January 2004

Social Security: The Windfall Benefit Provision

Laura Haltzel
Congressional Research Service

Social Security: The Windfall Benefit Provision

Keywords
Federal, key workplace documents, Catherwood, ILR, social security, pension, earnings, windfall, worker, employment, benefit, elimination, provision

Comments
CRS Report

Order Code 98-35 EPW
Updated January 9, 2004

Social Security: The Windfall Benefit Provision

Laura Haltzel
Domestic Social Policy Division

Summary

The windfall elimination provision 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 both the 107th and 108th Congresses, five bills have been introduced that would modify or repeal the provision. This report will be updated annually or upon legislative activity.[1]

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 2004, the PIA is determined thus:

Factor	Average career monthly earnings
90%	first $612, plus
32%	$612 through $3,689, plus
15%	over $3,689

[1] This report by written by former CRS analyst Geoffrey Kollmann.

A different Social Security benefit formula — referred to as the "windfall elimination provision" — 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). 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 2004.

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

Regular formula		"Windfall elimination formula"	
90% of first $612	$550.80	**40%** of first $612	$244.80
32% of $612 through $3,689	124.16	32% of $612 through $3,689	124.16
15% over $3,689	00.00	15% over $3,689	00.00
Total	674.96	Total	368.96

Thus, under the windfall elimination formula the benefit for the worker is $306.00 ($674.96-$368.96) less per month than under the regular formula. Note that once average monthly earnings exceed the first level in the formula of $612, the amount of the reduction remains at $306.00 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 $306.00 per month.

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 Social Security maximum taxable wage base for each year in question). Also, lesser reductions apply to workers with 21 through 29 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 1993, 3% of recipients affected by the WEP had incomes below the poverty line. For comparison purposes, at that time 15% of the general population had incomes below the poverty line.

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 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

Five bills were introduced in the *107th Congress* that would have affected the windfall elimination provision. H.R. 848, by Representative Sandlin, H.R. 2638, by

Representative McKeon, and S. 1523, by Senator Feinstein, would have eliminated the provision entirely, effective in 2002. H.R. 1073, by Representative Frank, and S. 2521, by Senator Kerry, would have eliminated the application of the provision to those whose monthly combination of Social Security worker benefits and non Social Security-covered pension is $2,000 or less, effective upon enactment. For those whose monthly combination of Social Security worker benefits and other government benefits is more than $3,000, the provision would remain fully applicable. For those whose monthly combination of Social Security worker benefits and other government benefits is between $2,000 and $3,000, the provision would be phased in, according to the following schedule:

Table 2. Percentage of Windfall Elimination Provision Applicable

Combined Monthly Benefit	Percentage
$2,000.01 to $2,250	20%
$2,250.01 to $2,500	40%
$2,500.01 to $2,750	60%
$2,750.01 to $3,000	80%
More than $3,000	100%

The SSA estimated that H.R. 1073 would increase benefit outlays by $6.9 billion over five years and 18.9 billion over 10 years.

In the *108th Congress*, H.R. 594, introduced by Representative McKeon, and S. 349, introduced by Senator Feinstein, would repeal the provision entirely, effective in 2004. 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%). Representative Frank and Senator Kerry also introduced H.R. 2011 and S. 1011, which are essentially the same as H.R. 1073 and S. 2521 in the 107th Congress(i.e., they would eliminate the application of the provision to those whose monthly combination of Social Security worker benefits and non Social Security-covered pension is $2,000 or less). H.R. 2611, introduced by Representative Michaud, would exempt from the provision retired members of the military who have at least 20 years of service.

On May 1, 2003, the Social Security Subcommittee of the House Committee on Ways and Means held a hearing on the WEP, in which Members and witnesses discussed approaches to modifying the provision. The SSA testified that if any action were taken affecting the WEP, it should be done in the context of overall reform of the Social Security system. The General Accounting Office testified that eliminating the WEP would cost $19 billion over 10 years.