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Minutes of the
Connecticut Higher Education Trust (CHET) Advisory Committee
Friday, December 6, 2007

Members Present:

James Blake	Executive Vice President of Finance & Administration Southern Connecticut State University
Ray Bordeau	Bursar, Fairfield University
Rich Calvario	Program Manager, Education Savings Division, TIAA-CREF Tuition Financing, Inc.
Andrew Fleischmann	Chairman, House Education Committee, Connecticut General Assembly
Michael Hall	Program Consultant, TIAA-CREF Tuition Financing Inc.
Sylvie Hangen	Associate Dean, Sacred Heart University [On behalf of Julie Savino]
Carol Heller	Director of Financial Education, Office of the Connecticut State Treasurer
Mary Johnson	Associate Commissioner, Department of Higher Education
R. Chuck Lockert	Designee, Chairman Thomas P. Gaffey, Senate Education Committee Connecticut General Assembly
Pamela McNulty	Regional Director and Program Manager, TIAA-CREF Tuition Financing, Inc.
John Mengacci	Undersecretary for Policy Development and Planning Office of Policy and Management
Christine Palm	Communications, Office of the Connecticut State Treasurer
Howard Rifkin	Deputy Treasurer, Office of the Connecticut State Treasurer
Margaret Wolf	Director of Financial Education, Capital Community College

Mr. Rifkin called the meeting to order at 1:35 p.m. (EST), followed by a roll call of attendees.

Approval of Minutes

Ms. Heller presented the Minutes from the December 6, 2006, Connecticut Higher Education Trust ("CHET") Advisory Council Meeting. Mr. Rifkin made a motion to approve the Minutes; the motion was seconded and the Minutes were unanimously accepted.

Recap of YTD 2007 Statistics and Overall Performance

Ms. Heller began the meeting with a PowerPoint presentation[1] ("Presentation") of YTD 2007 statistics of the participation in, and overall performance of, CHET. She noted that FY 2007 has seen marked growth in the CHET program with over 70,000 active accounts, 16,000 of which are net new accounts opened after November 30, 2006. In December 2006 alone, 4,500 accounts were opened, exceeding the yearly total in 2005. Much of the 2006 growth occurred after July 1, 2006, when the CHET income tax deduction legislation went into effect; as expected, growth in the number of net new CHET accounts further accelerated as FY 2006 drew to a close.

Ms. Heller noted that the strong growth rate continued throughout YTD 2007 in terms of both net new accounts and increased contributions to existing accounts. In previous years, an average of 24 percent of CHET contributions during a calendar year would originate from new CHET accounts; in 2007, that ratio increased to roughly 50 percent.

[1] CHET Advisory Committee 2007 Annual Meeting, PowerPoint Presentation, 6 December 2007.

Mr. Rifkin took a moment to acknowledge the instrumental roles Mr. Fleischmann and State Senator Thomas P. Gaffey played in marshalling support for the CHET tax deduction legislation and getting it through the General Assembly. He thanked all CHET advisory board members for their collective efforts in support of the state income tax deduction, including that of retiring State Department of Higher Education Commissioner Valerie Lewis.

Mr. Rifkin also acknowledged deceased advisory board member Dick Belden's active role on the committee since the program's inception.

Ms. Heller continued with a discussion of the sources of CHET account and asset growth over the past year, noting that growth has come from existing accountholders who have increased annual contribution rates, and from contributions made by new plan participants. In addition, many program participants began contributing to their CHET accounts via automated payroll deductions and electronic transfers from their bank accounts. A lot of the new account holders are folks who are saving for the first time, which is really the objective of the tax deduction.

Ms. Johnson asked whether increased program contributions and average account balances were heavily skewed by a small number of large account depositors, and whether the new state tax deduction benefit was being effectively utilized by families of varying economic means saving for college.

Ms. McNulty and Ms. Heller responded by stating that CHET account balances were slightly above the national average for 529 plans. The program has a maximum account contribution limit that is in line with other 529 plans and corresponds to IRS guidelines. Mr. Hall further stated that the new tax deduction has attracted a broader, more economically diverse base of plan participants, with declining income disparity levels among accountholders.

Ms. McNulty, Ms. Heller and Mr. Hall also noted that this year's exceptional asset growth is projected to continue strong through the final few weeks of the year, as account holders are expected to maximize their annual contributions for the state income tax benefit by year end. CHET took in approximately a record $200 million in account contributions thru the end of November and $221 million over the last 12 months.

Ms. Heller highlighted other key quantitative measures of account activity and growth over the past year. The average new account size increased from $4,000 in 2006 to over $5,000 through the 3rd Quarter of 2007. While average new account balances were comparatively larger than in the previous year, there was also significant variation in new account opening balances, including several accounts that were opened with low opening deposit levels but that are expected to grown with established payroll deduction or automated contributions.

Ms. Heller also noted that as CHET beneficiaries began to reach college age over the past year, CHET realized the largest volume of program withdrawals for qualified higher education expenses in the plan's history.

State Income Tax Deduction Benefits and Fiscal Impact

Mr. Lockert asked about the new state tax deduction income eligibility and financial benefits. Ms. Heller responded that the new state income tax provides for a maximum benefit per eligible joint state income tax filer of approximately $500 per year, tied to the maximum annual CHET contribution level of $10,000 for joint, and $5,000 for single, tax filers.

Mr. Rifkin provided a cautionary note, stating that there is no value to the new state tax deduction unless a family itemizes deductions on their state income tax return form, which is accomplished by adjusting (decreasing) their Federal Adjusted Gross Income by the eligible amount of annual CHET contributions.

Ms. Heller added that the plan had not received the final state revenue impact from the Connecticut Department of Revenue Services (CT DRS) for the first year of the new state tax deduction. Recent CT DRS estimates suggest that the fiscal impact may somewhat fall below the original projections of $6-8 million for the 2006 tax year.

Ms. Heller announced that the program's asset levels topped the $1 billion milestone in October. In addition, the Treasury worked with TIAA-CREF on actively monitoring non-qualified withdrawal and rollover activity, in order to guard against prospective misuse of the new state tax deduction. Early indications suggested that total non-qualified withdrawal activity was lower in the first reporting period of 2007 when compared to similar periods prior to the implementation of the state income tax deduction in 2006. Continued close monitoring of non-qualified withdrawal activity, especially over a short term investment period, is recommended.

Mr. Rifkin mentioned that there has been considerable interest on the part of investment firms and paid final advisors in opening up the state tax deduction for all 529 plans operating in Connecticut. A few state tax parity bills had been raised in the last legislative session proposing such a change, but were not successful in getting enough traction to succeed. Interest in this matter is expected to continue due to the financial interests of folks running 529 plans in other parts of the country and their desire to realize the tax deduction. He noted that it is likely that we will be hearing from lobbyists hired by these firms, and less from any kind of grassroots movement. However, the upcoming short session may constrain such efforts.

Investment Option Usage and Performance; Program Fees

Ms. Heller reported on accountholder preferences by individual investment option. The age-based Managed Allocation Option continued to be the most popular of all options followed by the High Equity and the fixed rate Principal Plus Interest Options. However, the 100% Equity Index Option has grown in popularity in a relatively short time since its inception in June 2006. On November 19, CHET introduced two additional options, an aggressive tier Managed Allocation Option and a new Social Choice Option, and announced the planned introduction of a Money Market Option in February 2008. These new options provided an expanded array of investment offerings for more sophisticated investors with varied risk tolerances and investment return objectives.

Ms. McNulty provided an overview of CHET's investment performance by individual option as of September 30, 2007. (See attached chart.) She noted that the primary investment objectives of the plan's investment options have been to keep pace with tuition inflation. Due to the preponderance of index based underlying TIAA-CREF institutional mutual funds, returns for the majority of CHET investment options generally tracked their index benchmarks (including multi-asset class options with blended benchmarks,) after accounting for the CHET program management fee of 65 basis points. Selected individual options, including most notably the High Equity Option, realized periodic returns that exceeded benchmarks before taking into account CHET 65 basis point program management fee.

Ms. Heller reminded committee members that the Municipal Securities Rulemaking Board requires that all 529 investment returns are reported on a net of total fees basis, but that consumers are often confused as to how to compare and evaluate investment option returns to with respect to their peer indexes.

Mr. Rifkin further explained that while program returns are net of fees, benchmarks returns are based on gross returns. He used an analogy of mutual fund reporting, when average returns for mutual funds generally do not meet benchmarks because of the additional management fees added on top of underlying fund performance.

Ms. Johnson inquired as to whether the Managed Allocation Option utilized blended benchmarks by age, and how such investment performance information could be monitored.

Ms. McNulty responded that the benchmarks were comprised of matched indexes, such as the S&P 500, Russell 3000, Morgan Stanley, Lehman Brothers and others. She noted that current CHET investment return data is available online and updated monthly on the 10th of the month. She further instructed Ms. Johnson to click on the investment performance page for actual periodic returns, and to click on the tab for underlying mutual funds to see performance of individual funds. Investment option performance by underlying index and other active funds have been very strong in aggregate, and far exceeded its benchmarks over the past twelve month period ending in September, with the exception of a real estate fund.

Mr. Rifkin added that when 529 plans were first established by Congress, the original goal was to have state-sponsored programs offer with aged-based multi asset class managed allocation options designed to cover the term of the investment horizon. Since then, the 529 market has grown to provide expanded options and offerings of advisor-sold plans, including many plans which feature multiple asset groups and classes of funds as well as individual standalone mutual funds. The industry has come a long way from the 529 plan's original intent.

Ms. McNulty suggested that while consumers have access to an extensive array of choices in advisor sold programs, two thirds of investors still invest in traditional age-based options, similar to CHET's popular Managed Allocation Option, which adjusts sub asset allocations as the beneficiary's age increases. With the recent addition of the new aggressive tier Managed Allocation Option, CHET has provided less risk averse investors options for increased equity weightings in each age band.

Mr. Rifkin further noted that managed allocations plans are typically configured with the expectation that when a beneficiary reaches 18 or 19 years old, an accountholder will start withdrawing money for college with the expectation that over that investment time horizon s/he would return an amount that meets or exceeds education inflation.

Committee members posed questions regarding CHET's current fee structure and comparability to other state 529 plans.

Mr. Hall responded that each CHET investment option has flat pricing totaling 65 basis points, with the exception of fees for the Principal Plus Interest guaranteed fixed rate option which are only one basis point. Ms. McNulty confirmed that the fee is constant and compares very favorably to the universe of direct and indirect 529 plans. Currently 529 plan fees generally range from 45 to 115 basis points, with some advisor sold plans charging even higher fees for actively managed investment options.

Ms. Heller confirmed that CHET's fees were amongst the lowest third of 529 plans in the country, as of a recent survey. Mr. Rifkin stated that the Treasury has consistently pushed back on TIAA-CREF to keep fees competitive, and plans to encourage further pricing adjustments now that CHET has attained the $1 billion threshold in program assets. Ms. McNulty added that TIAA-CREF continues to review plan pricing and offerings to make CHET as competitive as possible, and as a not-for-profit organization, has actively sought to pass program savings and cost efficiencies along to accountholders.

Mr. Fleischmann stated that if you start out with CHET as a competitive plan with regard to pricing and then figure in the value of the state tax deduction, this is the best available 529 option on the market, as long as we keep the state tax deduction.

Ms. McNulty noted that over the summer of 2007, *Money* magazine ranked CHET as the best 529 college savings plan for Connecticut residents compared with state programs nationwide. She noted that the focus for CHET is to have a low-cost and affordable plan for state residents of all income levels, with success based on investment managers meeting certain benchmarks while exercising due diligence.

Ms. McNulty also mentioned that CHET's rating on savingforcollege.com was upgraded to a 4.5 "cap" rating on a 0 to 5 scale. She also mentioned that TIAA-CREF's recent underlying mutual fund ratings from Morningstar included one 5-star, four 4-star and four 3-star ratings.

2007 Program Updates and Asset Allocation Changes

Ms. Heller mentioned that the industry has seen a recent flight to investment quality and fixed income security in 529 plans. She reminded the committee that in November CHET introduced an Aggressive Managed Allocation Option and a Socially Responsible Equity Option. In the first month since the introduction of the two latest options, accountholders have been most attracted to the new aggressive age based managed allocation option. In February 2008, a new Money Market Option will be offered that is expected to attract attention, given current instability in the financial markets.

Mr. Lockert commented that college education costs continue to rise at a heightened pace and then questioned how anyone could afford to leave money in money market fund and what value such new option would have to the overall portfolio. He suggested employing target funds, which could pre-estimate future education expenses and savings needs. In response, Mr. Rifkin noted that keeping pace with college costs was conceptually the objective of CHET's core Managed Allocation option, and that the Money Market option may be an attractive short term option for those looking to liquidate funds with a 17 or 18 year old child planning on attending college soon.

Ms. Heller noted that the Treasury had looked into prepaid college plans which have had mixed results and significant liquidity issues in some other states. The consensus of the committee was that investors have differing risk tolerances and generally seek choice and flexibility in a plan.

Ms. McNulty pointed out an article in this week's Wall Street Journal that addresses the question of what 529 investors have been looking for in plan options. The article made positive mention of the CHET plan.

Ms. Heller noted that the Principal Plus Interest option's guaranteed fixed rate was reset to 3.80% for the current annual period ending on June 30, 2008, up from 3.55% in the previous year.

Ms. Heller discussed the plan's annual asset allocation review process. Each winter, TIAA-CREF presents recommendations for new investment options and sub asset allocation changes to the Treasury for consideration. Over the past year, the Trust adopted three new investment options as previously described. In addition, international equity exposure levels were increased and made consistent at the 20 percent of total equity exposure level amongst all options with equities.

Mr. Rifkin noted that the Treasury recently went through an asset allocation review for the state pension plans and had decided to make a similar movement in international exposure from 18% to 20% in the state pension plan.

Marketing, Outreach and Public Relations

Ms. Heller then directed Mr. Calvario to present an overview of 2007 marketing activities. One of the major changes for 2007 was an increased focus on encouraging families who inquire about the plan to take action and open an account. Mr. Calvario described this comprehensive new initiative as a "prospecting engine." If a prospective account owner inquires about the plan and has established a minimum level of interest, he/she may need to better understand the plan's value proposition and/or may require several follow up reminders before finally taking action. To keep CHET top of mind, the new "prospecting engine" communicates with prospects in regular 30, 60 and 90 day intervals after the initial inquiry, promoting time sensitive recommendations such as reminders about the state income tax deduction deadline.

Mr. Calvario reviewed the past year's advertising schedule that encompassed six seasonal campaigns throughout year, including "New Year", "Tax Time", "Graduation", "Back to School", "College Savings Month" and "Year End". Advertising mediums included radio (a lower cost electronic media alternative to television), internet and search term marketing and direct mail. Of all advertising forms, search term marketing proved to be most efficient and cost effective, with the highest conversion rate for purchases. E-newsletters were also used as an inexpensive form of existing account owner communication to keep account owners informed.

CHET received media exposure during 2007 for outreach activities including the new CHET College Savings Challenge contest, but overall was lighter than in 2006 when significant newsworthy program enhancements and benefits including the tax deduction and tax permanency dominated the news.

Ms. Heller and Mr. Calvario described the 2007 CHET College Savings Challenge ("CHET Challenge") as a first-time creative writing and art contest, sponsored by CHET and the Office of the Connecticut State Treasurer. The CHET Challenge was designed to encourage young students to learn the importance of saving and planning for college. Through participation in the contest, over 250 students and their families also learned how CHET can help them achieve these goals in the face of escalating higher education costs. The Challenge, which was launched in September and ran through November 16 was open to children in Kindergarten through sixth grade who attend Connecticut public and private schools or are home schooled. Superintendents throughout the state were notified about the contest at the beginning of the school year.

The Challenge called on Kindergarten to third grade students to draw an original picture illustrating their answer to the question, "What do I want to do after I go to college?" Fourth and fifth graders wrote essays, and sixth graders wrote poems responding to the question, "How will I change the world after I go to college?" To help inspire students' imagination, the CHET College Savings Challenge also provided free classroom materials and animated educational videos that teach students about saving money and planning for their future. The Challenge was successful in generating considerable enthusiasm and interest in CHET from participating students, teachers and schools, all of which were eligible for cash prizes, and awards which will be presented at a recognition ceremony at the State Capitol in January 2008.

Mr. Hall other outreach efforts for the past year, which increasingly focused on jointly conducted seminars with financial and education influencers including the CT Society of Certified Public Accountants, Financial Planners Association, and CT Student Loan Foundation. CHET was also actively promoted to through employers at multiple state run agencies and universities, which promoted many benefits including the ease of saving using the plan's payroll deduction and automatic bank contribution features.

He further described recent family oriented community events which have provided program visibility across the state, in addition to educational forums including the CT Money Conference for Women and seminars at local libraries.

Ms. Hangen and Mr. Fleischmann suggested promoting the program through healthcare providers and hospitals for newborns as well as daycare centers and other venues frequented by young parents. Other ideas for targeted outreach included senior citizens and grandparents.

Ms. Johnson described a complementary college readiness public awareness and informational campaign called "KnowHow2Go – CT," which is sponsored by the State Departments of Education and Higher Education. She said that the new initiative aims to attract and help minority students learn how to prepare for college, and noted that one important piece of the process is to help families learn how and why it is important to prepare from a savings perspective.

Ms. Heller concurred with the importance of educating families about saving for college. She noted that over the last five years, college tuition and fees has risen over 51%. As costs increase, demographics of the student population are also changing and more non-traditional and minority students will need to plan for their futures and compete for limited financial aid.

Mr. Mengacci inquired about whether there were annual goals set for the plan and what kind of account and asset growth CHET had been striving to achieve. Ms. McNulty responded that CHET's 15% annual account growth rate for the past twelve months far exceeded 2007 goals. While 2008 goals had not been set at the time of the annual meeting, she suggested that their goals, which are typically internal, could be incorporated into next year's presentation. She also cautioned that while the plan has been on a strong growth trajectory due to the state tax deduction and recent tax permanency, the marketplace may be maturing.

529 Industry Trends and Issues

In response to committee questions, Ms. McNulty spoke about common concerns regarding the impact of accumulated accountholder savings on financial aid as well as the realities and misconceptions of the college savings impact on Medicaid eligibility. Students and parents often fear that they are not eligible for financial aid if they participate in a 529 plan, but in the vast majority of cases they still are. As their savings are typically held in the name of the parent on behalf of their children, the portion of their assets that are factored into the expected family contribution calculation for student aid is low—in the 5% range. She suggested that we can do a better job educating prospective and current participants on financial aid eligibility issues tied to 529 plan participation, especially given that a growing portion of student aid is provided via loans.

Mr. Rifkin brought up the high-profile *Kentucky v. Davis* case pending before the U.S. Supreme Court that could impact on the future exclusivity of state income tax benefits for the CHET program. *Kentucky* considers disparate treatment by some states for bonds sold by other states. A decision is expected by Spring 2008, and if the Court sides with the defendant, it may set a precedent that could have a spillover impact on disparate tax treatment of 529 plans in Connecticut.

Ms. Heller concluded the meeting with a forward-looking discussion regarding potential areas for CHET program enhancement in 2008. She mentioned that TIAA-CREF was looking into potentially adding non-proprietary mutual funds to the existing investment options and also planned to explore the potential for establishing new pricing tiers for indexed versus actively managed funds.

Mr. Rifkin encouraged committee members to pick up new supplemental printed materials on the program as well as recent newspaper and magazine articles describing the CHET and recent industry trends.

Meeting Adjournment

At 3:10 p.m. Mr. Rifkin made a motion to adjourn the meeting. The motion was so moved and the meeting was adjourned.