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Updated November 9, 2021

The Windfall Elimination Provision (WEP) in Social Security: Proposals for a New Proportional Formula

Background

Social Security is a work-based federal insurance program that provides monthly cash benefits to workers and their eligible family members in the event of a worker's retirement, disability, or death. Although participation in Social Security is compulsory for most workers, about 6% of workers in paid employment or self-employment are not covered by Social Security (i.e., earnings are not taxable or creditable for program purposes).

The regular Social Security benefit formula is progressive, replacing a greater share of career-average earnings for low-paid workers than for high-paid workers. Career-average earnings in Social Security are calculated as *average indexed monthly earnings* (AIME), which is the monthly average of the highest 35 years of covered earnings after indexing for wage growth. If a person has earnings not covered by Social Security, those noncovered earnings are shown as zeros in their Social Security earnings records. As a result, the regular formula cannot distinguish workers who have low career-average earnings because they worked for many years at low earnings in covered employment from workers who appear to have low career-average earnings because they worked for many years in jobs not covered by Social Security. Therefore, based on the regular formula, a worker who worked in both covered and noncovered employment might receive a higher replacement rate of career-average earnings than a worker with the same earnings who spent an entire career in covered employment (see **Table 1**, column [1]). The windfall elimination provision (WEP) is designed to remove such an unintended advantage, or *windfall*, for certain beneficiaries with earnings not covered by Social Security.

The Current WEP Formula

The regular Social Security benefit formula applies three factors—90%, 32%, and 15%—to three different brackets of a worker's AIME. The result is the *primary insurance amount* (PIA), which is the worker's basic monthly benefit at the full retirement age before any adjustments. Under current law, the WEP reduction is based on years of coverage (YOCs). The amount of substantial covered earnings needed for a YOC is $26,550 in 2021. For people with 20 or fewer YOCs, the WEP reduces the first factor from 90% to 40%. For each year of substantial covered earnings in excess of 20, the first factor increases by 5%. The WEP factor reaches 90% for those with 30 or more YOCs, and at that point it is phased out. In addition, the WEP reduction cannot exceed one-half of the pension benefit based on the worker's noncovered employment, and it does not apply to those who do not receive such a pension.

The Proportional Formula

Shortly before the WEP was enacted in 1983 (P.L. 98-21), the bipartisan National Commission on Social Security Reform (the Greenspan Commission) described two different methods of eliminating the *windfall* benefits: (1) the current-law method of adjusting the first replacement factor (90%) as discussed above; and (2) a proportional formula. The proportional formula for WEP purposes would apply the regular Social Security benefit formula to all past earnings from both covered *and* noncovered employment. The resulting benefit would then be multiplied by the ratio of career-average earnings (AIME) from covered employment only to career-average earnings (AIME) from both covered and noncovered employment.

The proportional formula better reflects the Greenspan Commission's recommendation for people with some earnings from noncovered employment to receive the same replacement rate as those workers who spent their entire careers in covered employment (see **Table 1**, column [3]), whereas the current-law WEP can only *approximately* achieve that goal (see **Table 1**, column [2]). However, in 1983, the Social Security Administration (SSA) lacked the data on noncovered earnings needed to make the benefit adjustment under the proportional formula, so Congress adopted the current WEP formula instead. As of 2017, SSA has 35 years of data on earnings from both covered and noncovered employment. This data's availability means that the proportional formula is now an option for Congress to consider.

Table 1. Illustrative Examples: Replacement Rates (Benefits as a Share of AIME) Under Alternative Formulas

Employment	Regular Formula (w/o WEP) (1)	Current-law WEP (2)	Proportional Formula (3)
Covered: 35 years; Noncovered: 0 years	47%	47%	47%
Covered: 15 years; Noncovered: 20 years	68%	37%	47%

Source: Congressional Research Service.

Notes: The worker is assumed to earn $45,000 (indexed by average wage growth) per year and becomes eligible for benefits in 2021.

Comparing the Current WEP and the Proportional Formula

If the proportional formula had applied to current beneficiaries in 2018, SSA's Office of the Chief Actuary

(OCACT) estimates that about 1.1 million beneficiaries affected by the current WEP (or 69%) would have received a *higher* benefit and about 0.5 million (or 31%) would have received a *lower* benefit. In addition, 13.5 million beneficiaries with some noncovered earnings who were not affected by the current WEP would have received a *lower* benefit. Therefore, if the proportional formula were applied to new beneficiaries, it would generate program savings.

Below are two examples in which beneficiaries affected by the current WEP would receive lower benefits under the proportional formula:

- *Beneficiaries with YOCs near 30*. Certain beneficiaries with YOCs near 30 would have a relatively high replacement factor (e.g., 85% for 29 YOCs) under current law. Therefore, those beneficiaries' benefit reduction under the current WEP might be smaller than under the proportional formula.

- *Beneficiaries with relatively high career-average earnings*. Since the current WEP reduction is limited to the first bracket in the PIA formula, it might under-adjust the benefit for some high earners with noncovered employment, resulting in a smaller benefit reduction under current law than under the proportional formula.

Current beneficiaries who had noncovered earnings and are exempt from the current-law WEP but would receive a lower benefit using the proportional formula might include (1) beneficiaries with 30 or more years of substantial covered earning; (2) beneficiaries who do not receive a pension based on noncovered work; and (3) beneficiaries who fit both categories.

Legislation in 117th Congress

Two bills introduced in 2021 would replace the current-law WEP approach with a proportional formula for certain individuals who would become eligible for Social Security benefits in 2023 or later: (1) H.R. 2337 (the Public Servants Protection and Fairness Act), introduced by Representative Richard E. Neal; and (2) H.R. 5834 (the Equal Treatment of Public Servants Act), introduced by Representative Kevin Brady.

No Benefit Cuts Relative to Current Law

Because the proportional formula could reduce Social Security benefits for some future beneficiaries with noncovered employment compared to current law, both bills provide a protection provision, wherein individuals would receive a benefit based on the higher of the current WEP formula or the proportional formula. H.R. 2337 would apply the protection provision to all future beneficiaries, and as with current law, the proportional formula would not apply to workers who do not receive a noncovered pension or who have 30 or more years of substantial covered earnings. In contrast, H.R. 5834 would apply the protection provision during the transitional period for new beneficiaries who become eligible for benefits during 2023 through 2061. For those who become eligible in 2062 and later, benefits would be based solely on the proportional formula.

Additional Monthly Payments to Current Beneficiaries

As discussed earlier, the proportional formula could provide a higher benefit to certain beneficiaries compared to current law, so both bills would provide additional monthly payments to current WEP-affected beneficiaries who are first eligible for benefits *before* 2023. H.R. 2337 would provide worker beneficiaries (but not dependents) an additional monthly payment equal to the lesser of $150 or the current WEP reduction amount. H.R. 5834 would provide an additional monthly payment of $100 to workers and $50 to dependents. The additional monthly payments would begin nine months after enactment of the respective bill, would increase with cost-of-living adjustments, and would be exempt from most benefit adjustments under Social Security. The additional monthly payment under H.R. 2337 would be excluded in determining eligibility and the benefit amount under the Supplemental Security Income program.

Cost Estimates and Funding Rules

The OCACT estimates that H.R. 2337 would cost about $29.0 billion from 2021 through 2030, net of additional revenue from income taxation, including $1.4 billion for the new proportional formula and $27.5 billion for the additional monthly payments. Over the 75-year projection period, the present value of the overall net cost would be about $98.3 billion. The bill would provide transfers from the General Fund of the Treasury to the Social Security trust funds in amounts needed to fully offset the bill's costs, so it would have no effect on Social Security's long-term financial outlook.

The OCACT estimates that H.R. 5834 would cost about $26.3 billion from 2022 through 2031, net of additional revenue from income taxation, including $1.8 billion for the new proportional formula and $24.5 billion for the additional monthly payments. Over the 75-year projection period, future savings from the proportional formula would offset the cost of the additional monthly payments and the protection provision during the transitional period, so the bill would have no significant effect on Social Security's long-term financial outlook.

Other Provisions

The annual Social Security statements that SSA makes available to all eligible workers provide benefit estimates based only on covered employment, with no estimates of the WEP adjustment. Because of this limitation, beneficiaries have argued that they were not given sufficient notice of how much their benefits would be reduced by the WEP. To address this issue, both bills would require SSA to show noncovered as well as covered earnings records on the statements. Moreover, H.R. 2337 would require the statements to include projected benefits using the proportional formula for those workers who would likely be subject to the WEP.

In addition, both bills would require studies on ways to facilitate data exchanges between SSA and state and local governments for purposes of improving WEP administration.

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