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CORRESPONDENCE MEMORANDUM

DATE: June 1, 2015

TO: Deferred Compensation Board

FROM: Bob Willett, Chief Trust Financial Officer
Shelly Schueller, Deferred Compensation Director

SUBJECT: Allocation of Investment Provider Reimbursements and Participant Fees

Staff recommends the Board approve a January 1, 2016 date for revisions to the fee structure and the annual participant administrative fees that help fund the Wisconsin Deferred Compensation Program as proposed.

At the March 12, 2015 Board meeting, the Board discussed a memo (Ref. DC | 3.12.15 | 8) outlining a new investment provider reimbursements policy and likely participant administrative fee changes resulting from the proposed reallocation of investment provider reimbursements. The draft reimbursements policy the Board reviewed in March 2015 (attached) states:

> "When an investment option provides reimbursements, these reimbursements may be allocated back to the participants in the option that generated the revenue when the reimbursement on individual WDC accounts exceeds one cent during a month."

Implementing this policy was tabled until the Board learned more about how application of the policy would change annual participant administrative fees, as it was apparent that reallocating investment provider reimbursements to participants would significantly decrease the reserve in the Board's administrative account.

The Board requested the Department provide the Board with an expanded fee structure proposal using an anticipated reimbursement allocation implementation date of January 1, 2016.

Reviewed and approved by Matt Stohr, Administrator
Division of Retirement Services
Matt Stohr Electronically Signed 6/2/15

Board	Mtg Date	Item #
DC	6.16.15	5A

Participant Fee Analysis

The Board maintains an administrative account to pay the administrative expenses for the Wisconsin Deferred Compensation Program (WDC). These expenses consist primarily of the administrative services contract with Empower Retirement but also include the costs for Employee Trust Funds staff, audits and other plan expenses.

The proposed fees address two policies adopted by the Board: the reallocation of mutual fund reimbursements to participants and the target administrative account balance.

The allocation of mutual fund reimbursements to participants removes almost $2 million a year in funding for administrative costs. This funding will need to be replaced by participant fees. The size of the fee increase is dependent on the target reserve balance adopted by the Board.

At the end of 2014, the administrative account represented approximately 80% of annual administrative expenses. If the current target of 100% of annual expenses is maintained, a fee increase of 81% will be needed. The 100% target balance is projected to be reached in 2018.

Table 1 – Fee Increase 100% Reserve Balance

Participant Account Balance	Number of Participants	Current Monthly Fee	Proposed Fee 100% Reserve Balance		
			Monthly Fee	% Increase	Basis Points
$1 – 5,000	12,046	$0.00	$0.00	0%	0.0
$5,001 – 25,000	14,742	$1.00	$1.00	0%	8.0
$25,001 – 50,000	8,626	$2.00	$2.50	25%	8.0
$50,001 – 100,000	8,474	$4.00	$5.00	25%	8.0
$100,000 – 150,000	4,083	$5.50	$8.50	55%	8.2
$150,001 – 250,000	3,955	$5.50	$13.00	136%	7.8
Over $250,000	3,804	$5.50	$19.00	245%	7.6
Average	55,730	$2.35	$4.25	81%	7.2

If the Board were to adopt an administrative account target of 75% of annual expenses, an average participant fee increase of 65% would be needed. Since the current account balance is very close to the 75% target, the fees would maintain rather than increase the account balance.

Table 2 – Fee Increase 75% Reserve Balance					
Participant Account Balance	Number of Participants	Current Monthly Fee	Proposed Fee 75% Reserve Balance		
			Monthly Fee	% Increase	Basis Points
$1 – 5,000	12,046	$0.00	$0.00	0%	0.0
$5,001 – 25,000	14,742	$1.00	$1.00	0%	8.0
$25,001 – 50,000	8,626	$2.00	$2.50	25%	8.0
$50,001 – 100,000	8,474	$4.00	$5.00	25%	8.0
$100,000 – 150,000	4,083	$5.50	$7.50	36%	7.2
$150,001 – 250,000	3,955	$5.50	$11.00	100%	6.6
Over $250,000	3,804	$5.50	$16.50	200%	6.6
Average	55,730	$2.35	$3.87	65%	6.6

If the Board were to revert to the historical target of 50% of annual expenses, a 56% increase in average participant fees would be needed. The current account balance would be slowly reduced to the 50% target by 2019.

Table 3 – Fee Increase 50% Reserve Balance					
Participant Account Balance	Number of Participants	Current Monthly Fee	Proposed Fee 50% Reserve Balance		
			Monthly Fee	% Increase	Basis Points
$1 – 5,000	12,046	$0.00	$0.00	0%	0.0
$5,001 – 25,000	14,742	$1.00	$1.00	0%	8.0
$25,001 – 50,000	8,626	$2.00	$2.50	25%	8.0
$50,001 – 100,000	8,474	$4.00	$5.00	25%	8.0
$100,000 – 150,000	4,083	$5.50	$7.00	27%	6.7
$150,001 – 250,000	3,955	$5.50	$10.00	82%	6.0
Over $250,000	3,804	$5.50	$15.00	173%	6.0
Average	55,730	$2.35	$3.66	56%	6.2

Pursuant to the Board’s discussion in March, some adjustments have been made to the tier structure in all of these proposed fee schedules, rather than simply increasing each tier proportionately. We have retained the free tier for participant accounts under $5,000. Allowing the smallest accounts to grow without fees provides a good incentive for new participants to join the program. Given the small account balances, the loss in fees for the program is negligible.

The fee for accounts between $5,000 and $25,000 also has not been changed. The $1 per month fee represents approximately 8 basis points, slightly higher than the average plan fee.

Previously, approximately 12,000 accounts in excess of $100,000 were combined in a single tier. We are recommending splitting this group into three tiers to make fees more proportionate to account balances. While fees for these groups will increase substantially, in basis points they are still less than those paid in the lower tiers.
While all of these fee proposals represent a significant increase, the net result is still a very reasonable participant fee. With fees ranging from 6–8 basis points, the plan is operating very economically.

It should also be noted that almost half of the participants will be receiving distributions of the provider reimbursements. In many cases, the savings from provider reimbursements will more than offset the increase in fees resulting in a net lower cost for the participant.

<u>Recommendations</u>
Staff recommends the Board approve:

1) A January 1, 2016 effective date for the Investment Option Selection and Reimbursements Policy.

   Implementing the allocation of investment provider reimbursements to participants as of January 1, 2016 will enable the WDC's administrator to implement any record keeping system changes necessary.

2) Revisions to the fee structure and the participant annual administrative fees that help fund the Wisconsin Deferred Compensation Program.

   A January 1, 2016 start for the new fees will provide time for the WDC to develop materials to communicate the changes to participants. Anticipated communications would include the following:

   Phase 1: Explain Fee Restructuring
   - July-December 2015
   - Explain the new reallocation of reimbursements and how participant administrative fees will be calculated and deducted. The focus will be communicated through the WDC website, newsletter, and an informational hand-out. The WDC's administrator may also develop a short presentation that can be used at on-site presentations.

Phase 2: Implement Reimbursement Reallocation

- January 1, 2016
- Implement the mutual fund reimbursements to the respective participant accounts. Dedicate the majority of the WDC newsletter to explaining the fee reimbursement and where participants can see the amount on their statement.

Staff will be at the Board meeting to discuss the contents of this memo with the Board.