Social Security’s Windfall Elimination Provision & Government Pension Offset:

Congress Should Create More Equitable, Accurate & Efficient Rules

Contents

EXECUTIVE SUMMARY

When workers have non-covered earnings, the Social Security Administration (SSA) may adjust their Social Security benefits using the Windfall Elimination Provision (WEP) and/or Government Pension Offset (GPO) rules. In establishing these rules, Congress intended to treat workers with non-covered earnings and workers whose entire careers were covered by Social Security comparably.

There were difficulties in creating these rules from the outset. Complete earnings histories are necessary to calculate Social Security's primary insurance amount (PIA) formula. However, when the WEP and GPO were established, SSA only had records of earnings from covered earnings, not non-covered earnings. As a result, Congress structured the WEP using an arbitrary adjustment to the PIA formula, which applied only to covered earnings, and based the GPO on self-reports of non-covered pensions.

The current WEP and GPO formulas are flawed. First, the WEP and GPO rules are arbitrary and do not mirror Social Security's rules for determining benefits. As a result, workers affected by the provisions are treated unequally: some receive higher benefits than they would if their entire careers had been covered by Social Security; others receive less. Second, SSA does not have the data it needs on non-covered pensions to implement the law accurately. Third, the WEP and GPO are difficult to administer and communicate.

Congress now has the ability to achieve its original intention of treating beneficiaries with non-covered work the same way as covered workers, and to address the flaws of the current law formulas. SSA began to collect data on non-covered earnings in 1978, when Congress removed the cap on the Medicare payroll tax. It has complete non-covered earnings data starting in 1982. In order to calculate a PIA, SSA needs at least 35 years of earnings data. SSA will have at least 35 years of earnings data--covered and non-covered--for all Americans in 2017.

The Board recommends that Congress replace the WEP and GPO with proportional formulas to calculate offsets for beneficiaries with non-covered work who become eligible in 2017 or later. All Social Security benefits would be calculated using the same PIA formula, regardless of whether a person's work was covered, non-covered, or a combination. Then the portion attributable to non-covered work would be subtracted. This provision is included in the bipartisan Equal Treatment of Public Servants Act of 2014.

The Board also recommends that Congress give the IRS the authority to collect data from non-covered pension administrators and share it with SSA. Combining the two approaches is necessary, because the new proportional formulas would only affect new beneficiaries. Current beneficiaries would continue to be subject to the current law WEP and GPO. Without better data collection, the WEP and GPO would continue to be a source of improper payments. The Government Accountability Office (GAO) has long recommended collecting the necessary data through IRS forms.

BACKGROUND

Nearly all American workers are covered by Social Security—in other words, they pay Social Security payroll taxes and receive benefits based on their earnings.[1] However, 4% of all workers and about a quarter of government employees are not covered. These workers are mostly state and local government employees whose jurisdictions have alternative retirement plans that take the place of Social Security. Similarly, some federal workers hired before 1984 are covered by the Civil Service Retirement System instead of Social Security.[2]

Almost all non-covered workers become eligible for Social Security, either based on their own or their spouses' covered work.[3] The Social Security Administration (SSA) may adjust these workers' Social Security benefits using the Windfall Elimination Provision (WEP) and/or Government Pension Offset (GPO) rules. In establishing these rules, Congress intended to treat workers with non-covered earnings and workers whose entire careers were covered by Social Security comparably.[4]

How the WEP & GPO Work

Windfall Elimination Provision (WEP)

Social Security benefits are based on covered earnings, indexed to wage growth, and averaged over a lifetime. The Social Security benefit formula is progressive—that is, the Social Security benefits of lower earners replace a greater proportion of their lifetime earnings than those of higher earners. The basic Social Security benefit formula only counts earnings from jobs covered by Social Security. Therefore, workers with many years of non-covered work may appear to be lifetime low earners, even if they earned high wages outside the system. As a result, the basic Social Security formula would replace a greater proportion of their earnings than is warranted. This is the "windfall" to which the Windfall Elimination Provision refers.

The typical Social Security beneficiary's basic benefit amount is calculated using the Primary Insurance Amount (PIA) formula, which is part of the Social Security Act. The PIA formula, as noted above, ensures that Social Security benefits are progressive, replacing a higher proportion of taxable earnings for low-wage workers than high-wage workers. It is based on a worker's average indexed monthly earnings (AIME). The AIME is calculated by indexing a worker's annual covered earnings to wage growth, taking the highest 35 years of those earnings, and then averaging them and dividing by 12. To calculate the PIA, the AIME is split into three dollar amounts, or PIA bend points, as shown in Table 1. In 2014, the first bend point includes the first $826 of AIME, the second includes the amount between $826 and $4,980 of AIME, and the third includes the amount over

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[1] All Members of Congress and the President are covered by Social Security. http://www.ssa.gov/OACT/FACTS/
[2] See CRS Report RL30631, *Retirement Benefits for Members of Congress,* by Katelin P. Isaacs.
[3] Government Accountability Office, *Social Security: Issues Regarding the Coverage of Public Employees*, GAO 08-248T, November 6, 2007.
[4] National Commission on Social Security Reform Recommendations, *Hearing before the Subcommittee on Social Security and Income Maintenance Programs*, S361-31, Part 1 of 3, February 15 and 16 1983.

$4,980 of AIME. (These dollar values are indexed to wage growth.) The PIA equals the sum of 90% of earnings under the first bend point, 32% of earnings between the first and second bend points, and 15% of earnings between the second and third bend points. The WEP formula is the same as the PIA formula, with one major exception. Rather than multiplying the first portion of earnings by 90%, the WEP formula multiplies it by 40%, as shown in Table 1.

Table 1. PIA and WEP formulas for 2014

PIA factor	WEP factor	Average Indexed Monthly Earnings (AIME) of
90%	40%	up to $826 +
32%	32%	over $816 up to $4,980 +
15%	15%	over $4,980

The WEP is designed to provide roughly equal replacement rates[5] to all workers, whether or not their work was covered by Social Security. However, SSA did not have the non-covered earnings data necessary to do that. As a result, Congress adopted a rough rule of thumb in the WEP formula, replacing the 90% bend point factor with a 40% bend point factor.

There are two limitations on the WEP. First, the WEP adjustment cannot exceed half the amount of a beneficiary's non-covered pension. For example, if a worker's non-covered pension is $300 per month, the WEP reduction is limited to $150 per month. This provision reduces the size of the WEP for many beneficiaries and prevents the WEP from disproportionately affecting the lowest earners.[6]

Second, the WEP phases out based on years of "substantial earnings" covered by Social Security. In 2014, substantial earnings are defined as covered earnings of at least $21,750.[7] The WEP applies fully if the worker has fewer than 20 years of substantial earnings. For workers with 20 to 30 years of substantial earnings, the WEP offset is smaller: the replacement rate under the first bend point gradually rises from 40% to 90% of AIME. If a worker pays Social Security tax on 30 years of substantial earnings, he or she is not affected by the WEP at all.

To understand how the WEP formula works, consider the three illustrative workers in Table 2. Amy works for 35 years in jobs covered by Social Security. Her wages average $44,000 per year, making her a typical wage earner. Beth, similarly, works for 35 years in covered employment, but earns much less—only $19,000 per year. Amy's Social Security benefit ($1,647) is larger than Beth's ($980), which reflects her greater earnings. However, Beth's replacement rate (62%) is larger than Amy's (45%), as a result of Social Security's progressive benefit formula.

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[5] For the purposes of this report, "replacement rate" can be defined as the percentage of a worker's average pre-retirement lifetime earnings that is paid out by Social Security upon retirement.

[6] Alan L. Gustman, Thomas L. Steinmeier, and Nahid Tabatabai, SSA Office of Retirement Policy, *The Social Security Windfall Elimination and Government Pension Offset Provisions for Public Employees in the Health and Retirement Study.* November 3, 2013. http://www.ssa.gov/policy/docs/ssb/v74n3/v74n3p55.html

[7] As part of the 1977 Amendments, Congress defined "substantial earnings" as 25% of the old-law wage base (i.e., what the annual taxable maximum would have been had the 1977 Amendments not been enacted). The old-law wage base is indexed to wage growth. For more information, see: http://www.ssa.gov/oact/cola/oldcbb.html.

Now consider a third worker, Carol, who has worked in both covered and non-covered employment. Carol's average lifetime earnings—including 15 years of covered employment and 20 years of non-covered employment—are equal to Amy's, $44,000. Averaged over 35 years, Carol's *covered* earnings only amount to about $19,000. Therefore, based on her covered earnings alone, she appears to be a lifetime low earner, like Beth. Before the WEP is applied, she would receive the same replacement rate as Beth, despite total lifetime earnings that were more than twice as high. This artificially high replacement rate is what is known as the "windfall." After the WEP is applied, she would receive a substantially smaller benefit ($568) and replacement rate (36%). However, Carol's replacement rate is significantly lower than it would have been if, like Amy, she had spent her entire career in covered work. (Amy's replacement rate is 45%, compared to Carol's 36%.) In this case, the WEP reduction is too large.

Table 2. Illustrations of Windfall Elimination Provision

	Amy	Beth	Carol	
			before WEP	*after WEP*
Total Average Earnings	**$44,000**	**$19,000**	**$44,000**	**$44,000**
Average Social Security-Covered Earnings	$44,000	$19,000	$19,000	$19,000
Years of Covered Employment	35	35	15	15
Years of Non-covered Employment	0	0	20	20
AIME	$3,670	$1,580	$1,580	$1,580
Social Security benefit	$1,650	$980	$980	$570
Replacement Rate	**45%**	**62%**	**62%**	**36%**

Note: Some figures rounded for simplicity.

Though some workers subject to the WEP receive lower benefits than they would have if all their earnings had been covered by Social Security, other workers receive higher benefits. Consider the illustration shown in Table 3. Doug and Earl, like Amy and Beth, spent their entire careers in covered employment. Doug and Earl earned $100,000 and $43,000, respectively. Frank, like Carol, spent 15 years of his career in covered employment and another 20 years in non-covered employment. His total lifetime earnings average $100,000, like Doug. But his covered earnings alone average $43,000, like Earl.

Before the WEP is applied, Frank would receive the same benefit—and the same replacement rate—as Earl, despite total lifetime earnings that were more than twice as high. After the WEP is applied, he would receive a substantially smaller benefit and replacement rate. However, his replacement rate (34%) is still larger than it would have been if his entire career, like Doug's, were covered by Social Security. (Doug receives a 31% replacement rate.) In this case, the WEP reduction is too small.

Table 3. Further Illustrations of Windfall Elimination Provision

	Doug	Earl	Frank	
			before WEP	*after WEP*
Total Average Earnings	**$100,000**	**$43,000**	**$100,000**	**$100,000**
Average Social Security-Covered Earnings	$100,000	$43,000	$43,000	$43,000
Years of Covered Employment	35	35	15	15
Years of Non-covered Employment	0	0	20	20
AIME	$8,333	$3,583	$3,571	$3,571
Social Security benefit	$2,559	$1,620	$1,620	$1,208
Replacement Rate	**31%**	**45%**	**45%**	**34%**

Note: Some figures rounded for simplicity.

The WEP formula is inherently imprecise: it can only roughly approximate the PIA formula applied to all other workers. In some cases, beneficiaries subject to the WEP have higher Social Security replacement rates than people with similar lifetime earnings (like Frank, above); in other cases (like Carol, above), beneficiaries have lower replacement rates.

Legislative History

When Social Security was enacted in 1935, government employees were not covered. Typically, these workers were covered by employer programs. Congress also had Constitutional concerns about the federal government's right to tax state governments. In the 1950s, Congress allowed state and local governments to opt into Social Security. Eventually, most state and local government employees became covered by Social Security, though there are at least some non-covered workers in every state.

Congress enacted the WEP as part of the 1983 Amendments to the Social Security Act, which also made major changes to Social Security coverage, financing, taxes, and benefits. Congress intended the WEP to remove the unfair advantage that people with many years of non-covered work receive from the regular PIA formula, as discussed above. However, it lacked the data to apply the PIA formula properly to all workers. As a result, the WEP formula only approximates the PIA formula very roughly.

The WEP formula established in the 1983 Amendments, which is still used today, was the result of a compromise between the House and Senate. A House bill would have substituted a 61% factor for the 90% bend point factor in the PIA formula, while a Senate proposal would have substituted a 32% factor. A compromise between the two chambers led to the 40% factor.

Government Pension Offset (GPO)

In addition to the WEP, workers with non-covered pensions may be subject to the Government Pension Offset (GPO). The WEP applies to a beneficiary's Social Security *worker* benefit, which is the benefit based on a worker's own earnings. The GPO applies to the beneficiary's *spousal* or *survivor* benefit, which is the benefit based on his or her spouse's earnings. Spousal benefits are equal to one-half of the worker's benefit. Aged survivor benefits are equal to 100% of the worker's benefit. For workers who have earned their own worker benefits, their spousal or survivor benefits are limited by the dual entitlement rule which prevents what some refer to as "double-dipping" (when each spouse would claim both a spouse's own worker benefit and a spousal benefit). The dual entitlement rule essentially limits a beneficiary's total Social Security benefit to the greater of the spouse's own worker benefit or the spousal or survivor benefit.[8] If the beneficiary's own worker benefit exceeds his or her spousal or survivor benefit, the beneficiary receives only the worker benefit.

For beneficiaries subject to the GPO because of their non-covered pensions, spousal and survivor benefits are offset by 2/3 of the value of their non-covered pension. The GPO is similar to the dual entitlement rule. Before the GPO was enacted, a person working only in non-covered employment would be entitled to both a full non-covered pension and a full Social Security spousal benefit.

This 2/3 offset is smaller than the dollar-for-dollar offset that applies to dually entitled beneficiaries. It should be noted that non-covered pensions take the place of both Social Security benefits and traditional employer-sponsored pensions for these workers. (In contrast, *covered* state and local government employees typically receive both Social Security and an employer-sponsored pension.) In essence, the GPO rule treats the non-covered pension as if 2/3 of it replaces Social Security.

Legislative History

Congress first established the GPO as part of the 1977 Amendments to the Social Security Act. It mirrored the dual entitlement rule, in which every dollar of a beneficiary's Social Security worker benefit is subtracted from his or her spousal or survivor benefit. However, unlike the dual entitlement rule, which determines the offset amount using the beneficiary's worker benefit, the GPO used the beneficiary's non-covered pension amount.

In the 1983 Social Security amendments, the House proposed to change the GPO offset to one-third of the non-covered pension and the Senate proposed no changes to the law (in effect maintaining the 100% offset). Congress compromised to establish a 2/3 offset, the formula that remains to this day.

EQUITY, ACCURACY & EFFICIENCY CONCERNS

As discussed in more detail below, the current WEP and GPO formulas are flawed. First, workers affected by the WEP and GPO may be treated unequally: some receive higher benefits than they would if their entire careers had been covered by Social Security; others receive less. Second, SSA does not have the data it needs on non-covered pensions to implement the law accurately. Third, the WEP and GPO are difficult to administer and communicate.

Unequal Treatment

Both the WEP and the GPO treat workers unequally, compared to workers whose entire careers are spent in non-covered work.

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[8] Beneficiaries always receive their entire worker benefit. If they also qualify for a spousal benefit, that spousal benefit is reduced dollar for dollar by the amount of the worker benefit.

Windfall Elimination Provision

The WEP is calculated using different rules than Social Security's benefit formula. Though Congress intended to treat workers with non-covered earnings and workers whose entire careers were covered by Social Security comparably,[9] beneficiaries subject to the WEP receive bigger or smaller benefits than they would have if all of their work had been covered by Social Security.

In addition, the WEP tends to be regressive[10], reducing the benefits of people with lower lifetime earnings more than those with higher lifetime earnings. As shown in Tables 2 and 3, the WEP reduction tends to be too small for higher earners and too large for lower earners, compared to what these workers would receive if all their work had been covered by Social Security. The reduction in the WEP formula only applies to earnings below the first bend point of the PIA formula, so the adjustment is relatively larger for people with lower earnings. Lower earners lose a higher percentage of their benefits than higher earners do. The more earnings a worker has earned above the first bend point amount, the less he or she is affected by the WEP.[11]

The WEP phase-out for people with over 20 years of earnings above the threshold is also regressive. People who earn less than the threshold are less likely to qualify for the phase-out because years of non-covered work below the threshold do not count. As a result, small changes in covered earnings can lead to large changes in Social Security replacement rates.[12]

Government Pension Offset

The GPO often results in higher benefits than the Social Security formula would, according to a 2007 Congressional Research Service memorandum.[13] This comprehensive analysis compares the outcomes of Social Security rules and pension rules in the states with the greatest number of workers affected by the GPO. It examines workers with various earnings levels and work histories. The analysis concludes that many individuals affected by the GPO have much higher Social Security benefits than they would have received if all their work had been covered. The GPO offset would need to be increased by up to 900% to replicate ordinary Social Security rules. Other beneficiaries affected by the GPO receive somewhat smaller benefits than they would have if all their work had been covered. The GPO offset would need to be decreased by up to 50% to replicate ordinary Social Security rules in these cases.

One of the main reasons for this disparity in outcomes is that the GPO is based on the amount of a worker's non-covered *pension*, while the dual entitlement offset is based on his or her own *Social Security worker benefit*. Pension rules and Social Security rules are very different. Pension amounts depend on the specifics of a worker's non-covered employment: how long it was, when it occurred, how much the worker earned, and the rules of the pension system. Each of these variables can

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[9] CRS Report 98-35, *Social Security: The Windfall Elimination Provision (WEP)*, by Alison M. Shelton.

[10] Verify with SSA data

[11] The WEP formula's regressive effect is mitigated somewhat by the rule that limits the size of the offset to half the value of a worker's non-covered pension.

[12] Jeffrey R. Brown and Scott Weisbenner. *The Distributional Effects of the Social Security Windfall Elimination Provision*, National Bureau of Economic Research. 2012.

[13] Cite memo, and note that this section draws heavily from its analysis.

affect the size of a worker's pension dramatically—and as a result, can significantly change the size of his or her GPO adjustment. For example, beneficiaries whose non-covered work comes later in their careers have bigger pensions—and bigger GPO reductions—than beneficiaries with the same number of years at the same wages earlier in their careers. Social Security's PIA formula has no such distortion, as all earnings are indexed to wages. As a result, later years of earnings are not valued more than earlier years, all else equal. Similarly, higher earners have bigger non-covered pensions—and bigger GPO offsets—than lower earners, all else equal. Social Security's PIA formula is progressive and limited by the cap on taxable wages; non-covered pensions are not. As a result, higher earnings would have a bigger impact on a person's non-covered pension amount (and thus GPO amount) than on his or her Social Security benefit amount. Using non-covered pension amounts as the basis for the GPO is an apples-to-oranges comparison that leads to highly distorted outcomes.

Incomplete Data

Complete earnings histories are necessary to calculate Social Security's primary insurance amount (PIA) formula. However, when the WEP and GPO were established, SSA only had records of earnings from covered earnings, not non-covered earnings. As a result, Congress structured the WEP using an arbitrary adjustment to the PIA formula, which applied only to covered earnings, and based the GPO on self-reports of non-covered pensions.

Implementing the WEP and GPO requires complete data on non-covered pensions. However, SSA does not have access to this data. To identify beneficiaries who may be subject to WEP and GPO, SSA asks beneficiaries to report their non-covered pensions. (One notable exception to self-reporting is retired federal employees. SSA has received data on their non-covered pensions directly from the Office of Personnel Management since 2000.) SSA has no way to verify the accuracy of beneficiary's self-reports for non-covered state or local government pensions. Beneficiaries sometimes fail to report their non-covered pensions. As a result, the WEP and GPO are a source of improper payments in Social Security. SSA's Inspector General estimates that if SSA does not confirm beneficiaries' pension receipt and apply the WEP and/or GPO appropriately, it will overpay $869.9 million over the beneficiaries' lifetimes.[14]

Difficult Implementation

The WEP and GPO are difficult to administer. The rules are complex and have many possible exceptions, such as the phase-out for substantial covered earnings. As a result, the policies are labor-intensive and prone to error. SSA makes errors calculating the complex rules, particularly for beneficiaries who are dually entitled to both a worker benefit and a spousal or survivor benefit. In a 2008 audit, SSA's Inspector General estimated that SSA overpays $53.2 million annually to dually entitled beneficiaries subject to the WEP and GPO.[15] A 2011 audit on the same population found

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[14] OIG Report, *Old-Age, Survivors and Disability Insurance Benefits Affected by State or Local Government Pensions (A-13-10-10143)* November 9, 2011. http://oig.ssa.gov/sites/default/files/audit/full/pdf/A-13-10-10143.pdf

[15] OIG Report, *Dually Entitled Beneficiaries who are Subject to Government Pension Offset and the Windfall Elimination Provision (A-09-07-27010)* September 10, 2008. http://www.retirementsecurity.org/SSA-AuditReport-2008.pdf

that SSA did not correct the errors OIG had identified in 2008, and that other errors resulted in another $12.7 million each year in overpayments.[16]

The WEP and GPO rules are also difficult to convey to beneficiaries, and SSA and non-covered employers have not always communicated them clearly. Many affected beneficiaries do not understand the rules until they apply for Social Security benefits at retirement. The Social Security Protection Act of 2004 required both SSA and state and local governments to notify potentially affected beneficiaries about the WEP and GPO.[17] Starting in 2007, SSA added sections on the WEP and GPO to the Statement.

Communication problems remain. The Statement continues to provide Social Security benefit estimates based only on covered employment, with no offset for WEP or GPO. SSA cannot provide accurate estimates of WEP and GPO without information from workers about whether they are eligible for non-covered pensions, if they are married, and other factors. Potentially affected workers can use SSA's online benefit calculators to create their own estimates of WEP and GPO's effects, but many do not.

In addition, SSA's communication about the WEP and GPO could exacerbate its unpopularity. SSA's publications consistently characterize the WEP and GPO as benefit *reductions*, rather than corrections or adjustments. Research shows that framing something as a loss can influence attitudes and behaviors.[18]

BOARD RECOMMENDATIONS

Options to reform the WEP and GPO fall into two major categories.[19] The first set of changes would change the current-law rules for future beneficiaries with non-covered earnings. In this category, the Board believes the most promising approach is to replace the WEP and the GPO with proportional formulas. The second set of changes would improve data collection for current beneficiaries, who would continue to be to subject to the current law WEP and GPO. In this category, the Board believes the most promising approach is to give the IRS the authority to collect data on non-covered pensions and share it with SSA.

Proportional Formulas for Beneficiaries with Non-Covered Work

The Board recommends that Congress replace the WEP and GPO with proportional formulas to calculate offsets for beneficiaries with non-covered work who become eligible in 2017 or later. All Social Security benefits would be calculated using the same PIA formula, regardless of whether a

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[16] OIG Report, *Dually Entitled Beneficiaries Who Are Subject to the Windfall Elimination Provision and Government Pension Offset (A-09-12-11210)* January 31, 2013. http://oig.ssa.gov/sites/default/files/audit/full/pdf/A-09-12-11210.pdf

[17] Barbara A. Smith and Kenneth A. Couch, SSA Office of Retirement Policy, *The Social Security Statement: Background, Implementation, and Recent Developments*, November 2, 2014. http://www.ssa.gov/policy/docs/ssb/v74n2/v74n2p1.html#mt22

[18] Jeffrey R. Brown and Scott Weisbenner. *The Distributional Effects of the Social Security Windfall Elimination Provision*, National Bureau of Economic Research. 2012.

[19] For more information about other alternatives—mandatory Social Security coverage for state and government employees and repealing the WEP and GPO entirely—see GAO 08-248T

person's work was covered, non-covered, or a combination. Then the portion attributable to non-covered work would be subtracted.

It is now possible for SSA to implement such a proportional approach. SSA began to collect data on non-covered earnings in 1978, when Congress removed the cap on the Medicare payroll tax. It has complete non-covered earnings data starting in 1982. In order to calculate a PIA, SSA needs at least 35 years of earnings data. In 2017, SSA will have at least 35 years of earnings data--covered and non-covered--for all Americans.

Proportional Formula to Replace WEP

The Equal Treatment of Public Servants Act of 2014 has proposed replacing the WEP with such a proportional approach, which the bill terms the "public servant fairness formula."[20] First, SSA would apply the current-law PIA formula to all of the worker's earnings, in both covered and non-covered employment. Second, SSA would multiply this amount by the ratio of the worker's covered earnings to total earnings. This PIA would represent the benefit the worker had earned in covered employment, and would be the new basis for the worker's Social Security benefit. For example, if a third of a person's lifetime earnings came from covered employment, and two-thirds from non-covered employment, then he or she would receive a third of the PIA calculated with all of his or her earnings.

SSA's actuaries project that, combined with two other provisions (which together are cost neutral), using this new formula will save $2.7 billion total over 10 years and improve Social Security's 75-year solvency by 0.02% of payroll.

The proportional rules would increase benefits for some workers and reduce benefits for others. Importantly, the bill would remove two exemptions from the current-law WEP rules: workers with 30 or more years of covered earnings and workers with non-covered earnings who never vest in a non-covered pension. These workers would be subject to the new rules. The actuarial memo on the bill projects "small benefit reductions from the [new formula] for a relatively large number of workers who would not be reduced by the WEP."

The proportional approach would be equitable, using the same formula for all workers, whether in covered or non-covered employment. It would simplify a complex set of rules and allow SSA to stop relying on self-reported pension data, and instead use the non-covered earnings data that it already possesses. This would reduce overpayments and administrative complexity. The proportional approach would also be easier to communicate to beneficiaries. SSA could include accurate estimates of Social Security benefits in the Statements of workers in non-covered employment.

As noted above, the current law WEP does not affect workers who never receive a non-covered pension, but under a pure proportional approach, these workers' Social Security benefits would be reduced. On the one hand, this would be consistent with Social Security's rules for other beneficiaries: pensions are not considered as part of the formula. On the other hand, these workers' years in non-covered employment count toward neither Social Security nor a non-covered pension that was designed to replace Social Security. These workers could fall through the cracks of the retirement system. Therefore, it might be more equitable to exclude those years from the formula. An increasing number of non-covered workers fall into this category. State and local governments

[20] The bill also includes two other provisions not covered in this report.

are gradually lengthening vesting periods: employees typically must wait 5 years to vest in their pensions; about a quarter of plans require a vesting period of at least 10 years.[21]

Proportional Formula to Replace GPO

The GPO could also be replaced with a formula that uses the same rules that apply to covered workers. As in the proportional formula that could replace WEP, a worker's covered and non-covered earnings could be included in the current law PIA formula. This amount would be equivalent to the Social Security retired worker benefit the worker would have received had all of his or her work been in covered employment. As under the current law dual entitlement rule, the amount of this worker benefit (based on both covered and non-covered earnings) would be subtracted dollar for dollar from his or her Social Security spousal benefit. However, this new formula would be based solely on a worker's *earnings*, and would not consider the size of his or her non-covered *pension*, significantly simplifying and rationalizing the rules. It would not require any approximation of what proportion of the non-covered pension is intended to replace Social Security (as the current-law two-thirds offset does implicitly).

As with the proportional WEP formula, this approach would be more equitable, simpler, and easier to communicate. It would reduce some workers' benefits, compared to current law.

Improving Data to Implement the Current Law WEP and GPO

The new proportional formulas would only affect new beneficiaries, for whom SSA has complete earnings histories. Current beneficiaries would continue to be subject to the current law WEP and GPO. Without better data collection, the WEP and GPO would continue to be a source of improper payments. For example, a beneficiary retiring today who fails to report a non-covered pension could receive overpayments for decades to come.

SSA already receives data on federal workers' non-covered pension from OPM, but lacks data on state and local government workers' non-covered pensions. However, it would be impractical for SSA to gather this data from the thousands of non-covered pension systems across the country.[22] There are also potential legal challenges to SSA's use of this data to administer its programs.

The Board recommends that Congress give the IRS the authority to collect data from non-covered pension administrators and share it with SSA. The Government Accountability Office (GAO) has long recommended such an approach, which OMB estimates will save almost $3 billion over ten years.[23]

This approach has many advantages.[24] The data would be provided by the state and local pension systems, which have up-to-date, accurate, and detailed information about non-covered pensions.

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[21] Alicia H. Munnell, Jean-Pierre Aubry, Joshua Hurwitz, and Laura Quinby. *The Impact of Long Vesting Periods on State and Local Workers,* Center for Retirement Research at Boston College, November 2012. http://crr.bc.edu/briefs/the-impact-of-long-vesting-periods-on-state-and-local-workers/

[22] This approach is proposed in the President's Budget. However, GAO has found that it would be difficult to implement. GAO 98-76 Report*, Social Security: Better Payment Controls for Benefit Reduction Provisions Could Save Millions*, April 1998, http://www.gao.gov/assets/230/225406.pdf

[23] GAO estimates $2.4-$2.9 billion savings within 10 years. GAO-11-318SP Report*, Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue*, March 2011, http://www.gao.gov/assets/320/315920.pdf

[24] GAO 98-76 Report*, Social Security: Better Payment Controls for Benefit Reduction Provisions Could Save Millions*, April 1998, http://www.gao.gov/assets/230/225406.pdf

This information would be reported uniformly to SSA from a single source, the IRS, rather than the thousands of non-covered pension systems across the country. Collecting the data would require only a small change to a single form, IRS Form 1099R. IRS officials told GAO that such a change would minimally affect their processing costs. Similarly, pension managers said that reporting the information would require only minor programming changes. Finally, SSA is already permitted to access 1099R records for program administration, eliminating a possible legal hurdle.

Giving SSA access to more information on non-covered pensions would reduce improper payments and simplify administration. However, it would not address the equity and complexity concerns raised by the WEP and GPO's arbitrary formulas. Only the proportional formulas endorsed by the Board could do that, but these formulas can be applied only to those who retire starting in 2017.

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