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 or "windfall" these workers would otherwise receive as a result of the interaction between the Social Security benefit formula and the workers' relatively short careers in Social Security-covered employment. Opponents contend the provision is basically imprecise and can be unfair.

This report will be updated annually or upon legislative activity.

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Background

The Social Security benefit formula is designed so that workers with low average lifetime earnings in Social Security-covered employment receive a benefit that is a larger proportion of their earnings than do workers with high average lifetime earnings. The benefit formula does not distinguish, however, between workers who have low average earnings because they worked for many years at low wages in Social Security-covered employment and workers who have low average earnings because they worked briefly in Social Security-covered employment. The generous benefit that would be provided to workers with short careers in Social Security-covered employment—in particular, workers who have split their careers between Social Security-covered and non-covered employment—is sometimes referred to as a "windfall" that would exist in the absence of the windfall elimination provision (WEP). The WEP reduces the Social Security benefits of workers who also have pension benefits from employment not covered by Social Security.

A worker is eligible for Social Security after he or she works in Social Security-covered employment for 10 or more years (40 or more quarters). The worker's earning history is indexed to wage growth to bring earlier years of his or her earnings up to a comparable, current basis. Average indexed earnings are found by totaling the highest 35 years of indexed wages and then dividing by 35. Next, a monthly average, known as Average Indexed Monthly Earnings (AIME), is found by dividing the annual average by 12.

The Social Security benefit formula is designed to provide a progressive benefit. The benefit formula applies three progressive factors—90%, 32%, and 15%—to three different levels, or brackets, of AIME.[1] The result is known as the "primary insurance amount" (PIA) and is rounded down to the nearest 10 cents. For persons who reach age the age of 62, die, or become disabled in 2013, the PIA is determined in **Table 1** as follows:

Table 1. Social Security Benefit Formula in 2013

Factor	Average Indexed Monthly Earnings
90%	of the first $791, plus
32%	of AIME over $791 and through $4,768, plus
15%	of AIME over $4,768

The averaging provision in the benefit formula tends to cause workers with short careers in Social Security-covered employment to have low AIMEs, similar to persons who worked for low wages in covered employment throughout their careers. This is because years of zero covered earnings are entered as zeros into the formula that averages the worker's wage history over 35 years. For example, a person with 10 years in Social Security-covered employment would have an AIME that reflects 25 years of zero earnings.

Consequently, for a worker with a low AIME because she split her career between covered and non-covered employment, the benefit formula replaces more of covered earnings at the 90% rate than if this worker had spent his or her full 35-year career in covered employment at the same

[1] Both the annual earnings amounts over the worker's lifetime and the bracket amounts are indexed to national wage growth so that the Social Security benefit replaces the same proportion of wages for each generation.

wage level. The higher replacement rate[2] for workers who have split their careers between Social Security-covered and non-covered jobs is sometimes referred to as a "windfall."[3]

A different Social Security benefit formula, referred to as the "windfall elimination provision," applies to many workers who are entitled to Social Security as well as to a pension from work not covered by Social Security (e.g., individuals who work for certain state and local governments, or under the Federal Civil Service Retirement System).[4] Under these rules, the 90% factor in the first bracket of the formula is replaced by a factor of 40%. The effect is to lower the proportion of earnings in the first bracket that are converted to benefits. **Table 2** illustrates how the regular and WEP provisions work in 2013.

Table 2. Monthly PIA for a Worker With Average Indexed Monthly Earnings of $1,500 and Retiring in 2013

Regular Formula		Windfall Elimination Formula	
90% of first $791	$711.90	**40%** of first $791	$316.40
32% of earnings over $791 and through $4,768	$226.88	32% of earnings over $791 and through $4,768	$226.88
15% over $4,768	0.00	15% over $4,768	0.00
Total	$938.78	Total	$543.28

Source: Calculations were made by the Congressional Research Service (CRS).

Note: To simplify the example, rounding conventions that would normally apply are not used here.

Under the WEP formula, the benefit for the worker is reduced by $395.50 ($938.78 - $543.28) per month relative to the regular benefit formula. Note that the WEP reduction is limited to the first bracket in the AIME formula (90% vs. 40% formula rates), while the 32% and 15% factors for the second and third brackets are the same as in the regular benefit formula. As a result, for AIME amounts that exceed the first formula threshold of $791, the amount of the WEP reduction remains a flat $395.50 per month. For example, if the worker had an AIME of $4,000 instead of $1,500, the WEP reduction would still be $395.50 per month. The WEP therefore causes a proportionally larger reduction in benefits for workers with lower AIMEs and monthly benefit amounts. [5]

A "guarantee" in the WEP provision ensures that a worker's WEP reduction cannot exceed more than one half of the government pension based on the worker's non-covered work. This

[2] A worker's replacement rate is the ratio of his or her Social Security benefit to pre-retirement income.

[3] The WEP is sometimes confused with the Government Pension Offset (GPO), which reduces Social Security *spousal* benefits of a worker who also has a government pension based on work that was not covered by Social Security. For more information on the GPO, please refer to CRS Report RL32453, *Social Security: The Government Pension Offset (GPO)*, by Christine Scott.

[4] Social Security Act §215(a)(7). Federal service where Social Security taxes are withheld (Federal Employees' Retirement System or CSRS Offset) is not affected by the WEP.

[5] For the worker shown in **Table 2,** with an AIME of $1,500 and a monthly benefit of $938.78 under the regular benefit formula in 2013, the WEP reduction of $395.50 represents a 42% cut to the regular formula monthly benefit amount. By comparison, a worker with an AIME of $4,000 would be entitled to a PIA of $1,738.78 under the 2013 regular benefit formula, and the same WEP reduction of $395.50 per month would represent a 23% reduction in this worker's monthly benefit amount (CRS calculations).

"guarantee" is designed to help protect workers with low non-covered pensions and also ensures that the WEP can never completely eliminate a worker's Social Security benefit. The WEP also exempts workers who have 30 or more years of "substantial" employment covered under Social Security, with lesser reductions for workers with 21 through 29 years of substantial covered employment, as shown in **Table 3**.[6]

Table 3. WEP Reduction Falls with Years of Substantial Coverage

	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%
Maximum dollar amount of monthly WEP reduction in 2013[a]	$395.50	$355.95	$316.40	$276.85	$237.30	$197.75	$158.20	$118.65	$79.10	$39.55	$0.00

Source: Social Security Administration, *How the Windfall Elimination Provision Can Affect Your Social Security Benefit*, Washington, DC, http://www.socialsecurity.gov/retire2/wep-chart.htm.

a. WEP reduction may be lower than the amount shown because the reduction is limited to one-half of the worker's pension from non-covered employment.

The WEP does *not* apply to (1) an individual who on January 1, 1984, was an employee of a government or nonprofit organization and to whom Social Security coverage was mandatorily extended by the 1983 amendments to the Social Security Act (e.g., the President, Members of Congress in office on December 31, 1983); (2) benefits for survivors; (3) workers who reached the age of 62, became disabled, or were first eligible for a pension from non-covered employment, before 1986; (4) benefits from foreign Social Security systems that are based on a "totalization" agreement with the United States; and (5) people whose only non-covered employment that resulted in a pension was in military service before 1957 or is based on railroad employment.

Who is Affected by the WEP?

According to the Social Security Administration (SSA), as of December 2011, about 1.4 million Social Security beneficiaries were affected by the WEP, as shown in **Table 4**. About 1.3 million people (91.9%) affected by the WEP were retired workers. About 2.5% of all Social Security beneficiaries (including disabled and spouse beneficiaries), and about 3.5% of all retired worker

[6] For determining years of coverage after 1978 for individuals with pensions from non-covered employment, "substantial coverage" is defined as 25% of the "old law" (i.e., if the 1977 Social Security Amendments had not been enacted) Social Security maximum taxable wage base for each year in question. In 2013, the "old-law" taxable wage base is equal to $84,300, therefore to earn credit for one year of "substantial" employment under the WEP a worker would have to earn at least $21,075 in Social Security-covered employment.

beneficiaries, were affected by the WEP in December 2011.[7] Of retired workers affected by the WEP, approximately 62.7% were men.[8]

Table 4. Number of Beneficiaries in Current Payment Status with Benefits Affected by Windfall Elimination Provision (WEP), by State and Type of Benefit, December 2011

		Type of Benefit		
State	Total	Retired workers	Disabled workers	Spouses and children
Total	1,370,688	1,259,310	17,958	93,420
Alabama	16,905	15,219	346	1,340
Alaska	7,361	6,915	106	340
Arizona	25,357	23,483	295	1,579
Arkansas	9,685	8,943	213	529
California	181,048	167,675	2,125	11,248
Colorado	41,714	38,952	593	2,169
Connecticut	13,507	12,796	175	536
Delaware	3,110	2,912	48	150
District of Columbia	7,360	6,968	131	261
Florida	77,311	71,317	877	5,117
Georgia	39,401	36,901	525	1,975
Hawaii	8,494	7,787	77	630
Idaho	5,948	5,472	76	400
Illinois	70,984	67,044	601	3,339
Indiana	13,534	12,544	226	764
Iowa	7,251	6,766	78	407
Kansas	7,898	7,334	128	436
Kentucky	17,725	16,376	345	1,004
Louisiana	27,755	25,053	628	2,074
Maine	12,697	11,899	176	622
Maryland	40,393	37,768	511	2,114
Massachusetts	49,106	46,490	692	1,924
Michigan	17,121	15,682	290	1,149
Minnesota	15,137	14,190	151	796
Mississippi	8,423	7,715	164	544

[7] Social Security data on the Social Security beneficiary and retired worker populations are available from the *Monthly Statistical Snapshot, December 2011*, at http://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/index.html.

[8] Social Security Administration, Office of Research, Evaluation and Statistics, January 27, 2012, unpublished table W01.

State	Total	Type of Benefit: Retired workers	Disabled workers	Spouses and children
Missouri	29,024	27,359	423	1,242
Montana	5,008	4,619	66	323
Nebraska	4,728	4,441	37	250
Nevada	20,324	19,244	232	848
New Hampshire	6,143	5,734	109	300
New Jersey	19,651	18,041	362	1,248
New Mexico	11,378	10,215	178	985
New York	27,898	25,548	477	1,873
North Carolina	24,721	22,972	336	1,413
North Dakota	2,202	2,036	24	142
Ohio	99,306	92,739	1,153	5,414
Oklahoma	15,742	14,324	314	1,104
Oregon	13,472	12,514	158	800
Pennsylvania	31,228	28,708	545	1,975
Rhode Island	4,373	4,085	85	203
South Carolina	15,226	14,033	227	966
South Dakota	3,420	3,208	34	178
Tennessee	17,014	15,624	248	1,142
Texas	120,032	110,935	1,530	7,567
Utah	11,503	10,361	154	988
Vermont	2,255	2,087	20	148
Virginia	42,245	38,909	449	2,887
Washington	25,938	23,529	318	2,091
West Virginia	5,548	4,952	126	470
Wisconsin	10,534	9,821	116	597
Wyoming	2,081	1,935	28	118
Outlying areas and foreign countries	74,469	57,136	632	16,701

Source: Social Security Administration, Office of Research, Evaluation and Statistics, January 27, 2012, unpublished Table B.

Legislative History and Rationale

The windfall elimination provision was enacted in 1983 as part of major amendments designed to shore up the financing of the Social Security program. The 40% WEP formula factor was the result of a compromise between a House bill that would have substituted a 61% factor for the regular 90% factor and a Senate proposal that would have substituted a 32% factor for the 90% formula.[9]

The purpose of the 1983 law 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 lifetimes in low paying jobs, by providing them with a benefit that replaces a higher proportion of their earnings than the benefit that is provided to 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. 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. The windfall elimination 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 because by definition they also receive government pensions from non-covered work. The guarantee provision ensures that the reduction in Social Security benefits cannot exceed half of the pension from non-covered work, which protects persons with small pensions from non-covered work. In addition, the impact of the WEP is reduced for workers who spend 21 to 29 years in Social Security-covered work and is eliminated for persons who spend 30 years or more in Social Security-covered work.

Arguments Against the Windfall Elimination Provision

Some opponents believe the provision is unfair because it substantially reduces a benefit that workers may have included in their retirement plans. Others criticize how the provision works. They say the arbitrary 40% factor in the windfall elimination formula is an imprecise way to determine the actual windfall when applied to individual cases.

The WEP's Impact on Low-Income Workers

The impact of the WEP on low-income workers has been the subject of debate. Jeffrey Brown and Scott Weisbenner (hereinafter referred to as "Brown and Weisbenner") point out two reasons why the WEP can be regressive.[10] First, because the WEP adjustment is confined to the first bracket of the benefit formula ($791 in 2013), it causes a proportionally larger reduction in benefits for workers with lower AIMEs and benefit amounts. Second, a high earner is more likely

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[9] *Conference Report to Accompany H.R. 1900*, 98th Cong., March 24, 1983 (Washington: GPO, 1983), p. 120.

[10] Jeffrey R. Brown and Scott Weisbenner, *The Distributional Effects of the Social Security Windfall Elimination Provision*, NBER, Working Paper no. 18342, August 2012, http://www.nber.org/papers/w18342.

than a low earner to cross the "substantial work" threshold for accumulating years of covered earnings (in 2013 this threshold is $21,075 in Social Security-covered earnings); therefore, high earners are more likely to benefit from the provision that phases out of the WEP for persons with between 21 and 30 years of covered employment.

Brown and Weisbenner found that the WEP does reduce benefits disproportionately for lower-earning households than for higher-earning households. For some high-income households, applying the WEP to covered earnings even provides a higher replacement rate than if the WEP were applied proportionately to all earnings, covered and non-covered. Brown and Weisbenner also found that the WEP can also lead to large changes in Social Security replacement rates based on small changes in covered earnings, particularly when a small increase in covered earnings carries a person over the threshold for an additional year of substantial covered earnings, leading to a modification in the WEP formula.

SSA estimated 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 aged 65 and older had incomes below the poverty line and 11.3% of the general population had incomes below the poverty line.[11] A potential conclusion is that persons who are subject to the WEP, who by definition also have pensions from non-covered employment, face a somewhat reduced risk of poverty compared with other Social Security beneficiaries.

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This report was originally written by Alison M. Shelton, a former Analyst at the Congressional Research Service. All questions should be directed to the current author.

[11] These are the most recent estimates available. 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 size for the WEP poverty rate is relatively small (230 cases) and only includes persons for whom SSA administrative records could be matched.