



STATE OF WISCONSIN
Department of Employee Trust Funds
David A. Stella
SECRETARY

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CORRESPONDENCE MEMORANDUM

DATE: September 15, 2011
TO: Employee Trust Funds Board
FROM: David Stella, Secretary
SUBJECT: Secretary's Report

Now that 2011 Wisconsin Acts 10, 13 and 32 are being implemented, I would like to highlight some of the provisions of these laws and their potential impact on the Wisconsin Retirement System (WRS).

Attorney General's Opinion on the \$28 Million Transfer Required in Act 13

Attached is a copy of my request for an Attorney General opinion on the provisions of 2011 Wisconsin Act 13 requiring the ETF Secretary to transfer \$28 million to the state from the health insurance trust fund reserves, and the Attorney General's opinion that responds to my request. The key issue addressed in the response is whether the non-statutory provision contained in Act 13 would constitute a taking of accrued property rights of WRS participants.

The Department of Justice indicated that as long as the Secretary apportioned the allocation consistent with the provisions of s.40.03 (6) (e) Wis. Stats., the Secretary would satisfy the provisions of Act 13, but not impair the property rights of WRS participants. This means that the Secretary would have to allocate the health insurance reserves to reduce premiums across-the-board for employees, retirees and employers or hold the reserves in order to stabilize premium costs in the future.

At its August 23, 2011, meeting, the Group Insurance Board (GIB) adopted a policy on what constitutes "excess" reserves in the Health Insurance Trust Fund and then allocated \$30 million of the excess reserves to reduce premiums in 2012. At that same meeting, I exercised my authority under Section 9115 of 2011 Wisconsin Act 13 and concurrently allocated \$28 million of the \$30 million already allocated by the GIB toward that same purpose. The Department of Justice opinion contains important legal guidance on the need to harmonize existing and new statutory requirements so as not to impair the property rights of WRS participants.

Board	Mtg Date	Item #
ETF	9.15.11	5A

WRS Study Required in Act 32 (2011-2013 Biennial Budget)

The Biennial Budget contained a non-statutory provision that provides the following:

SECTION 9115.0 Nonstatutory provisions; Employee Trust Funds.

(3q) MODIFICATIONS TO WISCONSIN RETIREMENT SYSTEM. (a) The secretary of administration, the director of the office of state employment relations, and the secretary of employee trust funds shall study the structure of the Wisconsin Retirement System and benefits provided under the Wisconsin Retirement System. The study shall specifically address the following issues:

1. Establishing a defined contribution plan as an option for participating employees, as defined in section 40.02 (46) of the statutes.
2. Permitting employees to not make employee required contributions under section 40.05 (1) (a) of the statutes and limiting retirement benefits for employees who do not make employee required contributions to a money purchase annuity calculated under section 40.23 (3) of the statutes.

(b) No later than June 30, 2012, the secretary of administration, the director of the office of state employment relations, and the secretary of employee trust funds shall report their findings and recommendations to the governor and the joint committee on finance.

While the due date to submit the report to the Legislature is nine months away, ETF has started to develop a framework for this required study. It should be noted that the Legislature provided no funding for the study, even though an actuarial analysis is needed to provide information about the costs of such modifications and other essential information. Under a 1960 Supreme Court decision in State Teachers' Retirement Board v. E.C. Giessel the Legislature does not have the authority to direct the expenditure of Trust Funds for legislative studies.

Once we have completed the framework for this study, we will need to obtain cost estimates from the consulting actuary and decide if ETF will fund those study elements that we believe will serve the best interest of the Trust Fund and its participants.

ETF 13.10 Request to the Joint Committee on Finance

On August 24, 2011, ETF received notice that requests to the Legislature's Joint Finance Committee (JFC) for supplemental funding under the 13.10 process were due no later than August 30, 2011. As you may be aware in 2011 Wisconsin Act 32 (Biennial Budget), the JFC created an unallocated reserve of \$2.8 million in FY11-12 and \$3.6 million in FY12-13 for ETF which could be requested under the 13.10 process.

Despite this short notice, the department submitted a request for release of some of the supplemental funds in order to address the significant costs being incurred in the implementation of Acts 10, 13 and 32.

ETF requested passive review authority in its last three biennial budgets, but has not been successful in convincing the JFC about the advantages of this approach. I would note that of the last four 13.10 requests made by ETF, the JFC has acted on only two of them. The other two were never considered because the JFC did not meet.

Impact of Employee Contribution Changes to the WRS as Contained in Act 10

One of the provisions of Act 10 that has been controversial is the splitting of the total contribution rate and the requirement that WRS active members pay one-half of the total contribution rate. From ETF's perspective, the critical issue is that the full amount of the required contributions be paid. Who pays which portion is a matter for state and local policy makers to decide.

However, there are impacts that we are just beginning to see as a result of this change. Most immediately, we are seeing that employees are eliminating or reducing coverage under optional benefit plans that we administer such as the health, life, disability and deferred compensation plans. Many employees have a limited amount of discretionary income and they will drop or reduce participation in these optional plans as a greater portion of their income is used for WRS retirement and health insurance costs.

In addition, we are receiving more inquiries from active members asking if they can stop participation in the WRS. Some employers are asking if they can withdraw from participating in the WRS. It is likely that as the financial impact of the new laws become more apparent, the requests to withdraw from the WRS will increase. Current state law and federal law do not allow individual active members to voluntarily rescind participation in a qualified retirement plan. But there is no doubt members experiencing financial difficulties due to pay reductions associated with benefit cost increases will become more vocal in seeking ways to "opt out" of the WRS.

The study on offering an optional defined contribution retirement plan and allowing employees not to make required contributions should provide information showing the financial impact such a change would have on the WRS. Several studies conducted in other states about the feasibility of offering defined contribution plans in the place of existing defined benefit plans have shown that the cost to the state would increase dramatically for many years in the event such a proposal were implemented.



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July 21, 2011

ATTORNEY GENERAL J B VAN HOLLEN
WISCONSIN DEPT OF JUSTICE
P O BOX 7857
MADISON WI 53707-7857

Dear Attorney General Van Hollen:

I write to request an Attorney General's opinion regarding my responsibilities under Section 9115 of 2011 Wisconsin Act 13. That section of Act 13 created a nonstatutory provision regarding the allocation of certain reserves in the Public Employee Trust Fund and reads as follows:

Section 9115. Nonstatutory provisions; Employee Trust Funds.

(1) ALLOCATION OF CERTAIN EXCESS RESERVES IN THE PUBLIC EMPLOYEE TRUST FUND TO REDUCE EMPLOYER HEALTH INSURANCE COSTS DURING 2011. *Notwithstanding any action of the group insurance board under section 40.03 (6) (d) of the statutes, from reserve accounts established under section 20.515 (1) (r) of the statutes for group health insurance and pharmacy benefits for state employees, the secretary of employee trust funds shall allocate an amount equal to \$28,000,000 to reduce employer costs for providing group health insurance for state employees for the period beginning on July 1, 2011, and ending on December 31, 2011.*

The Public Employee Trust Fund is a public trust which is to be managed and administered solely for the purpose of ensuring the fulfillment at the lowest possible cost of the benefit commitments to participants as set forth in Wis. Stat. ch. 40, and may not be used for any other purpose. [Wis. Stat. § 40.01 (2)] It is generally understood that money in the Public Employee Trust Fund from health insurance premiums are not "state funds" and that the Legislature does not have free reign to use the funds as it sees fit. [OAG 1-95] The Department of Employee Trust Funds (ETF), the Employee Trust Funds Board (ETF Board), and the Group Insurance Board (GIB) have a duty as trustees to manage the trust consistent with Wis. Stat. § 40.01(2). *Wisconsin Retired Teachers Ass'n v. Employee Trust Funds Bd*, 207 Wis. 2d 1, 26, 558 N.W.2d 83 (1997).

As noted above, Act 13 requires the ETF Secretary to allocate moneys from the Trust Fund to reduce employer costs for providing health insurance for state employees for the period between July 1 and December 31, 2011. Act 13 did not amend Wis. Stat. ch. 40. Thus, the requirement in Act 13 appears to be a different purpose than that for

which the reserves were established and does not appear to be authorized by Wis. Stat. ch. 40. In the past, the Wisconsin Supreme Court has taken a dim view of the practice of using assets from a trust fund, including the Public Employee Trust Fund, for a purpose for which they were not intended. This is so because the beneficiaries of a trust fund have a protected property interest in the fund. For that reason, an inappropriate use of Trust Fund assets may be considered an unconstitutional taking. See, e.g., *Wisconsin Retired Teachers Ass'n*, 207 Wis. 2d 1, *Professional Police Ass'n v. Lightbourn*, 2001 WI 59, 243 Wis. 2d 512, 627 N.W.2d 807, and *Wisconsin Medical Society, Inc. v. Morgan*, 2010 WI 94, 328 Wis. 2d 469, 787 N.W.2d 22.

Existing law is specific in authorizing the establishment and apportionment of health insurance reserves and pharmacy benefit reserves. The Group Insurance Board (GIB) is authorized to establish reserves. [Wis. Stat. § 40.03 (6) (d)] Excess moneys becoming available to the GIB through the operation of the group insurance plans must be apportioned by the GIB to reduce premium payments in following contract years or to establish reserves to stabilize costs in subsequent years. [Wis. Stat. § 40.03 (6) (e)] If it is determined that the excess became available due to favorable experience of specific groups of employers or specific employee groups, the GIB may apportion the moneys in a manner designated to benefit the specific employers or employee groups only, or to a greater extent than other employers and employee groups. [Wis. Stat. § 40.03 (6) (e)] The ETF Secretary's statutory authority does not include establishing or allocating health insurance reserves or pharmacy reserves. [Wis. Stat. § 40.03 (2)] The GIB has used its authority to establish reserves. Those reserves are held in the Public Employee Trust Fund. The funds in the reserves are derived from premiums paid by employers, employees and retirees who participate in the GIB's self-funded health insurance and pharmacy benefit program.

Each August, the GIB considers whether, based upon the advice of its consulting actuary, to use a certain portion of the reserves to reduce premium costs in the following plan year. The remainder of the reserves is held to cover any unanticipated health or pharmacy benefit costs in those programs.

Generally, state agencies lack standing in court to challenge the constitutionality of statutes created by the Legislature. *Lightbourn*, 243 Wis. 2d 512; *State v. City of Oak Creek*, 2000 WI 9, 232 Wis. 2d 612, 605 N.W.2d 526; *Columbia County v. Bd. of Trustees of Wis. Ret. Fund*, 17 Wis. 2d 310, 116 N.W.2d 142 (1962). However, as fiduciaries of the Public Employee Trust Fund, the ETF Board, GIB and the Department have a duty to seek the advice of counsel when we perceive a conflict between the Public Employee Trust Fund and the provisions of a new act before implementing the act.

Therefore, on behalf of the ETF Board, GIB and the Department, I am seeking your counsel on the following questions:

1. Does Section 9115 of 2011 Wisconsin Act 13, by requiring an allocation of moneys from the Public Employee Trust Fund to reduce employer costs for providing health insurance for state employees, constitute a taking of property in violation of the Wisconsin and U.S. Constitutions?
2. If so, am I obligated to carry out the allocation?
3. If I must carry out the allocation:
 - a. By what date must the allocation be completed?
 - b. In making the allocation, do I have discretion in determining how it is to be made? For example, must all of the \$28 million go to the employer or may I allocate it to all beneficiaries of the reserve fund? May I allocate it directly to the health plan and pharmacy benefit manager as premium or may I allocate it to the state's General Fund?
 - c. In making the allocation, must I first determine that an "excess" exists? For example, because Act 13 did not change the authority of the GIB to manage the reserves under Wis. Stat. § 40.03 (6) (e), it is conceivable that the GIB could, in August, apply any excess reserves that exist to lower premiums for calendar year 2012 before I choose to allocate the reserves under Act 13. If I were to determine that no excess exists in such a case, must I still allocate the \$28 million?
4. Does this nonstatutory provision pertaining to the ETF Secretary effectively amend Wis. Stat. § 40.03 (6) (e), which places the authority to allocate reserves solely with the GIB? Does the legislature have the authority to amend the statutory provisions governing the Trust Fund in this manner?
5. Is this new nonstatutory duty of the ETF Secretary in conflict with the statutory authority of the GIB to allocate reserves? If so, by performing the duty created in Section 9115 of Act 13, would the Secretary be acting in violation of Wis. Stat. § 40.03 (6) (e)?

If you have any questions about this request, or need additional information, please do not hesitate to contact David Nispel, General Counsel of the Department at (608) 264-6936.

Thank you for your attention to this matter.

Sincerely,



David A. Stella
Secretary

cc: Group Insurance Board



STATE OF WISCONSIN
DEPARTMENT OF JUSTICE

J.B. VAN HOLLEN
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August 22, 2011

Mr. David A. Stella
Secretary
Department of Employee Trust Funds
801 W. Badger Rd.
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Madison, WI 53701-7931

Re: Request for advice regarding application of section 9115 of 2011
Wisconsin Act 13

Dear Secretary Stella:

You have requested an opinion regarding whether section 9115 of Wisconsin Act 13, requiring an allocation of monies from the public employee trust fund, would constitute a taking of property in violation of the Wisconsin and U.S. Constitutions. I conclude that, as long as the allocation is made consistently with Wis. Stat. § 40.03(6)(e), it would not.

Section 9115 of 2011 Wisconsin Act 13 provides in relevant part:

[F]rom reserve accounts established under section 20.515(1)(r) of the statutes for group health insurance and pharmacy benefits for state employees, the secretary of employee trust funds shall allocate an amount equal to \$28,000,000 to reduce employer costs for providing group health insurance for state employees for the period beginning on July 1, 2011, and ending on December 31, 2011.

You ask whether the non-statutory provision requires that all \$28 million of the allocation be used to directly offset employer costs on a dollar-for-dollar basis. The statute does not specifically so require and should not be so interpreted.

The Group Insurance Board is authorized to establish and apportion health insurance and pharmacy benefit reserves. Wis. Stat. § 40.03(6)(d). Those reserves consist of health insurance premiums paid by employees, employers, and annuitants and are part of the trust fund. Wisconsin Stat. § 40.03(6)(e) provides the exclusive mechanism for the treatment of such reserves, requiring that they shall be used to "reduce premium payments in following contract years or to establish reserves to stabilize costs in subsequent years." Apportionment may be

Mr. David A. Stella
Secretary
Department of Employee Trust Funds
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made to specific groups of employers or employees based only on favorable experience. Wis. Stat. § 40.03(6)(e).

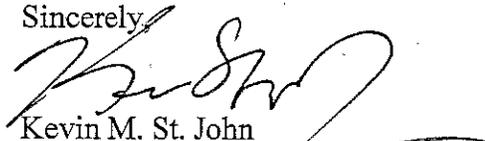
Section 9115 requires the apportionment of \$28 million from the reserve accounts "to reduce employer costs." The question is whether section 9115 requires the entirety of the apportionment to be made in favor of employers. On its face, the statute requires no dollar-for-dollar offset in favor of employers. An apportionment resulting in across-the-board premium reductions, as provided for in Wis. Stat. § 40.03(6)(e), would "reduce employer costs" by decreasing the amount owed by employers toward employee health insurance premiums.

Reading section 9115 as providing reductions that benefit only employers would be inconsistent with Wis. Stat. § 40.03(6)(e), which permits no apportionment limited to a specific group absent a finding of favorable experience. That inconsistency, in turn, would create a potential taking of the accrued rights of Wisconsin Retirement System participants under the Wisconsin and U.S. Constitutions.

Participants in the Wisconsin Retirement System have certain property rights in that fund. Under Wis. Stat. § 40.19, participants are protected from the abrogation of accrued benefits unless the benefits are replaced by benefits of equal or great value. Wis. Stat. § 40.19; *Wis. Prof'l Police Ass'n, Inc. v. Lightbourn*, 2001 WI 59, ¶ 111, 243 Wis. 2d 512, 627 N.W.2d 807. With respect to amounts currently held in the reserve accounts, participants have an accrued right to have those amounts apportioned consistently with Wis. Stat. § 40.03(6)(e): either for across-the-board premium reductions, or held in reserve in order to stabilize costs in future years.

We should construe statutes so as to avoid constitutional infirmities. *Paulhe v. Riley*, 2006 WI App 171, ¶ 23, 295 Wis. 2d 541, 722 N.W.2d 155. Statutes involving the same subject matter must be construed in a manner that harmonizes them. *State v. Schaefer*, 2008 WI 25, ¶ 55, 308 Wis. 2d 279, 746 N.W.2d 457. In light of those canons, I read section 9115 as requiring the Secretary to apportion \$28 million from the reserve accounts consistently with Wis. Stat. § 40.03(6)(e). This result will satisfy the Secretary's obligation under section 9115 to "reduce employer costs" while still protecting the accrued rights of participants in the Wisconsin Retirement System.

Sincerely,



Kevin M. St. John
Deputy Attorney General

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