

To: Andrew Klein, Speaker, Texas A&M University Faculty Senate
From: Gregory Heim, Faculty Senate SEBAC Representative
Date: February 28, 2020
RE: Retirement Plan Discussion with System Benefits Administration Directors

On January 15, 2020, I met with Ellen Gerescher (Director, TAMU System Benefits Administration) and Sheri Meyer (Assistant Director, TAMU System Benefits Administration) for an hour-long meeting to discuss details regarding our overall retirement program, retirement plan vendors, and individual retirement contribution benefits. Ms. Meyer is the specialist in the benefits office who focuses on retirement issues. This memo summarizes my findings regarding our present retirement savings programs as well as approximate answers to the questions I posed regarding TAMU retirement plans.

Retirement Plan Overview

For readers unfamiliar with the breadth of retirement plans available to Texas A&M University employees, a brief overview follows:

- **Mandatory Retirement Plans:**
 - Each full-time Staff employee must participate in the **Teacher's Retirement System (TRS)** defined benefit plan. In return for an employee contributing a portion of salary (presently 7.7% in 2020), the State of Texas contributes 7.5% of that salary amount to the employee's TRS fund. Retirement benefits are based on TRS's contractual obligations, and are roughly calculated as:
 - $\text{TRS Standard Annuity} = (\text{Years of Service Credit in TRS}) \times (2.3) \times (\text{Average of Five Highest Years of Salary})$
 - TAMU faculty members have the option to choose TRS, or within the first 90 days of employment at TAMU, may elect instead to participate in the **Optional Retirement Program (ORP)**. The ORP defined contribution plan is a 403(b)(1) or 403(b)(7) employee-managed retirement account, which may consist of a mix of annuity investments and/or mutual fund investments. In return for an employee contributing a portion of salary (presently 6.65%), the State of Texas contributes 6.6% of the salary amount to the employee's ORP account. Depending on the retirement plan vendor, employees may choose to use a Traditional (pre-tax) and/or Roth (post-tax) contribution approach. The employee's retirement balance depends on how the employee invests those contributions.
- **Voluntary Retirement Plans:**
 - The **Tax-Deferred Account (TDA) Program** is a 403(b) account in which TAMU employees may choose to contribute up to \$19,500 per year (up to \$26,000 for employees over 50 years old) in 2020. The vendors for these accounts offer a selection of annuities and mutual funds. Employees may choose to use a Traditional (pre-tax) and/or Roth (post-tax) contribution approach. The employee's account balance depends on how the employee invests those contributions.
 - The Employees Retirement System (ERS) of Texas **TexaSaver 457(b) Deferred Compensation Plan (DCP)** is a 457(b) account in which TAMU

employees may choose to contribute up to \$19,500 per year (up to \$26,000 for employees over 50 years old) in 2020. During (or after) the three years prior to reaching *normal retirement age* for TAMUS, an employee can use a “catch-up provision” to contribute up to three times the annual contribution amount (e.g., for 2020, approximately $3 \times \$19,500 = \$58,500$). Employees may choose from a selection of mutual funds and may choose to use a Traditional (pre-tax) and/or Roth (post-tax) contribution approach.

Details about the above plans can be found at: <https://employees.tamu.edu/benefits/retirement/>

Each TAMU faculty member must contribute retirement funds to (i) TRS or ORP, and voluntarily may contribute to (ii) TDA and/or (iii) the Texa\$aver 457(b) plan.

Each TAMU staff member must contribute to (i) TRS, and may voluntarily choose to contribute to (ii) TDA and/or (iii) the Texa\$aver 457(b) plan.

Any TAMU employee (including graduate and undergraduate student workers) may voluntarily contribute to (i) TDA and/or (ii) the Texa\$aver 457(b) plan.

In total, the 2020 contribution limit is \$56,000 for TRS/ORP + TDA (\$62,000 for age 50 and over). Together with Texa\$aver, the overall annual retirement contribution limit is approximately $\$56,000 + \$19,500 = \$75,500$ (or $\$56,000 + \$26,000 = \$82,000$ for age 50 and over). During the three year catch-up provision period for the Texa\$aver plan, the total contribution limit is approximately $\$56,000 + (3 \times \$19,500) = \$114,500$.

Motivation Behind the Meeting

The System Employees Benefits Advisory Committee (SEBAC) has not been reporting about the performance of TAMU or TAMUS sister school employees with respect to the financial wellness of the employees’ retirement planning. Thus, I started examining the structure and offerings of the retirement plans available to TAMU employees. In particular, I focused on the mutual fund offerings of the six active plan vendors (prior to this meeting, I was not aware there are also several “grandfathered” retirement plan vendors).

In particular, I examined the relative number of low-cost passively managed index mutual fund offerings (annual expenses for these funds is typically below 0.20%) versus high-cost actively managed mutual fund offerings (annual expenses for these funds typically ranges between 0.50% and 2.00%).

The data I collected for each retirement plan vendor are presented in Table 1, which shows that certain vendors primarily offer high-cost (i.e., high expense) funds to TAMU employees, presumably to cover their plan administration costs and to make a profit.

Table 1. TAMU retirement plans: low-cost mutual fund vs. high-cost mutual fund offerings

| Vendor Name | Number of Low-Cost Index Mutual Funds Available | Number of High-Cost Mutual Funds Available |
|-------------------------|--|---|
| Fidelity | 26 | 270 |
| Pentegra (a) | 19 | 1000s |
| TIAA | 10 | 61 |
| Voya | 5 | 102 |
| Lincoln Financial Group | 2 | 27 |
| Valic | 1 | 63 |
| | | |
| ERS Texa\$aver 457(b) | 16 | 6 |

Sources: Retirement plan information collected from each vendor’s website. The count of index funds is determined by the name of the fund having the word “Index” and/or the Net Fund Expense being below 0.20% annually. (a) The Pentegra plan is set up as a holding account, where the account owner can pay a 0.30% (below \$500,000 in account value) or 0.20% (above \$500,000 in account value) annual expense to Pentegra to gain access to essentially a very large assortment of mutual funds. Any mutual fund expense would thus be in addition to the 0.30% or 0.20% account management expense.

TAMUS Benefits Office Must Administer Legislative Priorities

Texas A&M University System benefits office administrators report that the TAMUS benefits office must administer the Teachers Retirement System (TRS) and Optional Retirement Program (ORP) retirement programs (as well as the voluntary programs) in a manner as determined by the Texas state Legislature. A primer for legislators about how Texas state employee retirement programs work can be found at: https://www.lbb.state.tx.us/Documents/Publications/Primer/4603_Benefits_Primer_July2018.pdf

In particular, benefits administrators perceive certain constraints upon their actions:

- They cannot favor one retirement plan vendor vs. another plan vendor.
- They cannot make suggestions regarding one vendors’ offerings vs. another’s offerings.
- They cannot give advice to employees that would put the TAMUS in a position of playing a fiduciary role, for legal reasons.

Moreover, they perceive a lack of clarity about what the benefits staff of TAMU is trying to carry out to guide employees toward the various plans and mutual fund or annuity options available to them (i.e., TRS or ORP, TDA, and 457(b) Texa\$aver).

Further, historically the ERS 457(b) Texa\$aver program has not been proactive with telling Texas employees that they are qualified to participate in that program. As such, employees have sometimes expressed confusion regarding participation in the 457(b) program.

Q: Will the federal SECURE ACT passage change anything about our retirement programs?

A: No, any changes will depend on legislator action, outside of basic requirements like the change in contribution age and age for mandatory withdrawals from 70.5 years to 72 years.

What is the Overall Situation with TAMU Retirement Benefits?

Benefits administrators have secure access to comparative statistics (i.e., TAMU vs. other universities) on the backends of each retirement plan vendor’s website. In comparison to other top universities, the opinion of Ms. Meyer is that our employees in the ORP plan are doing quite well.

However, this is not the situation for the optional TDA program or for the optional ERS TexaSaver 457(b) program. Overall, we have a low employee participation rate for the TDA program and a very low employee participation rate for the 457(b) program.

Table 2 below calculates approximate participation rates for TAMU/TAMUS employees who might choose to participate in these two programs (please note that these statistics are approximate, as the total number of employees changes dynamically). The calculations are based on FY2019 assumptions of 18,354 employees who are required to, or have chosen to, participate in the TRS program, and the 5,126 employees who elected to participate in the ORP program. The total number of these full-time benefits eligible employees is 23,480 employees.

With respect to the optional retirement contribution programs, there are approximately 45,000 employees (i.e., administrators, faculty, staff who must participate in TRS, graduate students, and undergraduate students) who, as employees of the state of Texas, qualify to contribute funds either to the TDA program and/or to the ERS 457(b) TexaSaver program.

Table 2. Program participation in TDA and 457(b) retirement contribution programs

| | Of full time employees who must participate in TRS/ORP ... | Percent Participation | Of the voluntary eligible employees ... | Percent Participation |
|---------------|---|------------------------------|--|------------------------------|
| TDA | 4,383/23,480 = | 18.7% | 4,383/45,000 = | 9.7% |
| 457(b) | 684/23,480 = | 2.9% | 684/45,000 = | 1.5% |

During our conversation, I asked whether there might be a role for the Faculty Senate in improving knowledge about retirement options and improving employee participation. Since the TAMUS Benefits office cannot provide fiduciary advice, it might be useful if the Faculty Senate could figure out ways to:

- Encourage faculty and staff to participate in the TDA and 457(b) programs.
- Educate TAMU employees about the differences between the types of mutual funds and other offerings.
- Educate TAMU employees about the fees and expenses for different types of mutual funds and annuities (e.g., commissions and 12b-1 fees).
- Communicate to departments and schools that retirement vendors are allowed to provide educational presentations that can help employees to understand the

offerings at TAMU. Note that vendors cannot provide presentations specific to their own investment instrument offerings.

- Help departments to request to have educational events about retirement programs and plans.
- Sponsor financial education speakers to help employees better understand their own retirement plans.

Competitive Positioning of TAMU Via Retirement Programs

I was interested to find out whether TAMUS has been managing the retirement programs in a manner to demonstrate to faculty and staff recruits that we offer the demonstrably best retirement program as compared to peer institutions. Personally, I have found that some competitor schools offer better retirement programs – I observed this through helping PhD students evaluate job offers for those institutions.

Q: Have you compared the structure of our retirement program offerings against our peer and aspirant schools?

A: No, not yet.

Employee Satisfaction with Retirement Plan Offerings

Approximately five years ago, the TAMUS Benefits office performed a survey regarding general employee satisfaction with retirement offerings. I was interested in whether this is an annual survey, or whether it had been updated.

Q: When was the last time a satisfaction survey was done for each individual retirement vendor plan?

A: Not recently. Previous surveys have suggested most people say they are highly satisfied with their existing plans.

Breadth of Retirement Plan Offerings

The specific issue that interested me in evaluating the retirement programs for the Faculty Senate concerned the lack of low-cost index funds in several of the retirement vendors' offerings. Three of the available funds offer only one or a handful of low-cost index funds while offering mainly high-cost actively managed mutual funds or annuities. Research generally shows that high-cost funds generally offer no guarantee of outperforming the index funds. Indeed, much research shows that high-cost funds generally will provide worse performance over the long term than low-cost index funds.

Based on our conversation, it turns out that, prior to 2008, TAMUS apparently had 70+ vendors qualified to provide retirement program services. After a regulatory/policy change in 2008, the number of vendors was reduced to 7 vendors plus a limited number of grandfathered vendors.

Overall, benefits administrators suggest that it is fairly easy to add more funds to a vendor's list of offerings, if employees want certain mutual funds available. However, it is difficult to get rid of the higher fee mutual funds in vendors' programs, as long as some of our TAMUS employees are still invested in those high cost funds.

Q: How frequently does TAMUS evaluate the mutual fund offerings of each retirement plan vendor?

A: Annually. TAMUS tries to convince the vendors to consider newer, lower cost funds. It is generally easy to get vendors to agree to add another fund to the offerings.

Q: Why can I buy a low-cost mutual fund directly from Fidelity now, and these funds have a 0% annual expense, yet these same funds are not available to me via the TAMUS TDA/ORP accounts?

A: The vendors are covering their costs.

Q: Why do so many of the vendors offer almost no low-cost index fund options? (Examples: Lincoln Financial Group, Voya, Valic)

A: With these vendors, the fees they charge are covering the vendors' costs of administering these plans. The vendors annually tabulate the costs of operating the programs. If the fee revenues do not cover the vendors' costs of operating the retirement programs, they will approach the System Benefits administrators with requests to make changes to cover their costs fully.

Q: Have you asked Pentegra to reduce their 0.3%/0.2% custodial account fee?

A: No. It is difficult to exert such pressure. This vendor is best to use if you have a huge amount of money to transfer from another vendor, or from a previous employer, and you want access to their very broad list of mutual funds, including many low-cost index funds.

Q: Why does TAMUS need to retain six TDA/ORP vendors?

A: TAMUS is required by the Legislature to offer at least four vendors to employees. We are required to make available financial advisors for employees. The financial advisors are legally allowed to charge up to a 2% annual fee (200 basis points) for the service of managing the employee's assets under their management.

Q: Is it possible that consolidating the number of vendors can save some costs?

A: This is limited by the Legislature, since we must offer at least four different retirement program vendors.

Q: The ERS Texa\$aver 457(b) annual account management fees were recently reduced to approximately 0.15% annually. Will these 457(b) fees continue to decrease?

A: We have no information about Texa\$aver. It is a mystery as to why and when fees change for the 457(b) program.