

# EXECUTIVE SUMMARY OF SUNSET STAFF REPORT

## Teacher Retirement System of Texas

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The Sunset review of the Teacher Retirement System of Texas (TRS) took place during a controversial period for the agency, with significant attention surrounding TRS' decision to lease office space for its investment staff in a new, expensive building in downtown Austin. While TRS changed course on this decision in February 2020, the agency's lack of transparency in making the initial decision highlighted growing mistrust from its members and some legislators. This controversy followed a successful legislative session for TRS and its members in 2019, with the Legislature increasing contribution levels and authorizing a one-time supplemental payment for retirees.

Unlike most state agencies Sunset reviews, TRS is constitutionally created and not subject to abolishment. The Sunset review therefore did not consider the question of the fundamental need for the agency, but instead whether TRS operates efficiently, effectively, and in the best interest of its members. TRS' 1.6 million members span a broad range of Texas teachers and other public education staff, who depend on TRS to ensure they can retire securely. While TRS has a critical fiduciary duty to manage the \$157 billion trust fund in the best interest of its members, the agency also has an important responsibility to ensure its members have the support and information needed to be secure in retirement.

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TRS' benefit counseling options do not meet members' needs, with limited member-specific information available by phone and unequal access to in-person counseling for members throughout the state, most of whom must travel to Austin for one-on-one retirement sessions. TRS also does not provide enough member-friendly financial planning information to ensure members understand what they need to prepare for retirement, such as the importance of additional savings beyond their TRS pension benefits.

As a state agency with a large and sophisticated investment program, TRS is in a unique and precarious position. TRS' status as a major institutional investor affords the agency significant respect and deference in the investment arena, but the billions TRS manages ultimately belong to the members it serves. With one foot in the high-powered investment world and the other in the more modest public arena, TRS struggles to find the balance between managing the pension fund appropriately while serving its members and conducting itself as a judicious state agency. In addition to needing to focus more on its members, the review also found that, as a large, public investor, TRS needs

greater transparency and oversight for its investment functions. Additionally, TRS manages about \$2.5 billion in active contracts, but lacks the centralized structure and contract management tools needed to ensure the agency gets what it pays for. In particular, TRS has struggled to enforce a major contract for an information technology system overhaul, which the agency ultimately terminated during this review, assuming completion of the project itself.

The following material highlights Sunset staff's key recommendations for the Teacher Retirement System of Texas.

## Sunset Staff Issues and Recommendations

### ISSUE 1

#### TRS Needs to Repair Its Relationship With Its Members by Focusing on Their Needs.

TRS has an important fiduciary responsibility to act in the best interest of its 1.6 million members, which includes both ensuring the pension trust fund is sound and also helping members make important retirement decisions. However, TRS has not provided the information and support its members need to be secure in retirement, with overly complex explanations, insufficient retirement information, and inadequate counseling options. Additionally, TRS does not provide employers the resources they need to assist TRS members who often come to them with questions about their benefits. Overall, TRS' recent actions and questionable decisions have made members uncertain of whether TRS is acting in their best interest or its own.

#### Key Recommendations

- Require TRS to develop a communication and outreach plan to better help members and employers plan for retirement.
- Require TRS to make improved efforts to return contributions to inactive members before funds are forfeit.
- Direct TRS to adopt a member engagement policy to increase transparency on key decisions.

### ISSUE 2

#### TRS Needs More Effective Contract Management and Oversight.

To carry out its mission to provide benefits to its members, TRS has nearly \$2.5 billion in active contracts. Sunset staff found several TRS contracting and procurement procedures do not align with best practices, limiting the agency's ability to oversee and manage contracts effectively. While TRS has begun making improvements to its contracting and procurement processes, the agency needs to address a lack of centralization, poor performance monitoring, ineffective use of contract remedies, and insufficient contract training.

### Key Recommendations

- Direct TRS to fully centralize contracting functions and clarify roles and responsibilities between central contracts department staff and division staff managing contracts.
- Direct TRS to enhance its contract monitoring process and require staff who procure or manage contracts to complete the comptroller's contract training.
- Direct TRS to include standard remedies in contracts and consistently apply enforcement tools.

## ISSUE 3

### As One of the Largest Public Pension Funds in the U.S., TRS Would Benefit From Additional Oversight and Greater Transparency of Its Investment Practices.

TRS manages a trust fund valued at more than \$157 billion and uses investment income to help pay for members' benefits. TRS contracts with a custodian bank to hold fund assets, settle transactions, and perform investment reporting and accounting for the agency. Sunset staff found TRS could reduce risks in its investment accounting by using a fully independent or automated system to better identify accounting inconsistencies. Sunset staff also found the agency lacks a formalized process for reviewing internal investments. Finally, TRS does not provide stakeholder-friendly information about alternative investments in its *Comprehensive Annual Financial Report*.

### Key Recommendations

- Direct TRS to perform a cost-benefit analysis of implementing an enhanced investment accounting system to provide increased oversight of the custodian bank's accounting data.
- Direct TRS to have its Internal Investment Committee review internal investments and strategies.
- Direct TRS to include clear, easily understandable information about alternative investments in its *Comprehensive Annual Financial Report*.

## ISSUE 4

### TRS' Statutes Do Not Reflect Some Standard Elements of Sunset Reviews.

Among the standard elements considered in a Sunset review are across-the-board recommendations that reflect criteria in the Sunset Act designed to ensure open, responsive, and effective government. TRS' statute does not contain updated requirements for board member training, such as a training manual and discussion of the board's rulemaking authority. While TRS' governing statutes contain standard language requiring the agency to maintain complaint information, TRS has not developed an agencywide process to track and resolve complaints.

### Key Recommendations

- Update the standard across-the-board requirement related to board member training.
- Direct TRS to develop and maintain an agencywide system for receiving and responding to complaints.

## Fiscal Implication Summary

Overall, the recommendations in this report would not have a fiscal impact to the state because TRS' operating expenses are not appropriated from general revenue. Most recommendations could be accomplished within TRS' existing resources and should not result in a cost to the pension trust fund. Some recommendations that could have minimal impacts to TRS are discussed below.

*Issue 2* — Centralizing the agency's contracting functions and increasing contract monitoring could result in some additional operating expenses. TRS is currently hiring additional contract management staff, and these recommendations would not require expanding that effort.

*Issue 4* — The recommendation to centrally track and report on complaints could result in a cost to the agency, but the cost would depend on how TRS chooses to implement a complaint tracking system and cannot be estimated at this time.