



Department of Employee Trust Funds

Wisconsin Retirement System



Interest

vs.



Annuity Adjustments

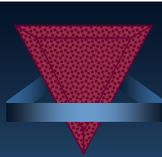
By Kathryn Fields - Trust Funds Specialist

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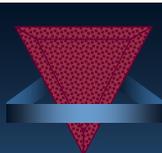
Frequently Asked Questions

- ✎ What is the difference between Interest Crediting and Annual Annuity Adjustments?
- ✎ Why are *annuity adjustments* not as high as *interest*?
- ✎ How are core and variable adjustments calculated and who figures it out ?
- ✎ At what point can ETF begin paying adjustments (minimum annuity threshold)?
- ✎ Are there ever decreases in payments? Why?
- ✎ How much money is left in my account after I retire?
- ✎ I'm in the Variable, so how much of my benefit is Core and how much is Variable?
- ✎ What have the interest rates and adjustments been in past years?



Understanding The Wisconsin Retirement System

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Wisconsin Retirement System (WRS)

- ↘ Individual accounts and benefits under the WRS are managed by ETF
- ↘ Investing of WRS assets is the responsibility of the State of Wisconsin Investment Board (SWIB)
 - ↘ Assets are invested in two trust funds
 - Core (fully diversified) and Variable (all stocks)
- ↘ The funds in the trusts are used to pay WRS benefits
- ↘ Most employees receive a monthly pension (annuity) when they retire and the benefit is calculated by ETF

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First Things First

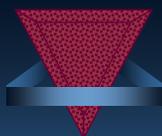
Interest Earnings *and* Annual Annuity Adjustments (by law) depend solely on how the trust funds perform each year

- ↘ There is no guarantee of interest earnings or annuity adjustments
 - ↘ There is no such thing as a “cost of living” increase for retirees



The WRS remains one of the best funded public retirement plans in the country

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- The Basics - Core Fund Performance

Investment results are based on calendar year returns

- ↘ Core Fund
 - ↘ This *Market Recognition Account* smoothes returns over five year periods (recognizes gains and losses evenly)
 - ↘ This helps stabilize
 - ↘ Interest crediting
 - ↘ Contribution rates
 - ↘ Annuity adjustments



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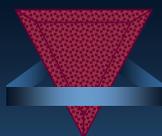


- The Basics - Variable Fund Performance

Investment results are based on
calendar year returns

Variable Fund

- Market gains/losses are not smoothed
- Returns are fully recognized each year
- Has larger & more immediate impact on participants



Calculating Core Fund Effective Rate

After SWIB reports the final return
(as of 12/31)



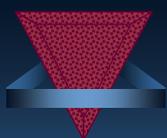
ETF actuaries calculate

- Effective rate of interest
- Annuity adjustments



Calculating Core Fund Effective Rate (In \$ Millions)

2006 Investment Income		\$	9,872
Adjustments for Market Recognition Account			
2006 Gain Deferred to Future Years	(4,918)		
Gains and Losses Carried Over From:			
2002	(1,764)		
2003	1,341		
2004	518		
2005	86		
2006	<u>984</u>		
Total MRA Adjustment			(3,753)
Current Year Recognized Income			6,119
Less: Allocations and Adjustments (ICI, LTDI, ASLCC, Duty Dis)			(258)
Income Available for Core Effective Rate			5,860
Adjusted Beginning Reserve Balance		\$	59,227
Effective Rate (\$5,860 / \$59,227)			9.8%



Calculating Variable Fund Effective Rate (\$ Millions)

2006 Investment Income	\$	1,089
Adjusted Beginning Reserve Balance		5,829
Effective Rate (\$1,089 / \$5,829)		18.0%

Actual is 18.1868%, but it's truncated (by law) to a whole % so the .1868 is carried over to the next year - See next section on calculating dividends



After Interest is Calculated and Credited to the Annuity Reserve . . .

ETF actuaries can calculate the Core and Variable annuity adjustments

Calculation is based on . . .

- ↘ The amount of money in the reserve (including the interest just credited)

COMPARED TO

- ↘ The amount needed to pay all benefits for the projected lifetimes of annuities in force (including assumed 5% annual interest)

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Understanding Annuity Adjustments . . .

requires an explanation of how WRS annuities are "funded"



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Understanding Annuity Adjustments . . .

When participants retire:

- Sufficient monies needed to pay annuities for *projected lifetimes* are transferred from participant accounts (the Employee Reserve Fund) and the Employer Reserve, to the Annuity Reserve

(Amount transferred is calculated based on assumption that the annuity reserve will earn 5% annual interest)

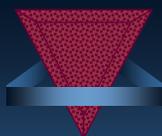
- Account is "closed"

‣ The Annuity Reserve is the account from which all annuities are paid

- There are separate Core and Variable funds in the Annuity Reserve

- Interest is credited to both funds in the Reserve

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Understanding Annuity Adjustments . . .



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Understanding Annuity Adjustments

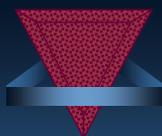
Many factors (established by law) are used to calculate annuity adjustments

↘ The three most significant factors are:

1. 5% assumed interest
2. Mortality rates
3. Carryover



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Calculating Annuity Adjustments 5% Assumed Interest

- ↘ Amount of dollars (\$) transferred to the reserve assumes the funds will earn 5% interest each year
- ↘ The reserve must be credited with 5% just to break even!
- ↘ Only investment earnings in *excess* of the assumed 5% are available to fund increases

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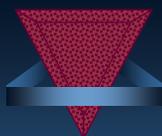
Calculating Annuity Adjustments 5% Assumed Interest

If fund earns less than 5% - that shortfall must be "made up" by . . .

1. Not granting an increase that year and/or
2. Taking back previously-granted increases

Core annuities are guaranteed never to decrease to less than the original monthly amount

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Calculating Annuity Adjustments Mortality Rates

- ↘ WRS annuitant life expectancies continue to increase
- ↘ Good for annuitants, however . . .
- ↘ Fund will have to pay annuities for a longer period of time than originally anticipated at retirement





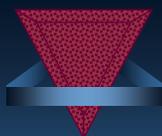
Calculating Annuity Adjustments Mortality Rates

Life Expectancy For 70-year-old

	<u>Males</u>	<u>Females</u>
1996	13.4	17.3
2006	14.5	17.8

- ✦ For each month of added longevity, the dividend adjustment is decreased by about 0.25%. This translates into approximately \$5 per month for the average annuitant
- ✦ However, improved longevity means members are receiving benefits for a longer period of time

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Calculating Annuity Adjustments Carryover

- ✦ By law, variable adjustment percentages are truncated to a "whole percentage"
- ✦ The fund rarely has the precise amount of dollars to fund exactly a whole percent
 - ✦ Remaining funds (or deficits) must be carried over to the next year

Example: If adjustment is 2.4%, and we can only use whole %'s, the .4% is held back and carried over to next year and used in that calculation

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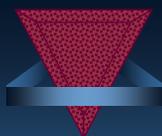
Calculating Annuity Adjustments

Summary of Results - 12/31/2006

The ratio of *what we have* divided by *what we need* to pay = adjustment amount payable

In \$ Millions

	Core	Variable
Number of Annuitants	137,117	32,683
Annual Amount	\$ 2,843.6	\$ 391.8
Fund Balance (<i>what we have</i>)	\$ 31,180.5	\$ 4,594.2
Actuarial Reserve (<i>what we need</i>)	\$ 30,273.9	\$ 4,145.2
Ratio	1.03	1.108
Total Adjustment payable	= 3%	= 10%



Core Smoothing Mechanism

Smoothing allowed ETF to give core annuity *increases* in 2001 and 2002 even though there were losses in **2000-2002**. (Still distributing gains from previous years)

Losses from **2002** were included in the calculation of the Core annuity adjustment for 2006!

Year	SWIB's Actual Investment Returns	WRS Core Effective Rate	WRS Core Annuity Rate
2000	- .8% (loss)	10.9%	5.7%
2001	-2.3% (loss)	8.4%	3.3%
2002	- 8.8% (loss)	5.0%	0.0%
2003	24.1%	7.4%	1.4%
2004	12.8%	8.5%	2.6%
2005	8.6%	6.5%	0.8%
2006	15.8%	9.8%	3.0%

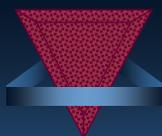
5 year smoothing period



At what point can the WRS begin to pay an increase (Minimum Annuity Threshold)

- ▶ A Core dividend (adjustment) will be paid only if the annuity reserve surplus provides at least a **0.5%** increase
- ▶ A Core annuity will be reduced only if there's a shortfall requiring at least a **-0.5%** adjustment
- ▶ Variable increases or decreases occur only when there is enough funds to give EVERYONE with a variable annuity either (at least) a **2%** increase or decrease
- ▶ If increase or decrease would be less than **2%** the surplus/deficit is carried over to the next year

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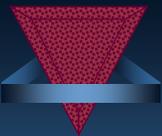
Annuities: Core vs Variable

When you retire, you will receive a
Final Annuity Calculation Statement



(ET-4820)

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Annuity benefit amount in Core vs Variable

Sample:
Notice of Final Retirement Annuity Calculation
ET-4820 - Page 2

Section 2
Your required retirement annuity was calculated under the **money purchase method** based on the balance of \$362,832.25 in your account multiplied by an actuarial factor (and option conversion factor if applicable).

You currently participate in the **variable trust** or have participated in the past. The variable excess/deficiency in your account resulted in a \$84.14 increase in your final benefit, compared to the amount you would be receiving if you had never participated in the variable program. **Note: This is included in your current payment amount.**

Your benefit was calculated under **1999 Wisconsin Act 11**, the benefit improvement legislation. If a formula calculation, the higher factor(s) for Act 11 was (were) applied to your service that was credited before 2000.

Section 3

	Gross Monthly Amount		Final with Dividend	Retroactive Amount	
	Estimate	Final			
Required	\$2,395.00	\$2,420.01	N/A	\$216.32	75% Continued to Named Survivor
Additional					

You selected the above option in the Accelerated Payment Option from your Required Account. The amount shown above is the amount of your annuity before age 62. Your "after age 62" benefit amount is \$1,168.36. Your monthly annuity is \$1,168.36 in plus \$1,251.65 in variable.

Note: To be eligible to change your annuity option, the Department must receive your written option change request WITHIN 60 DAYS AFTER THE DATE OF YOUR FIRST ANNUITY PAYMENT.

NOTE: If you have any questions about this notice or wish to request any brochures, you may contact us by writing to the Department of Employee Trust Funds, or by phoning us toll-free 1-877-533-5020 or 266-3285 (local Madison), or visit our Internet site at: <http://badger.state.wi.us/agencies/etf>. The number for the TTY (Teletypewriter for the Hearing and Speech Impaired) is (608) 267-0676.

After asking questions, if you still disagree with any of the information shown above and wish to appeal this determination of your benefit, the Department must receive your written appeal no later than 90 days after the date of this notice. Address any appeal to the Department of Employee Trust Funds, c/o Appeals Coordinator, P.O. Box 7931, Madison, WI 53707-7931.

Have you heard what the annuity adjustment will be this year?

What have the annuity adjustments been in past years?



Interest and Adjustment Rates

ETF Core Fund Percentages			
Year	SWIB Investment Return	ETF Effective Rate	ETF Annuity Dividend
2007	8.7%	13.1%	6.6%
2006	15.8%	9.8%	3.0%
2005	8.6%	6.5%	0.8%
2004	12.8%	8.5%	2.6%
2003	24.1%	7.4%	1.4%
2002	-8.8%	5.0%	0.0%
2001	-2.3%	8.4%	3.3%
2000	-0.8%	10.9%	5.7%
1999	15.5%	24.1%	17.1%
1998	14.6%	13.1%	7.2%
1997	17.2%	12.8%	7.7%
1996	14.4%	12.5%	6.6%
1995	23.1%	11.3%	5.6%
1994	-0.6%	7.7%	2.8%
1993	15.0%	11.0%	4.9%
		10 - yr ave: 10.6%	10 - yr ave: 4.67%
		5 - yr ave: 9.0%	5 - yr ave: 2.86%

Interest and Adjustment Rates

ETF Variable Fund Percentages			
Year	SWIB Investment Return	ETF Effective Rate	ETF Annuity Dividend
2007	5.6%	6.0%	0.0%
2006	17.6%	18.0%	10.0%
2005	8.3%	9.0%	3.0%
2004	12.7%	12.0%	7.0%
2003	32.7%	34.0%	25.0%
2002	-21.9%	-23.0%	-27.0%
2001	-8.3%	-9.0%	-14.0%
2000	-7.2%	-7.0%	-11.0%
1999	27.8%	28.0%	21.0%
1998	17.5%	18.0%	12.0%
1997	21.6%	23.0%	18.0%
1996	19.8%	20.0%	14.0%
1995	25.6%	27.0%	19.0%
1994	0.8%	0.0%	0.0%
1993	16.5%	17.0%	11.0%
		10 - yr ave: 7.3%	10 - yr ave: 1.39%
		5 - yr ave: 15.4%	5 - yr ave: 8.67%



Information Resources

ETF's Web site

ETF's Video Library

- ✦ WRS Trust Funds: Core & Variable
- ✦ Annual Retirement Annuity Adjustments
- ✦ Canceling Variable Participation
- ✦ Your Annual Statement of Benefits

SWIB's Web site (direct link from ETF)

- ✦ www.swib.state.wi.us

ETF Forms & Brochures

- ✦ How Participation in the Variable Fund Affects your WRS Benefits: ET-4930
- ✦ Additional Contributions: ET-2123

Summary

* Interest earnings and annuity adjustments are credited or paid solely on how the trust funds perform each year



Interest earnings and increases are not guaranteed



There can be negative adjustments to annuities



Negative Core adjustments can only be used to reduce dividends granted in prior years



WRS assets are not immune from the volatility of the stock markets



Variable annuities have no minimum benefit guarantee



The WRS remains solvent and able to provide retirement benefits long into the future because of the excellent investment team at SWIB and their long term investment strategy

THE END