

**STATE OF WISCONSIN
DEPARTMENT OF EMPLOYEE TRUST FUNDS
801 West Badger Road
Madison, WI 53702**

CORRESPONDENCE MEMORANDUM

DATE: April 30, 2003

TO: Deferred Compensation Board

FROM: Pam Henning, Director
Office of Strategic Services

SUBJECT: Update on Review of Participant Loan Feature

At the November 2002 Deferred Compensation Board (Board) meeting, staff provided an informational report to the Board on the ability of the Wisconsin Deferred Compensation (WDC) program to offer loans. The Board directed staff to work with Nationwide Retirement Solutions (NRS) to determine what effect loans have had on other Section 457 plans.

Possible Considerations for Adding a Loan Feature

- Encourages employees to participate at a younger age if they know they can access their money before separation through a loan feature.
- Participants may contribute a larger amount to their deferred compensation account if they know they have access to the funds via loans should the need arise.
- Older participants may find a loan from their account desirable to help the transition into retirement.
- Participants who do not qualify for a financial hardship withdrawal under Section 457 may be eligible for a loan to meet a current financial need.

Findings

The report prepared by NRS found that there is no supporting documentation or confirmation that the reasons for adding a loan feature have been realized for Section 457 plans. The report detailed the following issues:

- A large percentage of participants have defaulted on loans, in some cases over 31%.

- Older participants were not taking advantage of the loan feature.
- There was no documented increase in enrollments in the younger age group.
- The loan feature is expensive to administer; loan origination and maintenance fees are becoming more common.
- A Section 457 plan loan is subject to double taxation – the loan is repaid with after-tax dollars, meaning those dollars are taxed a second time when participants request a distribution from the plan.

Summary

The NRS report does not provide sufficient rationale for adding a loan feature to the WDC program. Therefore, no action is recommended at this time.