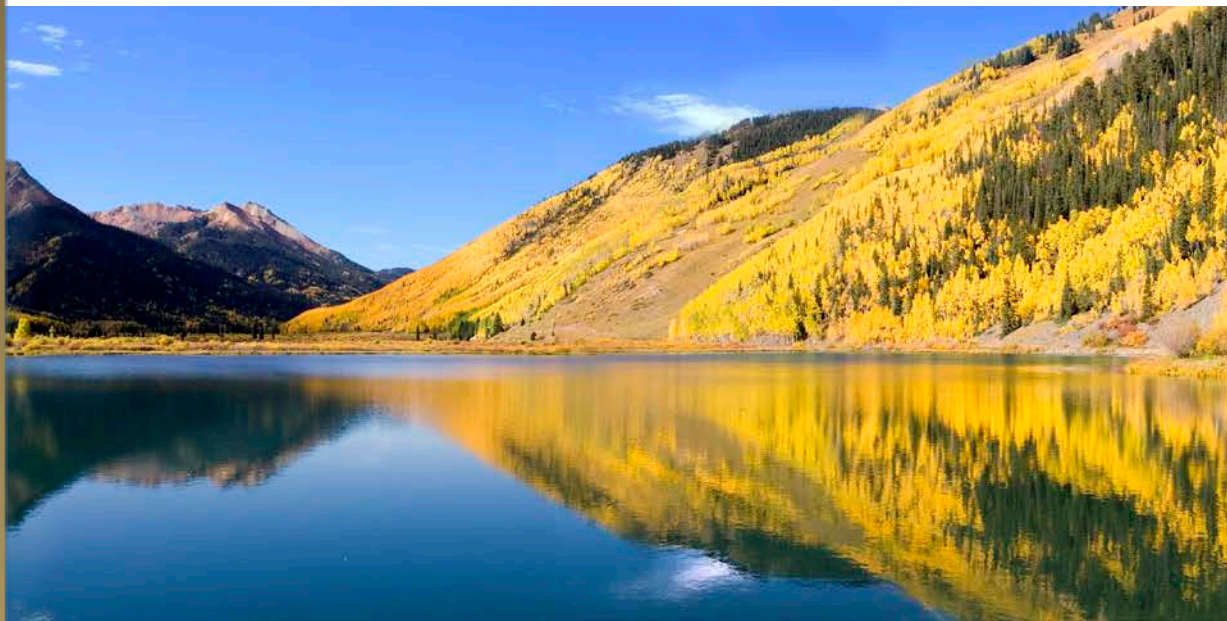


A Comprehensive Review of the CU Optional Retirement Plan (the 401(a) Plan) and the 403(b) Plan



*prepared by the Retirement Vendor Review Project Committee
June 6, 2014*

Background Summary

The University of Colorado system has not conducted a comprehensive review of employee retirement programs for more than two decades – a period of considerable change in the complexity of the financial landscape and accumulation of research about best practices in retirement plan administration. In the coming months, a team of CU employees, listed at the conclusion of this paper, will work with CU System to review and recommend, as appropriate, modifications to two aspects of our 401(a) Plan and 403(b) Plan. One aspect is the set of *retirement investment products* to offer eligible employees. The second aspect is choosing the firm or firms to be the Plans' "recordkeeper".

Recordkeepers are typically investment firms that keep track of the investments, withdrawals, allocations, etc., made by employees enrolled in the plan(s). They act as a "purchasing agent" when buying and selling mutual funds and other securities. Recordkeepers can also provide data to the employer to see where there are pockets of low retirement preparedness among employees. The use of recordkeepers is common in the private sector.

Recordkeepers also provide statements to participating employees and provide web-based platforms to keep track of transactions as well as online money management tools. They also provide an education function to employees and can assist employees in developing a sound retirement plan.

In the current system these two roles of determining the investment options and providing recordkeeping are combined at the vendor level. Currently, CU has formal 401(a) agreements with three vendor firms: TIAA-CREF, Vanguard and Fidelity. In addition, CU has formal 403(b) agreements with eight vendor firms, each offering a full array of retirement investment vehicles. The 403(b) vendors, in order of amount of plan assets invested as of December 31, 2013, include TIAA-CREF, Fidelity, Vanguard, VALIC, MetLife, American Century, DWS and Dreyfus. Each vendor provides recordkeeping services for employees who are invested in that vendor's investment products. In addition, each vendor offers some number of mutual funds covering different sectors of the market. These multiple offerings have led to duplication of investment offerings within each the 401(a) and 403(b) plan. For example, the CU 403(b) plan currently has 552 different investment choices.

Since each vendor is responsible for providing recordkeeping, this function is also duplicated, which leads to higher costs of providing the program. The vendors are also responsible for providing participant education. The investor education is spotty at best and can be inconsistent since eight separate vendors provide education. The trend in the industry is to reduce the number of recordkeepers. For example, Harvard University has two recordkeeping firms offering the identical menu of 24 investment options. Robert Steyer, in a December 2011 *Pensions&Investments* article, points out that the trend for many universities is to reduce both the number of vendors and the number of investment choices available in 403(b).¹ CU's current review of its 401(a) and 403(b) plans puts it ahead of the curve compared to many other universities across the country.

¹ See <http://www.pionline.com/article/20111226/PRINT/312269984/403b-record-keepers-see-heated-battles-continuing>.

Advantages to CU Employees of Vendor Reduction

The financial industry is finding that decreasing the number of vendors has a number of advantages. For employees, too many vendors means higher fees. The university can receive lower fees on the same funds if it buys in bulk through fewer vendors. Preliminary analysis suggests CU may be able to save several million dollars in annual expense-related fees through reduction in the number of vendors. In addition, a better focus on fund performance in a reduced set of available fund choices from among multiple investment firms is expected to lead to higher risk adjusted returns over time.

Another important benefit is improved financial education and advice for employees. Having fewer vendors is expected to lead to having dedicated financial advisors from each vendor to offer financial education and access to individual financial advising sessions so that employees get an unbiased expert's look at financial preparedness for retirement. Currently, most of the eight vendors' representatives visit the individual campuses on an irregular and unpredictable schedule, making it difficult to obtain timely advice. In addition, the message coming from so many vendors can be inconsistent and favor proprietary funds over funds offered by other mutual fund families which may have a much better overall track record.

Finally, industry research shows that people are actually more likely to participate in elective retirement plans and make better informed investment selections when the number of options has been culled to a smaller set. One might think that it would be an advantage to have as many choices as possible to find something that exactly fits an individual's needs, but the advantage of more choice in matching criteria faces diminishing returns if many or most of the choices overlap. This is the current situation in both of the CU plans, particularly in the 403(b) plan. For example, the 403(b) plan currently has 36 mutual funds described as "large cap core." All of these funds essentially track the Standard & Poors index of 500 large market capitalization stocks. Clearly, the plan does not need this many choices of one stock tracking index. The needless duplication can lead to confusion and employees opting out of participation. There is considerable literature on "too much choice" and "choice overload" that shows that people faced with too many options just give up in various ways and never make the choice to invest.

Researchers at Columbia University and the University of Chicago analyzed pension choices at over 600 corporate 401(k) plans to investigate how employees respond to the number of investment options available to them. Every 10 more 401k investment options caused a decrease in the chance that the employee would allocate anything to equities, which is historically a source of the higher returns necessary for retirement security. Tilting investment choices away from equities can mean favoring lower return alternatives that may not provide a sufficient buildup of savings needed for retirement. Other research shows that too much choice leads to procrastination because people are not sure which option is best, and they are frozen by conflict. They think that next month they will sit down to figure it out but don't follow through.



Advantages to CU Retirement Plan and Benefits Administration of Vendor Reduction

ADVANTAGES OF FEWER VENDORS FOR EMPLOYEES IN THE CU SYSTEM

- Fee reductions: Volume discounts will permit substantial fee reductions on investment options offered to employees.
- Increased access to financial advice with better quality and consistency of advice
- Greater employee participation by reducing the “choice overload” problem

Having such a large number of investment vendors causes unnecessary complexity and risk of federal non-compliance in the closely regulated administration of CU’s 401(a) and 403(b) plans. In addition, having eight different vendors makes it impossible to get a complete picture of the retirement readiness of the entire range of CU employees. Most importantly, the cacophony of information systems makes it impossible for the CU retirement system to be proactive, to understand when particular employee groups are having problems and to provide tools to help them get back on track and stay on track, e.g., by providing more or better access to unbiased financial advice.

CU Employee Services, therefore, is undertaking a study this year to conduct a comprehensive analysis of the plans’ components. In addition to contracting with Innovest Portfolio Solutions, a national firm specializing in such work, Employee Services has assembled a project advisory committee to assist with the review:

- Geoff Barsch-Associate Vice President, Budget and Finance, System
- Peter C. Bowers-Contract Manager, Employee Services, System
- Gary Colbert-Associate Professor, Accounting; Director of the 11-Month MBA Program, CU Denver
- Erin Foster-Finance Manager, Academic Affairs, CU-Boulder
- John Lynch-Director of the Center for Consumer Financial Decision Making and Ted Anderson Professor of Free Enterprise, CU-Boulder
- William Marine-Professor (retired), Colorado School of Public Health, Anschutz Medical Campus
- Thomas Martinez-Pension/Savings Specialist, Employee Services, System
- Michael Preston-Emeritus Professor, English, CU-Boulder
- Bryn Samuelson-Director of Business Operations, University Information Systems, System
- Katie Sauer-Director of Financial Education, Employee Services, System
- Ravinder Singh - Associate Professor, MCD Biology, CU-Boulder
- Thomas Zwirlein – Professor, Finance, UCCS

ADVANTAGES OF FEWER VENDORS FOR THE CU SYSTEM

- Permits the CU system and its employees to get a clearer view of the university’s retirement plan financial picture
- Allows the CU system to be proactive in spotting and addressing trouble spots for employees in the system
- Minimizes risks of legal non-compliance in plan administration



As part of its role, the committee may formulate a Request for Documented Quote (RDQ), to identify and ultimately retain a national financial investment firm or firms with extensive experience in serving higher education, to act as vendor(s)/recordkeeper(s) for CU's retirement plans. The committee expects a number of the current vendors for the CU plans to respond to the RDQ, in addition to firms not currently associated with the university.

The committee will solicit information from CU employees to better inform the process. Innovest will be assisting the committee in a data-driven approach to provide guidance throughout the entire project.

