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

801 W Badger Road
PO Box 7931
Madison WI 53707-7931

1-877-533-5020 (toll free)
Fax (608) 267-4549
http://etf.wi.gov

CORRESPONDENCE MEMORANDUM

DATE: September 19, 2008

TO: Employee Trust Funds Board

FROM: David Stella, Secretary

SUBJECT: Secretary's Report

This memo is my first Secretary's Report. As you recall, the board indicated that it would like to see a report from me at each ETF Board meeting to provide pertinent information and commentary about internal and external issues affecting the Department and the benefit plans we administer.

I. Federal and National Issues

Market Value of Liabilities (MVL) - This is an ongoing issue between the American Academy of Actuaries (AAA) and the public pension industry. MVL reflects pension plans' settlement cost or the amount the plan would owe if it were terminated and required to settle its liabilities with a so-called risk-free portfolio of bonds. MVL involves three elements that are not currently part of the conventional method for determining public sector pension liabilities. These elements are: 1) investment return based on a portfolio of high quality bonds; 2) use of the accrued benefit (plan termination) obligation; and 3) marking assets to market, which precludes smoothing of assets.

The AAA's Public Interest Committee held a public hearing on September 4th to take testimony in a public forum to hear views on the disclosure of market value of assets and liabilities for public pension plans. The committee will use information obtained through this forum to determine whether a statement from the Academy's board of directors on the issue is appropriately in the public interest.

Public pension plans oppose the use of this standard for many reasons, including that it would incorrectly state the status of the plan's funding and mislead the public about the actual financial condition of a pension plan. The hearing served as an opportunity for proponents and the opponents to publicly express views regarding MVL. The Committee is expected to study the commentary and make a recommendation to the AAA.

IRS Increased Scrutiny of Governmental Pension Plans - The IRS has stated its intent to significantly increase audits of governmental pension plans. On April 22, 2008 the IRS hosted a meeting with various representatives from the state and local governmental pension plans to communicate its intent. The IRS action plan is to issue multiple surveys to various public pension plans to determine the "status" of the plans and focus on "areas of concern" in their compliance

Board	Mtg Date	Item #
ETF	09/19/08	6

efforts. The IRS shared a survey document with those in attendance. The consensus of the public pension plan community was that the survey was very problematic. The questionnaire reaches far beyond tax-qualification issues and asks open-ended questions dealing with ERISA standards that are inapplicable to public plans and are entirely outside the jurisdiction of the IRS. The proposed questionnaire includes such topics as "Plan Expenses," "Investment of Plan Assets," "Conflicts of Interest," and "Plan Governance" -- all of which Congress explicitly excluded from Federal regulation when it adopted ERISA, deciding instead that State and local government enforcement mechanisms were more effective than the IRC in appropriately addressing such issues with respect to state and local government plans.

Several questionnaire topics, such as "Provisions to Ensure that New Promises are Affordable," deal with issues that are not typically within the control of a plan, but fall more within the realm of the plan sponsor or other governing authority. Even when the questionnaire deals with more appropriate topics, such as "Demographic Information," "Basic Plan Document /Amendment Information," and "Operational Information," the specific questions are often vague, confusing, or more appropriate if asked of a private sector plan.

The public pension plan community enlisted the assistance of Ways and Means Chairman, Congressman Charles Rangel and other Committee members to engage the IRS in a dialogue to arrive a mutually agreeable approach in engaging public pension plans. A meeting will be held with Chairman Rangel, Congressmen Earl Pomeroy of North Dakota, and Sam Johnson of Texas on September 19th to discuss the areas of concern.

II. Internal ETF Issues/Activites

Results of Internal Privacy Study - This Spring, Governor Doyle issued a letter to the Secretaries of state agencies, informing them of the results of a state privacy assessment conducted by Metavante Corporation. The letter contained specific privacy directives to agencies based on the assessment and indicated that the Secretary of the Department of Administration would work with agencies to implement the directives. ETF has not been contacted yet by DOA, but ETF has appointed staff to an in-house workgroup to begin addressing the recommendations in the assessment and in the Governor's letter. The workgroup has found that ETF's policies and practices rate very well. Some of the recommendations and ETF's responses are identified below:

1. Appoint a Privacy Officer for the Department: ETF has had a privacy officer since early 2003.
2. Provide Privacy Training to Department Employees: ETF provides privacy training to each new employee and is in the planning stages to provide work-specific privacy training for the entire Department this year.
3. Develop Standardized Vendor Contract Language & Due Diligence Processes: ETF has HIPAA-compliant contracts with vendors, and has been directly addressing the security of personal information in contracts for several years, with an eye on consistent and stringent contract terms for safeguarding personal information.
4. Conduct Annual Risk Assessments of Privacy Policies and Practices: ETF recently conducted a survey of its privacy practices and policies; the LAB conducts an annual audit of ETF; in 2003, Deloitte conducted a significant privacy risk assessment of ETF; and is currently developing a Department-wide privacy audit that will be conducted internally.

5. <u>Replace Social Security Numbers with Randomly Generated ID Numbers Wherever Possible</u>: ETF is required to collect and use SSN's for tax-related processes, administration of the WRS and certain products related to Medicare D and Medicare Private Fee for service plans of the state health insurance program. The Department has implemented policies to reduce unnecessary use and transmission of full SSN's, and is examining options for eliminating the SSN as the primary identifier for WRS participants.

Mandatory Electronic Direct Deposit – The Department is in the process of developing a policy to require electronic direct deposit of WRS annuity payments. The Social Security Administration and many public retirement systems have adopted mandatory electronic deposit policies. While we are in the developmental stage of the policy, we believe that it will eliminate the risks of lost and stolen checks, postal system delays and delivery failures. Electronic direct deposit will also improve confidentiality of personal information. Even though almost 90% of our annuitants currently use electronic direct deposit, almost 181,000 checks are still produced and mailed annually. The Department estimates a savings of $87,000 per year, not including labor savings, after the mandatory electronic deposit is implemented. As with any policy some flexibility and exceptions will be necessary to address individual circumstances.

Implementation of 2008 Wis Act 226 (Pension Protection Act) – The Department continues work on implementation of Wisconsin Act 226 which provides a tax exemption of up to $3,000 for health insurance premiums paid from annuities of WRS annuitants who are retired public safety officers. An implementation team is developing the necessary policies, procedures, informational and enrollment procedures.

If the Board has questions on other topics or issues that you would like me to cover at a future Board meeting please let me know.