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Alternative Retirement Plans May Reduce Social Security Benefits

There are two federal laws that may reduce social security benefits for certain government retirees who are eligible for social security and also a government pension from a job where they did not pay social security taxes. The non-covered pension can be from either a defined benefit plan, such as KTRS, or a defined contribution plan, such as a Section 457 deferred compensation plan if used as an alternative retirement plan.

The two laws--the windfall elimination provision (WEP) and government pension offset (GPO)--are designed to resolve inequities in the law that had, in the past, permitted some government employees to collect more in social security benefits than was originally intended.

WEP and GPO may impact government employees who do not pay social security (such as public school teachers who participate in KTRS) and any participant in a deferred compensation plan which is used strictly as a retirement plan.

Defining a Pension for WEP/GPO Purposes

The Omnibus Budget Reconciliation Act 1990 contained a provision which extended Social Security coverage to those governmental employees who are not members of a retirement system—commonly referred to as mandatory Social Security. The provision does not apply if the employee is already covered under a Section 218 Agreement of the Social Security Act or is a member of a qualified retirement system as defined by IRS regulations. Mandatory Social Security coverage ceases when the governmental employee becomes a member of an employer provided retirement system that conforms to IRS regulations. For example, substitute teachers must contribute to mandatory social security if they are not participating members of a qualified retirement plan.

Some employers have opted for other than the standard notion of a retirement system such as a deferred compensation plan—a defined contribution plan that allows participation by governmental employees in lieu of mandatory Social Security coverage. This and other plans raise several questions about the applicability of WEP and GPO.

The first step in determining if GPO and/or WEP will apply is to determine if the periodic or lump sum payment is a pension for GPO/WEP purposes. SSA applies the following general rule to each case when determining if a periodic payment or lump sum benefit from a defined contribution plan (or any other plan) is a pension.

If an employee voluntarily contributes to a plan which is separate from and in addition to a primary retirement plan; the employer makes no contributions to the plan; the withdrawals from the plan do not exceed

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the employee's contributions (plus interest); and withdrawals are not based upon age, length of service or earnings, then the plan is considered a savings plan and is <u>not</u> a pension plan for GPO/WEP purposes.

Examples:

1) A substitute teacher is not covered by the Section 218 Agreement. In July 1991, the employee elected to participate in the school board's alternative retirement plan--a Section 457 deferred compensation plan--in lieu of mandatory Social Security coverage. The employee, upon retirement, will receive a payment from the deferred compensation plan based on contributions to the plan, as this is the only retirement plan to which the employee contributes. This plan is not considered a savings plan for GPO/WEP purposes and the payment will be considered a pension and may activate the GPO/WEP provisions. (See WEP reminders.)

2) A teacher is not covered by a Section 218 Agreement, but is covered by KTRS and has also elected to make contributions to a deferred compensation plan. The payment from this deferred compensation plan is separate from and in addition to the KTRS, the employer make no contributions to the plan and the payment from the plan is not based on age, length of service or earnings. While the payment from KTRS may activate the GPO/WEP provisions, the payment from the deferred compensation plan will not.

The Windfall Elimination Provision (WEP)

The WEP primarily affects workers who spent most of the careers working for a government agency in a position not covered for social security, but who also worked at other jobs where they paid Social Security taxes long enough to qualify for retirement or disability benefits. In these cases, Social Security benefits will be figured using a formula different from the one used for those who spent most or all of their working years paying Social Security taxes. The windfall elimination formula results in a reduced Social Security benefit.

Before this provision was enacted in 1983, government employees had their benefits computed as if they were long-term, low-wage workers. Thus, they received the advantage of the higher percentage Social Security benefits in addition to their non-covered government pension.

The Government Pension Offset (GPO)

The GPO applies only to workers who get a non-covered government pension and are eligible for Social Security as a spouse or widow(er). Two-thirds of the government pension is used to offset any spouse's or widow(er)'s Social Security benefit.

Before the offset provisions were enacted, many government employees qualified for a pension from their agency and for a spouse's benefit from Social Security, even though they were not dependent on their husband or wife.

WEP Reminders

Withdrawal of contributions: WEP and GPO policy differs in the treatment of the withdrawal of contributions. WEP uses eligibility to determine if WEP applies. If the individual is eligible for a pension when contributions are withdrawn, then WEP applies. If contributions are withdrawn prior to the first point of eligibility, WEP will not apply.

For GPO purposes, a true withdrawal of contributions at any point would prevent GPO offset. If the individual withdrew his/her contributions after he/she was first eligible and relinquish all rights to any benefit under the pension plan, the offset would not apply. If contributions were withdrawn and some type of pension could still be paid, the offset would be imposed.

Assistance

SSA Publication 05-10045, covering WEP, and SSA Publication 05-10007, addressing GPO, are available from the Social Security Administration or the Division of Social Security web site. School boards assisting in retirement planning are urged to provide copies of these publications to their employees.

This fact sheet is designed to provide awareness of certain social security benefit provisions. It should not be cited or used as authority with respect to obtaining social security benefits. The Social Security Act, along with appropriate regulations, rulings and case law, are the only valid citations of authority for benefit matters.