



Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026

Office of the Executive Director

May 16, 2006

The Honorable Edward J. Markey
The Honorable George Miller
United States House of Representatives
Washington, D. C. 20515

Dear Representatives Markey and Miller:

I am responding to your letter of May 2 regarding PBGC's contractual relationships for investment consulting services. PBGC has a keen interest in ensuring that its programs and policies serve the best interests of the pension insurance program's stakeholders: participants in trustee pension plans, workers in ongoing pension plans, premium payers, and the broader public interest.

PBGC is concerned with any activity or behavior that causes pension plans to be less well funded than would otherwise be the case. That is why we have focused so closely these past few years on helping the Administration and Congress craft responsible reforms to the nation's pension laws. We are also committed to ensuring that those who are responsible for administering or advising pension plans comply with the requirements of the Employee Retirement Income Security Act.

Like most private and public pension plans, PBGC employs an investment consultant to help the agency develop the best strategy for achieving its investment goals. In many cases, we follow the consultant's advice or recommendation. In other cases, we do not. With that, I would be pleased to answer your specific questions:

1. What are the contractual terms of the PBGC's contract with Wilshire Associates?

A: Wilshire Associates provides PBGC with investment consulting services, not asset management services (see below in the response to Question #2 for a list of PBGC's existing investment managers). The current contract was effective April 1, 2000 and, as a result of the exercise of options and extensions, expires on July 31, 2006. The contract's fee structure includes an annual fixed fee (\$350,000 – approximately 0.00075 percent of invested assets) and an optional, on-site consultant fee (billed at an hourly rate not to exceed \$142,080 annually).

A new PBGC investment consultant contract is currently being re-competed through full and open competition consistent with Federal Acquisition Regulations. The submission deadline for proposals was March 6, 2006 and technical evaluation of the responses is now underway. The solicitation as publicly posted can be viewed at the Federal Business Opportunities website (www.fedbizopps.gov).

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As specified below, under the contract as currently structured, Wilshire provides ongoing advice and analysis regarding various matters pertaining to PBGC's investment policy and the implementation thereof. Such advice and analysis may include:

- Investment Policy (as set by PBGC's Board)

Providing advice on PBGC's investment program and policies including detailed analysis, recommendations and summary reports on strategies, structures and approaches to enable PBGC to formulate and achieve its investment objectives.

- Asset Allocation

Providing detailed analysis and periodic reports regarding asset allocation strategy. This includes evaluating alternative asset classes, their expected returns, volatility, liquidity, cost and relationship to achieving PBGC's investment objectives.

- Asset/Liability Analysis

Modeling and evaluating how alternative investment strategies might impact PBGC's future financial situation. Also, providing ongoing advice, as well as specific analysis, of PBGC's liability structure and alternative strategies to effectively manage and deal with that risk exposure.

- Investment Structure

Providing detailed analysis and summary reports related to the structure of PBGC's investment managers (i.e., number of investment managers, manager style, active versus passive management), as well as providing similar analyses and reports on an ad hoc and "as required" basis.

- Manager Selection and Evaluation

Maintaining and publishing a database of institutional grade investment managers in various asset classes. Providing access to software that allows PBGC staff to screen investment managers, evaluate historical performance and style adherence, and analyze PBGC investment structure. Providing detailed analyses and summary reports on existing and prospective managers, as needed, and continuously monitoring those managers and updating the database for current performance and events.

- Performance Measurement

Providing a detailed review and analysis of PBGC's investment performance and that of its investment managers following the end of each calendar quarter. This analysis includes appropriate universe comparisons, style indices, custom benchmarks, attribution analysis, market analysis and such other reports as are necessary to evaluate the results of PBGC's investment program.

- Transfer Management

Providing advice, analysis, reports and assistance as needed on the most efficient means of effecting the transfer of assets from newly trustee pension plans and on the reallocation of PBGC's assets. This includes portfolio analysis, liquidation alternatives, transaction monitoring and price verification.

- Cost Containment

Providing advice on investment management fees and security transaction fees including brokerage commissions and market impact costs.

- Procurement

Assisting with the evaluation and selection of investment management services.

- Special Studies and Advice

Providing additional studies and advice, as requested, to assist PBGC in fulfilling its mission. This must include information on master custodians, evaluation of and assistance in negotiating manager and custodian fees, special reports on alternative asset classes and other investment related studies.

2. Does the PBGC currently, or has it in the past, employed consultants other than Wilshire to perform asset management services for the PBGC? If yes, please indicate which consultants, when they provided the services, and which services were provided.

A: Wilshire has not and does not provide asset management services for PBGC. As noted in the response to Question #1, Wilshire Associates provides a variety of investment consulting services to PBGC. PBGC does not have a contractual relationship with any other investment consultant.

PBGC does use external investment managers to manage its assets. Presently, PBGC has contractual relationships with eight investment managers: Ark Asset Management Company, Inc.; Barclays Global Investors; JP Morgan Investment Management; Pacific Investment Management Company; Prudential Investment Management Inc.; State Street Global Advisors; Wellington Management Company; and Western Asset Management Company.

The key difference between an investment consultant and investment manager is that a consultant only offers advice on macro investment program decisions based upon its expertise in capital markets, while the investment manager typically is fully delegated to execute investment decisions regarding the purchase and sale of individual securities consistent with the client's investment guidelines and policies. The client does not interfere with the discretionary decision making authority of the investment manager.

The client can choose to take the advice of the investment consultant or to ignore it, or to alter it to suit its purposes as the client is the discretionary decision maker in its relationship with an investment consultant.

3. Did Wilshire ever disclose to the PBGC that it might have a conflict of interest with any of its other clients?

A: No, Wilshire has not disclosed any such potential conflicts of interest (see below and also in the response to Question #4 for further details).

PBGC has asked on a regular basis and Wilshire has not identified any conflicts of interest with any of its other clients. Specifically, SEC Adviser Act Rules 203-1 and 204-3, promulgated under the Investment Advisers Act of 1940, require investment advisers such as Wilshire to file an annual registration form with the SEC (Form ADV) disclosing conflicts of interest, and also to provide a disclosure statement to its clients that can be a copy of the disclosure section of the form ADV.

Further, as explained next, the procurement process under which PBGC selected Wilshire as its investment consultant has been conducted in accordance with section 9.5 of the Federal Acquisition Regulations, "Organizational and Consultant Conflicts of Interest."

4. Did the PBGC ever ask Wilshire to ascertain if it has any possible conflicts of interest? If yes, when and what was the result of this request? If not, why not?

A: Yes. PBGC goes through a due diligence process with all of its investment program related contractors, including Wilshire Associates. That process begins with a procurement process consistent with the Federal Acquisitions Regulations. PBGC independently evaluates and ultimately selects qualified investment advisors, investment managers and all other investment related contractors. Through this process, PBGC seeks to identify any potential conflicts of interest that may preclude contract award.

Post award of the contract, PBGC has met with Wilshire approximately six times per year and there has been an annual review of the firm's ADV (as noted in the response to Question #3) to identify, among other things, potential conflicts of interest. In response to findings from an SEC examination in 2004, Wilshire expanded its ADV disclosure to provide additional detail regarding its various lines of businesses and corresponding revenue sources. Through its existing due diligence process, PBGC was already aware of the information Wilshire additionally disclosed in response to the SEC examination.

- 5. Has the PBGC requested that Wilshire respond to the questions contained in the SEC-DOL "Tips for Plan Fiduciaries" distributed to pension plans following completion of the SEC's May 2005 staff report ("SEC Report") on pension consultant conflicts of interest? If yes, please provide a copy of Wilshire's responses. If not, why not?**

A: Please find attached below the responses to the SEC-DOL questions that Wilshire prepared for its clients.

- 6. Did the DOL or SEC notify the PBGC of the names of any of the firms with possible conflicts of interest?**

A: See below in responses to Questions #7, #8 and #9.

- 7. Did the PBGC ask the SEC or DOL for any of the names?**

A: The SEC referred the firms to DOL for follow-up investigation. PBGC subsequently provided DOL with a list of its investment consultant and investment managers to determine if any of them were listed as having possible conflicts of interest. DOL has provided that information to PBGC. However, PBGC is unable to provide further information due to confidentiality requirements of ongoing DOL investigations.

- 8. Did any of the firms identified by the SEC as having conflicts of interest provide consulting services to any of the terminated plans now under the control of the PBGC? If yes, how many?**

A: PBGC is aware of one such firm, but is unable to provide further information because of confidentiality requirements imposed as a condition on its access to this nonpublic information.

- 9. If any of the firms identified by the SEC as having conflicts of interest provided consulting services to terminated plans now under PBGC's control, will the PBGC investigate whether conflicts of interest, hidden financial arrangements or unlawful activities occurred in the course of the consultants' work for the terminated plans? If yes, how will this work be conducted, when will it be completed and what will the PBGC do in the event it determines that a terminated plan's consultant had a conflict of interest, hid fees or engaged in unlawful activities while employed by the terminated plan? If PBGC will not investigate, why not?**

A: PBGC conducts audits of plan assets and plan and employee records when it assumes responsibility for terminated pension plans. When it finds evidence of wrongdoing,

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PBGC will pursue appropriate remedies, including bringing actions for breach of fiduciary duty. For example, PBGC has brought numerous actions against defalcating plan fiduciaries in appropriate circumstances. Over the last decade, some 26 actions have been pursued, and there are currently five active lawsuits. These cases involve plan sponsors, officers, directors and trustees. None of these cases has involved pension consultants. PBGC will also make referrals to other agencies as appropriate on matters within their jurisdiction.

In August 2005, PBGC executives met with the SEC to review the implications of the pension-consultant report for its trusteeship activities. There is not necessarily a connection between the failure to disclose conflicts of interest as found by the SEC, and resulting harm to a pension plan. Making that determination requires substantial work. First, in order to pursue actions against consulting firms identified in the SEC Report as having conflicts of interest, PBGC must match them with the lists of service providers and advisors identified in the records of terminated plans now under PBGC trusteeship. To illustrate the potential scope of this matter, PBGC has trusteeed 469 plans during the last three fiscal years alone (specifically, 152 plans were trusteeed in FY 2003, 178 plans in FY 2004, and 138 plans in FY 2005). In addition, large plans, particularly, are likely to have used multiple consultants that may have changed over time. Then, PBGC would need to evaluate plan records to ascertain whether there is a reasonable basis to conclude that the SEC-identified firm was in a position to direct or control the purchase of any specific plan assets, as well as whether the firm could control or direct the selection or compensation of any other service provider. Finally, PBGC would need to establish a causal connection between the conflict and losses sustained by the plan. PBGC is reviewing these issues to determine what follow-up actions would be appropriate.

10. In light of the subpoena issued to Wilshire, what action is and will DOL take to ensure that Wilshire has no conflicts of interest that affect its ability to protect the interests of the PBGC and participants and beneficiaries of terminated plans?

A: This question should be directed to DOL.

Please let me know if PBGC can provide further assistance on this or related matters. You may reach me at (202) 326-4010 for further information or to set up a meeting.

Sincerely,



Bradley D. Belt

Attachment (see below)



Wilshire Consulting Responses to Suggested SEC Questions

1. Are you registered with the SEC or a state securities regulator as an investment adviser? If so, have you provided me with all the disclosures required under those laws (including Part II of Form ADV)?

Yes. Wilshire Associates has been registered as an investment advisor with the SEC under the Investment Advisers Act of 1940 since July 1972. We registered at that time even though we had not yet established a consulting practice. We understand that Wilshire Associates was among the first group of firms not offering personalized investment advisory services to register.

It is the policy of Wilshire Associates to provide at the times required all disclosures required under the Investment Advisers Act of 1940, including Part II of Form ADV.

2. Do you or a related company have relationships with money managers that you recommend, consider for recommendation, or otherwise mention to the plan for our consideration? If so, describe those relationships?

In 2004, Wilshire Associates received over 40% of its total revenues from the sale of analytics services that are provided by Wilshire Analytics. A significant amount of this business is with portfolio managers, including most, if not all, of the largest organizations in the investment industry. In addition, Wilshire Associates did business for over thirty years as a broker-dealer. Wilshire Associates ended its brokerage business on October 29, 2004. Until then, Wilshire Associates received revenues from securities execution and clearance services that we provided to numerous portfolio managers. Numerous organizations that purchase or have purchased Wilshire Analytics solutions and services and/or formerly used Wilshire's former brokerage services are past, current and prospective portfolio managers of clients of Wilshire Consulting

While this presents a conflict of interest, it is the policy of Wilshire Associates that recommendations of portfolio managers be based solely on the best interests of our clients. Furthermore, consultants in Wilshire Consulting do not have internal access to the identity of Wilshire Analytics clients or how much those clients pay for Analytics solutions and services. Finally, Wilshire Associates is adopting procedures to provide Wilshire Consulting clients directly with information about revenues that we receive from managers and other financial services vendors (*See Response to Question # 3 below*).

Investment advisors sometimes arrange to obtain research services from an investment research firm by having a broker-dealer contract to pay for those services on behalf of the advisor (a "Third Party Agreement"). In October 2004, Wilshire Associates sold certain assets of its former brokerage business to BNY Brokerage. As part of that sale, Wilshire

Associates agreed to refer its Wilshire Analytics clients to BNY Brokerage as the preferred provider for the provision of Third Party Agreements and to encourage those of its Wilshire Analytics clients who wish to pay for their Analytics solutions and services through Third Party Agreements to use BNY Brokerage for those purposes. Wilshire Associates also agreed that in the event that a Wilshire Analytics client informs Wilshire Associates that it desires to use soft dollars to pay for Wilshire Analytics solutions and services, but that it is unwilling to use BNY Brokerage for that purpose, Wilshire Associates will encourage that client to use a broker-dealer that is accessed through Westminster Research Associates, Inc. ("WRA"), an affiliate of BNY Brokerage. These broker-dealers are listed in Part II of Wilshire Associate's Form ADV. Wilshire Associates has an incentive for referring Wilshire Analytics clients to BNY Brokerage and WRA broker-dealers for third party agreements because Wilshire Associates may be entitled to contingent payments from BNY Brokerage following the first and second anniversaries of the sale to BNY Brokerage if specific dollar amount levels are reached of Third Party Agreements among Wilshire Associates, Wilshire Analytics clients, and BNY Brokerage and/or WRA brokers. Wilshire Associates' potential revenue, if either or both of these contingent payments is/are realized, could adversely affect Wilshire Associate's objectivity. As of October 2006, these financial incentives cease.

3. **Do you or a related company receive any payments from money managers you recommend, consider for recommendation, or otherwise mention to the plan for our consideration? If so, what is the extent of these payments in relation to your other income (revenue)?**

Yes. As discussed in response to Question # 2 above, Wilshire Associates receives a significant amount of its total revenues (over 40% in 2004) from the sale of analytics solutions and services that are provided by Wilshire Analytics.

To ensure that Wilshire Associates' consulting clients receive timely disclosure about conflicts of interest in the form of compensation received by Wilshire Associates for Wilshire Analytics solutions and services to the clients' investment managers and other financial services vendors, we adopted procedures for sending a "conflicts check report". This report provides information about the amount Wilshire Associates bills and has billed for Wilshire Analytics solutions and services during the current calendar year and the most recently completed calendar year (to the extent that the managers and other vendors have consented to such disclosure). The report includes information about Third Party Agreements that the managers and other vendors have entered into with Wilshire Associates and either BNY Brokerage or broker-dealers accessed through WRA. The conflict checks report will be sent directly to the client and will not be given to anyone within Wilshire Consulting.

4. **Do you have any policies or procedures to address conflicts of interest or to prevent these payments or relationships from being considered when you provide advice to your clients?**

Yes. It is the policy of Wilshire Associates that all recommendations concerning portfolio managers made to investment consulting clients be based solely on the best interests of the client and without regard to any revenue that Wilshire Associates receives, might receive, or has received in the past, directly or indirectly, from portfolio

managers for services provide by us. Accordingly, Wilshire Associates operates Wilshire Consulting and Wilshire Analytics as separate divisions. Each division has its own leadership team and professional and support staff. Moreover, we have adopted policies and procedures that are designed to prevent consultants from having internal access to information that otherwise might appear to compromise their objectivity. For example, Wilshire Associates' computer systems do not allow employees who work for Wilshire Consulting to have access to the information of Wilshire Analytics or the Accounting department.

It is also the policy of Wilshire Associates that all material facts concerning any conflicts of interest that do arise are disclosed to our clients. In addition to the conflicts of interest identified in Part II of Form ADV, Wilshire Associates is implementing a program for providing a "conflicts check report" to clients (*See* Response to Question # 3 above).

Wilshire Associates requires all of its employees to comply with its *Compliance Manual, Standards of Business Conduct and Code of Ethics*, and any business unit's *Code of Ethics*. All employees are required to be familiar with all procedures and policies that are applicable to them and are subject to discipline for violations.

Wilshire Associates has appointed a Chief Compliance Officer who administers our compliance policies and procedures. The Chief Compliance Officer reports directly to Wilshire Associates' board of directors.

5. **If you allow plans to pay your consulting fees using the plan's brokerage commissions, do you monitor the amount of commissions paid and alert plans when consulting fees have been paid in full? If not, how can a plan make sure it does not over-pay its consulting fees?**

Wilshire Associates does not offer brokerage services so plans cannot pay our fees using this mechanism.

6. **If you allow plans to pay your consulting fees using the plan's brokerage commissions, what steps do you take to ensure that the plan receives best execution for its securities trades?**

No, Wilshire Associates does not offer brokerage services.

7. **Do you have any arrangements with broker-dealers under which you or a related company will benefit if money managers place trades for their clients with such broker-dealers?**

Investment advisors sometimes arrange to obtain research services from an investment research firm by having a broker-dealer contract to pay for those services on behalf of the advisor (a "Third Party Agreement"). In October 2004, Wilshire Associates sold certain assets of its former brokerage business to BNY Brokerage. As part of that sale, Wilshire Associates agreed to refer its Wilshire Analytics clients to BNY Brokerage as the preferred provider for the provision of Third Party Agreements and to encourage those of

its Wilshire Analytics clients who wish to pay for their Analytics solutions and services through Third Party Agreements to use BNY Brokerage for those purposes. Wilshire Associates also agreed that in the event that a Wilshire Analytics client informs Wilshire Associates that it desires to use soft dollars to pay for Wilshire Analytics solutions and services but that it is unwilling to use BNY Brokerage for that purpose, Wilshire Associates will encourage that client to use a broker-dealer that is accessed through Westminster Research Associates, Inc. ("WRA"), an affiliate of BNY Brokerage. These broker-dealers are listed in Part II of Wilshire Associate's Form ADV. Wilshire Associates has an incentive for referring its Analytics clients to BNY Brokerage and WRA broker-dealers for third party agreements because Wilshire Associates may be entitled to contingent payments from BNY Brokerage following the first and second anniversaries of the sale to BNY Brokerage if specific dollar amount levels are reached of third party agreements among Wilshire Associates, Wilshire Analytics clients, and BNY Brokerage and/or WRA Brokers. Wilshire Associates' potential revenue, if either or both of these contingent payments is/are realized, could adversely affect Wilshire Associate's objectivity. As of October 2006, these financial incentives cease.

8. **If you are hired, will you acknowledge in writing that you have a fiduciary obligation as an investment adviser to the plan while providing the consulting services we are seeking?**

Yes. We have always thought of ourselves as fiduciaries to our investment consulting clients and will happy to sign a document indicating that we have a fiduciary obligation to the plan.

9. **Do you consider yourself a fiduciary under ERISA with respect to the recommendations you provide the plan?**

Yes. We have always thought of ourselves as fiduciaries to our investment consulting clients and have acted accordingly.

10. **What percentage of your plan clients utilize money managers, investment funds, brokerage services or other service providers from whom you receive fees?**

Wilshire Analytics is in the midst of preparing a report on this topic but cannot currently provide that information. Wilshire Consulting staff members do not have internal access to the identity of the managers that are clients of the Analytics Division.