The K-12 403(b) is broken. Together we can fix it.

To: The FBC Board and Executive Committee

San Diego County Office of Education

From: 403bwise.org

Daniel Otter, Ph.D

Scott Dauenhauer, CFP, MPAS

Re: Public Comment for January 12th, 2024 Meeting

Please accept this letter as a public comment from the Executive Director and the Director of Research of 403bwise.org. Our non-profit organization advocates for better retirement plans for public school employees. See the bios of Daniel Otter, Ph.D., and Scott Dauenhauer, CFP, MPAS, at the end of this letter.

Our concern today is the Request For Information issued in April 2023, which became a contract for a new Program Manager in August.

Our specific concerns are as follows:

1. A vendor should not be the Program Manager (PM)

Hiring a vendor to serve as Program Manager will require an enormous amount of oversight to ensure that participants' best interests are served. This will require expertise and time that we are not sure a committee meeting monthly possesses.

We do not doubt the talent and intelligence of your committee members. However, the financial services world is complicated and often driven by hidden incentives. It takes more than intelligence to police a Broker/Dealer. The one thing you cannot do is allow a Broker/Dealer to police itself.

2. In our opinion, It's not possible for the winner of the RFI to act as a fiduciary

We know you've been assured that the vendor chosen to manage this program will act as a fiduciary. As someone who has acted as a fiduciary for decades (Scott), this is impossible given the significant number of conflicts the new PM faces.

I've attached the Reg BI disclosure document for your new PM. It's 23 pages long.

You are not providing your membership the option of receiving investment advice; you are unleashing a professional sales organization on them.

It might come as a surprise, but the Security and Exchange's (SEC) Regulation Best Interest rule is NOT the same as being held to a fiduciary standard such as ERISA or the Investment Advisors Act. Your Program Manager needs to be held to a higher standard; in fact, they are required to under the California constitution.

The California constitution creates a fiduciary duty that mirrors ERISA (CA Government Code Article XVI, Section 17, code 53609).

Fred Reish White Paper on Fiduciary Duty in a California 457(b):
https://www.bfsg.com/knowledgecenter/Knowledge%20Center%20Paper%20-%20White%20Paper_Fiduciary%20Responsibilities.pdf

PlanMember Services Reg BI Disclosure:
https://pdfs.planmember.com/PDFs/PSEC%20Reg%20BI%20Disclosure%20FINAL%20202303301.pdf

3. The "discounted" fee negotiated is not a discount

1.50% is not a fee discount. A typical advisory fee in the financial services industry without a discount is 1.00%. A 2017 survey by Michael Kitces does show that the median fee could be as high as 1.25% for accounts under $250,000. In general, fees have dropped since the six-year old Kitces study. Even if fees hadn't dropped, your "discounted" fee on the low end is 20% higher than the median fee for that range. The median fee at $1 mm in the survey was around 1%; your new PM charges 1.15%. How is this a discount?

https://www.kitces.com/blog/independent-financial-advisor-fees-comparison-typical-aum-wealth-management-fee/

4. This contract is a transfer of wealth from your participants to the new program manager

To make money on this program, your new PM must sell financial products to your membership. They will most likely raid the low-cost, core FBC program to accomplish this. Wittingly or unwittingly, you are incentivizing the vendor to move assets out of a good, low-cost group contract that you currently control, and into individual contracts you likely will not control. Those assets may never come back to the program.

By our conservative estimates, the new PM could earn more than $30 million in fees in the first decade, rising to more than $100 million by year 17. You can see our model here. This is the most significant contract award we've ever seen in this space; it's undoubtedly the largest done without a complete Request For Proposal.

5. This is a massive windfall for the new Program Manager

The potential for profit for your new PM with this program is enormous. You are providing an implicit endorsement by hiring a vendor and then backing them with the FBC/SDCOE name. Professional salespeople will use this arrangement to move large amounts of money out of the core, low-cost program, and sell ancillary products.

6. You are creating an untenable situation if you move away from the current Program Manager. (You lose control of the assets once they are moved out of the Group contracts.)

Did you negotiate group custodial accounts? If so, it's not stated in the contract. The 1.50% account fee will not occur in the Empower program (the core); the money will need to be moved to individual accounts that the FBC will likely not have the same control or oversight of.

7. Your members are not prepared for the coming sales tactics

Your members are unprepared for the sales barrage about to hit them. They are intelligent people, but the amount of information asymmetry in the relationship between a conflicted financial salesperson and the participant is significant. The vendor's endorsement by the FBC will be enough to induce many of your participants to move their balance, even if it's not in their best interest.

8. You are risking a lawsuit that could bring down the entirety of the FBC

We are not lawyers, but a program with as many conflicts as this one could make it an inviting target. The lack of metrics to justify the costs associated with this new program and the fact that no RFP was issued will not work in your favor. If you value this program and the FBC as a whole, consider rescinding this decision to hire a vendor as Program Manager.

9. Has the PMS grid been explained to you, as well as the specific products that the PMS reps will be able to offer?

The financial representatives in this new program are heavily conflicted and have incentives to move money from the core FBC program to PMS products. Here is just one of many examples of a significant conflict of interest:

PlanMember Financial Centers conflicts:

"Additionally, some PSEC financial professionals own and operate locations known as PlanMember Financial Centers. These Financial Centers may be single advisor branches or may include two or more advisors. As these Financial Centers grow, their fee-based business within PSEC's suite of PSEC Programs, PSEC's economies of scale are shared with those Financial Centers by increasing the payout percentage to the Financial Center owner, making loans to the Financial Center owner that are forgivable when the Financial Center accumulates certain client asset levels in PSEC Programs, and accruing and paying a deferred growth participation bonus based on client assets accumulated in PSEC Programs. As the amount of the advisors' client assets in PSEC's programs grows above certain levels, the advisors receive more financial benefits than they would otherwise receive with fewer assets in PSEC's programs.

These increases in a financial professional or Financial Center's revenue translate into higher payouts for reaching various PSEC AUM levels which present a conflict of interest because they provide a financial incentive for financial professionals who receive the discounts to recommend PSEC's Programs over other available managed or wrap account programs that do not offer such discounts or higher payouts to the financial professionals."(emphasis added)

In layman's terms, there is an incentive to move money out of the low-cost "core" FBC program into PMS products as it increases the payouts for the representatives. A program manager should not be incentivized to move money, nor should the representatives working within the program.

403bwise.org formerly rated the FBC program as a Green vendor. We lowered the rating to Yellow (proceed with caution) when the FBC decided to promote non-fiduciary products from the National Life Group. With the latest decision of the board to hire PMS, we have lowered the rating to Red (the lowest rating). This is disappointing as we saw the FBC program as a force for good in an industry dominated by companies whose only goal is to extract as much money from participants as possible. The FBC program can be a Green vendor again, but only once it takes its fiduciary responsibilities seriously.

Scott's mother-in-law is a retired teacher, and his father-in-law is a retired bus driver who both served in San Diego. We understand the value a consortium can bring to its members. Our goal is not to destroy the FBC but to preserve and improve it. It takes brave people to stand up to the financial industry. We trust you will choose the right path.

Daniel Otter, Ph.D and Scott Dauenhauer, CFP, MPAS

403bwise.org

Short Biography of Daniel Otter, Ph.D and Scott Dauenhauer, CFP, MPAS

Daniel Otter, Ph.D

Named Money Magazine Money Hero in 2012 (https://money.cnn.com/galleries/2012/pf/1205/gallery.investor-protection.moneymag/4.html)

Named Investment News Innovator in 2023

(https://www.investmentnews.com/news/cover-story/how-a-former-teacher-is-educating-the-world-about-403bs-243271)

(https://iconsandinnovators.com/innovators/dan-otter/)

Two-time winner of The National Association of Government Defined Contribution Administrators, Inc. (NAGDCA) Media Recognition Award

Teach and Retire Rich Podcast

(Teach and Retire Rich, by Daniel Otter, Ph.D.teachandretirerich.comhttps://teachandretirerich.com)

Learned by Being Burned Podcast product (https://403bwise.org/burned)

Author of *The 403bwise Guide* (out of print)

Author of *Financial Literacy for the Young and Young at Heart*

Author of *Teach and Retire Rich* (https://teachandretirerich.com/)

403bwise was launched in March 2000 by Dan Otter and John Moore, two educators fed up with the lack of objective 403(b) information available to participants. If information was provided at all to employees, it was usually through sales pitches in classrooms, lunchrooms and union offices. In fact, Dan first learned about the 403(b) when a representative waltzed into his classroom one afternoon pitching something called "TSAs." He declined to enroll. It was only several years later that he learned this salesperson was selling high-fee variable annuity products.

In the years since our launch, 403bwise has been mentioned in *Kiplinger Personal Finance, Money Magazine, Los Angeles Times, The NY Times, US News & World Report, Wall Street Journal and the Washington Post*. Dan has appeared on NPR and on Bob Brinker's radio show. In 2012, *Money Magazine* named him a Money Hero for his "extraordinary efforts to improve others' financial well-being." Additionally, he is a two-time winner of The National Association of Government Defined Contribution Administrators, Inc. (NAGDCA) Media Recognition Award. While John left in 2005 to pursue other endeavors, the goal of the site remains the same as the day it launched: education and advocacy.

In 2019, 403bwise became a non profit organization that Dan runs full time, thanks to a generous donation from Tim Ranzetta, the founder of Next Gen Personal Finance, a non-profit organization that connects educators with free resources, professional development, and advocacy tools in order to equip students with the knowledge and skills to lead financially successful and fulfilling lives.

Dan is a former journalist and a veteran teacher. He has taught elementary school (California), middle school (Maryland and New Mexico), and high school (New Mexico). He has taught in-service teachers at California State University Fullerton, American University and the University of New Mexico, where he earned a doctorate in Language, Literacy, and Sociocultural Studies.

Scott Dauenhauer, CFP, MPAS

I've been working with educators and government agencies for over twenty years. I am an Investment Advisor Representative of my own Registered Investment Advisory firm, Meridian Wealth Management. I have a Master's Degree in Financial Planning and am a Certified Financial Planner. I also help run a non-profit, 403bwise.org, as the Director of Research and co-host of the Teach and Retire Rich Podcast.

I've written or co-written three books aimed at educators and those who serve educators and worked as a consultant to 403(b) and 457(b) plans for nearly 20 years.

My wife is a teacher, which is why I got into working with education employees. My company is not taking on new clients; this letter is about something other than building my business.

During my tenure as their consultant, I helped take the California State Teachers' Retirement System from under $100 million in assets to over $1 billion.

I've been a panelist at three different Security and Exchange (SEC) produced one-day conferences focused on the 403(b) industry.