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March 2, 2012

FOR IMMEDIATE RELEASE

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ETF Announces WRS Annuity Adjustments

Core Annuity Adjustment -7.0%
Variable Annuity Adjustment -7.0%

Madison, (WI) -- Department of Employee Trust Funds (ETF) Secretary Bob Conlin today announced the 2011 Wisconsin Retirement System (WRS) annuity adjustments. The rates were recommended by the Department's independent consulting actuary and approved by the ETF Board chair and Secretary Conlin.

WRS retirees will see reductions in both their Core and Variable annuities beginning May 1. This marks the fourth year in a row ETF has had to reduce Core annuities, primarily due to the effects of the financial market meltdown in 2008. Although WRS assets have experienced three consecutive years of positive returns since 2008, those returns have not been enough to offset 2008's losses. Core Fund gains and losses are recognized, or smoothed, over a five-year period.

Unlike many other retirement systems, the WRS, by law, does not guarantee post-retirement cost of living adjustments. Annual increases are solely dependent on WRS trust fund investment performance. When investment performance results in a shortfall in the annuity reserve, previously-granted increases must be recouped.

"The unique 'shared risk' structure of the WRS requires that the system adjust to compensate for good and bad years," said Conlin. "While taking back a previously-granted increase is not a hoped-for outcome, doing so helps keep the system sustainable."

This year's reduction, when added to previous annuity reductions implemented since the 2008 downturn, means a total of \$3.2 billion will have been recouped from retirees. **The maximum 2011 Core annuity adjustment is -7.0%. However, not all retirees will see a 7.0% reduction.**

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The amount of the reduction for an individual retiree depends on the extent to which the annuity reflects previously-granted Core annuity increases. By law, the effect of a shortfall in the annuity reserve – \$1.68 billion this year – is to be made up by repealing previous Core annuity increases.

As a result, in addition to the recognition of prior investment losses, the size of this year's negative Core annuity adjustment can also be attributed to the decreasing segment of retirees whose Core annuities can be reduced. Many annuities have been reduced to their original, guaranteed amounts (their "floor"), as previously-distributed increases have been taken back. This has left a smaller pool of annuities from which further reductions may be taken. If every WRS retiree would have been eligible for a Core annuity reduction this year, the adjustment for each retiree would have been about -4.0%.

Conlin said the Department's projection for this year's Core Annuity adjustment, which was prepared during 2011 and which projected a 4.0% to 4.5% reduction, was based on a model that focused more on the effect of investment losses and did not fully account for the growing number of retirees who will reach their floor because of annuity reductions in previous years.

Retirees who participate in the optional Variable Fund, in which investment gains and losses are fully recognized each year (not smoothed), will see a -7.0% adjustment in the Variable portion of their annuities. Annuities paid from the Variable Fund can be reduced below their original amounts.

ETF also announced the 2011 effective interest rates for active employees. The Core effective rate is 1.5% and the Variable effective rate is -3.0% (negative). Effective rates are applied to the retirement accounts of the system's 260,000 active employees and eligible inactive members.

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Additional information

- The WRS has approximately 167,000 retirees.
- Approximately 45,656 retirees will not have their Core annuities reduced at all; another 24,690 will have less than a 7.0% reduction because they will reach their “floor”.
- The effective rates and annuity adjustments are based on investment performance earned by the State of Wisconsin Investment Board, in addition to other actuarial factors. SWIB recently announced 2011 investment returns of 1.4% for the Core Fund and -3.0% for the Variable Fund.

Core Fund

- The average annual Core annuity adjustment rates (compounded) are as follows:
 - 10-year: 0.22%
 - 5-year: -1.09%
- Annuity reductions were approved in the previous three years, reducing future payments to WRS retirees by the following amounts:
 - 2010 \$350.1 million
 - 2009 \$416.9 million
 - 2008 \$753.4 million
- The Core Fund is the larger of the two WRS trust funds. It is a balanced fund of diversified holdings in domestic and international stocks, bonds and real estate.
- Core Fund investment returns (decreases as well as increases) are spread out (smoothed) over a period of five years. Thus, this year’s Core annuity adjustment rate calculation included a portion of 2008’s \$21 billion Core Fund **decrease**.
- All WRS retirees receive at least half of their pension in the form of a Core annuity.

Variable Fund

- The average annual Variable annuity adjustment rates (compounded) are as follows:
 - 10-year: -2.11%
 - 5-year: -6.09%

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