

**Report 20-16
September 2020**

Retiree Life Insurance Programs

Calendar Year 2019

STATE OF WISCONSIN



Legislative Audit Bureau ■

Retiree Life Insurance Programs

Calendar Year 2019

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OPINIONS PUBLISHED SEPARATELY

The financial statements and our opinions on them are included in the Department of Employee Trust Funds' *State of Wisconsin Retiree Life Insurance Financial Report*.



STATE OF WISCONSIN | Legislative Audit Bureau

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Joe Chrisman
State Auditor

September 30, 2020

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

As required by s. 13.94 (1) (dd), Wis. Stats., and as requested by the Department of Employee Trust Funds (ETF), we have completed an audit of ETF's financial statements of the State Retiree Life Insurance program and the Local Retiree Life Insurance program, as of and for the year ended December 31, 2019. ETF's *State of Wisconsin Retiree Life Insurance Financial Report*, which can be found on its website, includes these statements and our unmodified opinions on them.

As of December 31, 2019, the fiduciary net position, which represents resources available to pay benefits, was \$348.0 million for the State Retiree Life Insurance program and \$256.4 million for the Local Retiree Life Insurance program.

The State Retiree Life Insurance program and the Local Retiree Life Insurance program are each considered an other postemployment benefits (OPEB) plan. OPEB refers to the benefits, other than pensions, that a state or local government employee may receive after they have left employment, generally upon retirement. As of December 31, 2019, ETF calculated a net OPEB liability of \$683.1 million for the State Retiree Life Insurance program and a net OPEB liability of \$425.8 million for the Local Retiree Life Insurance program.

Under accounting standards, each employer participating in an OPEB plan is required to report its proportionate share of the net OPEB liability on its financial statements if prepared on the basis of generally accepted accounting principles. To assist employers with this reporting, ETF prepared employer schedules. We audited and provided unmodified opinions on these schedules for the State employers in report 20-17 and for local employers in report 20-18.

We appreciate the courtesy and cooperation extended to us by ETF staff during the audit. A response from the Secretary of ETF follows the Appendix.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Joe Chrisman".

Joe Chrisman
State Auditor

JC/SH/ss

Introduction ■

The Department of Employee Trust Funds (ETF) administers employee benefit programs for participating state and local government employees. One of these benefit programs is the group life insurance program, which is administered under the provisions of s. 40.70, Wis. Stats. This program offers group life insurance coverage for active employees and retired participants of the State and participating local governments. The group life insurance program consists of three programs, including one for current active employees, the Active Life Insurance program, and two for retired employees, the State Retiree Life Insurance program and Local Retiree Life Insurance program. The State of Wisconsin, including state agencies, such as the University of Wisconsin (UW) System, and state authorities, such as the UW Hospitals and Clinics Authority, as well as 721 local government employers participated in the group life insurance program as of December 31, 2019.

The State Retiree Life Insurance program and the Local Retiree Life Insurance program provide postemployment life insurance coverage to eligible employees of participating employers.

The State Retiree Life Insurance program and the Local Retiree Life Insurance program provide postemployment life insurance coverage to all eligible employees of participating employers. Participation in the Active Life Insurance program is required for participation in the program as a retired participant. To fund the retiree programs, employers pay contribution amounts that are based upon the active employee premium amounts. After retirement, basic coverage is continued for eligible employees for life, with the benefit being reduced by a stated amount based upon the age of the retiree.

Program Administration

The Group Insurance Board oversees certain benefit programs including the group life insurance program.

ETF was created to manage employee benefit programs for participating state and local government employees. Under s. 40.03, Wis. Stats., the 13-member ETF Board is responsible for the overall direction and oversight of ETF. In addition to the ETF Board, the 11-member Group Insurance Board is responsible for setting policies and overseeing administration of certain programs, including the group life insurance program. The 2019 Group Insurance Board members are shown in the Appendix and include:

- the Governor, or designee;
- the Administrator of the Division of Personnel Management in the Department of Administration, or designee;
- the Attorney General, or designee;
- the Secretary of the Department of Administration, or designee;
- the Commissioner of Insurance, or designee;
- a member appointed by the Governor;
- an insured participant in the Wisconsin Retirement System (WRS) who is a teacher and is appointed by the Governor;
- an insured participant in the WRS who is not a teacher and is appointed by the Governor;
- an insured participant in the WRS who is a retired employee and is appointed by the Governor;
- an insured participant who is an employee of a local unit of government and is appointed by the Governor; and
- the chief executive or member of the governing body of a local unit of government that is a participating employer in the WRS and is appointed by the Governor.

ETF contracts with a third-party administrator and an actuary to administer the group life insurance program.

ETF uses a third-party administrator for the group life insurance program. This third-party administrator is responsible for premium collection and benefit payments. The third-party administrator is also responsible for maintaining various reserves for the active and retired participants and investing the assets accumulated. ETF also uses an actuary to perform actuarial calculations for the group life insurance program. The actuary performs calculations to project future benefit payments, determines a liability for costs that have been incurred but not reported, and compares these liabilities against the projected assets that will be available. In addition, the actuary may recommend changes to contribution rates intended to increase or decrease contribution revenues that provide future assets to fund projected liabilities. However, the Group Insurance Board approves contribution rates.

Financial Condition

The financial activity of the State Retiree Life Insurance program and the Local Retiree Life Insurance program is included in a separately issued financial statement report prepared by ETF. ETF is not required by accounting standards to prepare financial statements for the portion of the life insurance program related to active employees because it is administered by a third party and ETF's responsibilities for the program are minimal.

As of December 31, 2019, the fiduciary net position of the State Retiree Life Insurance program and the Local Retiree Life Insurance program was \$348.0 million and \$256.4 million, respectively.

The Net Position Restricted for OPEBs (fiduciary net position) of the State Retiree Life Insurance program and the Local Retiree Life Insurance program represents the value of the plan's assets that are available to meet benefit obligations as they become due. As of December 31, 2019, the State Retiree Life Insurance program had a fiduciary net position of \$348.0 million, which was a 1.2 percent increase from the prior year. The Local Retiree Life Insurance program had a fiduciary net position of \$256.4 million, which was a 4.7 percent increase from the prior year. The increases are primarily attributed to a \$13.1 million transfer from the reserves maintained for state employees in the Active Life Insurance program to the State Retiree Life Insurance program and a \$12.9 million transfer from the reserves maintained for local employees in the Active Life Insurance program to the Local Retiree Life Insurance program. These transfers were authorized by the agreement between ETF and the third-party administrator, and were approved by the Group Insurance Board in August 2019 in order to consolidate the reserve funds, simplify the accounting, and to increase the reserves dedicated to the retiree life insurance programs.

Audit Results

As required by statutes, we have completed an audit of the financial statements and related notes of the State Retiree Life Insurance program and the Local Retiree Life Insurance program as of and for the year ended December 31, 2019. The financial statements were prepared by ETF using generally accepted accounting principles (GAAP) prescribed by the Governmental Accounting Standards Board (GASB). To complete our audit of the financial statements, we reviewed ETF's internal controls over financial reporting, tested financial transactions, and reviewed the financial statements, notes, and required supplementary information that were prepared by ETF management.

We provided unmodified opinions on the financial statements of the State Retiree Life Insurance and the Local Retiree Life Insurance programs administered by ETF for the year ended December 31, 2019.

In addition to providing unmodified opinions on the financial statements and related notes of the State Retiree Life Insurance program and the Local Retiree Life Insurance program as of and for the year ended December 31, 2019, we have issued our Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is required by *Government Auditing Standards* and begins on page 15. We did not identify any control or compliance concerns that are required to be reported under these standards.

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Other Postemployment Benefits (OPEB) ■

OPEB refers to the benefits, other than pensions, that a state or local government employee may receive after they have left employment, generally upon retirement. An OPEB plan can include medical, prescription drug, dental, vision, and other health-related benefits, whether provided separately or through a pension plan, as well as death benefits, life insurance, and long-term care coverage, when provided separately from a pension plan.

The State Retiree Life Insurance program and the Local Retiree Life Insurance program are considered OPEB plans.

OPEB accounting standards establish financial reporting requirements for measuring the OPEB liability for OPEB plans, as well as requirements for both the notes and required supplementary information to the OPEB plan financial statements, and the GAAP-based financial statements for the employers that participate in OPEB plans. The State Retiree Life Insurance program and the Local Retiree Life Insurance program are both considered OPEB plans.

Calculating the Total OPEB Liability

The total OPEB liability is the sum of amounts needed to pay for the OPEB benefits earned by each participant as of the date of the actuarial valuation. A liability exists because the employers participating in the OPEB plan have committed to providing the benefit at some point in the future. The calculation of the total OPEB liability is complex and includes various actuarial assumptions and calculations, such as:

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- a projection of future benefit payments for active and retired participants and their beneficiaries based upon the current terms of the plan;
- a discount of those payments to their present value, which is the amount of funds needed currently to provide the projected payments in the future; and
- an allocation of the present value of benefit payments over past, present, and future periods of employee service.

As of December 31, 2019, the total OPEB liability was \$1.0 billion for the State Retiree Life Insurance program and \$682.2 million for the Local Retiree Life Insurance program.

ETF's actuaries performed actuarial valuations as of January 1, 2019, and adjusted for changes such as interest earned, contributions paid, and benefits paid during 2019 to determine the total OPEB liability for the State Retiree Life Insurance program and for the Local Retiree Life Insurance program as of December 31, 2019. Based on these valuations, the total OPEB liability for the State Retiree Life Insurance program was \$1.0 billion as of December 31, 2019, and the total OPEB liability for the Local Retiree Life Insurance program was \$682.2 million as of December 31, 2019.

The discount rate can have a significant effect on the amount of the total OPEB liability.

The discount rate is a critical factor in calculating the total OPEB liability, and it can have a significant effect on the amount of the total OPEB liability. The discount rate, or interest rate, used to calculate the present value of projected benefit payments is specifically defined under the accounting standards. Because the assets accumulated for the State Retiree Life Insurance program and the Local Retiree Life Insurance program are projected to be insufficient to make all projected future benefit payments of current active and retired eligible employees, ETF was required to use a blended discount rate in calculating the total OPEB liability for each program. The long-term expected rate of return of 4.25 percent was blended with the municipal bond rate of 2.74 percent as of December 31, 2019, using the Bond Buyer GO 20-Bond Municipal Bond Index. The blended discount rate for the State Retiree Life Insurance program was 2.84 percent, and the blended discount rate for the Local Retiree Life Insurance program was 2.87 percent. As a result, the OPEB liability calculated for each program is larger than if the long-term expected rate of return of 4.25 percent was used.

Calculating the Net OPEB Liability

To determine the net OPEB liability or asset, the accounting standards require the total OPEB liability be subtracted from the OPEB plan's fiduciary net position. When the total OPEB liability is greater than the fiduciary net position, the OPEB plan will disclose a net OPEB liability in its notes. When the fiduciary net position is greater than the total OPEB liability, the OPEB plan will disclose a net OPEB asset in its notes.

As of December 31, 2019, the net OPEB liability was \$683.1 million for the State Retiree Life Insurance program and \$425.8 million for the Local Retiree Life Insurance program.

As of December 31, 2019, the State Retiree Life Insurance program and the Local Retiree Life Insurance program each reported a net OPEB liability. The State Retiree Life Insurance program had a fiduciary net position of \$348.0 million and a total OPEB liability of \$1.0 billion, which resulted in a net OPEB liability of \$683.1 million as of December 31, 2019. The Local Retiree Life Insurance program had a fiduciary net position of \$256.4 million and a total OPEB liability of \$682.2 million, which resulted in a net OPEB liability of \$425.8 million as of December 31, 2019. As shown in Table 1, this represents an increase from the net OPEB liability reported as of December 31, 2018, for both programs. This increase can be primarily attributed to a decrease in the discount rate of 1.36 percent and 1.35 percent for the State Retiree Life Insurance program and the Local Retiree Life Insurance program, respectively.

Table 1

Net OPEB Liability for the State Retiree Life Insurance Program and the Local Retiree Life Insurance Program

As of December 31
(in millions)

	State Retiree Life Insurance		Local Retiree Life Insurance	
	2018	2019	2018	2019
Fiduciary Net Position	\$ 344.0	\$ 348.0	\$ 244.9	\$ 256.4
Total OPEB Liability	(775.5)	(1,031.1)	(502.9)	(682.2)
Net OPEB Liability	\$(431.5)	\$(683.1)	\$(258.0)	\$(425.8)

A net OPEB liability indicates that, at that point in time, the projected liability for benefit payments to employees exceeded the assets of the program.

A net OPEB liability indicates that, at that point in time, the projected liability for benefit payments to employees exceeded the assets of the program. Based upon the calculation of the total OPEB liability and the fiduciary net position, the State Retiree Life Insurance program had a funded ratio of 33.8 percent and the Local Retiree Life Insurance program had a funded ratio of 37.6 percent as of December 31, 2019. Because GASB did not create the financial reporting methodology to be used for funding purposes, the existence of a net OPEB liability for the State Retiree Life Insurance program and the Local Retiree Life Insurance program should not be used to support a change in contribution rates for the programs. The Group Insurance Board has an approved funding policy for both the State Retiree Life Insurance program and the Local Retiree Life Insurance program and uses this policy, in addition to future liability calculations provided by the third-party administrator, in establishing contribution rates.

Employer Reporting

Employers have made a commitment to provide postemployment life insurance benefits to employees and have an obligation to make contributions to fund these benefits.

For the State Retiree Life Insurance program and the Local Retiree Life Insurance program, contributions from employers are combined, by program, and the benefits are paid out of the common pool of assets established for each program. By participating in the State Retiree Life Insurance program or the Local Retiree Life Insurance program, each employer has made a commitment to provide postemployment life insurance benefits to employees and is obligated to make contributions into the future to ensure that sufficient resources are available to make the benefit payments. Therefore, because the employer for the State Retiree Life Insurance program and the employers participating in the Local Retiree Life Insurance program have responsibility for the resulting OPEB obligations, each employer will be required to report its share of the net OPEB liability on its GAAP-based financial statements.

Each participating employer must report its share of the net OPEB liability in its GAAP-based financial statements.

The State Retiree Life Insurance program includes state agencies, including UW System, and the various authorities that participate in the program, such as the UW Hospitals and Clinics Authority. To assist the State of Wisconsin and those agencies and authorities that are part of the State's financial reporting entity but that prepare separately issued financial statements, ETF has prepared a Schedule of Employer Allocations and a Schedule of Collective OPEB Amounts as of and for the year ended December 31, 2019. We audited these schedules and provided unmodified opinions on them in report 20-17. The net OPEB liability of \$683.1 million for the State Retiree Life Insurance program will be included in the State's GAAP-based financial statements, which will be published in the

State of Wisconsin's Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2020.

To assist employers participating in the Local Retiree Life Insurance program in determining the employer proportionate share of the net OPEB liability, ETF also prepared a Schedule of Employer Allocations and a Schedule of Collective OPEB Amounts as of and for the year ended December 31, 2019, for the Local Retiree Life Insurance program. We audited these schedules and provided unmodified opinions on them in report 20-18. Each local government that participates in the Local Retiree Life Insurance program must report its proportionate share of the net OPEB liability of \$425.8 million for the Local Retiree Life Insurance program in its GAAP-based financial statements.

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Auditor's Report ■



Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles and
Representative Samantha Kerkman, Co-Chairpersons
Joint Legislative Audit Committee

Members of the Employee Trust Funds Board and
Mr. Robert J. Conlin, Secretary
Department of Employee Trust Funds

We have audited the financial statements and related notes for the State Retiree Life Insurance and Local Retiree Life Insurance programs administered by the State of Wisconsin Department of Employee Trust Funds (ETF) as of and for the year ended December 31, 2019. We have issued our report thereon dated September 28, 2020. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. The financial statements and related auditor's report have been included in ETF's *State of Wisconsin Retiree Life Insurance Financial Report*.

Internal Control over Financial Reporting

Management of ETF is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered ETF's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of ETF's internal control. Accordingly, we do not express an opinion on the effectiveness of ETF's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent misstatements, or to detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of ETF's financial statements will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ETF's financial statements are free from material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering ETF's internal control and compliance. The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of ETF's internal control or on compliance. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

September 28, 2020

Appendix ■

Appendix

**Group Insurance Board Membership
2020**

Name	Affiliation	Board Member Since
Herschel Day, Chair	Appointee of the Governor, insured participant in WRS who is a teacher	2013
Nathan Houdek, Vice Chair	Designee of the Commissioner of Insurance	2019
Nancy Thompson, Secretary	Appointee of the Governor, chief executive or member of the governing body of a local unit of government that participates in the Wisconsin Retirement System (WRS)	2012
Harper Donahue IV	Appointee of the Governor, insured participant in WRS who is an employee of a local unit of government	2019
Malika Evanco	Designee of the Administrator, Division of Personnel Management, Department of Administration	2019
Dan Fields	Appointee of the Governor, insured participant in WRS who is a retiree	2019
Walter Jackson	Appointee of the Governor, insured participant in WRS who is not a teacher	2019
Katy Lounsbury	Designee of the Governor	2020
Brian Pahnke	Designee of the Secretary, Department of Administration	2019
Bob Wimmer	Designee of the Attorney General	2018
Vacant	Appointee of the Governor	

Response ■



STATE OF WISCONSIN
Department of Employee Trust Funds
Robert J. Conlin
SECRETARY

Wisconsin Department
of Employee Trust Funds
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September 28, 2020

JOE CHRISMAN, STATE AUDITOR
LEGISLATIVE AUDIT BUREAU
22 E MIFFLIN ST SUITE 500
MADISON WI 53703

Dear Mr. Chrisman,

Thank you for the opportunity to review and comment on the audit of the State and Local Retiree Life Insurance programs for the year ended December 31, 2019. The group life insurance programs are important benefit programs that provide life insurance coverage to eligible active employees and retirees. We are pleased the results of your tests found no instances of noncompliance or other matters that are required to be reported under the Government Auditing Standards.

As noted in the report, the financial reporting methodology prescribed by the Governmental Accounting Standards Board (GASB) is not intended to be used for funding purposes. The Group Insurance Board (GIB), in consultation with its actuary and ETF staff, monitor the financial condition of the group life insurance programs and set contribution rates in accordance with the GIB funding policy. The GIB recently approved contribution rate increases that will result in a fully funded plan. Accordingly, we believe the programs are in a good financial position.

In closing, we appreciate the efforts of your staff in conducting the audit.

Sincerely,

Robert J. Conlin
Secretary