

BALTIMORE COUNTY PUBLIC SCHOOLS

DATE: September 23, 2008

TO: **BOARD OF EDUCATION**

FROM: Dr. Joe A. Hairston, Superintendent

SUBJECT: **REPORT ON 403(B) PROGRAM**

ORIGINATOR: J. Robert Haines, Deputy Superintendent

RESOURCE PERSON(S): Barbara Burnopp, Chief Financial Officer
Donald Peccia, Assistant Superintendent, Human Resources
Dan Capozzi, Manager, Office of Staff Relations

INFORMATION

That the Board of Education receive a report from Michael Beckzowski from Bolton Partners Investment Consulting Group, Inc., on the 403(b) voluntary elective program. The Board will need a vendor(s) in place for January 1, 2009. A contract proposal will be forwarded to the Board as soon as October 2008.

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Attachment I – Voluntary Elective 403(b) Program Vendor Selection

Board of Education of Baltimore County

Work Session

September 23, 2008

Voluntary Elective 403(b) Program Vendor Selection

Voluntary Elective 403(b) Program

- Commonly referred to as “tax-sheltered annuity” or “403(b) plan”
 - Investment vehicles are limited to annuity contracts and mutual funds
 - Allows employees to defer (save) money for retirement on a pre-tax basis
- Currently, employees can choose from among 10 different 403(b) vendors
- No “employer” (BCPS) contributions

Regulatory Background

- Changing the historical perspective of 403(b) programs to an employer plan:
 - Requires BCPS plan document
 - BCPS has increased responsibility for contribution limits, distributions, withdrawals, and transfers
 - 403(b) plan moving closer to traditional 401(k) plan in terms of employer responsibility
 - Need method to ensure compliance with new regulations

Current BCPS 403(b) Program

- There are 10 current vendors
- Annual cash flow of \$29 million
- Assets are approximately \$478.6 million
- Plan plagued by too many vendors/ investment choices
- Inability to effectively communicate program
- Insurance fees of 3 largest providers cost participants at least \$2.3 million annually

Elective 403(b) Contributions as of April 2008

- Total 403(b) contributions from BCPS participants = **\$ 478,606,861**
- Total 403(b) annual cash flow from BCPS voluntary participants = **\$ 28,755,119**

Elective 403(b) Participation as of August 8, 2008

Union	Number of Participants	Percentage of All Participants	Percentage of Union Members Participating
AFSCME	275	5.0%	11.2%
BACE	523	9.5%	26.6%
CASE	521	9.4%	58.1%
SEIU	67	1.2%	55.8%
TABCO	4,084	73.8%	46.6%
Non-represented	61	1.1%	8.3%
TOTAL	5,531	100%	

Growth Fund of America

(Same mutual fund in a single or multi vendor scenario)

Scenario	Front End Sales Charge	Morningstar Rating	Annualized Return		\$10,000 Invested 10 Yrs. Ago Would Be Worth
			5 years	10 years	
Multi Vendor "A" - Class Shares	5.75% on each deposit	4 stars	9.98%	8.53%	\$22,672
Single Vendor "R4" - Class Shares	None	5 stars	11.26%	9.16%	\$24,023

Source: Morningstar; Data as of 6/30/08

Impact of Asset-based Fees

- Single participant
- Contributing \$250 per month (\$3,000 annually)
- Compounded at 8% annually

Scenario	10 Years	30 Years	Difference After 30 Years	Percent of Impact
<u>Group Contract:</u> (Single Vendor or Low cost option) 0.00% M&E; \$30 admin. Fee	\$46,502	\$363,639	\$0	0%
<u>Individual Contract:</u> (Multi-Vendor) 1.25% M&E; \$30 admin. Fee	\$43,318	\$286,530	\$77,109	21.20%
<u>Individual Contract:</u> 1.25% M&E; 1.25% Investment Advisory fee; \$30 admin. Fee	\$40,364	\$237,085	\$126,554	34.80%

- Assumes \$3,000 contributed annually at the beginning of each year and an 8% annual rate of return net of investment management fees.
- This model assumes no additional contributions after Year 30.
- The above table is for illustrative purposes only and is not intended to be representative of any particular vendors program.
- M&E fees are usually found in variable annuity contracts; not mutual fund contracts.

Comparison of Single vs. Multi Vendor S&P 500 Index Fund

Bolton Partners Investment Consulting Group, Inc.
 Comparison of single vs. multi-vendor S&P 500 index fund

Stock Index - Performance as of June 30, 2008									Growth of \$10,000 if Invested 5 Years Ago
Vendor	Fund	YTD	1 Year	Annld. 3 Year	Annld. 5 Year	Mstar CAT.	Inception Date	Expense Ratio	
Vendor 1 (Annuity Vendor)	Stock Index Fund	-16.43%	-18.13%	1.46%	5.35%	Stock Index	4/20/1987	1.35%	\$12,977
Vendor 2 (Annuity Vendor)	VP Index Plus LgCap Port	N/A	-20.37%	-0.02%	4.20%	Stock Index	10/31/1996	1.69%	\$12,284
Vendor 3 (Annuity Vendor)	Maxim Stock Index	-17.92%	-19.90%	1.18%	5.43%	Large Blend	1/2/1992	1.55%	\$13,026
Mutual Fund Program	Dreyfus S&P 500 Index	-12.12%	-13.51%	3.92%	7.08%	Large Blend	1/2/1990	0.50%	\$14,078

Observation: Mutual fund program provides lower fees and higher returns.

Bid Process

- Developed criteria and pre-qualifications with assistance of an independent consultant
- Office of Purchasing issued the requests for proposals (RFP) to 21 vendors
- 13 vendors declined to submit proposals
- 3 respondents submitted proposals that did not qualify
- 5 vendors were evaluated

RFP Evaluation Criteria

- Ability to meet IRS requirements – record keeping and compliance
- Credit rating and profitability of vendor
- Current litigation involving the vendor
- 403(b) experience and market penetration
- Quality of services provided to enrolled participants
- Investment products available
- Depth of investment choices
- Proposed fee structure
- Overall pricing
- Transition choices for current voluntary participants
- Strength and depth of staff available to serve BCPS
- Extent of marketing to all BCPS employees about the benefits of saving for retirement

Results of Evaluation

Options for Consideration

- **Single Vendor Solution**
 - Results in the most favorable pricing for participants
 - Eliminates redundancy of investment styles
 - Lower administrative burden for BCPS
 - Potentially higher participation rates
 - Surrender charge buyouts available
 - Single vendor for legal accountability

- **Multiple Vendors Solution**
 - Reduced pricing from current vendors
 - Additional cost of a third party administrator
 - Higher administrative burden for BCPS
 - Commissioned agents will be used
 - All fees are not transparent
 - Multiple vendors for legal compliance

Difference in Fees

- Single vendor: Eliminated all administrative fees
- Multiple vendors (4+): Reduced but did not eliminate administrative fees
- The fees ranged from (0.15%-0.50%); the average fee is 0.39%
 - Assuming annual contributions on \$30 million for 10 years earning 8%, the administrative fees will cost participants \$10.3 million
 - Assuming annual contributions on \$30 million for 20 years earning 8%, the administrative fees will cost participants \$67.7 million

Single Vendor Participation Rates

- Harford County Public Schools (March 2007)
 - Participation increased by 14%
 - Deferrals increased by 13%
- Prince William County Public School (January 2003)
 - Participation increased by 20%
- Richmond City Public Schools (August 2005)
 - Participation increased by 53%
- Chesterfield County Public Schools (Sept. 2007)
 - Participation increased by 87%

403(b) History and Upcoming Dates

October 23, 2007	Date of closed session discussion of new IRS regulations with the Board of Education
November 16, 2007	Presentation to the unions on the new IRS regulations
July 31, 2008	Staff review of the 403(b) bid submission with Bolton (consultant)
August 20, 2008	Presentation of the 403(b) bid submission by Bolton to the unions
September 8, 2008	Follow-up meeting with unions on the 403(b) bid submission
September 9, 2008	Review with Board of Education in closed session on legal issues update by Venable and results of follow-up meeting with unions
September 23, 2008	Work session review by the Board of Education of the 403(b) bid submission
October 7, 2008	Proposed Board of Education contract approval of 403(b) vendor