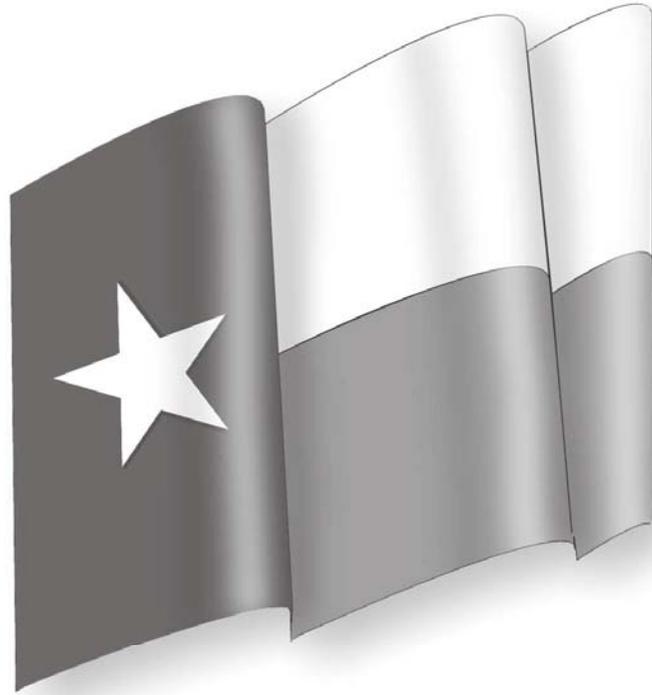


*Summary of Sunset
Commission Recommendations*



**Prepaid Higher Education
Tuition Board**

February 2007





Prepaid Higher Education Tuition Board

Board at a Glance

The mission of the Prepaid Higher Education Tuition Board (the Board) is to help Texas students attend college. The Board accomplishes its mission by overseeing the State's two 529 college savings programs, named after the section of the Internal Revenue Code that authorizes them. The Texas Guaranteed Tuition Plan (Prepaid Plan) allows buyers to lock in future college tuition and required fees at today's prices, and Tomorrow's College Investment Plan (Savings Plan) is a savings program that works much like a 401(k) but with after-tax dollars.

In 2003, the Board temporarily suspended enrollment in the Prepaid Plan because of the uncertain effects of the deregulation of tuition. The Board feared that, because it could not accurately predict future costs of tuition, it could potentially sell new tuition contracts at inadequate prices and jeopardize the Plan's assets. To date, the Prepaid Plan remains closed to new applicants, but Texas families can continue to invest in the State's Savings Plan to help cover future college expenses.



*For additional information,
please contact Amy Trost
at (512) 463-1300.*

Key Facts

- ◆ **Staffing.** The Board has no staff of its own, but reimburses the Office of the Comptroller of Public Accounts for 20.5 staff positions to support the day-to-day operations of the Board. Because the Board contracts out administration of the Savings Plan, the 20.5 staff primarily support the Prepaid Plan.
- ◆ **Funding.** The Board receives no appropriation to operate the two plans, but instead relies on prepaid tuition contract payments, investment income, and fees to cover administrative costs and tuition benefits. In fiscal year 2006, the Board spent about \$8.3 million in Prepaid Plan administrative costs, which included staff salaries and payments to fund managers. The Board also received almost \$730,000 from the Savings Plan contractor for reimbursement of administrative and marketing expenses for that program.
- ◆ **Texas Guaranteed Tuition Plan (Prepaid Plan).** From 1996 to 2003, the Board sold more than 158,000 prepaid tuition contracts to Texas families, allowing them to pay for future college tuition and fees at current prices. With \$1.7 billion in assets at the end of fiscal year 2006, the Prepaid Plan Fund is one of the State's largest investment funds and is backed by the full faith and credit of the State. The Plan has paid almost \$226 million in tuition and fees in the last five academic years.
- ◆ **Tomorrow's College Investment Plan (Savings Plan).** By the end of fiscal year 2006, more than 19,000 account holders had invested more than \$175 million in Savings Plan accounts. The Plan has disbursed approximately \$22.4 million for college costs from its inception in 2002 through fiscal year 2006.

Board Members (7)

The Honorable Susan Combs, Comptroller of
Public Accounts, Presiding Officer (Austin)
The Honorable John C. Anderson (Plainview)
Theresa W. Chang (Houston)
Richard Collins (Dallas)
Jack R. Hamilton, CFA (Houston)
Harrison Keller, Ph.D. (Austin)
Zan S. Statham (Weatherford)

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Recommendations

1. Facilitate the Board's ability to reopen the Prepaid Plan through changes in law that enable better pricing of contracts given a tuition deregulated environment.
2. Direct the Board to consider changes to encourage greater interest in managing the Savings Plan and to regularly evaluate the cost-effectiveness of its advertising.
3. Require in law an ethics policy for Board members and staff to help ensure against any potential conflicts of interest.
4. Require the Board to study how it could leverage prepaid tuition contracts to secure benefits for Prepaid Plan beneficiaries from Texas universities.
5. Continue the Prepaid Higher Education Tuition Board, housed at the Comptroller's Office, for the standard 12-year period.

Issue 1

Statutory Changes Could Help Facilitate the Board's Ability to Reopen the Prepaid Plan Within a Tuition Deregulated Environment.

Key Findings

- ◆ The Board has suspended any new enrollment in the Texas Guaranteed Tuition Plan since 2003, but continues to manage its more than 158,000 existing prepaid tuition contracts.
- ◆ Deregulation has caused tuition at four-year, public, Texas universities to diverge considerably, making it difficult for the Board to accurately price new contracts.
- ◆ Continuing to apply the weighted average requirement to new contracts could unfairly shift a growing portion of beneficiaries' future tuition costs to universities with tuition that exceeds the weighted average.
- ◆ The Board lacks authority to issue refunds for certain plans to help protect purchasers who pay more for the contract than the actual cost of tuition.
- ◆ Unlike Texas, most prepaid tuition plans in other states require a delay from the contract purchase date to when the student claims benefits, allowing time for investments to grow.

Through the Texas Guaranteed Tuition Plan (Prepaid Plan), the Board has helped thousands of Texas families afford college tuition for their young family members. However, the Board has not sold new prepaid tuition contracts since the Legislature deregulated tuition in 2003. Key obstacles to reopening the Prepaid Plan include the increasingly divergent tuition rates set by Texas universities, and limits in existing law that were created in the environment prior to tuition deregulation.

Recommendations

Change in Statute

1.1 Remove the weighted average requirement for any new prepaid tuition contracts the Board sells.

This recommendation would remove the requirement that any university with tuition and required fees above the weighted average of all four-year, public, Texas universities waive the difference in cost between their tuition and required fees and the weighted average amount. Because this provision is important to the soundness of tuition contracts the Board sold previously, the recommendation would only apply to new contracts issued if the Board reopens the Prepaid Plan in the future. The weighted average requirement would still apply to all Senior College contracts the Board sold from 1996 to 2003.

With the changes recommended in this report, the Board would have more opportunities to create a self-sustaining program that is capable of paying universities the actual cost of tuition.

1.2 Authorize the Board to issue refunds for new prepaid tuition contracts if a purchaser pays more for a contract than the actual cost of the beneficiary's tuition.

This recommendation would authorize, but not require, the Board to issue refunds for Junior, Senior, and Junior-Senior College Plans, if necessary. Pricing contracts higher could help protect the Board's assets and enable the sale of new contracts, but a refund provision may be necessary to protect future

purchasers' investments. The intent of the recommendation is to give the Board a tool that may help it reopen the Prepaid Plan.

1.3 Authorize the Board to require a delay from the contract purchase date to when the student claims benefits, allowing time for investments to grow.

This recommendation would authorize, but not require, the Board to require a maturity period before a beneficiary could use prepaid tuition benefits. Such a delay from the time a contract is purchased would ensure sufficient time for the Board's investments to grow before the beneficiary claims tuition benefits. The intent of the recommendation is to give the Board additional flexibility to protect the Plan's assets, which may help reopen the Prepaid Plan.

1.4 Require the Board to annually reassess whether it can reopen the Prepaid Plan as long as the Plan remains closed.

This recommendation would require the Board to create a procedure in rule that clearly outlines criteria to use when annually analyzing whether the Prepaid Plan may reopen. As part of this procedure, the Board should consider the Plan's current structure and whether additional statutory changes are needed for it to reopen.

Issue 2

The Savings Plan Could Benefit From the Board's Reconsideration of Restrictions in Its Request for Proposals and the Cost-Effectiveness of Its Advertising.

Key Findings

- ◆ Two key components of the Board's Request for Proposals (RFP) to run the Savings Plan may unnecessarily restrict fund manager applicants, reducing the competitiveness of the Plan.
- ◆ The Board devotes significant funds to television advertising for the Savings Plan but fails to clearly track its impact on new enrollment.

The Board is responsible for contracting with vendors to ensure that the State's 529 Savings Plan is well managed and accessible to individuals wishing to save for their children's or grandchildren's educations. Texas' 529 Savings Plan is relatively new and growing; however, many other states' plans, which began at approximately the same time, are significantly larger.

Two key components of the Board's contracting process may have limited the competitiveness of the Savings Plan. The Board restricted respondents to only those firms that did not manage other states' plans, and required a significant annual, upfront marketing contribution from the plan manager, potentially impacting the Board's ability to attract larger, more established plan managers.

The Board could also benefit from clearer oversight of the Savings Plan's advertising campaign to ensure the cost-effectiveness of its efforts to increase enrollment.

Recommendations

Management Action

2.1 The Board should consider restructuring its next Request for Proposals for the Savings Plan manager to encourage a wider variety of respondents.

This recommendation would direct the Board to consider restructuring the plan manager RFP to improve the volume and quality of respondents. The Board should evaluate eliminating the current requirement that the plan manager exclusively manage the Texas plan. By removing this requirement, the Board would allow many additional firms with good standing in the 529 market to respond. In addition, the Board should reconsider the marketing cost charged to the plan manager to ensure that the required contribution does not unreasonably restrict the RFP respondent pool.

2.2 The Board should regularly evaluate the impact of its advertising campaign to ensure that it is cost-effectively generating new enrollment.

This recommendation would ensure that the Board routinely reassesses the advertising plan for the State's Savings Plan, and for the Prepaid Plan should enrollment reopen. The Board should require that the contracted advertising vendor provide regular reports that assess the volume of new business generated by the advertising campaign. In addition, the advertising vendor and the Board should regularly evaluate the plan to ensure that it provides the best mix of advertising to effectively reach the broadest segment of individuals interested in investing and saving for college-bound Texans.

Issue 3

The Board's Statute Lacks Ethics Provisions That Are Important Safeguards for Boards With Significant Investment Oversight.

Key Findings

- ◆ Prepaid Higher Education Tuition Board members and staff are involved in investment decisions regarding the Board's two 529 college savings programs.
- ◆ Though the Board follows an ethics policy, and has not encountered any problems, the Board's statute does not specify ethical standards for Board members and staff.
- ◆ Other state agencies and boards with investment responsibilities have ethics requirements in their statutes.

The Board and its staff oversee investments of almost \$2 billion in Texas' two college savings plans. The Board has established and uses an ethics policy to guide its members and staff when dealing with a variety of potential ethical challenges. However, unlike other government bodies with investment authority, the Board has no requirement in law to have an ethics policy.

Recommendation

Change in Statute

3.1 Require in law an ethics policy for Board members and staff that includes disclosure of conflicts of interest and recusal when conflicts exist.

This recommendation would add a provision to the Board's statute that would require the Board to maintain an ethics policy that addresses the following issues for Board members and staff:

- ◆ general ethical standards;
- ◆ conflicts of interest, including disclosure and recusal requirements;
- ◆ acceptance of gifts and entertainment; and
- ◆ compliance with, and enforcement of, the ethics policy.

The Board's current policy contains these provisions, so the Board would not need to develop a new policy. Placing provisions of the Board's existing ethics policy in statute would help ensure that the actions of future Board members avoid any conflicts of interest or other ethical violations. Placing ethics policy requirements in statute also makes them more visible to the public and investors.

Issue 4

The Board Could Be Missing An Opportunity to Leverage Prepaid Tuition Contracts to Secure Benefits From Texas Universities for Plan Beneficiaries.

More than 120,000 college-bound Texas students have prepaid tuition contracts. In fiscal year 2006, 18,062 students used prepaid plan benefits, the majority of whom attended Texas public universities. These students provide a stable source of funding for universities, and they are more likely to graduate on time because their tuition has been paid for. Given this high volume of securely funded students, the Board could be missing an opportunity to obtain tuition discounts or other benefits from universities interested in encouraging students with prepaid contracts to attend their institutions.

Recommendation

Change in Statute

4.1 Require the Board to study how it could leverage its prepaid tuition contracts to secure benefits from Texas universities for plan beneficiaries.

This recommendation would require the Board to conduct a one-time study to determine whether it could negotiate with Texas universities to secure tuition discounts or other benefits for students with prepaid tuition contracts.

Issue 5

Texas Has a Continuing Need for the Prepaid Higher Education Tuition Board.

Key Findings

- ◆ The Prepaid Higher Education Tuition Board oversees the State's two tax-advantaged college savings plans.
- ◆ Texas has a continuing interest in, and the Board has been successful with, helping thousands of Texas families save for college.
- ◆ While other state agencies deal with higher education, none offer advantages over the Office of the Comptroller of Public Accounts for housing the Board's college savings plans.

The Legislature recognized the need to help Texans save for college expenses in 1995 when it established the Prepaid Higher Education Tuition Board. The Board administers both of the State's 529 college savings plans, the Texas Guaranteed Tuition Plan and Tomorrow's College Investment Plan. While organizational alternatives to housing the Board at the Office of the Comptroller of Public Accounts exist, no other agency could provide benefits over the current structure. The Board successfully accomplishes its mission and should be continued for 12 years.

Recommendation

Change in Statute

5.1 Continue the Prepaid Higher Education Tuition Board for 12 years.

This recommendation would continue the Board, housed at the Comptroller of Public Accounts, for the standard 12-year period.

Fiscal Implication Summary _____

None of these recommendations would have a significant fiscal impact to the State.

