STATE OF WISCONSIN
Legislative Audit Bureau
NONPARTISAN • INDEPENDENT • ACCURATE

Report 22-15
September 2022

# Retiree Life Insurance Programs

## Calendar Year 2021

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# Retiree Life Insurance Programs

Calendar Year 2021

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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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State Auditor

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September 28, 2022

Senator Robert Cowles, Co-chairperson
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles:

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, and the related notes, of the retiree life insurance programs, which include the State Retiree Life Insurance program and the Local Retiree Life Insurance program, as of and for the year ended December 31, 2021. 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. ETF chose to seperately issue the retiree life insurance programs financial statements and plans to issue its *2021 Annual Comprehensive Financial Report* (ACFR), which will also include the financial statements of the retiree life insurance programs, at a later date.

The fiduciary net position, which represents resources available to pay benefits, for the State Retiree Life Insurance program decreased from $333.8 million as of December 31, 2020, to $319.6 million as of December 31, 2021, or by 4.2 percent. The fiduciary net position for the Local Retiree Life Insurance program decreased from $251.4 million as of December 31, 2020, to $248.2 million as of December 31, 2021, or by 1.3 percent. These decreases are a result of benefits exceeding contributions and investment income for both programs.

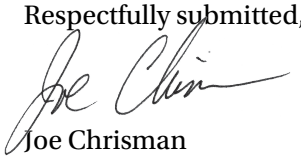
The State Retiree Life Insurance program and the Local Retiree Life Insurance program are each considered an other postemployment benefits (OPEB) plan. OPEB refers to the benefits, other than pensions, that a state or local government employee may receive after they have left employment, generally upon retirement. As of December 31, 2021, ETF calculated a net OPEB liability of $947.8 million for the State Retiree Life Insurance program and a net OPEB liability of $591.0 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 (GAAP). To assist employers with this reporting, ETF prepared employer schedules. We audited and provided unmodified opinions on these schedules for the State Retiree Life Insurance program in report 22-16 and for the Local Retiree Life Insurance program in report 22-17.

The Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which is required by *Government Auditing Standards,* begins on page 13.

We appreciate the courtesy and cooperation extended to us by ETF staff during the audit.

Respectfully submitted,



Joe Chrisman
State Auditor

JC/ES/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: the Active Life Insurance program for current active employees, and the State Retiree Life Insurance program and Local Retiree Life Insurance program for retired employees. 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 724 local government employers participated in the group life insurance program as of December 31, 2021.

***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 the Group Health Insurance, Group Life Insurance, Employee Reimbursement Accounts/Commuter Benefits, and Income Continuation Insurance programs.***

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 the Group Health Insurance, Group Life Insurance, Employee Reimbursement Accounts/Commuter Benefits (ERA/CB), and the Income Continuation Insurance programs. The 2022 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 (DOA), or designee;
- the Attorney General, or designee;
- the Secretary of DOA, 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, 2021, the fiduciary net position of the State Retiree Life Insurance program and the Local Retiree Life Insurance program was $319.6 million and $248.2 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, 2021, the State Retiree Life Insurance program had a fiduciary net position of $319.6 million, which was a 4.2 percent decrease from the prior year. The Local Retiree Life Insurance program had a fiduciary net position of $248.2 million, which was a 1.3 percent decrease from the prior year. These decreases are a result of benefits continuing to exceed contributions and investment income for both 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, 2021. 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.

For 2021 reporting, ETF chose to separately issue the financial statements of the retiree life insurance programs, and plans to issue its *2021 Annual Comprehensive Financial Report* (ACFR), which will also include the financial statements of the retiree life insurance programs, at a later date.

***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, 2021.***

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, 2021, 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 13.

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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 these 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.***

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:

- 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, 2021, the total OPEB liability was $1.3 billion for the State Retiree Life Insurance program and $839.2 million for the Local Retiree Life Insurance program.***

ETF's actuaries performed actuarial valuations as of January 1, 2021, and adjusted for changes such as interest earned, contributions paid, and benefits paid during 2021 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, 2021. Based on these valuations, the total OPEB liability for the State Retiree Life Insurance program was $1.3 billion as of December 31, 2021, and the total OPEB liability for the Local Retiree Life Insurance program was $839.2 million as of December 31, 2021.

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 2.06 percent as of December 31, 2021, using the Bond Buyer GO 20-Bond Municipal Bond Index. The blended discount rate for the State Retiree Life Insurance program was 2.15 percent, and the blended discount rate for the Local Retiree Life Insurance program was 2.17 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.

***The discount rate can have a significant effect on the amount of the total OPEB liability for the retiree life insurance programs.***

Increasing or decreasing the discount rate can have a significant effect on the total OPEB liability. For instance, a one percentage point decrease in the discount rate would increase the total OPEB liability for the State Retiree Life Insurance program to $1.6 billion and the Local Retiree Life Insurance program to $1.0 billion. A one percentage point increase in the discount rate would decrease the total OPEB liability for the State Retiree Life Insurance program to $1.0 billion and the Local Retiree Life Insurance program to $680.6 million.

## 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, 2021, the net OPEB liability was $947.8 million for the State Retiree Life Insurance program and $591.0 million for the Local Retiree Life Insurance program.***

As of December 31, 2021, 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 $319.6 million and a total OPEB liability of $1.3 billion, which resulted in a net OPEB liability of $947.8 million as of December 31, 2021. The Local Retiree Life Insurance program had a fiduciary net position of $248.2 million and a total OPEB liability of $839.2 million, which resulted in a net OPEB liability of $591.0 million as of December 31, 2021. As shown in Table 1, this represents an increase from the net OPEB liability reported as of December 31, 2020, for both programs. This increase can be primarily attributed to a decrease of 0.07 percent in the discount rate for the State Retiree Life Insurance program and 0.08 percent for the Local Retiree Life Insurance program.

Table 1

**Net OPEB Asset (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 | |
|---|---|---|---|---|
| | 2020 | 2021 | 2020 | 2021 |
| Fiduciary Net Position | $ 333.8 | $ 319.6 | $ 251.4 | $ 248.2 |
| Total OPEB Liability | (1,200.7) | (1,267.4) | (801.4) | (839.2) |
| **Net OPEB Asset (Liability)** | **$(867.0)** | **$(947.8)** | **$(550.1)** | **$(591.0)** |

***A net OPEB liability for the retiree life insurance programs 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 25.2 percent and the Local Retiree Life Insurance program had a funded ratio of 29.6 percent as of December 31, 2021. 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. In August 2019, the Group Insurance Board approved contribution rate increases of 5.0 percent annually for nine years, effective April 1, 2020. The Group Insurance Board reviews this increase annually to determine if it remains appropriate.

## Employer Reporting

***Employers have made a commitment to provide postemployment 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 these programs, each employer has made a commitment to provide postemployment 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 each employer has responsibility for the resulting OPEB obligations, each employer will be required to report its share of the net OPEB liability or asset for each program on its GAAP-based financial statements.

Employers participating in the State Retiree Life Insurance program include state agencies, such as 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 prepared a Schedule of Employer Allocations and a Schedule of Collective OPEB Amounts as of and for the year ended December 31, 2021, for the State Retiree Life Insurance program. We audited these schedules and provided unmodified opinions on them in report 22-16. The net OPEB liability 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 ACFR for the year ended June 30, 2022.

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

To assist local employers participating in the Local Retiree Life Insurance program in determining the employer's 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, 2021, for the Local Retiree Life Insurance program. We audited these schedules and provided unmodified opinions on them in report 22-17. Each local government that participates in the Local Retiree Life Insurance program must report its proportionate share of the net OPEB liability in its GAAP-based financial statements.

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# Auditor's Report

Report 22-15

STATE OF WISCONSIN
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# Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles, Co-chairperson
Joint Legislative Audit Committee

Members of the Employee Trust Funds Board and
Mr. A. John Voelker, Secretary
Department of Employee Trust Funds

We have audited the financial statements and the related notes of the State Retiree Life Insurance and Local Retiree Life Insurance programs of the State of Wisconsin, administered by the State of Wisconsin Department of Employee Trust Funds (ETF), as of and for the year ended December 31, 2021. We have issued our report thereon dated September 26, 2022. 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 opinions 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 as a basis for designing 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 the financial statements of the State Retiree Life Insurance and the Local Retiree Life Insurance programs 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 financial statements. 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

September 26, 2022

# Appendix

Appendix

# Group Insurance Board Membership

2022

| Name | Affiliation | Board Member Since |
|---|---|---|
| Herschel Day, Chair | Appointee of the Governor, insured participant in the Wisconsin Retirement System (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 WRS | 2012 |
| Dan Fields | Appointee of the Governor, insured participant in the WRS who is a retiree | 2019 |
| Jennifer Flogel | Administrator, Division of Personnel Management, Department of Administration | 2022 |
| Walter Jackson | Appointee of the Governor, insured participant in the WRS who is not a teacher | 2019 |
| Katy Lounsbury | Designee of the Governor | 2020 |
| Brian Pahnke | Designee of the Secretary, Department of Administration | 2019 |
| Nathan Ugoretz | Appointee of the Governor | 2022 |
| Bob Wimmer | Designee of the Attorney General | 2018 |
| Vacant | Appointee of the Governor, insured participant in the WRS who is an employee of a local unit of government | |