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June 16, 2009

AGENDA ITEM 3b

TO: MEMBERS OF THE BENEFITS AND PROGRAM ADMINISTRATION COMMITTEE

I. SUBJECT: AJR 10 (Torlakson) — As Amended May 18, 2009
Repeal of Social Security Benefit Offsets

Sponsors: California Federation of Teachers, California Retired Teachers Association, and the California Teachers Association

II. PROGRAM: Legislation

III. RECOMMENDATION: Support

Eliminating the WEP and the GPO provisions would benefit CalPERS members who have worked in state, school, and local government jobs not covered by Social Security.

IV. ANALYSIS:

This measure requests the President and the Congress of the United States enact the Social Security Fairness Act of 2009, which would repeal the Government Pension Offset and the Windfall Elimination Provision from the Social Security Act.

Background

When first enacted in 1935, the Social Security Act did not cover public employees. In the early 1950's, statutory changes allowed coverage to be extended to state and local government employees not covered by an existing public retirement plan; however, employees could not participate in both Social Security and a public pension plan simultaneously until 1954, when coverage was extended on a voluntary group basis.

In 1955 and again in 1959, members of the state's several public pension plans participated in referenda that would have allowed its retirees to receive Social Security benefits, but their State Employees' Retirement System (today,

CalPERS) benefits would have been offset by the amount of Social Security benefits payable. Known as the full offset plan, both referenda were defeated by wide margins. In 1961, chaptered legislation allowed the coordination of SERS miscellaneous plans with Social Security without an employee referendum, instead allowing individual members to elect whether or not to coordinate their SERS pension with Social Security.

While many groups of public employees participate in Social Security in addition to their employer-sponsored pension benefits, most public safety employees (including CalPERS State Peace Officer/Firefighter, State Patrol and State Safety members), teachers, and many miscellaneous local government employees (including many CalPERS contracting agency members) in California do not pay Social Security payroll taxes on earnings for their government service, and consequently, do not receive a benefit. If these workers receive a Social Security benefit, it is due either to other employment that was covered by Social Security, or by being a spouse or surviving spouse of a worker covered by Social Security.

The following table lists the number of covered and non-covered active CalPERS members.

CalPERS Active Employee Social Security Coverage
June 30, 2008

Total Actives	Miscellaneous		Safety		Total	
	State	144,831	21.47%	77,657	60.41%	222,488
Schools	314,098	46.57%	591	0.46%	314,689	39.19%
Public Agency	215,549	31.96%	50,296	39.13%	265,845	33.11%
Total	674,478	100.00%	128,544	100.00%	803,022	100.00%
Covered						
State	118,589	81.88%	0	0.00%	118,589	53.30%
Schools	303,255	96.55%	0	0.00%	303,255	96.37%
Public Agency	101,221	46.96%	4,311	8.57%	105,532	39.70%
Total	523,065	77.55%	4,311	3.35%	527,376	65.67%
Non-Covered						
State	26,242	18.12%	77,657	100.00%	103,899	46.70%
Schools	10,843	3.45%	591	100.00%	11,434	3.63%
Public Agency	114,328	53.04%	45,985	91.43%	160,313	60.30%
Total	151,413	22.45%	124,233	96.65%	275,646	34.33%

Prepared by OPPD
2008 Annual Sum Counts Formula pages 643-646

May
2009

NOTES:

To determine total active counts, safety included: POFF, Patrol, and Safety.
All other categories were included in Miscellaneous.

The previous table shows that approximately 36 percent of CalPERS active employees are not covered by Social Security. However, coverage levels for miscellaneous members vary among the state, schools, and public agency member groups. Approximately two-thirds of state miscellaneous employees are covered by Social Security, as are nearly all school miscellaneous employees. Less than half of public agency miscellaneous employees are covered. Very few CalPERS safety members are currently covered by Social Security. No state and school safety members are covered, and only three percent of public agency safety members are covered.

Social Security Benefit Structure

The Social Security benefits paid to a retired worker are based on the average monthly earnings, indexed for inflation, that were subject to Social Security payroll taxes during the 35 highest years of indexed earnings. The average indexed earnings are divided into three tiers based on when they first become eligible for benefits. For individuals who first become eligible for the Social Security old-age benefit in 2001, the primary insurance amount (PIA), or full benefit, is the sum of

90 percent of the first \$561 of the average indexed monthly earnings,
plus
32 percent of the averaged indexed monthly earnings of the next \$2,820,
plus
15 percent of the average indexed monthly earnings above \$3,381

Spouses and eligible ex-spouses of retired workers also can receive a benefit based on the earnings of the retired worker. The full benefit paid to a spouse or eligible ex-spouse equals 50 percent of the PIA paid to the retired worker if that amount is less than the benefit that would be paid based on the spouse's or ex-spouse's own covered earnings.

Finally, surviving spouses and eligible ex-spouses receive a benefit equal to the amount paid to the deceased workers if that amount is greater than the benefit that would be paid based on the surviving spouse's or ex-spouse's own earnings.

Under this benefit structure, the more money a worker earns the lower the percentage of those earnings are replaced by Social Security. For the lowest paid workers, Social Security replaces up to 90 percent of the average indexed monthly earnings. Similarly, if the spouse or surviving spouse has limited earnings, and therefore receives little or no Social Security benefits from his or her own earnings, the spouse or surviving spouse receives an additional amount based on the earnings of the worker.

Social Security Benefit Offsets

The Windfall Elimination Provision (WEP) is designed to prevent workers whose public pensions are not coordinated with Social Security from receiving higher benefits than they otherwise would if all of their earnings had been subject to Social Security. Under WEP, Social Security benefits are reduced for workers who paid into Social Security for less than 30 years and are receiving benefits from work not covered by Social Security. If the recipient has more than 20 years of what are considered "substantial earnings" covered by Social Security, the reduction is not as large. The WEP reduces a person's Social Security benefit from 90 percent to 40 percent of the first \$561 of their average indexed monthly earnings; however, it cannot reduce the benefit by more than 50 percent of the his or her governmental pension.

The Government Pension Offset (GPO) reduces Social Security benefits to spouses, ex-spouses, surviving spouses and surviving ex-spouses who receive a government pension for work not covered by Social Security. Under the GPO, the spouse's Social Security benefit is reduced by two-thirds of that person's uncoordinated public pension. For some, this can result in the total elimination of any Social Security survivor benefit, but it does not affect a person's eligibility for Medicare benefits. Although the GPO was enacted in 1977, most people do not become aware of these reduced Social Security benefits until the time they begin receiving payments.

Proposed Changes

Enactment of AJR 10 would result in a resolution being transmitted to the President and Vice President, to the Speaker of the House of Representatives, the Majority Leader of the Senate, and to each Senator and Congressional Representative from California requesting that they approve the Social Security Fairness Act of 2009, which would repeal the Government Pension Offset and the Windfall Elimination Provision from the Social Security Act.

Legislative History

Resolutions requesting Congress and the President to either reduce or repeal the government pension offsets have been introduced and approved by the California Legislature in almost every legislative session since the offsets were implemented. The last time the CalPERS Board of Administration considered this subject was when it supported Senate Joint Resolution 4 (Soto) in 2001, which memorialized the President and the Congress to enact legislation to limit application of the GPO and the WEP. The Board has also supported previous resolutions to eliminate the GPO and WEP.

2009 H.R.235 (Berman) and S.484 (Feinstein) The Social Security Fairness Act of 2009 would amend title II of the Social Security Act to repeal the GPO and WEP.

- 2007 Resolution Chapter 116 (AJR 4, Hernandez) requests the President and Congress to enact the Social Security Fairness Act to repeal the GPO and WEP from the Social Security Act.
- 1983 Public Law 98-21, reduced Social Security benefits to workers who also receive a pension from work not covered by Social Security; also changed the reduction in the Social Security Bill Analysis benefit paid to a spouse from 100 percent of that person's pension from work not covered by Social Security to two-thirds of the pension.
- 1977 Public Law 95-216, reduced the Social Security benefit paid to a spouse by the amount of the spouse's government pension from work not covered by Social Security, if the spouse was not eligible for retirement as of 1982.

Issues

1. Arguments in Support

According to the author:

"The WEP and GPO provisions of the Social Security Act penalize individuals who move from private sector employment to teaching, public safety, and other careers in public service and vice versa. California has a significant teacher shortage and requires more than 16,000 new teachers per year to meet enrollment growth needs, retirement replacement, as well as class size reduction in targeted schools."

"The penalty hamstrings the state's ability to recruit experienced professionals to enter the teaching profession, as they would lose their social security benefits if they changed careers."

Organizations in Support: California Federation of Teachers, California Retired Teachers Association, and the California Teachers Association (Co-sponsors). Association of California School Administrators, Association for Los Angeles Deputy Sheriffs, California Professional Firefighters, California School Employees Association, California State Employees Association, Faculty Association of California Community Colleges, Los Angeles County Probation Officers' Union, AFSCME, Local 685, Los Angeles Police Protective League, Orange County Employees Association, Orange County Professional Firefighters Association, Retired Public Employees Association, and the Riverside Sheriffs' Association.

2. Arguments by those in Opposition

There is currently no known opposition.

3. Rationale for Reducing Social Security Benefits

Social Security benefits reflect two factors; (1) the amount of Social Security taxes paid by a worker and (2) a formula that pays a proportionately higher benefit to lower-paid workers. When the worker's entire career has been covered by Social Security, the wages used by Social Security to calculate the benefit properly reflects the wages earned by the worker during that worker's career. When the worker has employment that was not covered by Social Security, the Social Security benefit formula understates the career earnings of the worker, and thereby overstates the Social Security benefit that should be paid, based on the objective of paying a relatively higher benefit to lower-paid workers. To compensate for the understatement of the worker's actual career earnings, the Social Security benefit formula is adjusted to reduce the benefit paid to workers who have been employed in jobs not covered by Social Security.

Similarly, spouses and surviving spouses of Social Security benefit recipients also receive Social Security benefits, but only to the extent that the spousal benefit exceeds the benefit paid to a person as a result of his or her own employment. In other words, the Social Security spousal benefit is reduced by 100 percent of the person's own Social Security benefit.

For members who do not receive a Social Security benefit from their CalPERS-covered employment, there may be no Social Security benefit to reduce the spousal benefit for such a person. Yet, if the member had worked in employment covered by Social Security, the spousal benefit would have been completely offset. As a result, some CalPERS members could receive a higher spousal benefit than would a similarly situated person who worked under Social Security, not because his or her own earnings were low and, therefore, he or she was financially dependent on the spouse, but because he or she did not pay the Social Security payroll taxes on earnings for the CalPERS-covered public safety service and therefore did not receive a Social Security benefit based on those earnings. The GPO is intended to compensate for that situation by reducing the benefit paid to a spouse or surviving spouse by two-thirds of the CalPERS or similar pension.

4. Current Application of the WEP and GPO May Be Inappropriate

Although there appears to be a justification for reducing Social Security benefits to government workers, the specific adjustments do not appear to be appropriate. For example, the WEP is intended to compensate for wages that were earned in employment not covered by Social Security, but the amount of the adjustment essentially bears no relation to the amount of such non-covered earnings. The only modification to the WEP, other than a relatively minor requirement that the WEP reduction not exceed 50 percent of the government pension, is that the WEP adjustment is reduced as the number of years of employment covered by Social Security increases.

Similarly, it does not appear that reducing the benefit paid to a spouse or a surviving spouse by two-thirds of the governmental pension properly adjusts for the distortion caused by the person working in employment not covered by Social Security. By reducing the benefit paid to the spouse and surviving spouse by two-thirds of the governmental pension, the governmental pension is used to approximate what the Social Security benefit would have been if the employment had been covered by Social Security. In effect, a two-thirds reduction implies that the earnings associated with non-covered government employment would result in a Social Security benefit equal to two-thirds of the governmental pension for the same earnings history. However, it is estimated that a typical public safety career, if covered by Social Security, would result in a Social Security benefit that is significantly less than the CalPERS benefit derived from that public safety service. This suggests that the GPO results in an excessive reduction in Social Security benefits.

5. Maintaining The Benefit Offsets Reduces Federal Costs

An Obama Administration fiscal year 2010 budget proposal would impose a new mandate on CalPERS, by requiring pension plans whose members are outside Social Security to provide data to the Social Security Administration. The 2010 budget estimates that this proposal would reduce federal spending by \$2.9 billion from 2013-2019.

A reduction or elimination of these benefit offsets will impact the federal treasury and could further exacerbate the fiscal problems of the Social Security program, which is forecast to begin running out of money in approximately 30 years. In addition, the greater the funding imbalance of Social Security, the greater the likelihood that lawmakers will consider other alternatives, such as mandatory coverage of newly hired State and local public workers, to shore up the program.

6. Legislative Policy Standards

The Board's Legislative Policy Standards do not specifically address this issue. However, staff recommends a support position because it appears that the WEP and GPO inappropriately reduce Social Security benefits for affected CalPERS members, and should be eliminated or modified.

V. STRATEGIC PLAN:

This item is not a specific product of the Annual or Strategic Plans, but is a part of the regular and ongoing workload of the Office of Governmental Affairs.

VI. RESULTS/COSTS:

Enactment of AJR 10 would result in a resolution to memorialize the President and Congress to enact legislation to eliminate the WEP and the GPO. This resolution would not result in any program or administrative costs to CalPERS.

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