History of Texas 403(b) Legislation

Since 2001

SB 273 - 2001

HB 2341 - 2007

HB 3480 - 2009

HB 2820 - 2019

Senate Bill 273
Section 21 – Governing 403(b) Plans of Public School Districts

AN ACT

relating to systems and programs administered by the Teacher Retirement System of Texas; providing a penalty.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 21. Section 1, Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), as amended by Chapters 1340 and 1341, Acts of the 75th Legislature, Regular Session, 1997, is amended to read as follows:

Sec. 1. (a) This section and Section 2 of this Act apply to:

(1) the governing boards [~~Local Boards of Education of the Public Schools of this State, the Governing Boards~~] of [~~the~~] state-supported institutions of higher education;

(2) [~~,~~] the Texas Higher Education Coordinating Board;

(3) [~~,~~] the Texas Education Agency;

(4) [~~,~~] the Texas School for the Deaf;

(5) [~~,~~] the Texas School for the Blind and Visually Impaired;

(6) [~~,~~] the Texas Department of Mental Health and Mental Retardation and the state schools, state hospitals, and other facilities and institutions under its jurisdiction;

(7) [~~,~~] the Texas Department of Health and facilities and institutions under its jurisdiction;

(8) [~~,~~] the Texas Youth Commission and facilities and institutions under its jurisdiction; [~~,~~] and

(9) the governing boards of Centers for Community Mental Health and Mental Retardation Services, county hospitals, city hospitals, city-county hospitals, hospital authorities, hospital districts, affiliated state agencies, and each of their political subdivisions.

(b) An entity described by Subsection (a) of this section [~~of each of them,~~] may enter into agreements with the entity's [~~their~~] employees for the purchase of annuities or for contributions to any type of investment for the entity's [~~their~~] employees as authorized in Section 403(b), [~~of the~~] Internal Revenue Code of 1986 [~~1954~~], and its subsequent amendments [~~as it existed on January 1, 1981~~].

SECTION 22. Section 2, Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 2. (a) If an employee of an [~~a governmental~~] entity covered by Section 1 of this Act is paid by the Comptroller of Public Accounts, the comptroller may take the action, in regard to that employee, that is authorized by Subsection (b) of this section. If an employee of an [~~a governmental~~] entity covered by Section 1 is not paid by the comptroller, the governing board of the [~~governmental~~] entity may take the action in regard to that employee.

(b) The comptroller or the governing board, as appropriate [~~the case may be~~], may:

(1) reduce the salary of participants when authorized by the participants and shall apply the amount of the reduction to the purchase of annuity contracts or to contributions to any type of investment authorized in Section 403(b), [~~of the~~] Internal Revenue Code of 1986 [~~1954~~], and its subsequent amendments [~~as it existed on January 1, 1981~~], the exclusive control of which will vest in the participants; and

(2) develop a system to allow or require participants to electronically authorize:

(A) participation under this Act;

(B) purchases of annuity contracts; and

(C) contributions to investments.

[~~(c) The employee is entitled to designate any agent, broker, or company through which the annuity or investment is to be purchased.~~]

SECTION 23. Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended by adding Sections 4, 5, 6, 7, 8, 9, 10, 11, and 12 to read as follows:

Sec. 4. In this section and in Sections 5, 6, 7, 8, 9, 10, and 11 of this Act:

(1) "Board of trustees" means the board of trustees of the Teacher Retirement System of Texas.

(2) "Educational institution" means a school district or an open-enrollment charter school.

(3) "Eligible qualified investment" means a qualified investment product offered by a company that:

(A) is certified to the board of trustees under Section 5 of this Act; or

(B) is eligible to certify to the board of trustees under Section 8 of this Act.

(4) "Employee" means an employee of an educational institution.

(5) "Qualified investment product" means an annuity or investment that:

(A) meets the requirements of Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) complies with applicable federal insurance and securities laws and regulations; and

(C) complies with applicable state insurance and securities laws and rules.

(6) "Retirement system" means the Teacher Retirement System of Texas.

(7) "Salary reduction agreement" means an agreement between an educational institution and an employee to reduce the employee's salary for the purpose of making direct contributions to or purchases of a qualified investment product.

Sec. 5. (a) An educational institution may enter into a salary reduction agreement with an employee of the institution only if the qualified investment product is an eligible qualified investment.

(b) A company may certify to the retirement system that the

company offers a qualified investment product that is an annuity contract under this section if the company:

(1) is authorized to issue annuity contracts in this state at the time the application is filed;

(2) does not assess fees, costs, or penalties on an annuity contract that exceed the maximum amounts established by rules adopted by the retirement system; and

(3) complies with the standards adopted under Section 6 of this Act.

(c) A company that certifies under this section shall notify the retirement system if, at any time, the company is not in compliance with Subsection (b) of this section or if an investment product that the company offers under this Act is the subject of a salary reduction agreement and the investment product is not a qualified investment product.

(d) The retirement system shall establish and maintain a list of companies that have certified under this section. The list must be available on the retirement system's Internet website.

(e) An employee is entitled to designate any agent, broker, or company through which a qualified investment product may be purchased or contributions may be made.

(f) To the greatest degree possible, employers of employees who participate in the program offered under this section shall require that contributions to eligible qualified investments be made by automatic payroll deduction and deposited directly in the investment accounts.

Sec. 6. (a) A company is eligible to certify to the retirement system under Section 5 of this Act if the company satisfies the following financial strength criteria:

(1) the company's actuarial opinions required under Articles 1.11 and 3.28, Insurance Code, have not been adverse or qualified in the five years preceding the date the application is filed;

(2) the company is subject to the annual audit requirements of Article 1.15A, Insurance Code, and its most recent audit of financial strength conducted by an independent certified public accountant is timely filed and does not indicate the existence of any material adverse financial conditions in the company for the five years preceding the filing deadline for the audit;

(3) the company has not been the subject of an administrative or regulatory action by the Texas Department of Insurance under Article 1.32 or 21.28-A or Section 83.051, Insurance Code, in the five years preceding the date the application is filed;

(4) the company has maintained during the five years preceding the date the application is filed an average of at least 400 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus requirements established in rules adopted by the Texas Department of Insurance;

(5) the company has not fallen below 300 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus established in rules adopted by the Texas Department of Insurance, at any time in the five years

preceding the date the application is filed; and

(6) the company has at least five years' experience in qualified investment products and has a specialized department dedicated to the service of qualified investment products.

(b) For purposes of Subsection (a)(4) of this section, the company must calculate the five-year average on the same date each year.

(c) After consultation with the Texas Department of Insurance and the State Securities Board, the retirement system may adopt rules only to administer this section and Sections 5, 7, 8, and 11 of this Act.

(d) The retirement system shall refer all complaints about qualified investment products to the appropriate division of the Texas Department of Insurance or the State Securities Board.

(e) The Texas Department of Insurance and the State Securities Board shall cooperate with the retirement system in the administration of this Act and shall notify the retirement system of any action or determination regarding a product or a company that violates Section 5 of this Act.

(f) The retirement system shall reject or revoke the certification of a company if the retirement system receives notice under Subsection (e) of this section or Section 5(c) of this Act of a violation regarding the company or the company's product. The company may recertify to the board of trustees.

(g) The retirement system shall prescribe the uniform notice required by Section 11 of this Act.

(h) A certification or recertification remains in effect for five years unless rejected or revoked.

(i) A company offering eligible qualified investments that are subject to salary reduction agreements must provide toll-free telephone transferring privileges each business day from 8 a.m. to 6 p.m. central standard time.

Sec. 7. (a) The retirement system may collect a fee, not to exceed the administrative cost to the retirement system, from a company that certifies or recertifies under Section 6 or 8 of this Act. The fee for certification or recertification may not exceed $5,000.

(b) Fees collected under this section shall be deposited to the credit of the 403(b) administrative trust fund. The 403(b) administrative trust fund is created as a trust fund with the comptroller and shall be administered by the retirement system as a trustee on behalf of the participants in qualified investment products offered under this Act.

Sec. 8. (a) A company that offers qualified investment products other than annuity contracts may certify to the retirement system based on rules adopted by the board of trustees. The rules shall be based on reasonable factors, including:

(1) the financial strength of the companies offering products; and

(2) the administrative cost to employees.

(b) The retirement system shall establish and maintain a list of companies that provide certification under this section. The list must be available on the retirement system's Internet website.

Sec. 9. An educational institution may not:

(1) refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment;

(2) require or coerce an employee's attendance at any meeting at which qualified investment products are marketed;

(3) limit the ability of an employee to initiate, change, or terminate a qualified investment product at any time the employee chooses;

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products; or

(7) use public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product.

Sec. 10. (a) A person commits an offense if the person:

(1) sells or offers for sale a qualified investment product that is not an eligible qualified investment and that the person knows will be the subject of a salary reduction agreement;

(2) violates the licensing requirements of Subchapter A, Chapter 21, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement; or

(3) engages in activity described by Section 4, Article 21.21, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement.

(b) An offense under this section is a Class A misdemeanor.

(c) If conduct that constitutes an offense under this section also constitutes a criminal offense under the Insurance Code, the actor may be prosecuted under this section or under the Insurance Code, but not under both this section and the Insurance Code.

Sec. 11. (a) A person who offers to sell an annuity contract that is or will likely be the subject of a salary reduction agreement shall provide notice to a potential purchaser as provided by this section.

(b) The retirement system shall make the notice available on request and post the form of the notice on the retirement system's Internet website.

(c) The notice required under this section must be uniform and:

(1) be in at least 14-point type;

(2) contain spaces for:

(A) the name, address, and telephone number of the agent and company offering the annuity contract for sale;

(B) the name, address, and telephone number of the company underwriting the annuity;

(C) the license number of the person offering to sell the product;

(D) the name of the state agency that issued the person's license;

(E) the name of the company account representative who has the authority to respond to inquiries or complaints; and

(F) with respect to fixed annuity products:

(i) the current interest rate or the formula used to calculate the current rate of interest;

(ii) the guaranteed rate of interest and the percentage of the premium to which the interest rate applies;

(iii) how interest is compounded;

(iv) the amount of any up-front, surrender, withdrawal, deferred sales, and market value adjustment charges or any other contract restriction that exceeds 10 years;

(v) the time, if any, the annuity is required to be in force before the purchaser is entitled to the full bonus accumulation value;

(vi) the manner in which the amount of the guaranteed benefit under the annuity is computed;

(vii) whether loans are guaranteed to be available under the annuity;

(viii) what restrictions, if any, apply to the availability of money attributable to the value of the annuity once the purchaser is retired or separated from the employment of the employer;

(ix) the amount of any other fees, costs, or penalties;

(x) whether the annuity guarantees the participant the right to surrender a percentage of the surrender value each year, and the percentage, if any; and

(xi) whether the annuity guarantees the interest rate associated with any settlement option; and

(3) state, in plain language:

(A) that the company offering the annuity must comply with Section 5 of this Act;

(B) that the potential purchaser may contact the retirement system or access its Internet website to determine which companies are in compliance with Section 5 of this Act;

(C) the civil remedies available to the employee;

(D) that the employee may purchase any eligible qualified investment through a salary reduction agreement;

(E) the name and telephone number of the Texas Department of Insurance division that specializes in consumer protection; and

(F) the name and telephone number of the attorney general's division that specializes in consumer protection.

(d) A variable annuity must be accompanied by:

(1) a notice that includes any item listed in Subsection (c) of this section that is applicable to variable annuities;

(2) the prospectus; and

(3) any other purchasing information required by law.

(e) An equity-based index contract must state in plain language how the annuity contract will be credited with growth.

(f) If a notice and other information required under this section is not provided, any annuity contract for which the notice is required is voidable at the discretion of the purchaser. Not later than the 30th day after the date an employee notifies the seller in writing of the employee's election to void the contract, the seller shall refund to the employee:

(1) the amount of all consideration paid to the purchaser; and

(2) 10 percent interest up to the date the employee provides the notice to the seller.

(g) A seller who receives a refund request under this section is not required to make a refund otherwise required by this section if, not later than the 30th day after the date the seller receives a request for a refund from the employee, the seller provides a copy of the notice signed by the employee.

Sec. 12. A company that offers an eligible qualified investment that is subject to a salary reduction agreement shall demonstrate annually to the retirement system that each of its representatives are properly licensed and qualified, by training and continuing education, to sell and service the company's eligible qualified investments.

SECTION 24. Subsection (h), Section 16, Article 3.50-4, Insurance Code, is amended to read as follows:

(h) An employing district that fails to remit, before the seventh [~~11th~~] day after the last day of the month, all member deposits required by this section to be remitted by the district for the month shall pay to the Texas public school retired employees group insurance fund, in addition to the deposits, interest on the unpaid amounts at the annual rate of six percent compounded monthly. On request, the trustee may grant a waiver of the deadline imposed by this subsection based on a district's financial or technological resources.

SECTION 31. (a) The changes in law made to Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), by this Act do not apply to a contract between an employee of a school district or open-enrollment charter school and a company offering investments or annuities that was entered into or is entered into under Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), before June 1, 2002.

(b) A contract described by Subsection (a) of this section is governed by the law in effect immediately before the effective date of this Act, and the former law is continued in effect for that purpose.

SECTION 34. (a) Except as otherwise provided by this section, this Act takes effect September 1, 2001.

(b) The changes in law made by this Act to the following laws take effect June 1, 2002:

(1) Sections 9, 10, 11, and 12,Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(2) Section 17.46, Business & Commerce Code; and

(3) Section 17.49, Business & Commerce Code.

(c) The changes in law made by this Act to the following laws take effect September 1, 2002:

(1) Subsection (a), Section 825.408, Government Code; and

(2) Subsection (h), Section 16, Article 3.50-4, Insurance Code.

(d)The changes in law made by this Act to Section 624.602, Government Code, apply beginning with the 2001-2002 school year.

Section 824.602, Government Code, as amended by this Act, takes effect immediately if this Act receives a vote of two-thirds of all the members elected to each house, as provided by Section 39, Article III, Texas Constitution. If this Act does not receive the vote necessary for immediate effect,Section 824.602, Government Code, as amended by this Act, takes effect September 1, 2001.

TEXAS LEGISLATIVE COUNCIL

P.O. Box 12128, Capitol Station
Austin, Texas 78711-2128
Telephone: 512/463-1151

BILL RATLIFF
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FEB 19 2002

February 15, 2002

The Honorable Ken Armbrister
State Senator
State Capitol
Room 1E.12
Austin, TX 78711

Dear Senator Armbrister:

Nick James of your office has asked whether a provision in Section 9, Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), prohibits a school district from accepting the free or reduced-cost administration of a retirement or other benefit plan from a company that offers certain investment products.

Section 9(6), Article 6228a-5, states that an educational institution may not "accept any benefit from a company or from an agent or affiliate of a company that offers [certain] investment products" that meet the requirements of Section 403(b), Internal Revenue Code of 1986. Section 4(2), Article 6228a-5, defines "educational institution" to include a school district. Mr. James said that one of your constituents has asked whether an investment company's offer to administer a retirement or other benefit plan for a school district at no cost or at a reduced cost is a benefit prohibited by Section 9(6), Article 6228a-5. Your constituent has also asked for clarification of the types of offers that would fall within the meaning of the term "offer" as used in that section.

Article 6228a-5 does not define "benefit" or "offer." Section 9 of that article was enacted by the 77th Legislature and will take effect June 1, 2002. Thus, no court has yet interpreted the terms "benefit" or "offer" as used in Section 9(6), Article 6228a-5.

When a court does interpret a statute, Section 312.005, Government Code, requires it to ascertain the legislature's intent. Article 6228a-5, in part, regulates the sale of annuities and investments to teachers and other school district employees as part of so-called "salary reduction" agreements. Section 9 of that article contains several restrictions relating to such agreements. For example, Sections 9(1) and (3), Article 6228a-5, state that if certain statutory requirements are met, a school district may not limit an employee's ability to enter into a salary reduction agreement or to change the agreement. Sections 9(2) and (7) state that a school district may not coerce employees

into attending marketing meetings with an investment company, nor may it use its funds to promote an investment company. Section 9(4) prohibits a school district from granting an investment company exclusive access to an employee by discriminating against other companies.

The general intent of these provisions appears to be to protect the ability of school district employees to freely enter into salary reduction agreements with investment companies of their choice and to allow all eligible companies to compete equally for employees' business. Under Section 312.005, Government Code, a court would interpret the prohibition against the acceptance of benefits in Section 9(6), Article 6228a-5, in light of the overall intent of Section 9.

Further, when construing a statutory term, Section 312.002, Government Code, requires words to be "given their ordinary meaning." The ordinary meaning of the word "benefit" includes "advantage" or "useful aid." *Merriam-Webster's Collegiate Dictionary*, 10th ed. The free or reduced-cost administration of a retirement or other benefit plan provides both a financial advantage and useful assistance for a school district. Thus, under the ordinary meaning of the word "benefit," the free or reduced-cost administration of a retirement plan is a benefit for a school district. Section 9(6), Article 6228a-5, would therefore prohibit a school district from accepting such a benefit.

This interpretation of "benefit" is consistent with the intent of Section 9, Article 6228a-5, to provide for fair competition among investment companies. A school district that accepts free or reduced-cost plan administration from a particular investment company might appear to be endorsing that company, and thus to be giving one company preferential treatment over another. Prohibiting the acceptance of such a benefit could help promote fair competition.

The acceptance of benefits by public officials is restricted in other statutory provisions as well. For example, Chapter 36, Penal Code, contains restrictions on payments and gifts to certain public officials. The definition of "benefit" provided in that chapter is somewhat narrower than its ordinary meaning. Section 36.01, Penal Code, defines "benefit" as "anything reasonably regarded as pecuniary gain or pecuniary advantage . . . ."

The Texas Ethics Commission, which is charged with issuing advisory opinions on the application of certain statutes, including the provisions in Chapter 36, Penal Code, has applied the definition of "benefit" in that chapter to specific situations. In its opinions, the commission has typically viewed the term "benefit" to include free or discounted goods and services, such as a

discount on child care costs (Op. Tex. Ethics Comm'n No. 282 (1995)), free use of office space (Op. Tex. Ethics Comm'n No. 235 (1994)), and unlimited free parking at an airport or in a metered space and unlimited free use of golf and tennis facilities (Op. Tex. Ethics Comm'n No. 75 (1992)). The view that a benefit includes the free or reduced-cost administration of a retirement plan would be consistent with the commission's other applications of the term "benefit" as defined in Chapter 36, Penal Code. Thus, even under the narrower definition of "benefit" provided in that chapter and construed by the Texas Ethics Commission, a school district would likely be prohibited from accepting free or reduced-cost plan administration.

Your constituent has also asked for clarification of the meaning of the term "offer" as used in Section 9(6), Article 6228a-5. That subdivision prohibits a school district from accepting any benefit from a company that "offers qualified investment products." *Merriam-Webster's Collegiate Dictionary*, 10th ed., provides two applicable definitions of "offer" used as a verb. One is "to present for acceptance or rejection"; the other is "to make available: AFFORD; esp: to place (merchandise) on sale." Thus, it appears that a company that places a "qualified" investment product on the market or that presents such a product to potential purchasers for their acceptance falls within the purview of Section 9(6), Article 6228a-5, and a school district is prohibited from accepting a benefit from such a company.

Please let me know if I can provide you with any other information on this issue. This letter is a confidential communication under Section 323.017, Government Code, and its disclosure to third parties is entirely within your discretion.

Yours truly,

Shana Judge
Legislative Counsel

02M2

December 20, 2005

VIA FACSIMILE
(512.306.9959)

1075.01

Mr. Mike Cochran
TCG Consulting LP
4201 Bee Caves Road, Suite C-101
Austin, Texas 78746

Re: Legal Opinion Regarding Vernon's Article 6228a-5, Sec. 9

Dear Mr. Cochran:

You have asked me to provide a legal opinion as to two questions involving the implementation of Vernon's Article 6228a-5, Sec. 9. You have asked: (1) who is responsible for the enforcement of Section 9; and (2) what are the sanctions for violation of Section 9?

I. Statutory Framework

Article 6228a-5 (the "Act") provides authority to certain government entities to enter into agreements with their employees for the purchase of "qualified investment products," generally through a payroll deduction deposited directly into the investment account. A "qualified investment product" is defined in the statute as: an annuity or investment that meets the requirements of Section 403 (b), Internal Revenue Code; complies with applicable federal insurance and securities laws and regulations; and complies with applicable state insurance and securities laws and rules. *See,* Article 6228a-5, Sec. 4 (5).

The statute provides that only "eligible qualified investments" may be the subject of a school district's payroll deduction. *See*, Article 6228a-5, Sec. 5. To become "eligible," an otherwise "qualified investment product" must be offered by a company that "certifies" to the Teacher Retirement System ("TRS") that the company and the product comply with certain standards as outlined in Section 5 and 6 of the Act. This "certification" may only be rejected or revoked by TRS if TRS receives notice from the company that it no longer meets the statutory standards for certification, *see* Section 5 (c), or if TRS receives notice from the Texas Department of Insurance or the State Securities Board that either agency has determined that a product or company has violated Section 5 of the Act. *See*, Sections 6 (e) and (f).

Section 9 of the Act provides that an educational institution, including a school district, may not, among other things, "refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment." Section 9 (1). The Act does not appear to allow any discretion to the school district regarding which companies and products to make available to its employees, other than they be "eligible qualified investments."

II. Enforcement of Section 9

You have expressed concern that some school districts may be confronted with a situation in which an otherwise "certified" investment may not be in compliance with federal law, particularly the proposed federal regulations that will require each school district to adopt a plan with uniform hardship withdrawal, loan, plan-to-plan and rollover provisions. Faced with such a conflict, you believe that some school districts might consider limiting eligible investments to only those products and companies that comply with the district's plan. You have asked what sanctions a school might be exposed to for such a decision.

As an initial matter, an argument could be made that a school district's decision to limit eligibility to only those products and companies that comply with its plan would not violate the provisions of Section 9. Section 9 prohibits a school district from refusing to enter into a salary reduction agreement for any "eligible qualified investment." An "eligible qualified investment" is a "qualified investment product" that is certified by a company to TRS. Even a "certified" product must meet the definition of a "qualified investment product," which includes that it "meets the requirements of Section 403(b), Internal Revenue Code 1986, and its subsequent amendments." Arguably, a product that does not comply with a school district's plan would not meet the requirements of Section 403(b).

For the purposes of this opinion, I will assume that a school district's decision to refuse to enter into a salary reduction agreement for a product or company duly certified to TRS would be a violation of Section 9. The Act does not explicitly provide for any enforcement mechanism for violations of its provisions, including Section 9, except for the provision of criminal sanctions for certain licensing/marketing violations, which would not apply to the school districts. However, the Act does designate TRS as the agency responsible for administering the provisions of the Act. *See,* Section 6(e). As such, TRS would have the authority to seek enforcement of Section 9, possibly through administrative procedures or by referral to the Attorney General's Office for legal action. Generally, one would expect these enforcement efforts to result in an order directing the non-conforming school district to comply with the Act and allow participation by all certified investment companies. The Act does not provide for any administrative or civil penalties for non-compliance.

A non-conforming school district should also expect enforcement efforts by companies barred from participation. While the Act does not expressly provide for a private cause of action,

a breach of statutory duty often gives rise to a private right of action on behalf of the injured group of persons for whose benefit the statute was enacted. *See, Serv. Employment Redevelopment v. Fort Worth Indep. Sch. Dist.*, 163 S.W. 3d 142, 147 (Tex. App.—Fort Worth 2005, pet. filed). Although one might argue that Section 9 was adopted for the benefit of the school district employees and, thus, only employees could bring an enforcement action, it is probable that a court would find that affected companies were also intended beneficiaries of the prohibitions in Section 9. In addition to an injunction to require a school district to permit all certified companies to participate in the district's retirement program, a company might also seek damages against the district. Whether or not an award of damages would be barred by the doctrine of sovereign immunity is an issue that is currently pending before the Texas Supreme Court. *See, San Antonio Indep. Sch. Dist. v. City of San Antonio*, 2004 WL 2450919 (Tex. App.—San Antonio 2004, pet filed).

III. Conclusion

Section 9 of the Act forbids a school district from refusing to enter into a salary reduction agreement for a qualified investment product if the product is an "eligible qualified investment." A product becomes an "eligible qualified investment" by a company's self-certification to TRS. A school district's failure to comply with Section 9 could result in legal action for an injunction against the school district by the Attorney General on behalf of TRS or legal action for an injunction and damages by the affected companies.

Please feel free to call me if you have any questions about this opinion.

Very truly yours,

Mary F. Keller

Proposed Pre-Emptive Legislation

Testimony to the Texas House of Representatives Pensions and Investments Committee
April 27, 2006
By Mike Cochran, Partner
TCG Consulting, LP
Austin, Texas

Background and Issues:

1. In November 2004 the U.S. Department of the Treasury, Internal Revenue Service (IRS) proposed regulations that would significantly increase the responsibility of public school districts and other employers for retirement plans offered under Section 403(b) of the Internal Revenue Code. The IRS has also announced that they plan to publish final regulations in 2006 that will be effective January 1, 2007. Most experts believe that the final regulations will be substantially the same as the proposed regulations.

2. Most Texas school districts offer 403(b) plans to their employees as the primary vehicle for voluntary tax-deferred payroll savings.

3. Current Texas law prohibits public school districts and other educational institutions from imposing restrictions on companies offering 403(b) accounts in these plans. *See* Vernon's Texas Civil Statutes Article 6228a-5, Section 9(1).

4. Thus, school districts face a strong possibility that they will be required under federal law to take much more responsibility for their plans beginning January 1, 2007, but will be prohibited by Texas law from implementing the controls necessary to comply.

5. We have obtained a legal opinion from Mary Keller, a prominent Austin attorney and former Senior Associate Commissioner of Insurance and General Counsel, Texas Department of Insurance, confirming that there will be a potential conflict between State and Federal law. Her opinion indicates that this conflict could result in litigation and other expenses for Texas public school districts and other educational institutions.

6. If school districts do not have relief on this issue when the new rules become effective January 1, 2007, there is likelihood that some districts will stop offering 403(b) plans to their employees. One of the largest districts in the state has told us that they will consider stopping their 403(b) plan if this conflict is not resolved.

7. Removing the ability for teachers and other school employees to contribute to voluntary tax-deferred payroll savings plans would appear to be an unfortunate and unintended consequence that does not benefit anyone.

8. We believe that Texas law can be changed in a minor way that will remove this potential legal conflict for school districts.

Proposed Pre-Emptive Legislation

Testimony to the Texas House of Representatives Pensions and Investments Committee
By Mike Cochran, Partner
TCG Consulting, LP
Austin, Texas

Outline of Testimony:

I. Background

a. Most Texas public school districts offer 403(b) plans as the primary tax-deferred payroll savings plan for their employees
b. Federal tax law and 403(b) plans
    i. 403(b) = 401(k) plans for public educators
    ii. How 403(b) plans are different from 401(k) and similar plans
        1. It is the only type of pre-tax payroll savings plan with little or no employer control or responsibility
            a. Congress has instructed the IRS to bring more uniformity to all types of tax-deferred payroll savings plans (Small Business Jobs Protection Act of 1996)
        2. There have been no major regulations written by the U.S. Department of Treasury/IRS giving guidance on 403(b) plans since the 1960s.
        3. Many practices with 403(b) plan legal issues are the result of "memorialized mythology" (quote from Tom Reeder, Associate Benefits Tax Counsel, U.S. Department of the Treasury, speaking in Washington, D.C. September 8, 2005).
    iii. In November, 2004, the IRS issued proposed regulations designed to address these three issues:
        1. Provide clear rules on what employers are required to do to assure compliance of 403(b) plans with federal tax laws
        2. Give guidance on all significant aspects of 403(b) plans
        3. Provide clear rules to address practices that have evolved in the industry over the past 40 years
    iv. The IRS has held hearings on the new rules and reviewed many comments from employers and the financial services industry
    v. The IRS has announced that it plans to release final regulations in 2006 with most provisions to be effective January 1, 2007
    vi. Most experts believe that the final regulations will not be substantially different from the proposed regulations, particularly in the area of employer responsibility
c. Texas law and 403(b) plans
    i. The 75th Texas Legislature added Vernon's Texas Civil Statutes Article 6228a-5, Section 9 and other changes to Texas law to provide uniform rules for the operation of these plans in public educational institutions and to protect the rights of employees participating in these plans.
    ii. The Texas Teachers Retirement System (TRS) now oversees which vendors may offer 403(b) plan investments and annuities to school district employees, using guidelines in the law.
    iii. These laws were written to accommodate the way 403(b) plans operated under federal law in 2001.

II. Current Issue

a. According to an opinion we obtained from Mary Keller, former Senior Associate Commissioner of Insurance and General Counsel, Texas Department of Insurance, the new regulations proposed by the IRS will potentially create conflicting liability for school districts.
   i. School districts will be required by the IRS to oversee and control certain 403(b) plan operations. This will include having a written plan that contains the local plan rules
   ii. The IRS rules revolve around local control of each plan. Any penalties or other sanctions for violating 403(b) plan rules will fall to the local school district. There is no concept in the regulations of the local district not having control of the plan under state law.
   iii. Under current Texas law, a school district may not refuse to accept an employee's choice of a 403(b) vendor for his or her payroll deductions, as long as the vendor is on the list of approved vendors maintained by TRS.
   iv. A vendor could easily comply with the rules for being on the TRS list but not cooperate with a local school district's plan rules.
      1. For example, the local district could require a single form for employees to request a distribution from the plan. If a vendor refuses to use the form, the only leverage the district has is to stop the vendor from participating in the district's plan. This action is prohibited under current Texas law.
   v. If a local school district violates Texas law in order to comply with federal regulations by removing a vendor from the district's plan, the district could be sued by the vendor. According to Mary Keller's opinion, the local district may not have sovereign immunity since it would be sued for violating State law.
   vi. On the other hand, if a local school district complies with State law and does not comply with federal regulations, they will face penalties and other sanctions by the IRS in the event of an audit.

b. School districts are not required to offer 403(b) plans to their employees. Thus, rather than fact the conflict between federal and state laws, they could choose to stop offering 403(b) plans. One of our clients, which is also one of the largest school districts in Texas, has indicated that they will seriously consider this solution if they have no other choice.

c. To the extent that this legal conflict causes school districts to stop offering 403(b) plans, the real losers in this issue will be teachers and other school district employees.

III. Proposed Solution

a. We are proposing a minor modification in Article 6228a-5, Section 9. This "housekeeping" amendment or "technical correction" to Texas law would offer relief to school districts.

b. A school district or other educational institution would be allowed to refuse to accept a 403(b) plan payroll deduction request using three criteria:
   i. If the 403(b) vendor does not comply with the educational institution's administrative requirements;
   ii. If such administrative requirements are uniformly imposed on all vendors;
   iii. If such administrative requirements are imposed for the sole reason of complying with changes in employer responsibilities under federal tax laws applicable to 403(b) plans effective after December 31, 2006.

c. We believe these changes would correct the conflict without disrupting the current Texas 403(b) rules as changed by the 75th Legislature.

Meeting with Rep. Vicki Truitt
February 8, 2007

TCG Consulting, LP
Mike Cochran, Partner

Items to Discuss:

1. Pre-Emptive Legislation on 403(b) Plans to Prevent Conflict between State and Federal Rules

2. Potential Harmful Legislation on 457(b) Plans

3. TRS Sunset Commission report on 403(b) Plans and Possible Unintended Consequences for Public School Districts

4. TRS Service Credit for Prior Service in Private Schools

-----Original Message-----
From: Mike Cochran [mailto:mike.cochran@pension-consulting.com]
Sent: Monday, April 09, 2007 12:50 PM
To: dan.sutherland@house.state.tx.us
Cc: Mike Cochran; Andrea McWilliams; John Pesce
Subject: HB 2341 Proposed change to accommodate TRS Sunset Bill

Dan -

Thank you for discussion the 403(b) issue in the TRS Sunset bill (HB 2427) with Andrea McWilliams and me on Thursday.

Attached is our proposed revision to HB 2341 that you suggested we make to address this issue.

My reasoning for the changed language is that (a) HB 2341 already would allow an educational institution to refuse to enter into a salary reduction agreement with a company that does not comply with its administrative requirements, (b) the requirements in the current bill must be imposed uniformly on all vendors and be required by a change in IRS rules, and (c) the proposed additional change would allow the imposition of such uniform administrative requirements due to a change in Article 6228a-5, Vernon's Texas Civil Statutes, that will require any action by an educational institution.

The latter (item (c)) is what HB 2427 would do -- it would change Article 6228a-5, Vernon's Texas Civil Statutes to add the requirement for registered products as well as registered companies and it would require the school districts to monitor this. The proposed change would allow school districts to impose administrative rules on the vendors to help enforce this. Thus, Grapevine-Colleyville ISD could have a rule requiring the vendors to certify that they will only sell registered products. If the vendor violates this, G-CISD could refuse to enter into any salary reduction agreements with them.

The wording is broad. However, it also keeps the statute flexible for future changes in this area. Anytime the Legislature changes this area of the law, and it adds administrative requirements to educational institutions, the institutions can impose rules on the vendors to help ease the administrative burden. It would be difficult to abuse this, since (a) the rules would still have to be imposed universally on all vendors and (b) the statute could only be invoked if the Legislature changes to Article 6228a-5 that would require some action by the institutions.

Please let us know what you think.

Thanks
Mike

Mike Cochran
TCG Consulting LP
4201 Bee Caves Road, Suite C-101
Austin, TX 78746
Phone 512-306-9939; Fax 512-306-9959
Cell 512-415-2854

Email: mike.cochran@pension-consulting.com
Website: www.pension-consulting.com

By: Truitt H.B. No. 2341

A BILL TO BE ENTITLED

AN ACT

relating to certain investment products made available to certain public school employees.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. Section 9, Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 9. (a) An educational institution may not:

(1) except as provided by Subsection (b) of this section, refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment;

(2) require or coerce an employee's attendance at any meeting at which qualified investment products are marketed;

(3) limit the ability of an employee to initiate, change, or terminate a qualified investment product at any time the employee chooses;

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products; or

(7) use public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product.

(b) An educational institution may refuse to enter into a salary reduction agreement with an employee if:

(1) the eligible qualified investment product that is the subject of the salary reduction agreement is offered by a company that does not comply with the educational institution's administrative requirements;

(2) the educational institution imposes the administrative requirements uniformly on all companies that offer eligible qualified investment products; and

(3) the administrative requirements are necessary to comply with employer responsibilities imposed by:

(A) Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) any other provision of the Internal Revenue Code of 1986 that applies to Section 403(b);

(C) any regulation adopted in relation to a law described by Paragraph (A) or (B) of this subdivision that is effective after December 31, 2007 or

(D) any change to this Act that becomes effective after January 1, 2007.

SECTION 2. This Act takes effect September 1, 2007.

FLOOR AMENDMENT NO._____ BY: _____

Amend H.B. No. 2341 (committee printing) as follows:

(1) On page 2, line 23, strike "or".

(2) On page 2, line 26, between "2007" and the underlined period, insert:

; or

(D) any change to this Act that becomes effective after January 1, 2007.

BILL ANALYSIS

H.B. 2341
By: Truitt
Pensions & Investments
Committee Report (Unamended)

BACKGROUND AND PURPOSE

In November 2004, the U.S. Department of the Treasury, Internal Revenue Service (IRS) proposed regulations that would increase the responsibility of public school districts and other employers for retirement plans offered under Section 403(b) of the Internal Revenue Code. Some Texas school districts offer 403(b) plans to their employees as the primary vehicle for voluntary tax-deferred payroll savings.

Current Texas law prohibits public school districts and other educational institutions from imposing restrictions on companies offering 403(b) accounts in these plans. Thus, school districts face the possibility that they will be required, under federal law, to take more responsibility for their plans beginning January 1, 2007, but will be prohibited by Texas law from implementing the controls necessary to comply.

This bill removes a potential conflict between federal and state law by allowing a school district or other educational institution to refuse to accept a 403(b) plan payroll reduction request under certain circumstances.

RULEMAKING AUTHORITY

It is the committee's opinion that this bill does not expressly grant any additional rulemaking authority to a state officer, department, agency, or institution.

ANALYSIS

This bill allows an educational institution to refuse to enter into a salary reduction agreement with an employee if the eligible qualified instrument that is the subject of the agreement is offered by a company and does not comply with the educational institution's administrative requirements so long as those administrative requirements are imposed uniformly on all companies that offer eligible qualified investment products and are necessary to comply with employer responsibilities imposed by Section 403(b), Internal Revenue Code of 1986, or any other provisions of the IRS Code.

EFFECTIVE DATE

September 1, 2007.

Writer's Letterhead

May 17, 2007

Senator Robert Duncan
P.O. Box 12068, Capitol Station
Austin, TX 78711

Re: HB 2341

Dear Senator Duncan:

This letter is to express my support of HB 2341 and to request that you introduce it for a vote of the Senate without any amendments.

The purpose of HB 2341 as it is written is simply to preempt a conflict between federal and state law. I understand this is likely to occur in January 2008 when the Internal Revenue Service is expected to make new final regulations regarding 403(b) plans effective.

If this bill does not pass, Texas public school districts will face a choice between complying with federal or state law, or eliminating their 403(b) plans. I am concerned that special interests are seeking amendments to HB 2341 that will change its simple intent to preempt this conflict.

Thank you for your consideration of my request.

Sincerely,

HB 2341

Authored by Representative Vicki Truitt

In 2001 the Texas Legislature passed Senate Bill 273 which became Article 6228 a-5, Vernon's Texas Civil Statutes and Texas Administrative Code Title 34, Part 3, Chapter 53. This bill attempted to address abuses in the 403(b) industry in Texas. It also restricted the authority of public schools to restrict access of employees to TRS approved vendors or create barriers interfering with teachers and school employees from access to a wide range of 403(b) choices.

When the IRS proposed new regulations for the 403(b) voluntary federal pension in 2004, it appeared that local districts would need the help of the legislature to meet both the SB 273 law and the new 403(b) regulations.

In 2001, 1st American provided consultation on all sections of SB 273 and was contacted in 2005 by TCG Consulting, L.P. (TCG) to join the effort in helping school districts comply with both IRS regulations and SB 273.

TCG obtained an opinion from attorney, Mary Keller, of the law firm of York, Keller & Field, L.L.P. (now Winstead PC) as to the potential effect of this conflict. Ms. Keller is a former Senior Associate Commissioner of Insurance in the Texas Department of Insurance and Deputy Attorney General in the Texas Attorney General's Office. Her opinion confirmed that districts would face a major conflict between state and federal law that could potentially leave districts with an untenable choice.

TCG contacted Rep. Craig Eiland, then Chair of the House Committee on Pensions and Investments, about the issue. He held hearings on the subject and introduced House Bill 169 in 2006 (the third special session) to provide relief to school districts on this issue.

When Rep. Vicki Truitt became Chair of the Committee in the 80th session of the Legislature, she and her staff reviewed the issue and worked diligently to get the bill passed unanimously through both houses of the Legislature. The Governor signed the bill in June 2007.

It is important to note that the law does not allow districts to exclude TRS approved vendors or products for any other reason than to comply administratively with IRS rules.

We want to gratefully acknowledge the leadership of Rep. Vicki Truitt, Chair of the Texas House Committee on Pensions & Investments and her predecessor Chair of this Committee, Representative Craig Eiland. Without the efforts of these legislators, Texas public school districts would face a major conflict between the requirements of the new 403(b) regulations and Texas law.

We also thank TCG Consulting for their foresight and willingness to help school districts. Other than TCG and 1st American, no other companies or entities outside of the Legislature assisted in this effort.

VERNON'S CIVIL STATUTES

TITLE 109. PENSIONS

Art. 6228a-5. ANNUITIES OR INVESTMENTS FOR CERTAIN PUBLIC EMPLOYEES; SALARY REDUCTIONS.

Sec. 1. (a) This section and Section 2 of this Act apply to:

(1) the governing boards of state-supported institutions of higher education;

(2) the Texas Higher Education Coordinating Board;

(3) the Texas Education Agency;

(4) the Texas School for the Deaf;

(5) the Texas School for the Blind and Visually Impaired;

(6) the Texas Department of Mental Health and Mental Retardation and the state schools, state hospitals, and other facilities and institutions under its jurisdiction;

(7) the Texas Department of Health and facilities and institutions under its jurisdiction;

(8) the Texas Juvenile Justice Department and facilities and institutions under its jurisdiction; and

(9) the governing boards of Centers for Community Mental Health and Mental Retardation Services, county hospitals, city hospitals, city-county hospitals, hospital authorities, hospital districts, affiliated state agencies, and each of their political subdivisions.

(b) An entity described by Subsection (a) of this section may enter into agreements with the entity's employees for the purchase of annuities or for contributions to any type of investment for the entity's employees as authorized in Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments.

Sec. 2. (a) If an employee of an entity covered by Section 1 of this Act is paid by the Comptroller of Public Accounts, the comptroller may take the action, in regard to that employee, that is authorized by Subsection (b) of this section. If an employee of an entity covered by Section 1 is not paid by the comptroller, the governing board of the entity may take the action in regard to that employee.

(b) The comptroller or the governing board, as appropriate, may:

(1) reduce the salary of participants when authorized by the participants and shall apply the amount of the reduction to the purchase of annuity contracts or to contributions to any type of investment authorized in

Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments, the exclusive control of which will vest in the participants; and

(2) develop a system to allow or require participants to electronically authorize:

(A) participation under this Act;

(B) purchases of annuity contracts; and

(C) contributions to investments.

Sec. 3. (a) A state agency may permit some or all of the employees of the agency to participate in an employer-sponsored program described by Section 457(f) of the Internal Revenue Code of 1986, including subsequent amendments of that law.

(b) Repealed by Acts 2003, 78th Leg., ch. 1111, Sec. 46(10), eff. Sept. 1, 2003.

(c) In this section, "state agency" means a board, office, commission, department, institution, court, or other agency in any branch of state government.

Sec. 4. In this section and in Sections 5, 6, 7, 8, 8A, 9, 9A, 9B, 10, 11, 12, and 13 of this Act:

(1) "Board of trustees" means the board of trustees of the Teacher Retirement System of Texas.

(2) "Educational institution" means a school district or an open-enrollment charter school.

(3) "Eligible qualified investment" means a qualified investment product offered by a company that:

(A) is certified to the board of trustees under Section 5 of this Act; or

(B) is eligible to certify to the board of trustees under Section 8 of this Act.

(4) "Employee" means an employee of an educational institution.

(5) "Qualified investment product" means an annuity or investment that:

(A) meets the requirements of Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) complies with applicable federal insurance and securities laws and regulations; and

(C) complies with applicable state insurance and securities laws and rules.

(6) "Retirement system" means the Teacher Retirement System of Texas.

(7) "Salary reduction agreement" means an agreement between an educational institution and an employee to reduce the employee's salary for the purpose of making direct contributions to or purchases of a qualified investment product.

Sec. 5. (a) An educational institution may enter into a salary reduction agreement with an employee of the institution only if the qualified investment product:

(1) is an eligible qualified investment; and

(2) is registered with the retirement system under Section 8A of this Act.

(b) A company may certify to the retirement system that the company offers a qualified investment product that is an annuity contract under this section if the company:

(1) is authorized to issue annuity contracts in this state at the time the application is filed;

(2) does not assess fees, costs, or penalties on an annuity contract that exceed the maximum amounts established by rules adopted by the retirement system; and

(3) complies with the standards adopted under Section 6 of this Act.

(c) A company that certifies under this section shall notify the retirement system if, at any time, the company is not in compliance with Subsection (b) of this section or if an investment product that the company offers under this Act is the subject of a salary reduction agreement and the investment product is not a qualified investment product.

(d) The retirement system shall establish and maintain a list of companies that have certified under this section. The list must be available on the retirement system's Internet website.

(e) An employee is entitled to designate any agent, broker, or company through which a qualified investment product may be purchased or contributions may be made.

(f) To the greatest degree possible, employers of employees who participate in the program offered under this section shall require that contributions to eligible qualified investments be made by automatic payroll deduction and deposited directly in the investment accounts.

Sec. 6. (a) A company is eligible to certify to the retirement system under Section 5 of this Act if the company satisfies the following financial strength criteria:

(1) the company's actuarial opinions required under Articles 1.11 and 3.28, Insurance Code, have not been adverse or qualified in the five years preceding the date the application is filed;

(2) the company is subject to the annual audit requirements of Article 1.15A, Insurance Code, and its most recent audit of financial strength conducted by an independent certified public accountant is timely filed and does not indicate the existence of any material adverse financial conditions in the company for the five years preceding the filing deadline for the audit;

(3) the company has not been the subject of an administrative or regulatory action by the Texas Department of Insurance under Article 1.32 or 21.28-A or Section 83.051, Insurance Code, in the five years preceding the date the application is filed;

(4) the company has maintained during the five years preceding the date the application is filed an average of at least 400 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus requirements established in rules adopted by the Texas Department of Insurance;

(5) the company has not fallen below 300 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus established in rules adopted by the Texas Department of Insurance, at any time in the five years preceding the date the application is filed; and

(6) the company has at least five years' experience in qualified investment products and has a specialized department dedicated to the service of qualified investment products.

(b) For purposes of Subsection (a)(4) of this section, the company must calculate the five-year average on the same date each year.

(c) After consultation with the Texas Department of Insurance, the Texas Department of Banking, and the State Securities Board, the retirement system may adopt rules only to administer this section and Sections 5, 7, 8, 8A, 9A, 9B, 11, 12, and 13 of this Act.

(d) The retirement system shall refer all complaints about qualified investment products, including complaints that allege violations of this Act by companies that certify to the retirement system under Section 5 or 8 of this Act that the companies offer qualified investment products, to the appropriate division of the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board.

(d-1) Except as provided by Subsection (d-2) of this section, the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board shall investigate a complaint received from the retirement system under Subsection (d) of this section. If as a result of the

investigation the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board, as applicable, determines that a violation of this Act may have occurred, the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board, as applicable, shall forward the results of the investigation relating to an alleged violation of this Act to the attorney general.

(d-2) If the Texas Department of Banking receives a complaint from the retirement system under Subsection (d) of this section that relates to a federally chartered financial institution, the Texas Department of Banking shall:

(1) refer the complaint to the appropriate federal regulatory agency; and

(2) notify the attorney general of the department's referral.

(e) The Texas Department of Insurance, the Texas Department of Banking, and the State Securities Board shall cooperate with the retirement system in the administration of this Act and shall:

(1) submit a report to the retirement system at the beginning of each quarter of the fiscal year that provides the status of any enforcement action taken or investigation or referral made regarding a product or a company that is the subject of a complaint under Subsection (d) of this section; and

(2) promptly notify the retirement system of any final enforcement order issued regarding the product or company.

(f) The retirement system may deny, suspend, or revoke the certification of a company if the retirement system receives notice that the company or the company's product was determined to be in violation of this Act or another law in any judicial or administrative proceeding.

(f-1) A company whose certification is denied, suspended, or revoked under this section may recertify to the board of trustees after any applicable period of suspension or revocation.

(g) The retirement system shall prescribe the uniform notice required by Section 11 of this Act.

(h) A certification or recertification remains in effect for five years unless denied, suspended, or revoked.

(i) A company offering eligible qualified investments that are subject to salary reduction agreements must provide toll-free telephone transferring privileges each business day from 8 a.m. to 6 p.m. central standard time.

Sec. 7. (a) The retirement system may collect a fee, not to exceed the administrative cost to the retirement system, from a company that certifies or recertifies under Section 6 or 8 of this Act or that registers a qualified investment product under Section 8A. The fee for certification or recertification may not exceed $5,000. The fee for registration of a

qualified investment product must be set by the retirement system in the reasonable amount necessary to recover the cost to the system of administering Section 8A of this Act.

(b) Fees collected under this section shall be deposited to the credit of the 403(b) administrative trust fund. The 403(b) administrative trust fund is created as a trust fund with the comptroller and shall be administered by the retirement system as a trustee on behalf of the participants in qualified investment products offered under this Act.

Sec. 8. (a) A company that offers qualified investment products other than annuity contracts, including a company that offers custodial accounts under Section 403(b)(7), Internal Revenue Code of 1986, that hold only investment products registered with the system under Section 8A of this Act, may certify to the retirement system based on rules adopted by the board of trustees. The rules shall be based on reasonable factors, including:

(1) the financial strength of the companies offering products; and

(2) the administrative cost to employees.

(b) The retirement system shall establish and maintain a list of companies that provide certification under this section. The list must be available on the retirement system's Internet website.

Sec. 8A. (a) A qualified investment product offered to an employee under Section 5 of this Act must be an eligible qualified investment registered with the retirement system under this section. To register a product, the company offering the product must submit an application to the retirement system in accordance with this section and pay the registration fee established under Section 7 of this Act.

(b) The retirement system shall adopt the form and content of the registration application.

(c) The retirement system shall designate not more than two registration periods each year during which a company may apply to register a qualified investment product and add the product to the list of qualified investment products maintained under Subsection (f) of this section. To register a qualified investment product, a company must submit an application for a designated registration period in the manner required by the retirement system.

(d) A company that registers a qualified investment product under this section shall notify the retirement system if, at any time, the product is not an eligible qualified investment.

(e) A registration under this section remains in effect for five years unless denied, suspended, or revoked.

(f) The retirement system shall establish and maintain a list of qualified investment products that are registered under this section. The list must include information concerning all the fees charged in connection

with each registered qualified investment product and the sale and administration of the product. The list must include other information concerning each product as determined by the retirement system. In implementing the list, the retirement system shall take action to avoid increasing the amount of work required of educational institutions, which may include assigning a unique identifying number to each product. The list must be available on the retirement system's Internet website.

Sec. 9. (a) An educational institution may not:

(1) except as provided by Subdivision (8) of this subsection and Subsection (b) of this section, refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment and is registered with the system under Section 8A;

(2) require or coerce an employee's attendance at any meeting at which qualified investment products are marketed;

(3) limit the ability of an employee to initiate, change, or terminate a qualified investment product at any time the employee chooses;

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent or affiliate of a company offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products;

(7) use public funds to recommend a qualified investment product offered by a company or an agent or affiliate of a company that offers a qualified investment product; or

(8) enter into or continue a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction agreement is not an eligible qualified investment, including the investment product of a company whose certification has been denied, suspended, or revoked without first providing the employee with notice in writing that:

(A) indicates the reason the subject of the salary reduction agreement is no longer an eligible qualified investment or why certification has been denied, suspended, or revoked; and

(B) clearly states that by signing the notice the employee is agreeing to enter into or continue the salary reduction agreement.

(b) An educational institution may refuse to enter into a salary reduction agreement with an employee if:

(1) the eligible qualified investment product that is the subject of the salary reduction agreement is offered by a company that does not comply with the educational institution's administrative requirements;

(2) the educational institution imposes the administrative requirements uniformly on all companies that offer eligible qualified investment products; and

(3) the administrative requirements are necessary to comply with employer responsibilities imposed by:

(A) Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) any other provision of the Internal Revenue Code of 1986 that applies to Section 403(b);

(C) any regulation adopted in relation to a law described by Paragraph (A) or (B) of this subdivision that is effective after December 31, 2007; or

(D) any change to this Act that becomes effective after January 1, 2007.

Sec. 9A. A person, other than an employee of an educational institution, or an affiliate of the person may not enter into or renew a contract under which the person is to provide services for or administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986, unless the person:

(1) holds a license or certificate of authority issued by the Texas Department of Insurance;

(2) is registered as a securities dealer or agent or investment advisor with the State Securities Board; or

(3) is a financial institution that:

(A) is authorized by state or federal law to exercise fiduciary powers; and

(B) has its main office, a branch office, or a trust office in this state.

Sec. 9B. (a) This section applies to an entity under this Act that enters into a contract with an educational institution to administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986.

(b) If a person described by Subsection (a) holds a meeting at which qualified investment products will be marketed to employees of the educational institution, the person must provide representatives of other companies certified to the retirement system under Section 5 or 8 of this Act an opportunity to attend and market their qualified investment products at the meeting.

Sec. 10. (a) A person commits an offense if the person:

(1) sells or offers for sale an investment product that is not an eligible qualified investment or that is not registered under Section 8A of this Act and that the person knows will be the subject of a salary reduction agreement;

(2) violates the licensing requirements of Title 13, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement; or

(3) engages in activity described by Subchapter B, Chapter 541, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement.

(b) An offense under this section is a Class A misdemeanor.

(c) If conduct that constitutes an offense under this section also constitutes a criminal offense under the Insurance Code, the actor may be prosecuted under this section or under the Insurance Code, but not under both this section and the Insurance Code.

Sec. 10A. (a) A person who violates this Act is subject to a civil penalty in an amount that does not exceed:

(1) $10,000 for a single violation; or

(2) $1,000,000 for multiple violations.

(b) For purposes of determining the amount of a civil penalty under this section, the court shall consider the following factors:

(1) the seriousness, nature, circumstances, extent, and persistence of the conduct constituting the violation;

(2) the harm to other persons resulting directly or indirectly from the violation;

(3) cooperation by the person in any inquiry conducted by the state concerning the violation, efforts to prevent future occurrences of the violation, and efforts to mitigate the harm caused by the violation;

(4) the history of previous violations by the person;

(5) the need to deter the person or others from committing such violations in the future; and

(6) other matters as justice may require.

(c) The attorney general may institute an action:

(1) for injunctive relief to restrain a violation by a person who is or who appears to be in violation of or threatening to violate this Act; or

(2) to collect a civil penalty under this section.

(d) An action under this section must be filed in a district court in Travis County.

(e) The attorney general may recover reasonable expenses incurred in obtaining injunctive relief under this section, including court costs, reasonable attorney's fees, investigative costs, witness fees, and deposition expenses.

Sec. 11. (a) A person who offers to sell an annuity contract that is or will likely be the subject of a salary reduction agreement shall provide notice to a potential purchaser as provided by this section.

(b) The retirement system shall make the notice available on request and post the form of the notice on the retirement system's Internet website.

(c) The notice required under this section must be uniform and:

(1) be in at least 14-point type;

(2) contain spaces for:

(A) the name, address, and telephone number of the agent and company offering the annuity contract for sale;

(B) the name, address, and telephone number of the company underwriting the annuity;

(C) the license number of the person offering to sell the product;

(D) the name of the state agency that issued the person's license;

(E) the name of the company account representative who has the authority to respond to inquiries or complaints; and

(F) with respect to fixed annuity products:

(i) the current interest rate or the formula used to calculate the current rate of interest;

(ii) the guaranteed rate of interest and the percentage of the premium to which the interest rate applies;

(iii) how interest is compounded;

(iv) the amount of any up-front, surrender, withdrawal, deferred sales, and market value adjustment charges or any other contract restriction that exceeds 10 years;

(v) the time, if any, the annuity is required to be in force before the purchaser is entitled to the full bonus accumulation value;

(vi) the manner in which the amount of the guaranteed benefit under the annuity is computed;

(vii) whether loans are guaranteed to be available under the annuity;

(viii) what restrictions, if any, apply to the availability of money attributable to the value of the annuity once the purchaser is retired or separated from the employment of the employer;

(ix) the amount of any other fees, costs, or penalties;

(x) whether the annuity guarantees the participant the right to surrender a percentage of the surrender value each year, and the percentage, if any; and

(xi) whether the annuity guarantees the interest rate associated with any settlement option; and

(3) state, in plain language:

(A) that the company offering the annuity must comply with Section 5 of this Act and that the annuity must be a qualified investment product registered under Section 8A of this Act;

(B) that the potential purchaser may contact the retirement system or access its Internet website to determine which companies are in compliance with Section 5 of this Act and which qualified investment products are registered under Section 8A of this Act;

(C) the civil remedies available to the employee;

(D) that the employee may purchase any eligible qualified investment through a salary reduction agreement;

(E) the name and telephone number of the Texas Department of Insurance division that specializes in consumer protection; and

(F) the name and telephone number of the attorney general's division that specializes in consumer protection.

(d) A variable annuity must be accompanied by:

(1) a notice that includes any item listed in Subsection (c) of this section that is applicable to variable annuities;

(2) the prospectus; and

(3) any other purchasing information required by law.

(e) An equity-based index contract must state in plain language how the annuity contract will be credited with growth.

(f) If a notice and other information required under this section is not provided, any annuity contract for which the notice is required is voidable at the discretion of the purchaser. Not later than the 30th day after the date an employee notifies the seller in writing of the employee's election to void the contract, the seller shall refund to the employee:

(1) the amount of all consideration paid to the purchaser; and

(2) 10 percent interest up to the date the employee provides the notice to the seller.

(g) A seller who receives a refund request under this section is not required to make a refund otherwise required by this section if, not later than the 30th day after the date the seller receives a request for a refund from the employee, the seller provides a copy of the notice signed by the employee.

Sec. 12. A company that offers an eligible qualified investment that is subject to a salary reduction agreement shall demonstrate annually to the retirement system that each of its representatives are properly licensed and qualified, by training and continuing education, to sell and service the company's eligible qualified investments.

Sec. 13. (a) The board of trustees may deny, suspend, or revoke the certification or recertification of a company if the company violates Section 5, 6, 7, 8, 8A, 10, 11, or 12 of this Act or a rule adopted under those sections.

(b) The board of trustees may deny, suspend, or revoke the registration of an investment product under this section if:

(1) the product is not an eligible qualified investment;

(2) the offer of the product violates Section 5, 6, 7, 8, 8A, 10, 11, or 12 of this Act or a rule adopted under those sections; or

(3) the company that offers the product violates Section 5, 6, 7, 8, 8A, 10, 11, or 12 of this Act or a rule adopted under those sections.

(c) A proceeding to suspend or revoke a certification, recertification, or registration under this section is a contested case under Chapter 2001, Government Code.

Acts 1962, 57th Leg., 3rd C.S. p. 60, ch. 22, Sec. 1. Amended by Acts 1969, 61st Leg., p. 2297, ch. 774, Sec. 2, eff. Sept. 1, 1969; Acts 1971, 62nd Leg., p. 925, ch. 139, Sec. 1, eff. May 10, 1971; Acts 1971, 62nd Leg., p. 2372, ch. 733, Sec. 1, eff. June 8, 1971; Acts 1981, 67th Leg., p. 1862, ch. 441, Sec. 1, eff. June 11, 1981; Acts 1983, 68th Leg., p. 188, ch. 44, art. IV, Sec. 6, eff. April 26, 1983; Acts 1985, 69th Leg., ch. 740, Sec. 1, eff. Aug. 26, 1985; Acts 1993, 73rd Leg., ch. 449, Sec. 6, eff. Sept. 1, 1993; Acts 1993, 73rd Leg., ch. 791, Sec. 53, eff. Sept. 1, 1993; Acts 1997, 75th Leg., ch. 1340, Sec. 8, eff. Sept. 1, 1997; Acts 1997, 75th Leg., ch. 1341, Sec. 7, eff. Sept. 1, 1997; Acts 2001, 77th Leg., ch. 1229, Sec. 21, 22, 23, eff. Sept. 1, 2001.

TCG Consulting
TOTAL COMPENSATION GROUP
Total Compensation Group Consulting LP
TCG Advisors LP, a Registered Investment Advisor
4201 Bee Caves Road, Suite C-101
Austin, TX 78746
Phone: (512) 306-9939 Fax: (512) 306-9959

October 14, 2007

Rep. Vicki Truitt
Texas House of Representatives
P.O. Box 2910
Austin, TX 78768

Re: H.B. 2341

Dear Rep. Truitt:

This letter is to thank you very much for sponsoring H.B. 2341 and for your efforts to get this passed. We also greatly appreciate the work of your staff on this issue, particularly that of Mr. Dan Sutherland.

The changes in Texas law that resulted from the bill are already helping Texas public school districts avoid a conflict between Internal Revenue Service rules on 403(b) plans and Texas law, as it existed previously.

The IRS issued 130 pages of new final 403(b) plan regulations in July of this year. As we predicted, these new rules create major additional responsibilities for Texas public school districts. Your bill is helping assure that districts have the power and tools to comply with the new IRS rules.

Enclosed is the Fall, 2007 issue of *Insight* magazine, the official journal of the Texas Association of School Administrators. On page 23 you will find an article that I wrote describing the new IRS rules and gives credit to you and your bill for allowing school districts to comply with these rules.

If you have any questions, please let me know.

Sincerely,

Mike Cochran
Partner

cc: Andrea McWilliams
Dean McWilliams
John Pesce

The Final 403(b) Regulations:
New School District Responsibilities on the Horizon

By Mike Cochran, TCG Group Holdings, LLP

Article in Fall Edition of *Insight Magazine*,
Official Publication of the Texas Association of School Administrators

Tens of thousands of Texas educators depend on 403(b) accounts ("tax sheltered annuities") to supplement their retirement savings. All or almost all Texas school districts offer these plans to their employees. Both school districts and their employees will soon experience radical changes in how their 403(b) plans work.

On July 23, 2007, the Internal Revenue Service (IRS) issued final regulations applicable to plans offered by employers under Section 403(b) of Internal Revenue Code (the Code). You can find the full publication at:

http://www.ustreas.gov/press/releases/reports/td%2093403_checked_.pdf

This article will discuss only the effect of the new regulations on public school districts, particularly those in Texas. It attempts to address the most important issues that will effect public educational organizations and their employees.

We also want to gratefully acknowledge the leadership of Representative Vicki Truitt, Chair of the Texas House Committee on Pensions & Investments and her predecessor Chair of this Committee, Representative Craig Eiland. Without the efforts of these legislators, Texas public school districts would face a major conflict between the requirements of the new 403(b) regulations and Texas law.

Background of New Regulations

It is important to understand the enforcement issues that the IRS is trying to address with the new rules.

In the mid-1990s the IRS issued audit guidelines for 403(b) plans and began a large-scale enforcement program. In public school districts and other applicable governmental organizations, this consisted primarily of auditing the annual contribution limits. As a result of the IRS enforcement efforts, most education organizations either hired third party administrators to monitor the contribution limits or programmed their payroll systems to monitor them.

The IRS is now focused on "cleaning up" the other aspects of 403(b) plan compliance. The final regulations address two areas that are necessary to assure compliance of 403(b) plans with all aspects of the tax rules:

1. **Outdated Rules.** The prior 403(b) regulations were outdated. For the most part, they had not been revised since the mid-1960s. In addition, many practices with regard to these plans were either unclear or were not documented in the Code and regulations. Tom Reeder, Associate Benefits Tax Counsel, U.S. Department of the Treasury, in one speech referred to many of these unwritten 403(b) rules as "memorialized mythology."

2. **Clear Accountability.** There has been no clear accountability with the prior 403(b) rules. In practice, it is difficult for employers to be held accountable for anything other than assuring that employees do not over-contribute to their plans. Most employers currently leave enforcement of other rules to the vendors. There are three primary problems with this practice:

    a. There is wide disparity in how vendors enforce (or do not enforce) rules regarding loans, distributions, hardship withdrawals and other tax/plan rules.
    b. Employees can transfer their funds to any vendor they choose, even if the vendor is not accepting payroll deductions from the employer. Thus, employers often have no idea what vendors are even handling funds in their plans.
    c. The IRS has little enforcement jurisdiction over the operations of vendors. It will be easier for the IRS to enforce 403(b) rules if employers have more control of and responsibility for 403(b) plans.

It is also important to note that the Treasury and IRS spokespeople have stated their intention to make 403(b) plan rules and enforcement much more like 401(k) and 457(b) plans, where employers already have significant compliance responsibility. The regulations include a statement that the effect of changes in 403(b) plan rules over the past 40 years has been to *"diminish the extent to which the rules governing section 403(b) plans differ from the rules governing other arrangements that include salary reduction contribution, i.e., section 401(k) plans and section 457(b) plans for State and local governmental entities."*

The final regulations take a significant step in making 403(b) plans much more like other employer sponsored and controlled tax-deferred plans.

Summary of New Regulations

Written Plan

The new IRS regulations require a "written plan." There is not a specified form that is required by the regulation. Thus, an employer is not required to have a "plan document" in the traditional sense. Rather, all the provisions of the employer's 403(b) plan must be written in one document or collection of documents that is maintained by the employer. The employer may also delegate duties to vendors or third party administrators. However, ultimately the IRS wants the employer to have some form of plan that coordinates all plan rules and assures that there are no conflicting rules.

The preamble to the final regulations states, "the final regulations clarify the requirement that the plan include all of the material provisions by permitting the plan to incorporate by reference other documents, including the insurance policy or custodial account, which as a result of such reference would become part of the plan. As a result, a plan may include a wide variety of documents, but it is important for the employer that adopts the plan to ensure that there is no conflict with other documents that are incorporated by reference. If a plan does incorporate other documents by reference, then, in the event of a conflict with another document, except in rare and unusual cases, the plan would govern. In the case of a plan that is funded through multiple issuers, it is expected that an employer would adopt a single plan document to coordinate administration among the issuers, rather than having a separate document for each issuer."

It is important to note that compliance responsibilities <u>may not</u> be delegated to participants. It has been the practice for some school districts to ask employees to sign forms taking responsibility for certain types

of compliance with 403(b) rules, such as keeping their contributions within the limits of the Code. The IRS expressly rejected this practice.

The IRS has announced that it will provide a model written plan for employers to use in the near future. In a web cast in August, Robert Architect, Senior Tax Law Specialist at the IRS, indicated that the model plan would be released sometime in October 2007.

Plan Distributions and Loans

Distributions and loans to participants will have to follow the written plan. The new regulations require an employer to monitor distributions to assure compliance with the written plan. This may be the second most significant change in the new regulations (next to the written plan requirement). Most employers have viewed the compliance responsibility for distributions and loans as an issue between the participant and his or her vendor. This will now change.

Like other duties, the employer may delegate this responsibility to a vendor or third party administrator. However, the employer must specify which duties are delegated and assure that the plan rules are followed in a consistent manner.

Participant Transfers from One 403(b) Vendor to Another

A major issue for employers and participants that will affect them immediately is the ability to transfer from one 403(b) account to another. The regulations will repeal Revenue Ruling 90-24 effective September 24, 2007. This ruling allowed participants to transfer funds from one 403(b) account to another 403(b) account on a tax-free basis at will.

The new regulations only allows for transfers of funds between 403(b) accounts when the following rules are met:

1. The written plan provides for the transfer.
2. The value transferred is the same after the transfer as it was immediately before. Since many annuity contracts have surrender charges, this would appear on the surface to stop transfers that would result in a reduction of the value of account after the transfer. Some industry comments have reflected this view. However, the regulations tie the final rule to Section 414(l) of the Code, which, according to Robert Architect (in several public speeches), does not prohibit the imposition of distribution charges, surrender charges and other similar arrangements.
3. The employer enters into an agreement with the vendors that are allowed to participate in the transfers to exchange data about the participants making transfers. This data will be used by the vendor and employer to assure compliance with 403(b) rules.

Thus, there appear to be two significant problems for participants who want to transfer their 403(b) accounts from one vendor to another. First, they may not be able to make the transfer if there is any penalty imposed on the account value by the transferor (depending on the interpretation of the rules, per item 2 above). Second, from September 25, 2007 to January 1, 2009, many participants may not be able to make transfers. This is because the old transfer rules end on September 24, 2007 but employers are not required to implement the new rules until January 1, 2009. The latter will depend on how and when employers and vendors implement new transfer rules. It is also important to note that these same rules apply to beneficiaries of participants' accounts, in the event of the participant's death.

Similar rules are provided for transfers between the 403(b) plan of one employer and another. However, normally a participant is transferring an account because he or she is changing employers. Termination of employment is a qualifying event that entitles the participant to receive a distribution. Under distribution rules, the participant can simply rollover their funds to an Individual Retirement Account (IRA) or other tax-qualified vehicle (see rollover discussion below).

An interesting additional issue will face Texas school districts in addressing transfers. Currently Texas statutes do not allow a participant to enter into a 403(b) salary reduction agreement with a vendor that is not on the approved list maintained by the Texas Teachers Retirement System (TRS). However, Texas statutes do not appear to address 403(b) transfers. Thus, a school district would appear to have the ability to allow transfers to a vendor that is not on the TRS approved list (but not ongoing salary deferrals), if they choose to do this in their written plan.

Rollovers

It is common for employers and participants to use the terms transfer and rollovers interchangeably. However, there are important distinctions between these. A transfer is either an exchange of 403(b) funds with one vendor to another vendor within the employer's plan, a transfer of a 403(b) account from one employer's plan to another, or a transfer of 403(b) funds to TRS to purchase certain types of service credit. A rollover occurs when a 403(b) account has been subject to a distributable event and the participant can then move the funds to an IRA or other tax qualified vehicle.

Under the regulations it is reasonably clear what the rules will be if an individual works for an employer and wants to transfer funds or leaves a job and wants to rollover the 403(b) funds. However, what happens to the many "orphan" 403(b) accounts owned by individuals retired or not employed by an employer having a 403(b) plan?

The law firm of Sutherland Asbill & Brennan LLP has published an article stating their belief that these orphan accounts will have to be rolled over to IRAs before January 1, 2009 or lose their tax deferred status. If this proves to be true, then a major additional problem is that IRAs cannot have loan provisions. Thus, all of the orphan 403(b) accounts that have outstanding loans could face the prospect of having to pay off the loans early. This could be done by using the funds in the 403(b) account to pay off the loan before rolling over the account to an IRA, since the loan should be collateralized by the funds in the account. To read more about this problem you can go to the Sutherland Asbill & Brennan LLP website at www.sablaw.com and find the article dated August 3, 2007 titled "Legal Alert: Intended Operation of New 403(b) Transfer Rules Requires Immediate Attention."

The regulations provide the IRS with authority to issue additional guidance on transfers and rollovers. Based on our reading of the regulations and the opinion of legal experts, it would appear that there are significant issues that need to be addressed so that "unintended consequences" do not affect tens of thousands of 403(b) account-holders.

Employer Paid Accounts

Many Texas school districts have plans, at least for key administrators, to which they make contributions for certain employees. These are commonly referred to as "annuities" in employment agreements. In a number of these arrangements the employee acquires a vested interest in the account for each year he or she remains employed with the district.

There are a number of provisions in the final regulations that address these arrangements. Employers should take two precautionary measures. First, employer contributions should be segregated in a separate account and not co-mingled with employee deferrals. Second, vested and non-vested employer paid funds should be segregated in different accounts. There are new tax rules related to non-vested funds so you should be sure that the company holding these funds is aware of the new rules and prepared to administer the account properly.

Timely Deposit of Funds

The new regulations hold employers to a standard for timely deposit of employee deferrals similar to the rules that apply to 401(k) plans. Under the new regulations 403(b) plans will be subject to a requirement that funds be remitted to the investment companies within a time period that is reasonable for the administration of the plan. The regulations use as an example 15 days after the end of the month in which the funds were deducted from the employee's pay.

Universal Availability and Nondiscrimination

One of the areas of greatest enforcement activity by the IRS in the past two years has been in the area of employer restrictions on the ability of employees to participate in 403(b) plans. Although governmental employers are generally exempt from pension nondiscrimination rules, 403(b) plans have specific nondiscrimination rules regarding plan availability ("universal availability") that apply to all employers. This rule requires that the plan be available to all employees who wish to contribute $200.00 or more each calendar year. The only exceptions to this rule are for "excludable employees."

From a practical perspective, school districts may only exclude employees from their 403(b) plans who are eligible to participate in a 457(b) deferred compensation plan, certain students and employees who normally work fewer than 20 hours per week.

The greatest problem in this rule for many school districts is part-time employees such as substitute teachers who do not receive regular recurring pay. Some school districts have payroll systems that may not handle setting up payroll deductions for these employees, or may not handle this well.

However, under the new regulations it is very important that (a) no employees be excluded from participation in the 403(b) plan unless the employer is absolutely certain that they can be excluded under the regulations and (b) the eligibility for employees to participate in the 403(b) plan be widely and clearly communicated to <u>*all*</u> employees. Where the IRS has found violations of this rule they have sought to have the offending employers make restitution to the excluded employees in the form of contributions to their 403(b) account. This could involve significant cost to the employer.

If it is necessary for the employer to exclude certain part-time employees (e.g., those working under 20 hours per week) then the employer should follow the following guidance excerpted from the regulations:

> An employee normally works fewer than 20 hours per week if and only if--
>
> (1) For the 12-month period beginning on the date the employee's employment commenced, the employer reasonably expects the employee to work fewer than 1,000 hours of service and
>
> (2) For each plan year ending after the close of the 12-month period beginning on the date the employee's employment commenced (or, if the plan so provides, each

subsequent 12-month period), the employee worked fewer than 1,000 hours of service in the preceding 12-month period.

The new regulations also state that the employer may not restrict the right of employees to make 403(b) Roth contributions, if Roth accounts are allowed in the employer's plan.

Elimination of Tax Sheltered Life

Under the new regulations, only annuity policies and mutual fund accounts established pursuant to Section 403(b)(7) of the Code may be used as 403(b) investments. Life insurance policies of any kind may no longer be issued as funding for 403(b) accounts after September 24, 2007.

Texas Law

In 2001 the Texas Legislature passed House Bill 273. This bill attempted to address abuses in the 403(b) industry in Texas. It also restricted the authority of public school districts and other educational organizations to control their 403(b) plans. When the IRS proposed the new 403(b) regulations in November 2004 it appeared that local districts would be required to impose their own plan rules. However, the ability to enforce these rules would depend on the cooperation of 403(b) vendors. Texas law no longer gave districts enforcement authority over these vendors.

Our company obtained an opinion from attorney Mary Keller of the law firm of York, Keller & Field, L.L.P. as to the potential effect of this conflict. Ms. Keller is a former Senior Associate Commissioner of Insurance Texas Department of Insurance and Deputy Attorney General in the Texas Attorney General's Office. Her opinion confirmed that districts would face a major conflict between state and federal law that could potentially leave districts with an untenable choice.

We contacted Rep. Craig Eiland, then Chair of the House Committee on Pensions & Investments about the issue. He held hearings on the subject and introduced House Bill 169 in 2006 (the third special session) to provide relief to school districts on this issue.

When Rep. Vicki Truitt became Chair of the Committee in the 80th session of the Legislature, she and her staff reviewed the issue. Rep. Truitt then introduced House Bill 2341 that provided relief on the 403(b) conflict. She and her staff worked diligently to get the bill through both houses of the Legislature. The Governor signed the bill in June 2007.

The new Texas law allows school districts and other educational institutions to exclude vendors from their 403(b) plans who do not comply with the district's administrative plan rules if such rules are necessary to comply with any change in federal 403(b) rules that occurs after January 1, 2008. *It is important to note that the law does <u>not</u> allow districts to exclude vendors for any other reason than to comply with IRS rules.*

Getting Ready to Comply

What should employers do to get ready to comply with the new rules? Our advice is as follows:

1. **Do not act hastily.** There is much uncertainty about exactly how the new regulations will actually work on a practical level. It is very likely that the IRS will provide some additional guidance, in the form of speeches by key officials, articles and perhaps more formal guidance.

2. **Beware of those selling a quick fix.** Many companies of every kind (vendors, consultants, third party administrators and others) are now trying to take advantage of the fear of these new regulations. They are telling employers that they have all of the answers and that the employer should buy their services now. No one has all of the answers right now and a hasty decision is likely to benefit only the company selling the services. Also, be careful about the background of the companies. Some vendors have good compliance programs and are up front about what they sell. Other companies present themselves as independent when they are actually selling 403(b) products.
3. **Be sure the company you use has regulatory expertise.** Ask specific questions about exactly how they propose to resolve the issues discussed in this article. Be sure they have in-depth knowledge of the Code and regulations.
4. **Read the opinions of different experts.** There are many articles being written right now about the new regulations. As the "dust settles" and the effect of the changes becomes more apparent, these opinions will become more consistent. Sources to find good information are www.benefitslink.com and www.403bwise.com.
5. **Be sure the material you review applies to public employers.** There are many issues under the regulations that effect only plans subject to ERISA. As public employers, school districts are not subject to ERISA. Many articles do not clearly make this distinction. You do not want to spend time on issues that do not effect your organization.

Conclusion

The final regulations cannot be ignored. The effect of these changes on employers and 403(b) plan participants will be far-reaching and significant. It is likely that these regulations will result in a very different 403(b) market five years from now. It is up to each employer to be sure that the resulting change for their employees is as positive as it can be.

About the Author. Mike Cochran is a partner in TCG Group Holdings, LLP. He has been managing retirement plans in both the public and private sectors since 1976. TCG owns several companies that provide consulting, investment advisory, employee benefits and third party administration services to public school districts, cities and other employers. TCG is a corporate sponsor of TASA. You can reach Mike at mike.cochran@pension-consulting.com.

Texas House of Representatives
Committee on Pensions and Investments

FILE # ML-45471-07
I.D. # 45471

November 29, 2007

The Honorable Greg Abbott
Attorney General of Texas
209 W. 14th Street
Austin, Texas 78701

RQ-0653-GA

Dear General Abbott:

As chair of the House Committee on Pensions and Investments, I ask for your opinion regarding the application of certain provisions of Section 9, Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), to Texas public school districts and open-enrollment charter schools (educational institutions) offering 403(b) plans.

A 403(b) tax-sheltered annuity plan (403(b) plan) is a tax-advantaged retirement plan available to employees of certain public educational institutions or tax-exempt organizations and to certain self-employed ministers. See Section 403(b)(1)(A), Internal Revenue Code of 1986. A 403(b) plan allows participants to defer taxable income by contributing to or purchasing qualified investment products from certain companies through payroll deductions made by their employers.

Texas educational institutions offering 403(b) plans often obtain the services of third party administrators (TPAs) to assist in the administration of their 403(b) plans. As part of the service provided to an educational institution, a TPA typically:

- receives employees' salary reduction agreements,[1] screens the agreements for compliance with applicable federal and state law, and approves the required employee payroll deductions; and
- receives the funds from the employees' payroll deductions and forwards those funds to the appropriate companies for deposit into the appropriate employees' 403(b) policies or accounts.

[1] A salary reduction agreement is the agreement between an educational institution and an employee to reduce the employee's salary for the purpose of making direct contributions to or purchases of a qualified investment product. See Section 4(7), Article 6228a-5, Vernon's Texas Civil Statutes.

Blake Rocap, Chief Clerk
P.O. Box 2910 • Austin 78768-2910
(512) 463-2054

In order to provide these services, TPAs are necessarily given access to certain personal and financial information of participating employees. For example, TPAs have access to:

- the name and identifying number (i.e., social security number or employee identification number) of each employee who purchases a qualified investment product;
- records related to purchasing the investment product, including the employee's salary reduction agreement;
- information regarding the investment product purchased, including information about the company from which the employee purchased the investment product; and
- information regarding the amount of the purchase.

As a result of new federal regulations issued by the Internal Revenue Service under Section 403(b) of the Internal Revenue Code,[2] the services provided by TPAs in administering 403(b) plans are likely to increase because under the new regulations employers are expected to assume greater responsibility in administering their 403(b) plans. Some of that responsibility may be assumed by TPAs that can offer the following services:

- assisting educational institutions with employee-initiated transfers of policy or account values from one company to another;
- approving loans requested by employees from qualified investment products;
- approving employee distributions from qualified investment products; and
- assisting educational institutions in preparing a written plan[3] that complies with the new federal regulations.

TPAs are not always independent from the companies that sell qualified investment products. In some instances, a company that sells qualified investment products may form a subsidiary organization to offer TPA services. In other instances, a company and a TPA might both be owned by the same parent company. Frequently, in these situations, the affiliated TPA offers services for fees reportedly ranging from $1,000 to $5,000 annually, fees that are well below the market rate charged by independent TPAs for the same services.

Section 9, Article 6228a-5, Vernon's Texas Civil Statutes, prohibits certain practices by educational institutions offering a 403(b) plan to its employees. In pertinent part, Section 9 provides:

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[2] Revised Regulations Concerning Section 403(b) Tax-Sheltered Annuity Contracts; Final Rule, 72 Fed. Reg. 41, 128 (July 26, 2007).

[3] The written plan includes which companies offer qualified investment products under the educational institution's 403(b) plan, plan eligibility for employees, plan contribution limits, distribution rules (including rules for loans, transfers, rollovers, hardship distributions, and lump-sum payments), and rules regarding the timeliness of sending salary reduction contributions to the companies offering the qualified investment products.

Sec. 9. (a) An educational institution may not:

. . .

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products; or

(7) use public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product.

In light of the above facts and statutory provisions, I ask you to answer the following questions:

(1) Does an educational institution violate Sections 9(a)(4) through (7), Article 6228a-5, Vernon's Texas Civil Statutes, if the institution contracts with a TPA that is owned by or otherwise affiliated with a company that sells qualified investment products to the institution's employees?

(2) Specifically, does an educational institution violate Section 9(a)(6), Article 6228a-5, Vernon's Texas Civil Statutes, if the institution contracts with a TPA described by question (1) and the TPA provides its services for free, for a nominal fee, or at a reduced rate?

Sincerely,

Vicki Truitt, State Representative
Chair, House Committee on Pensions and Investments

January 31, 2008

Ms. Nancy Fuller
Chair Opinions Committee
Office of the Attorney General
P.O. Box 12548
Austin, Texas 78711-2548

Re: A.G. Opinion Request #0653-GA

Dear Ms. Fuller:

Please accept the submission of this memorandum on behalf of United Educators Association. United Educators Association is an independent association representing more than 16,000 Texas public school employees in North Texas. We work to improve the salaries, benefits, and working conditions for public school employees. We appreciate the opportunity to respond to the issues in the Opinion Request #0653-GA.

Sincerely,

Cheryl Wicks Rauscher
Staff Attorney United Educators Association

UNITED EDUCATORS ASSOCIATION

MEMORANDUM FOR AG OPINION RQ-0653-GA

Questions Presented

1. Under Texas law, does an educational institution violate Section 9 (4) – (7), Article 6228a-5, VERNON'S TEXAS CIVIL STATUTES, if the institution contracts with a Third Party Administrator (TPA) that is owned by or otherwise affiliated with a company that sells qualified investment products to the institution's employees?

2. Under Texas law, does an educational institution violate Section 9(a)(6) Article6228a-5, VERNON'S TEXAS CIVIL STATUTES if the institution contracts with a TPA described by question (1) and the TPA provides its services for free, for a nominal fee, or at a reduced rate?

Background

In the 1980s school districts began to contract with TPAs. Unfortunately, some of the TPAs were owned or strongly affiliated with the companies that sold investment instruments. These companies began to offer school districts their services for reduced or no fees. Logically, a company does not reduce its fee without some type of *quid pro quo*. This *quid pro quo*, included but was not limited to high-priced hidden fees and exclusivity of the products sold by the TPA. These arrangements severely limited the investment opportunities for teachers. TPAs frequently passed along additional fees to unsuspecting teachers.

In 1985 the Texas Legislature enacted House Bill 1824, and Section 22, Article 21.14 Insurance Code. These were enacted to help regulate and stop the abusive practices of the TPA's. Abuses continued, and legislation regarding TPA's has grown. The statute in question, Section 9 Article 6228a-5, grew out of this environment.

QUESTION 1 (hereinafter Question 1)

> Under Texas law, does an educational institution violate Section 9 (4) – (7), Article 6228a-5, VERNON'S TEXAS CIVIL STATUTES, if the institution contracts with a Third Party Administrator (TPA) that is owned by or otherwise affiliated with a company that sells qualified investment products to the institution's employees ?

ANSWER:
Yes, allowing a TPA as delineated in question 1would violate Sections 9(4) – 9(7). Further this dual relationship of being both administrator and seller of financial instruments, is not in the best interest of the teachers, whose interests are now protected by these very statutes.

Section 9(4)

Section 9(4) states, "[a]n educational institution may not grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this act." The very nature of how a TPA operates, violates this provision. A TPA has access to information that no other party has access. In order for an employee to utilize a 403(b) program they must give the TPA information to which no agent or broker has access at this point. This alone is discriminatory and exclusive since **only the agency affiliated with the TPA** has access to the district's employees. Moreover, the fact that the TPA is hired by the district gives an implicit approval/endorsement of the TPA and the products they sell. Again this implicit approval gives the TPA an exclusive access denied to other companies selling investment instruments. However, the discriminatory practices and exclusivity do not stop at this point rather, these practices continue until another company can contact the employee.

Question 1 violates section 9(4). This is exactly the type of arrangement that is unfair to the classroom teacher. These arrangements limit a teacher's opportunities to make informed decisions concerning his or her financial instruments.

Section 9(5)

Section 9(5) states, "[a]n educational institution may not grant exclusive access to information about an employee's financial information, including information about any employee's qualified investment products, to a company or agent offering qualified investment products unless the employee consents in writing." This issue is quite similar to the issue in Section 9(4). We have determined that a TPA as set out in question 1 does have exclusive access to an employee's financial information. Since the TPA has exclusive access, the employee must consent in writing for the TPA to have access to his or her investments. What *real* choice does the Teacher/Employee have if the employee wants to take advantage of a 403(b). In effect the teacher/employee is coerced into giving the TPA access to his or her information if the employee wishes to participate in the plan.

Question 1 violates section 9(5) by first allowing exclusive access to information about an employee's qualified investment products, then effectively coercing the teacher/employee to agree to such an arrangement if the employee wishes to receive the benefit of a 403(b) plan.

Section 9(6)

Section 9(6) states, "[a]n educational institution may not accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products." For the full discussion involving this section please see question 2 *infra*.

Section 9(7)

Section 9(7) states, [a]n educational institution may not use public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product. The educational institution would not *per se* be recommending qualified investment products. However, the implicit approval of the TPA and the unprecedented access of the TPA are effectually a recommendation by the district to the products sold by TPA.

QUESTION 2 (hereinafter Question 2)

> Under Texas law, does an educational institution violate Section 9(a)(6) Article6228a-5, VERNON'S TEXAS CIVIL STATUTES if the institution contracts with a TPA described by question (1) and the TPA provides its services for free, for a nominal fee, or at a reduced rate.

ANSWER:
Yes, allowing a TPA as delineated would violate Sections 9(a)(6). Section 9(a)(6) states; "[a]n educational institution may not accept **any benefit** from a company or from an agent or affiliate of a company that offers qualified products." (emphasis added.) The plain language of the statute states "any benefit."

Offering services for free, for a nominal fee, or at a reduced rate, clearly confers a substantial benefit upon the educational intuition. It is this type of arrangement that caused teachers in the past, to pay high-priced hidden fees or to have limited opportunities to purchase instruments. This type of arrangement meets the threshold for "any benefit" and undoubtedly is a "substantial benefit" which clearly violates both the letter and spirit of the law. Therefore, question 2 violates section 9(a)(6).

It is not in the best interest of the more than 16,000 members of United Educators Association, to over-turn the protections of the statutes currently in place by allowing the districts to hire TPAs owned by the very companies that wish to sell their products. In addition, the Section 9 Education Prohibitions are for K-12 only. This is important as members of UEA are K-12 employees, and are concerned about the outcome of this matter. UEA appreciates the opportunity to voice the opinion of our more than 16, 000 members on this matter.

Respectfully Submitted,

Cheryl Wicks Rauscher
Staff Attorney
United Educators Association

ATTORNEY GENERAL OF TEXAS
GREG ABBOTT

December 18, 2007

The Honorable Vicki Truitt
Chair, Committee on Pensions and Investments
Texas House of Representatives
Post Office Box 2910
Austin, Texas 78768-2910

Re: Whether an educational institution may contract with a third-party administrator that is owned by or otherwise affiliated with a company that sells qualified investment products to the institution's employees (RQ-0653-GA)

Dear Representative Truitt:

We have received your request for an attorney general opinion, dated November 29, 2007, and have designated it as Request No. 0653-GA. Please refer to that number in future correspondence with us about this matter. Section 402.042 of the Government Code provides that the Attorney General shall issue an opinion not later than the 180th day after the date that an opinion request is received. TEX. GOV'T CODE ANN. § 402.042(c)(2) (Vernon 2005). We received your request on December 3, 2007, setting a due date for your opinion of May 31, 2008. We will respond by that date, or before, if possible.

By copy of this letter we are notifying those listed below of your request and asking them to submit briefs if they care to do so. If you are aware of other interested parties, please let us know as soon as possible. We ask that the briefs be submitted by January 25, 2008 to ensure that the Opinion Committee will have adequate time to review and consider arguments relevant to the request from all interested parties. Written submissions are most useful, as the members of the Opinion Committee are not available to comment on or discuss the merits of legal questions at issue in an opinion request. Parties may request an extension of time to file a brief by calling (512) 463-2110.

Very truly yours,

Nancy S. Fuller
Chair, Opinion Committee

NSF/KKO/lnl
Enclosure: Request No. 0653-GA

cc: Mr. Robert Scott, Commissioner of Education, Texas Education Agency
Mr. William Franz, General Counsel, Texas Higher Education Coordinating Board
Mr. Barry D. Burgdorf, Vice Chancellor and General Counsel, University of Texas System
Mr. Pat Campbell, Vice Chancellor and General Counsel, Texas Tech University System
Ms. Francie A. Frederick, JD, General Counsel to the Board of Regents, University of Texas System
Ms. Dona G. Hamilton, Vice Chancellor for Legal Affairs and General Counsel, Office of the President, University of Houston
Mr. Jay Kimbrough, Deputy Chancellor and General Counsel, Texas A&M University System
Ms. Joy Baskin, Director, Legal Services, Texas Association of School Boards
Ms. Linda Bridges, President, Texas Federation of Teachers
Dr. Reynaldo García, President, Texas Association of Community Colleges
Mr. Tom Johnson, Executive Director, Texas Faculty Association
Ms. Joey Moore, Manager of Legal Services, Texas State Teachers Association
Mr. Richard Moore, Executive Director, Texas Community College Teachers Association
Ms. Jeri Stone, Executive Director/General Counsel, Texas Classroom Teachers Association
Mr. Johnny Veselka, Executive Director, Texas Association of School Administrators
Mr. Ken Anderson, Governor's Appointment Director

ATTORNEY GENERAL OF TEXAS

GREG ABBOTT

May 30, 2008

The Honorable Vicki Truitt
Chair, Committee on Pensions and Investments
Texas House of Representatives
Post Office Box 2910
Austin, Texas 78768-2910

Opinion No. GA-0633

Re: Whether an educational institution violates article 6228a-5, section 9(a)(4)-(7) of the Texas Revised Civil Statutes if the institution contracts with a third-party administrator that is owned by or otherwise affiliated with a company that sells qualified 403(b) investment products to the institution's employees (RQ-0653-GA)

Dear Representative Truitt:

Article 6228a-5, sections 4-13 of the Revised Civil Statutes provides the means by which an educational institution's employees may participate in investment plans that meet the requirements of section 403(b) of the Federal Internal Revenue Code (a "403(b) plan"). *See generally* 26 U.S.C.A. § 403(b) (West Supp. 2007); Tex. Rev. Civ. Stat. Ann. art. 6228a-5, §§ 4-13 (Vernon Supp. 2007). You tell us that "Texas educational institutions offering 403(b) plans often obtain the services of third party administrators (TPAs) to assist in" managing their 403(b) plans.[1] You ask two questions about an educational institution's use of a third-party administrator that is affiliated with a company offering qualified 403(b) investment products for sale to employees of the educational institution (an "affiliated third-party administrator"):

> (1) Does an educational institution violate Section 9(a)(4) through (7), Article 6228a-5 . . . if the institution contracts with a [third-party administrator] that is owned by or otherwise affiliated with a company that sells qualified investment products to the institution's employees?
>
> (2) Specifically, does an educational institution violate Section 9(a)(6) . . . if the institution contracts with a [third-party administrator] described by question (1) and the [third-party administrator] provides its services for free, for a nominal fee, or at a reduced rate?

See Request Letter, *supra* note 1, at 3. Your questions raise many issues of fact, which cannot be resolved in an opinion. *See* Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process."). We can, however, provide some guidance as to the interpretation of the statute at issue. We begin by examining article 6228a-5 in light of the facts you have provided.

I. Statutory and Factual Background

Under article 6228a-5, section 5(a), an educational institution "may enter into a salary reduction agreement with an employee of the institution" under which the educational institution agrees to reduce the employee's salary for the purpose of directly contributing to or purchasing certain qualified 403(b) investment products. Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 5(a) (Vernon Supp. 2007); *see id.* § 4(2), (4), (7) (defining "educational institution," "employee," and "salary reduction agreement"); *see also id.* § 5(f) ("To the greatest degree possible, employers of employees who participate in the program offered under this section shall require that contributions to eligible qualified investments be made by automatic payroll deduction and deposited directly in the investment accounts."). The employee is "entitled to designate any agent, broker, or company through which a qualified investment product may be purchased or contributions may be made," but may purchase only eligible qualified investment products (annuities or investments) that are registered with the Teacher Retirement System of Texas (the "Retirement System") in accordance with article 6228a-5, section 8A. *Id.* § 5(e); *see id.* § 5(a); *see also id.* § 4(3), (5)-(6) (defining "eligible qualified investment," "qualified investment product," and "retirement system"); *id.* § 5(d) (requiring the Retirement System to "establish and maintain" on the Retirement System's Internet website "a list of companies that have certified under this section"); *id.* § 8A (setting out the procedure by which a company offering a qualified investment product to an educational institution's employees may register the product with the Retirement System).

You tell us that educational institutions offering 403(b) plans often "obtain" the services of third-party administrators to assist in the administration of their 403(b) plans. Request Letter, *supra* note 1, at 1. You indicate that, in serving an educational institution, a third-party administrator typically

- receives employees' salary reduction agreements, screens the agreements for compliance with applicable federal and state law, and approves the required employee payroll deductions; and
- receives the funds from the employees' payroll deductions and forwards those funds to the appropriate companies for deposit into the appropriate employees' 403(b) policies or accounts.

See id. (footnote omitted). You also tell us that new federal regulations promulgated by the Internal Revenue Service place "greater responsibility" on employers "in administering their 403(b) plans" and that educational institutions are therefore likely to rely increasingly on third-party administrators. *Id.* at 2.

You explain that an educational institution must provide its third-party administrator with access to certain personal and financial information of participating employees, such as

- the name and identifying number (i.e., social security number or employee identification number) of each employee who purchases a qualified investment product;
- records related to purchasing the investment product, including the employee's salary reduction agreement;
- information regarding the investment product purchased, including information about the company from which the employee purchased the investment product; and
- information regarding the amount of the purchase.

Id.

And you further state that third-party administrators may be affiliated with companies selling qualified 403(b) investment products:

> [Third-party administrators] are not always independent from the companies that sell qualified investment products. In some instances, a company that sells qualified investment products may form a subsidiary organization to offer [third-party administrator] services. In other instances, a company and a [third-party administrator] might both be owned by the same parent company. Frequently, in these situations, the affiliated [third-party administrator] offers services for fees reportedly ranging from $1,000 to $5,000 annually, fees that are well below the market rate charged by independent [third-party administrators] for the same services.

Id.

You are concerned that an educational institution's use of an affiliated third-party administrator may violate article 6228a-5, section 9(a)(4)-(7). *See id.* at 3. With respect to section 9(a)(6) in particular, you are concerned about the practice of an educational institution accepting affiliated-third-party-administrator services for free or at a nominal or reduced rate. The provisions about which you ask limit the actions of an educational institution:

(a) An educational institution may not:

. . .

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products; or

(7) use public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product.

Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(4)-(7) (Vernon Supp. 2007).

On its face, section 9 applies to the actions of an "educational institution," which article 6228a-5 defines to mean a school district or an open-enrollment charter school. *See id.* §§ 4(2), 9. You do not ask whether the term "educational institution" in section 9 encompasses a third-party administrator as the educational institution's delegatee or agent, and therefore we do not consider the question. *See* Request Letter, *supra* note 1, at 3.[2] Moreover, whether an entity serves as a principal's agent depends upon the resolution of fact issues--specifically whether the principal "manifests assent to" the entity that the entity will "act on the principal's behalf and subject to the principal's control, and the [entity] manifests assent or otherwise consents so to act"--that cannot be resolved in an opinion. Restatement of the Law of Agency § 1.01 (3d ed. 2006); *see* Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process."); *see also* Restatement of the Law of Agency § 1.01 cmt. c (3d ed. 2006) (describing the elements of agency, which include the principal's right to control the agent). We turn now to the questions you ask, considering each subsection in turn. In this way, we combine our answers to your questions.

II. Analysis

A. Section 9(a)(4)

Section 9(a)(4) prohibits an educational institution from granting "exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides" qualified 403(b) investment products to the educational institution's employees. Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(4) (Vernon Supp. 2007). In our opinion, whether an educational institution grants "exclusive access to an employee by discriminating against or imposing barriers to" a qualified-investment-product provider by contracting with an affiliated third-party administrator is a question that requires the resolution of numerous fact questions. One must decide, for example, whether the educational institution's grant of exclusive access to a third-party administrator discriminates against or imposes barriers to an agent, a broker, or a company that sells qualified investment products. This office does not resolve fact questions. *See* Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process.").

B. Section 9(a)(5)

Section 9(a)(5) prohibits an educational institution from granting "exclusive access to information about an employee's financial information . . . to a company or agent offering qualified investment products unless the employee consents in writing to the access." Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(5) (Vernon Supp. 2007). If the term "company" encompasses only that portion of the entity selling qualified investment products, then the educational institution may provide the third-party administrator with exclusive access to employees' financial information without violating section 9(a)(5), but if the term "company" encompasses subsidiaries of the qualified-investment-product provider or entities owned by the same parent company, then providing exclusive access to an affiliated third-party administrator violates section 9(a)(5). We consequently consider the meaning of the term "company" for purposes of section 9(a)(5).

Article 6228a-5 does not define the term "company," but section 9(a)(6) distinguishes between a company and an affiliate of the company: "a *company or* . . . an agent or *affiliate* of a company that offers qualified investment products." *Id.* § 9(a)(6). While the term "affiliate" is not defined in article 6228a-5 and has not been defined by a court specifically in the context of article 6228a-5, the term ordinarily refers to "[a] corporation that is related to another corporation by shareholdings or other means of control" or "a 'company effectively controlled by another or associated with others under common ownership or control.'" *Eckland Consultants, Inc. v. Ryder, Stilwell Inc.*, 176 S.W.3d 80, 88 (Tex. App.--Houston [1st Dist.] 2004, no pet.) (quoting Black's Law Dictionary 59 (7th ed. 1999); Webster's Third New International Dictionary 35 (1971)); *see also* Tex. Gov't Code Ann. §§ 312.001-.002(a) (Vernon 2005) (directing that, with respect to the construction of "all civil statutes," "words shall be given their ordinary meaning"). Consequently, article 6228a-5, section 9(a)(6) indicates that the term "company" does not encompass affiliates of the company, i.e., companies with the same parent company or a company's subsidiary. And a term should be defined consistently throughout a statute. *See Helena Chem. Co. v. Wilkins*, 47 S.W.3d 486, 493 (Tex. 2001) (stating that a court should not give one provision in a legislative enactment a meaning out of harmony or inconsistent with other provisions). As a result, we construe the term "company" throughout section 9 not to include affiliates.[3]

Construing the term "company" in this way is consistent with the term's definition in rules adopted by the Retirement System. The Retirement System has express statutory authority to "adopt rules" for use in administering certain portions of article 6228a-5, not including section 9. *See* Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 6(c) (Vernon Supp. 2007) (authorizing the Retirement System to "adopt rules only to administer [Section 6] and Sections 5, 7, 8, 8A, 11, 12, and 13 of this Act"); *see also id.* art. 6228a-5, § 4(6) (defining "retirement system"). As the Retirement System defines the term, a company is

[a]n entity that offers and issues a qualified investment product and that has primary liability to the purchaser for performance of the obligations described in the product, contract, annuity contract or annuity certificate, or policy. Generally, "company" does not include . . . third party administrators, . . . unless such entities have primary liability for performance of the obligations in the product or contract.

34 Tex. Admin. Code § 53.1(5) (2008) (Retirement System, Definitions). While the Retirement System is not authorized to define the term for purposes of section 9, a term ideally should be construed consistently throughout a statute. *See Helena Chem. Co.*, 47 S.W.3d at 493 (stating that a court should not give one provision in a legislative enactment a meaning out of harmony or inconsistent with other provisions).

We therefore conclude that, for purposes of article 6228a-5, the term "company" encompasses only that portion of an entity selling qualified investment products; it does not encompass a subsidiary company or a company owned by the same parent corporation. Consequently, an educational institution may provide an affiliated third-party administrator with exclusive access to employees' financial information without violating section 9(a)(5). Nevertheless, whether providing such exclusive access violates section 9(a)(5) in particular circumstances is a decision for a court.[4] *Cf.* Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process.").

C. Section 9(a)(6)

The issue with respect to section 9(a)(6), which prohibits an educational institution from accepting "any benefit from . . . an . . . affiliate of a company that offers qualified investment products," is whether an educational institution accepts a benefit if an affiliated third-party administrator manages the 403(b) plan for free or for a nominal or reduced fee. Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(6) (Vernon Supp. 2007).

Article 6228a-5 does not define the term "benefit." *See generally id.* art. 6228a-5. But statutes that attempt to prevent corrupt influences on public servants define the term "benefit" to mean "anything reasonably regarded as pecuniary gain or pecuniary advantage." Tex. Penal Code Ann. § 36.01(3) (Vernon 2003); Tex. Transp. Code Ann. § 366.2521(a) (Vernon Supp. 2007); *see also* Tex. Penal Code Ann. § 1.07(a)(7) (Vernon Supp. 2007) ("'Benefit' means anything reasonably regarded as economic gain or advantage . . . ."). The Waco court of appeals has construed the term "benefit" in the context of one of these statutes to include "anything to which a price can be assigned," excepting goods or services of

minimal value. *Smith v. State*, 959 S.W.2d 1, 20-21 (Tex. App.--Waco 1997, pet. ref'd). The Texas Ethics Commission, the entity charged with administering the Penal Code provisions prohibiting a public servant's acceptance of a benefit, has determined that the waiver of a private organization's membership fees constitutes a benefit. *See* Op. Tex. Ethics Comm'n No. 268 (1995) at 1. Similarly, the Ethics Commission determined that, but for the fact that the Legislature has specifically excepted from the term "benefit" the use of a governmental entity's property or facilities, unlimited free parking in city-owned or city-leased spaces would constitute a benefit. *See* Op. Tex. Ethics Comm'n No. 186 (1994) at 1; *see also* Op. Tex. Ethics Comm'n No. 282 (1995) at 1 ("A discount on child care costs is a benefit."). [5]

Because article 6228a-5, section 9(6) appears on its face to discourage corrupt influences on educational institutions, the statutory definition, judicial definition, and the Ethics Commission's interpretations are instructive. In addition, this definition of the term "benefit" is consistent with the term's ordinary meaning. *See* The New Oxford American Dictionary 154 (2001) (defining "benefit" as "an advantage or profit gained from something"); *see also* Tex. Gov't Code Ann. §§ 312.001-.002(a) (Vernon 2005) (directing that, with respect to the construction of "all civil statutes," "words shall be given their ordinary meaning"). We thus construe the term "benefit" in article 6228a-5, section 9(a)(6) to encompass "anything reasonably regarded as pecuniary gain or pecuniary advantage," excepting perhaps goods or services of minimal value. [6] Tex. Penal Code Ann. § 36.01(3) (Vernon 2003); Tex. Transp. Code Ann. § 366.2521(a) (Vernon Supp. 2007); *see also* Tex. Penal Code Ann. § 1.07(a)(7) (Vernon Supp. 2007) ("'Benefit' means anything reasonably regarded as economic gain or advantage."); *Smith*, 959 S.W.2d at 20-21 ("a 'benefit' could . . . be anything to which a price can be assigned"). Based on the definition of the term "benefit" and the Ethics Commission's determinations, a court likely would find that the receipt of third-party-administrator services for free or for a reduced fee constitutes a benefit.

Section 9(a)(6) suggests, however, that the benefit must flow to the educational institution. *See* Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(6) (Vernon Supp. 2007) ("An educational institution may not accept any benefit . . . ."). Depending upon how the educational institution and third-party administrator structure their contractual arrangement, it may be the educational institution's employees, not the educational institution itself, that benefit. Determining the beneficiary in any particular arrangement is a question of fact that cannot be resolved in the opinion process. *See* Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process.").

D. Section 9(a)(7)

We finally consider section 9(a)(7), which prohibits an educational institution from using "public funds to recommend a qualified investment product offered by a company or an agent of a company that offers a qualified investment product." Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(7) (Vernon Supp. 2007). Whether the use of an affiliated third-party administrator in particular circumstances constitutes using public funds to recommend qualified 403(b) investment products sold by a particular company is a question of fact that cannot be resolved in the opinion process. *See*Tex. Att'y Gen. Op. No. GA-0446 (2006) at 18 ("Questions of fact are not appropriate to the opinion process.").

SUMMARY

Whether an educational institution violates article 6228a-5, section 9(a)(4), (6)-(7) of the Revised Civil Statutes by contracting with a third-party administrator that is affiliated with a company that sells qualified 403(b) investment products to the educational institution's employees is a question requiring the resolution of facts. An educational institution may provide a third-party administrator that is affiliated with a company offering qualified 403(b) investment products to employees of the educational institution with exclusive access to employees' financial information without violating section 9(a)(5), although a court may find a violation in particular circumstances.

Very truly yours,

GREG ABBOTT
Attorney General of Texas

KENT C. SULLIVAN
First Assistant Attorney General

ANDREW WEBER
Deputy Attorney General for Legal Counsel

NANCY S. FULLER
Chair, Opinion Committee

Kymberly K. Oltrogge
Assistant Attorney General, Opinion Committee

Footnotes

1. Letter from Honorable Vicki Truitt, Chair, Committee on Pensions and Investments, Texas House of Representatives, to Honorable Greg Abbott, Attorney General of Texas, at 1 (Nov. 29, 2007) (on file with the Opinion Committee, *also available at* http://www.texasattorneygeneral.gov) [hereinafter Request Letter].

2. *See also* Letter from Steve Bresnen, Steve Bresnen & Assocs., on behalf of 1st American Pension Services, Inc., to Honorable Greg Abbott, Attorney General of Texas, at 8 (Jan. 28, 2008) (suggesting that a third-party administrator is an agent of the educational institution "under the principle of *respondeat superior*"); Letter from Susan Jennings, General Counsel, Life Insurance Co. of the Southwest, to Honorable Greg Abbott, Attorney General of Texas, at 5 (Feb. 7, 2008) ("As the [third-party administrator] would be the school's agent (since the school is the principal who retained the [third-party administrator] to act on its behalf regarding the 403(b) plan)," a school could be liable for a third-party administrator's violation of section 9(a)(7)) (both letters on file with the Opinion Committee).

3. Other statutes define the term "company," but we are reluctant to apply any of these definitions to article 6228a-5 without considering the purposes for which the Legislature adopted each of the acts that define the term. *See, e.g.*, Tex. Rev. Civ. Stat. Ann. art. 581-4.B. (Vernon Supp. 2007) (defining the term "company" to "include a corporation, person, joint stock company, partnership, limited partnership, association, company, firm, syndicate, trust, incorporated or unincorporated"); Tex. Fin. Code Ann. § 61.002(6) (Vernon Supp. 2007) (defining "company" to mean "a corporation, partnership, trust, joint-stock company, association, unincorporated organization, or other similar entity or a combination of any of those entities acting together"); Tex. Gov't Code Ann. § 806.001(3) (Vernon Supp. 2007) (defining "company" to mean "a sole proprietorship, organization, association, corporation, partnership, joint venture, limited partnership, limited liability partnership, limited liability company, or other entity or business association whose securities are publicly traded, including a wholly owned subsidiary, majority-owned subsidiary, parent company, or affiliate of those entities or business associations, that exists to make a profit"). Additionally, to the extent other statutory definitions would include affiliates, they would be inconsistent with section 9(a)(6), which makes clear that for purposes of article 6228a-5, section 9, the term "company" does not include an affiliate.

4. Section 9(a)(5) prohibits the granting of exclusive access to an employee's financial information "unless the employee consents in writing to the access." Tex. Rev. Civ. Stat. Ann. art. 6228a-5, § 9(a)(5) (Vernon Supp. 2007). Accordingly, an educational institution that obtains the services of an affiliated third-party administrator may wish to protect itself by obtaining employees' consent in the event that providing information to the third-party administrator violates section 9(a)(5).

5. Coincidentally, the Texas Commissioner of Insurance recently has determined that the provision of administrative services by a third-party administrator "on a no-additional-fee basis" may "constitute an . . . inducement that is not specified in the" underlying insurance policy in violation of sections 541.056(a) and 543.003(1)(A), (C) of the Insurance Code. Commissioner's Bulletin #B-0004-08 (Jan. 31, 2008), *available at*

http://www.tdi.state.tx.us/ bulletins/index.html (last visited May 29, 2008). The Department of Insurance thus "strongly cautions" an insurance company, insurance agent or agency against directly or indirectly providing administrative services "at no additional fee." *Id.*

6. You do not suggest that a third-party administrator's waiver or reduction of fees is of "minimal value." *See* Request Letter, *supra* note 1, at 1-3. Therefore, we need not consider here whether article 6228a-5, section 9(a)(6) excepts benefits of minimal value.

TCG Consulting
TOTAL COMPENSATION GROUP
4201 Bee Caves Road, Suite C-101
Austin, TX 78746
Phone: (512) 306-9939 Fax: (512) 306-9959

Texas Attorney General Issues Opinion No. GA-0633
Use of 403(b) Product Vendor-Affiliates to Administer School Districts' 403(b) Plans

Summary of TCG's interpretation: It may be OK for school districts to use 403(b) vendor-affiliated administrators to administer their 403(b) plans, but districts must pay fees comparable to non-vendor affiliated administrators.

On May 30, 2008 the Texas Attorney General issued Opinion No. GA-0633 in response to a request from the Honorable Vicki Truitt, Chair, Committee on Pensions and Investments Texas House of Representatives. The request addressed the question of "Whether an educational institution violates article 6228a-5, section 9(a)(4)-(7) of the Texas Revised Civil Statutes if the institution contracts with a third-party administrator that is owned by or otherwise affiliated with a company that sells qualified 403(b) investment products to the institution's employees." The applicable section of Vernon's Texas Civil Statutes is attached.

TCG Consulting, LP (TCG) requested that attorney Mary Keller advise us as to the practical consequences for school districts of the Attorney General's ruling. Ms. Keller, currently a partner in the law firm of Winstead PC, was First Assistant Attorney General/Deputy Attorney General with the Texas Attorney General's Office for 8 years and Senior Associate Commissioner of Insurance Texas Department of Insurance for 6 years. Ms. Kelly has acted as a legal advisor to TCG for the past 5 years.

A summary of Ms. Keller's advice to TCG is as follows:

1. The Attorney General's ruling leaves a several questions on this issue unanswered, because, as the Summary of the opinion states, "Whether an educational institution violates article 6228a-5, section 9(a)(4), (6)-(7) of the Revised Civil Statutes by contracting with a third-party administrator that is affiliated with a company that sells qualified 403(b) investment products to the educational institution's employees is a question requiring the resolution of facts." Questions of fact would need to be settled by a court.

2. Depending on the facts applicable to a particular school district, it does not appear that use of a 403(b) vendor-affiliated administrator to administer the district's 403(b) plan would violate Texas law in many cases.

3. It is very clear that if the *district* benefits from the 403(b) services of a vendor-affiliated administrator, then the *district must pay the vendor-affiliated administrator fees comparable to what the district would pay a non-vendor affiliated administrator providing comparable services*.

TCG asked Ms. Keller what would be the likely consequences if a school district did not pay the vendor-affiliated administrator fees comparable to what the district would pay a non-vendor affiliated administrator providing comparable services.

Ms. Keller stated that a suit for injunctive relief to stop the school district from continuing to accept 403(b) administrative services from a vendor-affiliated administrator at below-market costs could be filed. Ms. Keller did not believe that a district could likely use sovereign immunity as a defense against such a request for injunctive relief. *Thus, the school district would face both the legal costs to defend its actions and possible negative publicity if found to be acting illegally.*

TCG's conclusion is that (a) school districts should act very cautiously in the use of 403(b) vendor-affiliated administrators to service their 403(b) plans and (b) if districts decide to use a 403(b) vendor-affiliated administrator, they must assure that they are paying such administrators fees comparable to those charged by non-affiliated 403(b) administrators.

TCG is a subsidiary of TCG Group Holdings, LLP, which also owns JEM Resource Partners, a third party administrator offering fee-only 403(b) administrative services.

HOUSE OF REPRESENTATIVES

CAPITOL OFFICE:
P.O. BOX 2910
AUSTIN, TX 78768-2910
(512) 463-0690
FAX: (512) 477-5770
E2.502 CAPITOL EXTENSION

VICKI TRUITT
DISTRICT 98

DISTRICT OFFICE:
1256 MAIN STREET, SUITE 245
SOUTHLAKE, TX 76092-7624
(817) 488-4098
FAX: (817) 488-4099
SOUTHLAKE TOWN SQUARE

FAX

To: Mike Cochran

Organization: _____

Phone Number: _____

Fax Number: 512/306-9959

From: TERRA TAYLOR

Subject: 403(6) letter

5 Page(s) to Follow

Comments:

_____

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_____

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HOUSE COMMITTEE ON PENSIONS AND INVESTMENTS
VICE CHAIRMAN:
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CAPITOL OFFICE:
P.O. BOX 2910
AUSTIN, TX 78768-2910
(512) 463-0690
FAX: (512) 477-5770
E2.502 CAPITOL EXTENSION

VICKI TRUITT
DISTRICT 98

DISTRICT OFFICE:
1256 MAIN STREET, SUITE 248
SOUTHLAKE, TX 76092-7624
(817) 488-4066
FAX: (817) 488-4099
SOUTHLAKE TOWN SQUARE

January 22, 2008

Mr. Ronnie Jung
Executive Director
Teacher Retirement System of Texas
1000 Red River Street
Austin, Texas 78701-2627

Dear Mr. Jung:

It has come to our attention that there are issues regarding Texas Teacher Retirement System of Texas' certification of companies offering 403(b) qualified investment products other than Annuity Contracts.

Section 403(b) of the Internal Revenue Code (the Code) allows educators to defer funds on a tax-deferred basis to a retirement plan similar to 401(k) plans in the private sector. Federal law restricts 403(b) plan investments to either (a) an annuity contract or (b) a mutual fund held under a custodial account as defined in Section 403(b)(7) of the Code.

There are several significant changes that will occur during the next 12 months in both Texas and federal rules concerning 403(b) plans. There is widespread belief in the retirement plan industry that after January 1, 2008, many of the lowest cost and highest performing mutual fund families will no longer choose to offer their products to Texas educators through 403(b) plans.

By way of background, in 2001, SB 273 (authored by Senator Armbrister), made major changes in how salary deferral retirement plans under Section 403(b) of the Internal Revenue Code (the Code) were marketed to Texas educators. One of these changes was to require TRS to certify which companies could offer 403(b) products for sale. In 2007, HB 2427 (authored by Representative Truitt) amended the process to require TRS to certify both 403(b) companies and products.

S.B. 273 amended Texas Civil Statutes, Vernon's Title 109, Article 6228a-5 to add qualifications for both annuity companies and other financial institutions to offer 403(b) products. Sections 5 and 6 of this Article provide fairly extensive guidelines for TRS to use in certifying annuity companies, then delegate the remaining certification rules to TRS.

CHAIRMAN:
HOUSE COMMITTEE ON PENSIONS AND INVESTMENTS
VICE CHAIRMAN:
SUNSET ADVISORY COMMISSION
MEMBER:
HOUSE COMMITTEE ON PUBLIC HEALTH

However, the Legislature provided much less guidance to TRS on non-annuity 403(b) products. This guidance is in Section 8 of the Article and reads as follows:

"Sec. 8. (a) A company that offers qualified investment products other than annuity contracts may certify to the retirement system based on rules adopted by the board of trustees. The rules shall be based on reasonable factors, including:
(1) the financial strength of the companies offering products; and
(2) the administrative cost to employees.
(b) The retirement system shall establish and maintain a list of companies that provide certification under this section. The list must be available on the retirement system's Internet website."

Thus, most of the rule making for non-annuity 403(b) products was left to TRS.

The Texas Administrative Code (TAC), as amended subsequent to the provisions of H.B. 2427, provides the rules for both company and product certification. These rules for non-annuity products are summarized below.

1. TAC Title 34, Part 3, Chapter 53, Rule §53.5 provides that companies seeking certification to offer Qualified Investment Products Other than Annuity Contracts must meet the following rules under §53.5(b):
   (1) The company has at least five years' experience in qualified investment products and has a specialized department dedicated to service of qualified investment products.
   (2) The company is qualified to do business in the State of Texas.
   (3) The company is registered with the Securities and Exchange Commission, the State Securities Board, or other regulatory entity, if required by law.
   (4) The company has not had a license or registration suspended or revoked by state or federal regulators within the five years preceding the date the certification is filed.
   (5) The company manages assets of at least $2 billion.
   (6) The company does not assess fees, costs, or penalties that exceed the maximum amounts established by this chapter.
   (7) The company's products comply with the registration requirements of Article 6228a-5, Texas Civil Statutes, and this chapter, as applicable.

2. TAC Title 34, Part 3, Chapter 53, Rule §53.3, subsections (c) through (d) provide the maximum fees and penalties that any 403(b) product, whether an annuity or non-annuity, may charge. These are straightforward and relatively simple for vendors to understand and implement.

The TAC was amended in 2007 to add individual product registration requirements, as provided in HB 2427. Rules §53.15, §53.16, §53.17, and §53.18 were added to implement the product registration rules. TRS also published an extensive 403(b) Product Registration System Manual to give detailed guidance to companies wishing to offer 403(b) qualified investment products.

TRS currently certifies only individual mutual fund families as non-annuity qualified investment products. TRS will not certify other non-annuity investment programs that offer mutual funds.

These non-annuity investment programs are common in the 401(k) market. Companies such as Charles Schwab, Fidelity and many others offer investment platforms that allow plan participants to purchase many different mutual funds from multiple companies at a low cost through a single source. Section 403(b)(7) of the Internal Revenue Code does not preclude this practice. In fact, 403(b)(7) non-annuity platforms that offer multiple mutual fund families are common in other states.

TRS *does* certify variable annuity products as qualified investment products. These annuity products typically offer mutual fund investments through insurance company "sub-accounts." However, many of these products have received widespread criticism in major publications. Articles have appeared in the Wall Street Journal, Forbes Magazine, the Los Angeles Times and other publications in recent years alleging that many 403(b) variable annuities have very high fees relative to other types of investments.

Some in the retirement plan industry believe that the current TRS practice is not a benefit to Texas educators. However, up to now the number of annuities and mutual funds has been adequate enough that a significant outcry has not occurred among educators.

This may now change for two reasons.

First, on July 24, 2007 the Internal Revenue Service (IRS) issued the final 403(b) regulations. These new rules, available on the IRS website at http://www.irs.gov/pub/irs-tege/td9340.pdf, go into effect for public education organizations on January 1, 2009.

These regulations make sweeping changes in 403(b) plans that will require educational institutions to exercise much greater oversight in administering these plans. The new rules will also involve much more work for the vendors that sell 403(b) products, since they must work within the framework of each individual employer's 403(b) plan rules.

Many experts in the 403(b) industry expect the new IRS regulations to result in an overall reduction in the number of investment options for participants.

Second, the new Texas 403(b) product rules will result in more work by mutual fund companies. The reason is that a vendor must complete several pages of information about each product it sells, then submit this to TRS.

A variable annuity product vendor must only fill out a single set of pages even if it offers hundreds or even thousands of mutual funds through its product sub-accounts. However, a mutual fund family must fill out the same set of pages for *each fund* it offers. For a fund family like Vanguard that offers hundreds of funds, this will result in significant and likely unacceptable increases overhead costs.

If the low-cost mutual fund companies do not submit product qualification applications to TRS, then beginning in 2008 they will have to be removed from payroll by school districts.

With the combination of TRS product rule requirements and the new federal 403(b) plan rules, the product vendors that would be most expected to withdraw from the Texas market (due to increased administrative expenses) are those that have the smallest profit margins. No-load and low-cost mutual fund families fit this profile. They offer their funds at a low cost and typically cannot increase administrative expenses significantly. Rather than raise their fees significantly, they are expected to withdraw their products from the Texas market due to the increased administrative expenses.

This outcome can be changed if TRS begins certifying non-annuity qualified investment products. It is our understanding that this would require little change in the current rules. All of the rules in TAC Title 34, Part 3, Chapter 53, Rules §53.3, §53.5. §53.15, §53.16, §53.17, and §53.18 could be applied. The only potential change in the interpretation and/or language of the TAC (depending on the interpretation by TRS) would be to make it clear that the term "company" would be defined as a trust company, custodian and/or brokerage firm that offers an administrative platform through which the mutual funds are offered, and not the mutual fund family itself.

We want to express one note of caution regarding non-annuity investment programs to be certified as 403(b) providers by TRS. Prior to the passage of S.B. 273 there were certain third party administrators (TPAs) that both administered 403(b) plans for school districts and sold 403(b) products. In some cases this resulted in a "layering" of fees paid by educators for 403(b) products. Educators paid for the TPA services then paid additional fees for the products. We believe that much of the abusive practice in this area was eliminated by implementation of S.B. 273.

If TRS implements a certification process for non-annuity investment programs we believe it is important to assure that there is no return to abusive fee practices. We hope that you will consider including requirements under the certification rules that provide (1) the limits on fees imposed by TAC Title 34, Part 3, Chapter 53, Rule §53.3, subsections (c) through (d) must include *all* fees related to the product or sale of the product charged by the investment company, custodian, marketing company, broker and/or TPA offering the product and (2) the investment company, custodian, marketing company, broker and/or TPA offering the product is not be allowed to administer the 403(b) plan of the educational institution.

TRS would probably have to undertake additional work to certify appropriate non-annuity investment platforms. However, it would appear that this would be well justified by the benefits this would provide to Texas educators.

Please understand that we believe an adjustment in TRS rules to allow the market to adjust in Texas as it is adjusting in other states thereby allowing the certification of companies offering qualified investment products other than Annuity Contracts is entirely consistent with the legislative intent of both SB 273 and HB 2427.

January 22, 2008

As the authors of these bills, we are hopeful that this correspondence will give you the guidance you need to allow these worthwhile products to continue to be available to our public school educators.

Sincerely,

Vicki Truitt, Chair
House Committee on Pensions & Investments

Senator Ken Armbrister (Retired)

cc: The Honorable Tom Craddick, Speaker
The Honorable Robert Duncan

403(b) Plan Issues
Addressed by HB 3480
Sponsored by Representative Vicki Truitt, Chair
House Committee on Pensions, Investments & Financial Services

Why HB 3480 Is Needed

1. Abusive Practices by TPAs affiliated with Companies Selling 403(b) Products

   (a) Issue. Certain Third Party Administrators (TPAs) offer to administer 403(b) plans for school districts at no cost or a greatly reduced cost. They do this in order to gain access to employees on a favorable basis to market 403(b) products. Since the charges to the employees in these products must be high enough to cover the "free" or reduced price administration for the district, the employee is paying for the administration. *This practice can also be deceptive since employees (a) often do not understand these product charges and (b) may believe that the TPA-affiliated vendor has an "implied endorsement" from the district since the TPA is also administering the 403(b) plan.*

   (b) Legislative Intent. In 2001 the Texas Legislature passed S.B. 273 and this was signed into law. Article 6228a-5, Section 9(a)(6) states that "An educational institution may not accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products." *The intent of this legislation was to prevent these types of marketing practices in public schools. Unfortunately, due to major changes in federal 403(b) rules school districts began to violate this provision and accept "free" services.*

   (c) HB 3480 Solution. HB 3480 would prohibit financial institutions or their affiliates that sell 403(b) products to offer 403(b) administration services to school districts. The companies would have a clear choice: administer 403(b) plans or sell 403(b) products. However, they could not do both because this is a conflict of interest.

2. Improved 403(b) Investment Choices for Educators

   (a) Issues.

      (1) Limitations on Certification. TRS certifies only individual mutual fund families as non-annuity qualified investment product options. TRS believes they need additional statutory authority to allow such other investment options options.

      (2) Multi-Fund Investment Platforms. Non-annuity investment programs are common in the 403(b) market in other states. Companies such as Charles Schwab, Fidelity and many others offer investment platforms that allow plan participants to purchase many different mutual funds from multiple companies at a low cost through a single source. HB 3480 would allow TRS to certify such options.

      (3) Variable Annuity Alternatives. Current law does allow TRS to certify variable annuity products as qualified investment products. These annuity products typically offer mutual fund investments through insurance company "sub-accounts." However, many of these products have received widespread criticism in major publications. Articles have appeared in the Wall Street Journal, Forbes Magazine, the Los Angeles Times and other publications in recent years alleging that many 403(b) variable annuities have very high fees relative to other types of investments.

   (b) HB 3480 Solution. HB 3480 would amend current law to specifically permit companies that offer a multi-mutual fund family 403(b) "platform" to receive TRS certification as long as all of the funds offered are also certified products under TRS rules.

To: State Representative Chairman Vicki Truitt April 6, 2009
Re: HB 3480
From: United Educators Association

Honorable Chairman Truitt,

United Educators Association (UEA) is an independent teacher association representing more than 16,000 educators in North Texas.

We are writing to give the support of our Association to HB 3480.

Whereas UEA has long supported the 7 teacher protections listed in Section 9, Article 6228a-5, Vernon's Texas Civil Statutes, and

Whereas our members are suffering by non-compliance of Section 9(a)(6), "..an educational institution may not accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products" meaning 403(b), and

Whereas our members are suffering financially by non-compliance of Section 9(a)(3),.."an educational institution may not limit the ability of an employee to initiate, change or terminate a qualified investment product at any time the employee chooses" and

Whereas our members are being denied their right to access over 70 de-listed TRS Certified products/companies for the purposes of IRS approved purchase of service credit, inexpensive loans and hardship relief to help prevent home foreclosure, and

Whereas our members who have contributed to those TRS Certified de-listed companies were denied the right of Section 9(a)(3) to begin a new contribution in any of the remaining 14 companies, for more than 3 months, and

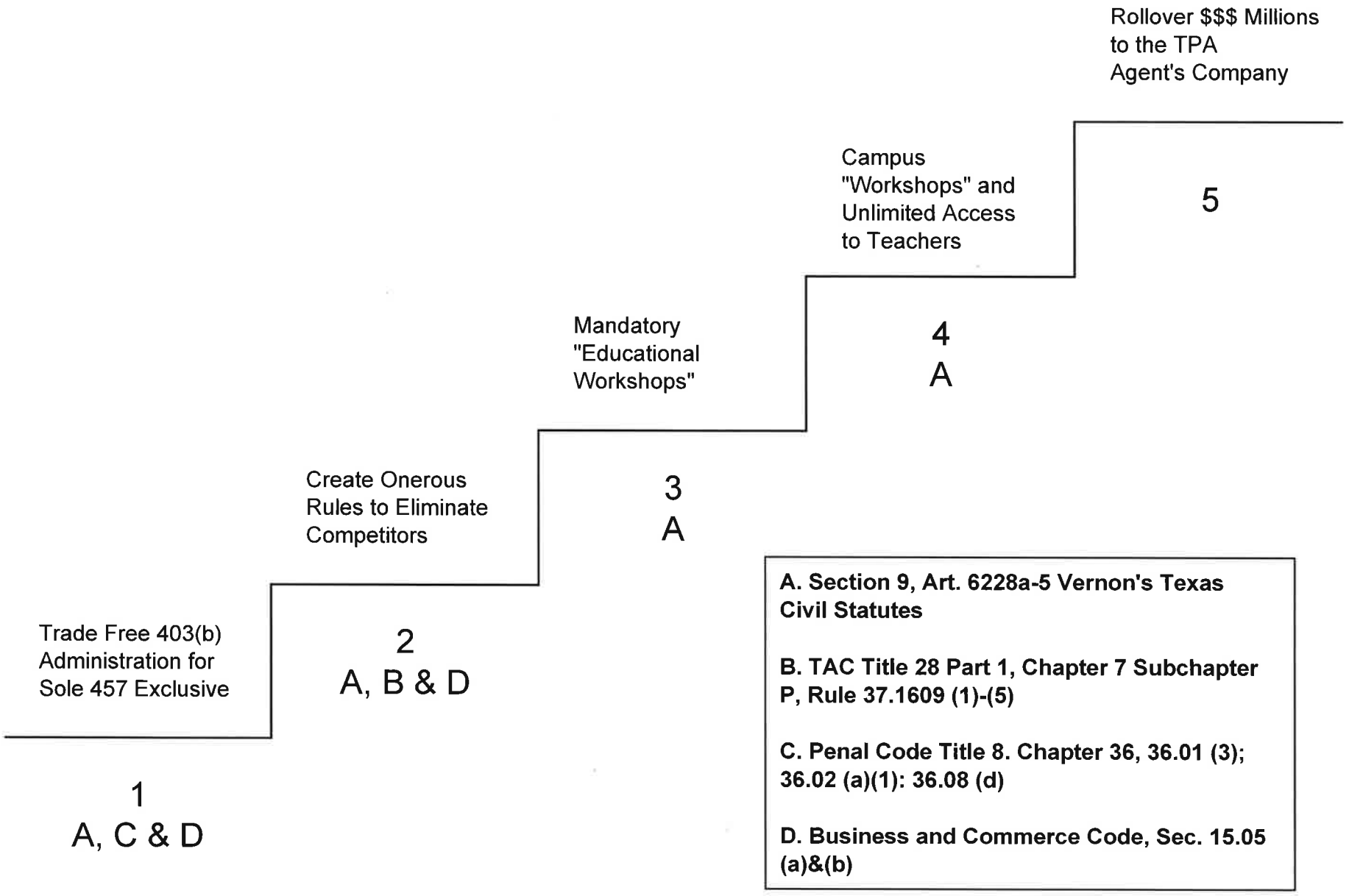
Whereas many of our members have been financially damaged to the point of not being allowed to shelter from taxation the maximum allowable amount permitted by the IRS in 2009, and

Whereas we oppose any 403(b) vendor or affiliate of a vendor any kind being involved in any way with the administration of the 403(b) voluntary federal pension, UEA therefore

Supports HB 3480 as the exact remedy for the financial damage done to our members and others.

Larry Shaw
Executive Director

HB 3480


Rollover $$$ Millions to the TPA Agent's Company
Campus "Workshops" and Unlimited Access to Teachers
5
Mandatory "Educational Workshops"
4
A
Create Onerous Rules to Eliminate Competitors
3
A
Trade Free 403(b) Administration for Sole 457 Exclusive
2
A, B & D
1
A, C & D
A. Section 9, Art. 6228a-5 Vernon's Texas Civil Statutes
B. TAC Title 28 Part 1, Chapter 7 Subchapter P, Rule 37.1609 (1)-(5)
C. Penal Code Title 8. Chapter 36, 36.01 (3); 36.02 (a)(1): 36.08 (d)
D. Business and Commerce Code, Sec. 15.05 (a)&(b)

Texas House of Representatives
Committee On Pensions, Investments & Financial Services
June 22, 2010

Chairwoman Truitt and members of the Committee: I am Mike Cochran and am here to thank the Chair and members of the Committee for their efforts on behalf of Texas educators in the 80th and 81st Sessions of the Legislature, with the passage of HB 2341 and HB 3480, respectively.

I am a partner in TCG Group Holdings, LLP, an Austin-based company that offers investment advisory services and retirement plan administration on a fee-for-service basis. Our third party administrator, JEM Resource Partners, administers the 403(b) plans of 135 Texas school districts and over ½ of the plans of the largest 20 districts. JEM is also the administrator of the California State Teachers Retirement System 403(b) administration program offered to all public school districts and community colleges in California.

We also administer 403(b) plans in a number of other states and are active in the 403(b) industry nationally.

The comment I wish to make is that we see many abuses in 403(b) plans across the nation. No state has a perfect regulatory environment. However, we believe that there are fewer abuses in Texas than any other state. The laws put in place by the Texas Legislature over the past 10 years have gone a long way in preventing many abuses of educators in 403(b) plans.

We also want to thank the Teacher Retirement System of Texas for the job they have done in overseeing the company and product certification process. The information available to Texas educators on the TRS website is comprehensive and easy to use.

We also want to add a note of caution. We would love to see every possible abuse ended by legislation. But we only have to look to the pension laws passed by the U.S. Congress to see what can happen when well-meaning lawmakers try to prevent every conceivable abuse. My career with pension plans started in the mid-1970s. I have seen Congress destroy some very good pension programs such as defined benefit plans for small employers, by over-

legislation. In my opinion, Congress has on occasion tried to can cure every conceivable disease and killed the patient.

So, thank you for the work you have done. You have not ended every possible abuse but, in my opinion, you have done a great job of creating an environment where the abuses are limited, well controlled and have provided good remedies for dealing with abuses that do occur.

AN ACT

relating to certain investment products made available to certain public school employees and the companies authorized to provide those products; providing civil penalties.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. Section 4, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 4. In this section and in Sections 5, 6, 7, 8, 8A, 9, 9A, 9B, 10, 11, 12, and 13 of this Act:

(1) "Board of trustees" means the board of trustees of the Teacher Retirement System of Texas.

(2) "Educational institution" means a school district or an open-enrollment charter school.

(3) "Eligible qualified investment" means a qualified investment product offered by a company that:

(A) is certified to the board of trustees under Section 5 of this Act; or

(B) is eligible to certify to the board of trustees under Section 8 of this Act.

(4) "Employee" means an employee of an educational institution.

(5) "Qualified investment product" means an annuity or investment that:

(A) meets the requirements of Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) complies with applicable federal insurance and securities laws and regulations; and

(C) complies with applicable state insurance and securities laws and rules.

(6) "Retirement system" means the Teacher Retirement System of Texas.

(7) "Salary reduction agreement" means an agreement between an educational institution and an employee to reduce the employee's salary for the purpose of making direct contributions to or purchases of a qualified investment product.

SECTION 2. Section 6, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended by amending Subsections (c), (d), (e), and (f) and adding Subsections (d-1), (d-2), and (f-1) to read as follows:

(c) After consultation with the Texas Department of Insurance, the Texas Department of Banking, and the State Securities Board, the retirement system may adopt rules only to administer this section and Sections 5, 7, 8, 8A, 9A, 9B, 11, 12, and 13 of this Act.

(d) The retirement system shall refer all complaints about qualified investment products, including complaints that allege violations of this Act by companies that certify to the retirement system under Section 5 or 8 of this Act that the companies offer qualified investment products, to the appropriate division of the

Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board.

(d-1) Except as provided by Subsection (d-2) of this section, the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board shall investigate a complaint received from the retirement system under Subsection (d) of this section. If as a result of the investigation the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board, as applicable, determines that a violation of this Act may have occurred, the Texas Department of Insurance, the Texas Department of Banking, or the State Securities Board, as applicable, shall forward the results of the investigation relating to an alleged violation of this Act to the attorney general.

(d-2) If the Texas Department of Banking receives a complaint from the retirement system under Subsection (d) of this section that relates to a federally chartered financial institution, the Texas Department of Banking shall:

(1) refer the complaint to the appropriate federal regulatory agency; and

(2) notify the attorney general of the department's referral.

(e) The Texas Department of Insurance, the Texas Department of Banking, and the State Securities Board shall cooperate with the retirement system in the administration of this Act and shall:

(1) submit a report to [~~notify~~] the retirement system at the beginning of each quarter of the fiscal year that provides the status of any enforcement action taken or investigation or

referral made [~~determination~~] regarding a product or a company that is the subject of a complaint under Subsection (d) of this section; and

(2) promptly notify the retirement system of any final enforcement order issued regarding the product or company [~~violates Section 5 or 8A of this Act~~].

(f) The retirement system may deny, suspend, [~~shall reject~~] or revoke the certification of a company if the retirement system receives notice that [~~under Subsection (e) of this section or Section 5(c) of this Act of a violation regarding~~] the company or the company's product was determined to be in violation of this Act or another law in any judicial or administrative proceeding.

(f-1) A [~~The~~] company whose certification is denied, suspended, or revoked under this section may recertify to the board of trustees after any applicable period of suspension or revocation.

SECTION 3. Section 8(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(a) A company that offers qualified investment products other than annuity contracts, including a company that offers custodial accounts under Section 403(b)(7), Internal Revenue Code of 1986, that hold only investment products registered with the system under Section 8A of this Act, may certify to the retirement system based on rules adopted by the board of trustees. The rules shall be based on reasonable factors, including:

(1) the financial strength of the companies offering

products; and

(2) the administrative cost to employees.

SECTION 4. Section 9(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(a) An educational institution may not:

(1) except as provided by Subdivision (8) of this subsection and Subsection (b) of this section, refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment and is registered with the system under Section 8A;

(2) require or coerce an employee's attendance at any meeting at which qualified investment products are marketed;

(3) limit the ability of an employee to initiate, change, or terminate a qualified investment product at any time the employee chooses;

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent or affiliate of a company offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent

or affiliate of a company that offers qualified investment products; [~~or~~]

(7) use public funds to recommend a qualified investment product offered by a company or an agent or affiliate of a company that offers a qualified investment product; or

(8) enter into or continue a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction agreement is not an eligible qualified investment, including the investment product of a company whose certification has been denied, suspended, or revoked without first providing the employee with notice in writing that:

(A) indicates the reason the subject of the salary reduction agreement is no longer an eligible qualified investment or why certification has been denied, suspended, or revoked; and

(B) clearly states that by signing the notice the employee is agreeing to enter into or continue the salary reduction agreement.

SECTION 5. Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended by adding Sections 9A and 9B to read as follows:

Sec. 9A. A person, other than an employee of an educational institution, or an affiliate of the person may not enter into or renew a contract under which the person is to provide services for or administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986, unless the person:

(1) holds a license or certificate of authority issued by the Texas Department of Insurance;

(2) is registered as a securities dealer or agent or investment advisor with the State Securities Board; or

(3) is a financial institution that:

(A) is authorized by state or federal law to exercise fiduciary powers; and

(B) has its main office, a branch office, or a trust office in this state.

Sec. 9B. (a) This section applies to an entity under this Act that enters into a contract with an educational institution to administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986.

(b) If a person described by Subsection (a) holds a meeting at which qualified investment products will be marketed to employees of the educational institution, the person must provide representatives of other companies certified to the retirement system under Section 5 or 8 of this Act an opportunity to attend and market their qualified investment products at the meeting.

SECTION 6. Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(a) A person commits an offense if the person:

(1) sells or offers for sale an [~~a qualified~~] investment product that is not an eligible qualified investment or that is not registered under Section 8A of this Act and that the person knows will be the subject of a salary reduction agreement;

(2) violates the licensing requirements of Title 13, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement; or

(3) engages in activity described by Subchapter B, Chapter 541, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement.

SECTION 7. Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended by adding Section 10A to read as follows:

Sec. 10A. (a) A person who violates this Act is subject to a civil penalty in an amount that does not exceed:

(1) $10,000 for a single violation; or

(2) $1,000,000 for multiple violations.

(b) For purposes of determining the amount of a civil penalty under this section, the court shall consider the following factors:

(1) the seriousness, nature, circumstances, extent, and persistence of the conduct constituting the violation;

(2) the harm to other persons resulting directly or indirectly from the violation;

(3) cooperation by the person in any inquiry conducted by the state concerning the violation, efforts to prevent future occurrences of the violation, and efforts to mitigate the harm caused by the violation;

(4) the history of previous violations by the person;

(5) the need to deter the person or others from committing such violations in the future; and

(6) other matters as justice may require.

(c) The attorney general may institute an action:

(1) for injunctive relief to restrain a violation by a person who is or who appears to be in violation of or threatening to violate this Act; or

(2) to collect a civil penalty under this section.

(d) An action under this section must be filed in a district court in Travis County.

(e) The attorney general may recover reasonable expenses incurred in obtaining injunctive relief under this section, including court costs, reasonable attorney's fees, investigative costs, witness fees, and deposition expenses.

SECTION 8. (a) Section 9(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), as amended by this Act, applies to a salary reduction agreement that is entered into or renewed on or after the effective date of this Act. A salary reduction agreement that is entered into or renewed before the effective date of this Act is governed by the law in effect on the date the agreement was entered into or renewed, and the former law remains in effect for that purpose.

(b) Sections 9A and 9B, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), as added by this Act, apply to a

contract to administer a plan under Section 403(b), Internal Revenue Code of 1986, offered by a school district or open-enrollment charter school that is entered into or renewed on or after the effective date of this Act. A contract entered into or renewed before the effective date of this Act is governed by the law in effect on the date the contract was entered into or renewed, and the former law remains in effect for that purpose.

(c) Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), as amended by this Act, and Section 10A, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), as added by this Act, apply only to a violation that occurs on or after the effective date of this Act. A violation that occurred before the effective date of this Act is covered by the law in effect at the time the violation occurred, and the former law is continued in effect for that purpose.

SECTION 9. This Act takes effect September 1, 2009.

President of the Senate

Speaker of the House

I certify that H.B. No. 3480 was passed by the House on May 14, 2009, by the following vote: Yeas 134, Nays 8, 3 present, not voting; and that the House concurred in Senate amendments to H.B. No. 3480 on May 29, 2009, by the following vote: Yeas 136, Nays 0, 1 present, not voting.

Chief Clerk of the House

I certify that H.B. No. 3480 was passed by the Senate, with amendments, on May 27, 2009, by the following vote: Yeas 31, Nays 0.

Secretary of the Senate

APPROVED: _____

Date

_____

Governor

HB 2820

The 86th Session of the Texas Legislature passed HB 2820 and its Senate companion, SB 1977, to end the Teacher Retirement System of Texas regulation of 403(b) companies and products in Texas. The bill was signed by the Governor in June 2019 and becomes effective September 1, 2019.

The following pages show the Bill Analysis of the final legislation as well as the language of HB 2820 showing the extensive changes made to the law.

BILL ANALYSIS

Senate Research Center
86R8229 KFF-F

H.B. 2820
By: Flynn (Hughes)
State Affairs
4/23/2019
Engrossed

AUTHOR'S / SPONSOR'S STATEMENT OF INTENT

Texas teachers and other school employees currently have the ability to use pre-tax dollars to purchase financial products through the Teacher Retirement System (TRS) 403(b) marketplace. This allows them to supplement their state pensions upon retirement—a practice the TRS Board's Policy Committee has said is advisable. Like 401(k) investment options, all 403(b) financial products are regulated by the state through the Texas Department of Insurance (TDI) and the State Securities Board and/or by the federal government through the SEC, FINRA, the IRS and the Department of Labor. This oversight includes registration, regulation and approval of these products, ensuring that strong consumer protection safeguards are in place. Additionally, if a teacher or other school employee chooses an insurance product such as an annuity, the beneficiary has access to Texas Life and Health Insurance Guaranty Association protections should the company offering the product become insolvent. TRS is currently charged with regulating 403(b) products—a role that is duplicative of existing state and federal regulation. TRS has limited funds and expertise to comply with these regulatory requirements, often turning to other state agencies and private consultants for assistance. In addition, current law requires the TRS Board of Trustees to set maximum fees for 403(b) products rather than allowing the market to determine these rates. Limiting fees may not only reduce product offerings, but also limits a company's ability to offer services that provide valuable advice and educational tools that can assist teachers in making appropriate choices for their retirement income. Further, focusing only on fees ignores product performance and could deny teachers access to products that may have higher returns.

Amending Texas law to remove TRS from 403(b) product regulation will eliminate dual regulation already being conducted by other appropriate state and federal agencies. Disclosures for those products and laws regulating market conduct will be overseen by TDI. Updating Texas law governing 403(b) products will allow TRS to focus on its core function of managing one of the largest public pension funds in the country.

H.B. 2820 amends current law relating to the registration and certification of certain investment products made available to public school employees.

RULEMAKING AUTHORITY

Rulemaking authority previously granted to the Teacher Retirement System of Texas is rescinded in SECTION 1.10 (Article 6228a-5, V.T.C.S.) of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1.01 Amends Section 4, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

> Sec. 4. Provides that in this section and in Sections 5, 6, 9, 9A, 9B, 10, 11, and 12, rather than Sections 5, 6, 7, 8, 8A, 9, 9A, 9B, 10, 11, 12, and 13 of this Act:
>
> > (1) Deletes existing definition of "board of trustees" and redesignates existing text of Subdivision (2) as Subdivision (1).
> >
> > (2) Defines "eligible qualified investment" to mean a qualified investment product offered by a company that is eligible to offer the product under Section 6 of this

Act, rather than to mean a qualified investment product offered by a company that is certified to the board of trustees under Section 5 of this Act, or is eligible to certify to the board of trustees under Section 8 of this Act.

(3) Redesignates existing text of Subdivision (4) as Subdivision (3).

(4) Redesignates existing text of Subdivision (5) as Subdivision (4).

(5) Redesignates existing text of Subdivision (7) as Subdivision (5). Deletes existing Subdivision (6) defining "retirement system."

SECTION 1.02. Amends Sections 5(a) and (f), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(a) Deletes existing text authorizing an educational institution to enter into a salary reduction agreement with an employee of the institution only if the qualified investment product is registered with the Teacher Retirement System of Texas (TRS) under Section 8A of this Act.

(f) Requires educational institutions that enter into a salary reduction agreement with employees under this section, rather than requiring employers of employees who participate in the program offered under this section, to the greatest degree possible, to require that contributions to eligible qualified investments be made by automatic payroll deduction and deposited directly in the investment accounts.

SECTION 1.03. Amends Sections 6(a) and (b), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(a) Provides that an insurance company is eligible to offer qualified investment products to the employees of educational institutions under this Act if the company satisfies the following criteria, rather than providing that a company is eligible to certify to TRS under Section 5 of this Act if the company satisfies the following financial strength criteria:

(1) the company is licensed by the Texas Department of Insurance (TDI) and is in compliance with minimum capital and surplus requirements, including applicable risk-based capital and surplus requirements prescribed by rules adopted by TDI, rather than the company's actuarial opinions required under Articles 1.11 and 3.28, Insurance Code, have not been adverse or qualified in the five years preceding the date the application is filed; and

(2) the company has experience in providing qualified investment products, rather than at least five years' experience in qualified investment products, and has a specialized department dedicated to the service of qualified investment products, as determined by the educational institution.

Deletes existing text of Subdivisions (2), (3), (4), and (5) and redesignates existing Subdivision (6) as Subdivision (2).

(b) Provides that a company that offers qualified investment products other than annuity contracts, including a company that offers custodial accounts under Section 403(b)(7), Internal Revenue Code of 1986, is eligible to offer qualified investment products to employees of educational institutions under this Act. Deletes existing text requiring the company, for purposes of Subsection (a)(4) of this section, to calculate the five-year average on the same date each year.

SECTION 1.04. Amends Section 9(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(a) Prohibits an educational institutional from:

(1) except as provided by Subdivision (8) of this subsection and Subsection (b) of this section, refusing to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment, rather than is an eligible qualified investment and is registered with the system under Section 8A;

(2)–(7) makes no changes to these subdivisions; or

(8) entering into or continuing a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction agreement is not an eligible qualified investment, rather than is not an eligible qualified investment, including the investment product of a company whose certification has been denied, suspended, or revoked, without first providing the employee with notice in writing that:

(A) indicates the reason the subject of the salary reduction agreement is no longer an eligible qualified investment, rather than indicates the reason the subject of the salary reduction agreement is no longer an eligible qualified investment or why certification has been denied, suspended, or revoked; and

(B) makes no changes to this paragraph.

SECTION 1.05. Amends Section 9A, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

Sec. 9A. Prohibits a person, other than an employee of an educational institution, or an affiliate of the person from entering into or renewing a contract under which the person is to provide services for or administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986, unless the person:

(1)–(2) makes no changes to these subdivisions; or

(3) is a financial institution that has sufficient presence in this state to serve the employees of educational institutions who participate in the plan, rather than has its main office, a branch office, or a trust office in this state.

SECTION 1.06. Amends Section 9B(b), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(b) Requires a person, if the person described by Subsection (a) holds a meeting at which qualified investment products will be marketed to employees of the educational institution, to provide representatives of other companies eligible to sell qualified investment products under Section 6, rather than provide representatives of other companies certified to TRS under Section 5 or 8, of this Act an opportunity to attend and market their qualified investment products at the meeting.

SECTION 1.07. Amends Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(a) Provides that a person commits an offense if the person sells or offers for sale an investment product that is not an eligible qualified investment, rather than if the person sells or offers for sale an investment product that is not an eligible qualified investment or that is not registered under Section 8A of this Act, and that the person knows will be the subject of a salary reduction agreement.

SECTION 1.08. Amends Section 11(c), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

(c) Requires the notice required under this section to be uniform and:

(1)–(2) makes no changes to these subdivisions; and

(3) to state, in plain language:

(A) that the company offering the annuity is required to comply with Section 6 of this Act and that the annuity is required to be a qualified investment product, rather than that the company offering the annuity is required to comply with Section 5 of this Act and that the annuity is required to be a qualified investment product registered under Section 8A of this Act;

(B) deletes existing text of Paragraph (B) providing that the notice is required to state, in plain language, that the potential purchaser is authorized to contact TRS or access its Internet website to determine which companies are in compliance with Section 5 of this Act and which qualified investment products are registered under Section 8A of this Act;

(C) Creates Paragraph (B) from existing Paragraph (C), redesignates existing text of Paragraph (D) as Paragraph (C), and renumbers the paragraphs accordingly.

SECTION 1.09. Amends Section 12, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), as follows:

Sec. 12. Requires a company that offers an eligible qualified investment that is subject to a salary reduction agreement to require, rather than to demonstrate annually to TRS, that each of its representatives are properly licensed and qualified, by training and continuing education, to sell and service the company's eligible qualified investments.

SECTION 1.10. Repealers: Sections 5(b) (relating to authorizing a company to certify to TRS that the company offers a qualified investment product), (c) (relating to requiring a company that certifies to notify TRS if the company is not in compliance), (d) (relating to requiring TRS to establish and maintain a list of companies that have certified), and (e) (relating to entitling an employee to designate any certain entity through which a qualified investment is authorized to be made), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Sections 6(c) (relating to authorizing TRS to adopt rules to administer certain sections of this Act), (d) (relating to requiring TRS to refer all complaints about qualified investment products to certain entities), (d-1) (relating to requiring certain entities to investigate a complaint received from TRS), (d-2) (relating to requiring the Texas Department of Banking to take certain actions if a certain complaint is received), (e) (relating to requiring certain entities to cooperate with TRS), (f) (relating to authorizing the retirement system to deny, suspend, or revoke the certification of a company), (f-1) (relating to authorizing a company to recertify under certain conditions), (g) (relating to requiring TRS to prescribe a required uniform notice), (h) (relating to the duration of a certification or recertification), and (i) (relating to requiring a company offering certain investments to provide toll-free telephone transferring privileges), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Section 7 (relating to authorizing TRS to collect certain fees), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Section 8 (relating to certification procedures for certain companies), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Section 8A (relating to registration application procedures for a company), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Section 11(b) (relating to requiring TRS to make a certain notice available on request and post the form of the notice on TRS's Internet website), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

Repealer: Section 13 (relating to authorizing the board of trustees of TRS to deny, suspend, or revoke the certification or recertification of a company), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.).

ARTICLE 2. CONFORMING CHANGE

SECTION 2.01. Reenacts Section 17.46(b), Business & Commerce Code, as amended by Chapters 324 (S.B. 1488), 858 (H.B. 2552), and 967 (S.B. 2065), Acts of the 85th Legislature, Regular Session, 2017, and amends it as follows:

(b) Redefines "false, misleading, or deceptive acts or practices," to include certain acts, including selling, offering to sell, or illegally promoting an annuity contract under Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), with the intent that the annuity contract will be the subject of a salary reduction agreement, as defined by that Act, if the annuity contract is not an eligible qualified investment under that Act, rather than selling, offering to sell, or illegally promoting an annuity contract under Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), with the intent that the annuity contract will be the subject of a salary reduction agreement, as defined by that Act, if the annuity contract is not an eligible qualified investment under that Act or is not registered with TRS as required by Section 8A of that Act. Makes nonsubstantive changes.

ARTICLE 3 TRANSITIONS; CONFLICT WITH OTHER LEGISLATION; EFFECTIVE DATE

SECTION 3.01. Makes application of Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), prospective.

SECTION 3.02. Makes application of Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, V.T.C.S.), prospective. Provides that, for purposes of this section, an offense is committed before the effective date of this Act if any element of the offense occurs before that date.

SECTION 3.03. Makes application of Section 17.46(b), Business & Commerce Code, as amended by this Act, prospective.

SECTION 3.04. Provides that, to the extent of any conflict, this Act prevails over another Act of the 86th Legislature, Regular Session, 2019, relating to nonsubstantive additions to and corrections in enacted codes.

SECTION 3.05. Effective date: September 1, 2019.

H.B. No. 2820

AN ACT

relating to the registration and certification of certain investment products made available to public school employees.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

ARTICLE 1. ELIGIBLE QUALIFIED INVESTMENTS

SECTION 1.01. Section 4, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 4. In this section and in Sections 5, 6, [~~7, 8, 8A,~~] 9, 9A, 9B, 10, 11, and 12[~~, and 13~~] of this Act:

(1) [~~"Board of trustees" means the board of trustees of the Teacher Retirement System of Texas.~~

[~~(2)~~] "Educational institution" means a school district or an open-enrollment charter school.

(2) [~~(3)~~] "Eligible qualified investment" means a qualified investment product offered by a company that[~~:~~

[~~(A)~~] is eligible to offer the product [~~certified to the board of trustees~~] under Section 6 [~~5~~] of this Act[~~; or~~

[~~(B) is eligible to certify to the board of~~

~~trustees under Section 8 of this Act~~].

(3) [~~(4)~~] "Employee" means an employee of an educational institution.

(4) [~~(5)~~] "Qualified investment product" means an annuity or investment that:

(A) meets the requirements of Section 403(b), Internal Revenue Code of 1986, and its subsequent amendments;

(B) complies with applicable federal insurance and securities laws and regulations; and

(C) complies with applicable state insurance and securities laws and rules.

(5) [~~(6) "Retirement system" means the Teacher Retirement System of Texas.~~

[~~(7)~~] "Salary reduction agreement" means an agreement between an educational institution and an employee to reduce the employee's salary for the purpose of making direct contributions to or purchases of a qualified investment product.

SECTION 1.02. Sections 5(a) and (f), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), are amended to read as follows:

(a) An educational institution may enter into a salary reduction agreement with an employee of the institution only if

the qualified investment product [~~:~~

[~~(1)~~] is an eligible qualified investment[~~; and~~

[~~(2) is registered with the retirement system under Section 8A of this Act~~].

(f) To the greatest degree possible, educational institutions that enter into a salary reduction agreement with [~~employers of~~] employees [~~who participate in the program offered~~] under this section shall require that contributions to eligible qualified investments be made by automatic payroll deduction and deposited directly in the investment accounts.

SECTION 1.03. Sections 6(a) and (b), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), are amended to read as follows:

(a) An insurance [~~A~~] company is eligible to offer qualified investment products to the employees of educational institutions under [~~certify to the retirement system under Section 5 of~~] this Act if the company satisfies the following [~~financial strength~~] criteria:

(1) the company is licensed by the Texas Department of Insurance and is in compliance with minimum capital and surplus requirements, including applicable risk-based capital and surplus requirements prescribed by rules adopted by the department

[~~company's actuarial opinions required under Articles 1.11 and 3.28, Insurance Code, have not been adverse or qualified in the five years preceding the date the application is filed;~~

[~~(2) the company is subject to the annual audit requirements of Article 1.15A, Insurance Code, and its most recent audit of financial strength conducted by an independent certified public accountant is timely filed and does not indicate the existence of any material adverse financial conditions in the company for the five years preceding the filing deadline for the audit;~~

[~~(3) the company has not been the subject of an administrative or regulatory action by the Texas Department of Insurance under Article 1.32 or 21.28-A or Section 83.051, Insurance Code, in the five years preceding the date the application is filed;~~

[~~(4) the company has maintained during the five years preceding the date the application is filed an average of at least 400 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus requirements established in rules adopted by the Texas Department of Insurance;~~

[~~(5) the company has not fallen below 300 percent of the authorized control level, as calculated in accordance with the risk-based capital and surplus established in rules adopted by the~~

~~Texas Department of Insurance, at any time in the five years preceding the date the application is filed~~]; and

(2) [~~(6)~~] the company has [~~at least five years'~~] experience in providing qualified investment products and has a specialized department dedicated to the service of qualified investment products, as determined by the educational institution.

(b) A company that offers qualified investment products other than annuity contracts, including a company that offers custodial accounts under Section 403(b)(7), Internal Revenue Code of 1986, is eligible to offer qualified investment products to employees of educational institutions under this Act [~~For purposes of Subsection (a)(4) of this section, the company must calculate the five-year average on the same date each year~~].

SECTION 1.04. Section 9(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(a) An educational institution may not:

(1) except as provided by Subdivision (8) of this subsection and Subsection (b) of this section, refuse to enter into a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction is an eligible qualified investment [~~and is registered with the system under Section 8A~~];

(2) require or coerce an employee's attendance at any meeting at which qualified investment products are marketed;

(3) limit the ability of an employee to initiate, change, or terminate a qualified investment product at any time the employee chooses;

(4) grant exclusive access to an employee by discriminating against or imposing barriers to any agent, broker, or company that provides qualified investment products under this Act;

(5) grant exclusive access to information about an employee's financial information, including information about an employee's qualified investment products, to a company or agent or affiliate of a company offering qualified investment products unless the employee consents in writing to the access;

(6) accept any benefit from a company or from an agent or affiliate of a company that offers qualified investment products;

(7) use public funds to recommend a qualified investment product offered by a company or an agent or affiliate of a company that offers a qualified investment product; or

(8) enter into or continue a salary reduction agreement with an employee if the qualified investment product that is the subject of the salary reduction agreement is not an eligible

qualified investment[~~, including the investment product of a company whose certification has been denied, suspended, or revoked~~] without first providing the employee with notice in writing that:

(A) indicates the reason the subject of the salary reduction agreement is no longer an eligible qualified investment [~~or why certification has been denied, suspended, or revoked~~]; and

(B) clearly states that by signing the notice the employee is agreeing to enter into or continue the salary reduction agreement.

SECTION 1.05. Section 9A, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 9A. A person, other than an employee of an educational institution, or an affiliate of the person may not enter into or renew a contract under which the person is to provide services for or administer a plan offered by the institution under Section 403(b), Internal Revenue Code of 1986, unless the person:

(1) holds a license or certificate of authority issued by the Texas Department of Insurance;

(2) is registered as a securities dealer or agent or investment advisor with the State Securities Board; or

(3) is a financial institution that:

(A) is authorized by state or federal law to exercise fiduciary powers; and

(B) has sufficient presence [~~its main office, a branch office, or a trust office~~] in this state to serve the employees of educational institutions who participate in the plan.

SECTION 1.06. Section 9B(b), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(b) If a person described by Subsection (a) holds a meeting at which qualified investment products will be marketed to employees of the educational institution, the person must provide representatives of other companies eligible to sell qualified investment products under Section 6 [~~certified to the retirement system under Section 5 or 8~~] of this Act an opportunity to attend and market their qualified investment products at the meeting.

SECTION 1.07. Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(a) A person commits an offense if the person:

(1) sells or offers for sale an investment product that is not an eligible qualified investment [~~or that is not registered under Section 8A of this Act~~] and that the person knows will be the subject of a salary reduction agreement;

(2) violates the licensing requirements of Title 13, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement; or

(3) engages in activity described by Subchapter B, Chapter 541, Insurance Code, with regard to a qualified investment product that the person knows will be the subject of a salary reduction agreement.

SECTION 1.08. Section 11(c), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

(c) The notice required under this section must be uniform and:

(1) be in at least 14-point type;

(2) contain spaces for:

(A) the name, address, and telephone number of the agent and company offering the annuity contract for sale;

(B) the name, address, and telephone number of the company underwriting the annuity;

(C) the license number of the person offering to sell the product;

(D) the name of the state agency that issued the person's license;

(E) the name of the company account representative who has the authority to respond to inquiries or complaints; and

(F) with respect to fixed annuity products:

(i) the current interest rate or the formula used to calculate the current rate of interest;

(ii) the guaranteed rate of interest and the percentage of the premium to which the interest rate applies;

(iii) how interest is compounded;

(iv) the amount of any up-front, surrender, withdrawal, deferred sales, and market value adjustment charges or any other contract restriction that exceeds 10 years;

(v) the time, if any, the annuity is required to be in force before the purchaser is entitled to the full bonus accumulation value;

(vi) the manner in which the amount of the guaranteed benefit under the annuity is computed;

(vii) whether loans are guaranteed to be available under the annuity;

(viii) what restrictions, if any, apply to the availability of money attributable to the value of the annuity once the purchaser is retired or separated from the employment of the employer;

(ix) the amount of any other fees, costs, or

penalties;

(x) whether the annuity guarantees the participant the right to surrender a percentage of the surrender value each year, and the percentage, if any; and

(xi) whether the annuity guarantees the interest rate associated with any settlement option; and

(3) state, in plain language:

(A) that the company offering the annuity must comply with Section 6 [~~5~~] of this Act and that the annuity must be a qualified investment product [~~registered under Section 8A of this Act~~];

(B) [~~that the potential purchaser may contact the retirement system or access its Internet website to determine which companies are in compliance with Section 5 of this Act and which qualified investment products are registered under Section 8A of this Act;~~

[~~(C)~~] the civil remedies available to the employee;

(C) [~~(D)~~] that the employee may purchase any eligible qualified investment through a salary reduction agreement;

(D) [~~(E)~~] the name and telephone number of the Texas Department of Insurance division that specializes in consumer protection; and

(E) [~~(F)~~] the name and telephone number of the attorney general's division that specializes in consumer protection.

SECTION 1.09. Section 12, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), is amended to read as follows:

Sec. 12. A company that offers an eligible qualified investment that is subject to a salary reduction agreement shall require [~~demonstrate annually to the retirement system~~] that each of its representatives are properly licensed and qualified, by training and continuing education, to sell and service the company's eligible qualified investments.

SECTION 1.10. The following laws are repealed:

(1) Sections 5(b), (c), (d), and (e), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(2) Sections 6(c), (d), (d-1), (d-2), (e), (f), (f-1), (g), (h), and (i), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(3) Section 7, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(4) Section 8, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(5) Section 8A, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes);

(6) Section 11(b), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes); and

(7) Section 13, Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes).

ARTICLE 2. CONFORMING CHANGE

SECTION 2.01. Section 17.46(b), Business & Commerce Code, as amended by Chapters 324 (S.B. 1488), 858 (H.B. 2552), and 967 (S.B. 2065), Acts of the 85th Legislature, Regular Session, 2017, is reenacted and amended to read as follows:

(b) Except as provided in Subsection (d) of this section, the term "false, misleading, or deceptive acts or practices" includes, but is not limited to, the following acts:

(1) passing off goods or services as those of another;

(2) causing confusion or misunderstanding as to the source, sponsorship, approval, or certification of goods or

services;

(3) causing confusion or misunderstanding as to affiliation, connection, or association with, or certification by, another;

(4) using deceptive representations or designations of geographic origin in connection with goods or services;

(5) representing that goods or services have sponsorship, approval, characteristics, ingredients, uses, benefits, or quantities which they do not have or that a person has a sponsorship, approval, status, affiliation, or connection which the person does not;

(6) representing that goods are original or new if they are deteriorated, reconditioned, reclaimed, used, or secondhand;

(7) representing that goods or services are of a particular standard, quality, or grade, or that goods are of a particular style or model, if they are of another;

(8) disparaging the goods, services, or business of another by false or misleading representation of facts;

(9) advertising goods or services with intent not to sell them as advertised;

(10) advertising goods or services with intent not to supply a reasonable expectable public demand, unless the advertisements disclosed a limitation of quantity;

(11) making false or misleading statements of fact concerning the reasons for, existence of, or amount of price reductions;

(12) representing that an agreement confers or involves rights, remedies, or obligations which it does not have or involve, or which are prohibited by law;

(13) knowingly making false or misleading statements of fact concerning the need for parts, replacement, or repair service;

(14) misrepresenting the authority of a salesman, representative or agent to negotiate the final terms of a consumer transaction;

(15) basing a charge for the repair of any item in whole or in part on a guaranty or warranty instead of on the value of the actual repairs made or work to be performed on the item without stating separately the charges for the work and the charge for the warranty or guaranty, if any;

(16) disconnecting, turning back, or resetting the odometer of any motor vehicle so as to reduce the number of miles indicated on the odometer gauge;

(17) advertising of any sale by fraudulently representing that a person is going out of business;

(18) advertising, selling, or distributing a card which purports to be a prescription drug identification card issued under

Section 4151.152, Insurance Code, in accordance with rules adopted by the commissioner of insurance, which offers a discount on the purchase of health care goods or services from a third party provider, and which is not evidence of insurance coverage, unless:

(A) the discount is authorized under an agreement between the seller of the card and the provider of those goods and services or the discount or card is offered to members of the seller;

(B) the seller does not represent that the card provides insurance coverage of any kind; and

(C) the discount is not false, misleading, or deceptive;

(19) using or employing a chain referral sales plan in connection with the sale or offer to sell of goods, merchandise, or anything of value, which uses the sales technique, plan, arrangement, or agreement in which the buyer or prospective buyer is offered the opportunity to purchase merchandise or goods and in connection with the purchase receives the seller's promise or representation that the buyer shall have the right to receive compensation or consideration in any form for furnishing to the seller the names of other prospective buyers if receipt of the compensation or consideration is contingent upon the occurrence of an event subsequent to the time the buyer purchases the merchandise

or goods;

(20) representing that a guaranty or warranty confers or involves rights or remedies which it does not have or involve, provided, however, that nothing in this subchapter shall be construed to expand the implied warranty of merchantability as defined in Sections 2.314 through 2.318 and Sections 2A.212 through 2A.216 to involve obligations in excess of those which are appropriate to the goods;

(21) promoting a pyramid promotional scheme, as defined by Section 17.461;

(22) representing that work or services have been performed on, or parts replaced in, goods when the work or services were not performed or the parts replaced;

(23) filing suit founded upon a written contractual obligation of and signed by the defendant to pay money arising out of or based on a consumer transaction for goods, services, loans, or extensions of credit intended primarily for personal, family, household, or agricultural use in any county other than in the county in which the defendant resides at the time of the commencement of the action or in the county in which the defendant in fact signed the contract; provided, however, that a violation of this subsection shall not occur where it is shown by the person filing such suit that the person neither knew or had reason to

know that the county in which such suit was filed was neither the county in which the defendant resides at the commencement of the suit nor the county in which the defendant in fact signed the contract;

(24) failing to disclose information concerning goods or services which was known at the time of the transaction if such failure to disclose such information was intended to induce the consumer into a transaction into which the consumer would not have entered had the information been disclosed;

(25) using the term "corporation," "incorporated," or an abbreviation of either of those terms in the name of a business entity that is not incorporated under the laws of this state or another jurisdiction;

(26) selling, offering to sell, or illegally promoting an annuity contract under Chapter 22, Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), with the intent that the annuity contract will be the subject of a salary reduction agreement, as defined by that Act, if the annuity contract is not an eligible qualified investment under that Act [~~or is not registered with the Teacher Retirement System of Texas as required by Section 8A of that Act~~];

(27) taking advantage of a disaster declared by the governor under Chapter 418, Government Code, by:

(A) selling or leasing fuel, food, medicine, or another necessity at an exorbitant or excessive price; or

(B) demanding an exorbitant or excessive price in connection with the sale or lease of fuel, food, medicine, or another necessity;

(28) using the translation into a foreign language of a title or other word, including "attorney," "immigration consultant," "immigration expert," "lawyer," "licensed," "notary," and "notary public," in any written or electronic material, including an advertisement, a business card, a letterhead, stationery, a website, or an online video, in reference to a person who is not an attorney in order to imply that the person is authorized to practice law in the United States;

(29) delivering or distributing a solicitation in connection with a good or service that:

(A) represents that the solicitation is sent on behalf of a governmental entity when it is not; or

(B) resembles a governmental notice or form that represents or implies that a criminal penalty may be imposed if the recipient does not remit payment for the good or service;

(30) delivering or distributing a solicitation in connection with a good or service that resembles a check or other negotiable instrument or invoice, unless the portion of the

solicitation that resembles a check or other negotiable instrument or invoice includes the following notice, clearly and conspicuously printed in at least 18-point type:

"SPECIMEN-NON-NEGOTIABLE";

(31) in the production, sale, distribution, or promotion of a synthetic substance that produces and is intended to produce an effect when consumed or ingested similar to, or in excess of, the effect of a controlled substance or controlled substance analogue, as those terms are defined by Section 481.002, Health and Safety Code:

(A) making a deceptive representation or designation about the synthetic substance; or

(B) causing confusion or misunderstanding as to the effects the synthetic substance causes when consumed or ingested;

(32) a licensed public insurance adjuster directly or indirectly soliciting employment, as defined by Section 38.01, Penal Code, for an attorney, or a licensed public insurance adjuster entering into a contract with an insured for the primary purpose of referring the insured to an attorney without the intent to actually perform the services customarily provided by a licensed public insurance adjuster, provided that this subdivision may not be construed to prohibit a licensed public insurance adjuster from

recommending a particular attorney to an insured; [~~or~~]

(33) owning, operating, maintaining, or advertising a massage establishment, as defined by Section 455.001, Occupations Code, that:

(A) is not appropriately licensed under Chapter 455, Occupations Code, or is not in compliance with the applicable licensing and other requirements of that chapter; or

(B) is not in compliance with an applicable local ordinance relating to the licensing or regulation of massage establishments; or

(34) [~~(33)~~] a warrantor of a vehicle protection product warranty using, in connection with the product, a name that includes "casualty," "surety," "insurance," "mutual," or any other word descriptive of an insurance business, including property or casualty insurance, or a surety business.

ARTICLE 3. TRANSITIONS; CONFLICT WITH OTHER LEGISLATION; EFFECTIVE DATE

SECTION 3.01. The changes in law made by this Act to Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), apply only to an offer of a qualified investment product under that Act that is made on or after the effective date of this Act. An offer of a qualified investment product that is made before the effective

date of this Act is governed by the law as it existed immediately before the effective date of this Act, and that law is continued in effect for that purpose.

SECTION 3.02. The change in law made by this Act to Section 10(a), Chapter 22 (S.B. 17), Acts of the 57th Legislature, 3rd Called Session, 1962 (Article 6228a-5, Vernon's Texas Civil Statutes), applies only to an offense committed on or after the effective date of this Act. For purposes of this section, an offense is committed before the effective date of this Act if any element of the offense occurs before that date. An offense committed before the effective date of this Act is governed by the law in effect when the offense was committed, and the former law is continued in effect for that purpose.

SECTION 3.03. Section 17.46(b), Business & Commerce Code, as amended by this Act, applies only to a cause of action that accrues on or after the effective date of this Act. A cause of action that accrues before the effective date of this Act is governed by the law as it existed immediately before the effective date of this Act, and that law is continued in effect for that purpose.

SECTION 3.04. To the extent of any conflict, this Act prevails over another Act of the 86th Legislature, Regular Session, 2019, relating to nonsubstantive additions to and corrections in enacted codes.

SECTION 3.05. This Act takes effect September 1, 2019.

President of the Senate

Speaker of the House

I certify that H.B. No. 2820 was passed by the House on April 10, 2019, by the following vote: Yeas 146, Nays 0, 1 present, not voting.

Chief Clerk of the House

I certify that H.B. No. 2820 was passed by the Senate on May 10, 2019, by the following vote: Yeas 31, Nays 0.

Secretary of the Senate

APPROVED: _____

Date

_____

Governor