Wisconsin Coalition of Annuitants
21st Annual Conference
May 14, 2012
American Family Headquarters, Madison, Wisconsin

The 21st Annual Conference began with an 8:00 a.m. registration and a continental breakfast. Registered were 139 participants and 10 guests.

The following summary is from the presenters handouts which are available at: www.wicoa.org. Minutes of the presentations were not taken.

The WCOA Chair, Jim Palmer, welcomed the participants and introduced the presenters.

Robert Conlin, Secretary of the Department of Employee Trust Funds

Mr. Conlin introduced newly appointed ETF Deputy Secretary, Rob Marchant.

Mr. Conlin shared several goals for customer service improvements including additional self service tools, availability of staff throughout the state, improving infrastructure to support agency goals, and incorporating best practices in agency activities.

The CEM benchmarking report indicates that ETF administrative cost in FY 2011 was $51 per active member and annuitant. This is $27 below the peer average. The service score was 69/100, which is below the peer median of 77, but a 10 point increase since 2008. Improvement in online services and greater emphasis on active employees will raise the score. A customer satisfaction survey was distributed to the conference participants.

The 2011-2012 Legislative Session requires ETF involvement, specifically Act 10 the budget repair bill and Act 32 the biennium budget. At the end of June a study of the WRS is to be completed by ETF, OSER and DOA.

Annuity adjustments and how they have affected annuitants was illustrated in numerous slides showing the change in value for specific years of retirement. The declining population of annuitants affected by negative annuity adjustments also was illustrated by numerous slides. With the May adjustment retirees from 2007 to present or 47.5% of annuities were not subject to the full negative adjustment and are at their base or floor. Less than half of all annuitants will be subject to any negative adjustment in 2013,.

Projections of a 7.2% investment return in 2012 will result in a maximum annuity adjustment between -12% and -16%. A return between 27% and 31% is needed to avoid a negative annuity adjustment.

Michael Knetter, President and CEO, University of Wisconsin Foundation

Mr. Knetters topic was the Durability of Economic Recovery.

Dr. Knetter began by sharing his 2011 forecasts. He forecast the stock market at 7% when actually it was 5.53%. Real GDP growth was forecasted at 3.5% and actual was 1.6%. Unemployment was forecast, around 9% and the actual was 8.5%. Inflation was forecast low but rising and actual core inflation increased between 1% and 2% with non-core increasing more. Overall economic growth was weak considering the gap in the labor market; concerns about Europe and credit quality seem to keep demand weak.

He shared several slides from the US Department of Commerce, Bureau of Economic Analysis showing the quarterly change in GDP% from 2007 to the present, job loss comparisons of the ‘81-’83 recession and January ‘08 to the present, and the unemployment rates since 1960.

Dr. Knetter’s 2012 forecast, as of January, is the stock market will increase 10%, the real GDP growth will be 3.5%, although this is weak considering there are 5 million fewer jobs than in January 2008, and unemployment at 7.5% at year end with core inflation continuing at a modest increase.

Challenges for Near Term Recovery: 1) Potential supply shocks: unexpected disruptions related to energy commodities or the Euro zone. 2) Policy uncertainty: clarity in tax policy and regulation of health care and finance will help investment climate. 3) Policy sustainability: government entities in US need to restore long-term fiscal balance. Did we replace the private debt problem of 2008 with a public debt problem? Is fiscal policy on an unsustainable path? 4) Politics: will we ever agree on anything again? The golf is getting wider, the views more entrenched. This makes it difficult to solve problems effectively.

Two Issues Driving Politics and Policy: Has the US economy become too reliant on debt to finance growth? If so, what adjustments will be made to restore sustainability? Financial market reform and/or tax increases or spending cuts to restore public fiscal balance. What are the facts, causes, and consequences of increased income equality? Why have the 1% done so well? Will the inequality increase or decrease from here? Do we emulate or envy the 1%? Is their economic power being put to public or personal purpose?

A slide showing a total credit market debt as a percent of GDP was displayed.

Is Our Problem Too Much Debt? Fundamental identity - one person's debt is another's asset. Has anyone ever said our problem is too many assets? The underlying problem in most financial crises is correlated mistakes in valuation of an asset. Examples are the Asian crisis, tech bubble and housing bubble. Overvaluation leads to over consumption, then correction. Housing bubble was the worse with financial institutions having big exposure. Root cause of valuation mistakes - complexity, poor information, lack of transparency and misaligned incentives. Bad contracts cause bad debts. Debt is not inherently bad.

Is Our Problem Private Debt? Are households borrowing and spending too much? Credit card debt. Student loans, 10% owe more than $50,000 and average is over $20,000. Mortgages? Better regulation can reduce these problems by increasing transparency and reducing conflicts of interest. But some people get rich off of the "problems". Most detailed research shows that households approaching retirement are saving enough. Private debt per se is not the problem.

Is Our Problem Public Finance? Current worry: Have we made another mistake in valuing future value entitlements or tax liabilities? If so, we may be over consuming today. Loss of confidence in value of future entitlements can increase saving and reduce consumption today. Assessing sustainability of government borrowing is very complicated. Keeping government finance simple and transparent is important so policy makers can't trade the future for the present. Our inability to agree to some obvious adjustments (e.g. raise retirement age incrementally in future) is troubling. Public Finance may be a real problem.

Facts on Income Inequality: Inequality is rising in many countries. In the US over the last three decades, after-tax incomes of top 1% quadrupled, after-tax income share of top 1% doubled, federal income tax became slightly more progressive. US taxation is relatively light in the middle, top 1% earned 20% of income and paid 40% of US federal income taxes (and other people take credit); top 1% paid 24% in the U.K. At the UW Madison, 83% of total philanthropy comes from 1% of alumni. OECD study, US income tax is as redistributive as Scandinavia. Overall US tax burden is low because of no national sales tax.

Contributors to Income Inequality: Mostly natural causes related to globalization and technology. Likely to self correct through labor supply. Globalization and technology change have increased returns to education and reduced returns to basic labor - manufacturing has been under global competitive pressure. Success of new knowledge economy startups has led to concentration of wealth among funders/owners - at 28 years of age Mark Zuckerberg may be worth nearly $20 billion. Success of young founders seemed to spill into executive compensation, abetted by complexity. Economic segregation is eroding access to good education and equality of opportunity. We must preserve equality of opportunity.

Likely Consequences: Pressure to increase marginal tax rates on high earners and increase transfer payments to equalize outcomes. Possible erosion of incentives for motivated producers. Money is pouring into politics to protect economic interests. That will not produce thoughtful policy. Conclusion, the heightened focus on top 1% is dangerous. We should put sharper focus on bottom 20% that really need help. Irony - the 1% is already doing a great deal to help them

Fundamentals Shaping the Future: Globalization and technology change. Preponderance of wealth creation in new industries, information technology, telecommunications, life-sciences. These new industries are disproportionately reliant on a highly educated workforce. Demographic shifts placing a fiscal burden on governments. Entitlement programs based on stable "dependency ratios" are burdensome with rapid rising rations. Entitlement programs may crowd out traditional public infrastructure investments, absent tough decisions.

Dr. Knetter's Long Term Forecast: US will remain among the most successful developed economies. US economic strength comes from abundant land and capital (human and physical) and economic institutions that have provided strong incentives to take risks and work hard. Low population density means immigration still an option. History of entrepreneurialism enabled US to benefit from globalization and technology change. US challenge - rally around pragmatic leadership focused on reform of public and private finance, healthcare, education; openness to immigration; and rewarding innovation.

Matt Stohr, Administrator, Division of Retirement Services, ETF

Mr. Stohr's presentation was titled WRS Hot Topics. Earlier ETF Secretary Conlin shared the WRS annuity adjustment projections.

The recent law changes from the 2011 Wisconsin Acts 10, 32 and 133 are in the process of being implemented. The laws will have limited impact on WRS annuitants other than some delay in finalized annuity accounts and finalized disability payments. There will be no delays for monthly annuity payments. WRS active members will see delays in annual WRS statement of benefit, the WRS lump sum/separation benefit payments and the 2013 WRS contribution rates.

WRS rehired annuitants has also been a hot topic. The Legislative Audit Bureau is conducting audits of WRS rehired annuitants having sent a survey to all WRS employers. The rehired annuitants bills introduced in the 2011-2012 legislative session did not pass.

ETF service levels, when compared to peers, is a low-cost administrator and continually makes improvements to customer service levels, as measured by CEM which is an independent benchmarking firm. Several of the examples are education and outreach, online tax calculator, sick leave application, and call center changes of expanded hours and additional staff. It is noted that the call center averages 3200 calls per week along with 300 e-mails each week, and nearly 5000 calls per week since the annuity mailer was sent out. Mr. Stohr provided a slide detailing outreach services, and number of participants.

ETF Division of Retirement Services processed over 18,000 retirements in 2011. A normal year is 9000-10,000. The increase call volume and e-mail volume impacted retirement services. In addition there have been an increasing number of rehired annuitant investigations along with implementation of substantial law changes. Despite all of this, the Division of Retirement Services was able to provide core services to annuitants and offer new services to meet customer demand.

Mr. Stohr thank the WCOA for the strong working relationship with ETF and helping to communicate WRS issues when they occur.

Blair Testin Awards

Mr. Testin was instrumental in the establishment of the WRS and also in the WCOA. Because of his involvement it was decided, in 1998, to present an annual award to individuals deemed exceptionally significant in the maintenance and operation of the Wisconsin Retirement System. This year the award is being presented to two individuals that the WCOA has recognized as truly deserving the recognition.

Keith Bozarth will be retiring as the Executive Director of SWIB.

Dave Stella recently retired as Secretary of ETF.

Keith Bozarth, Executive Director, State of Wisconsin Investment Board

Mr. Bozarth began with a 2012, year to date, preliminary earnings with a five and 10 year comparison. The core fund is at 7.5% with the five year at 2.7% and 10 year at 6.9%. The variable is at 11.7% with a five year at 0.4% and the 10 year at 5.2%. Benchmarks have all been exceeded with the exception of the ten-year variable which is down 0.1%.

Mr. Bozarth provided several charts, and explained a portfolio return equation based on total return equaling, cash rate, times risk premium, times active management. He shared a mathematically correct version. Using the portfolio return equation, the WRS actual total return since 1982 is 10.41%. The 20 year return is 8.46% and the 10 year return is 6.75%.

The economic global recovery appears ongoing, but to be considered are; oil price spike, Euro area debt crisis, further US home price decline, the emerging market inflation, China, and US monetary and fiscal policies.

Managing risk and active management variables are: avoid reaching for risk, discretionary rebalancing, opportunistic portfolios, slight increase in private markets, reduce overall volatility, global stock portfolios, and cost management.

The final chart that Mr. Bozarth discussed was the WRS 2010 investment costs. In 2010, SWIB's external management of assets was 85% at a cost of $207.6 million. Internal management of 15% cost $36 million and included agency operations. Agency operations was 11%, or $26.4 million, of the budget; and investment counsel was 4%, or $9.5 million which includes research and data services, consultants, legal counsel, and banking fees. The total year expenses were $243.5 million, with all expenses paid from trust funds.

The WCOA Chair, Jim Palmer, closed by thanking the presenters and the participants.