 introduced in the 110th Congress.

⁴ This estimate is based on the intermediate assumptions of the 2003 Social Security Trustees Report. More recent estimates are unavailable. However, the Social Security Office of the Chief Actuary does not believe that the results would be significantly different using the 2006 Trustees Report.

Representative Kevin Brady introduced H.R. 1714, the Public Servant Retirement Protection Act (PSRPA) of 2005.⁵ Senator Kay Bailey Hutchison introduced a companion bill, S. 866, in the Senate. The PSRPA would eliminate the current-law WEP for those first entering non-Social Security covered employment one year after the bill's enactment. Those workers who have worked in noncovered employment prior to this date would still be covered by the current-law WEP unless the PSRPA WEP provided them with a higher benefit. The PSRPA would substitute a new WEP formula that would provide a Social Security benefit in rough proportion to the percentage of earnings worked in Social Security covered employment.

⁵ With the exception of some administrative provisions, this bill is identical in effect to that introduced as H.R. 4391 in the 108th Congress. For additional information on the PSRPA, please refer to CRS Report RL32477, *Social Security: The Public Servant Retirement Protection Act (H.R. 4391/S. 2455)*, by Laura Haltzel.