Vanguard

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Fairness in investment choices

Modernize rules to allow collective investment trusts in 403(b) plans

Mutual funds and collective investment trusts (CITs) can both be excellent, low-cost options in retirement plans. And while the decision about which option—mutual funds or CITs—is better will depend on each plan's priorities for its participants, a fundamental point of fairness must be addressed.

Because of differences in tax and securities laws, most 403(b) plans—the typical retirement savings vehicle for workers in public education institutions (K-12 and postsecondary) as well as many private nonprofit hospitals, universities, and other charitable and educational organizations—cannot offer CITs. As a result, workers who save for retirement through 403(b) plans are not allowed to access these low-cost products and, as illustrated below, pay more than those who can access CITs. By contrast, many 401(k) plans—a common savings vehicle for the private sector—and 457 plans—retirement plans offered by state, local, and certain tax-exempt employers—can offer both CITs and mutual funds.

CITs at Vanguard on average have expense ratios that are almost 50% lower than those of our mutual funds. In Vanguard's case, the average expense ratio for CITs is about 5 basis points versus 9 basis points for mutual funds, and the average difference can be even higher industrywide.[1] Allowing 403(b) plans to offer CITs would level the playing field and could allow these plans to return hundreds of millions of dollars to participants in the form of lower fees. With roughly $1.26 trillion of 403(b) plan assets locked out of CITs, Vanguard estimates that the cost savings to participants in plans that offer CITs could amount to more than $250 million per year.[2] This would mean that over time, billions of dollars could go back to the participants, helping them to achieve even greater security in retirement.

To be sure, not all CITs have lower expense ratios than mutual funds, and retirement plan sponsors should, as always, carefully consider the relative advantages of each option.

The point is not to recommend one approach over the other but to highlight a basic unfairness in the system. The vast majority of workers in the nonprofit sector don't have access to CITs, and there is simply no reason for this. To address this inequity, legislation is required. (See the next page for information about legislation that Vanguard supports.)

Public educational and nonprofit employees cannot access all of the same investment options as private-company employees

Private-company plans have access to both CITs and mutual funds and have a **wider array of choices to pick the best options** for their participants.

	Investment vehicle	Average costs for Vanguard investors*
PRIVATE EMPLOYEES (with access to CITs)	401(k)	0.05%
NONPROFIT EMPLOYEES (without access to CITs) e.g., schools, hospitals, universities, etc.	403(b)	0.09%

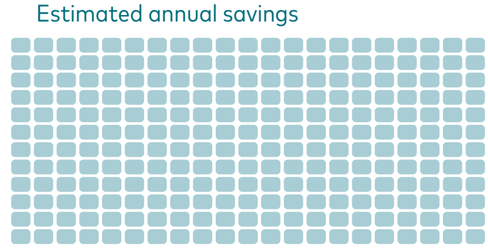
Workers in the nonprofit sector generally don't have access to CITs, which can mean **higher fees in their 403(b) retirement plans.**

But if those nonprofit workers were able to invest their roughly $1.26 trillion of 403(b) plan assets in CITs, the **savings could be substantial.**

■ = $1 million in annual savings

$252 MILLION

Estimated annual savings



* The 0.05% figure is the average expense ratio for Vanguard participants who use CITs in 401(k) plans, and the 0.09% figure is the average expense ratio for Vanguard participants in 403(b) plans who do not have access to CITs.

1 Jasmin Sethi, Lia Mitchell, and Aron Szapiro, June 2020. *CITs: A welcome addition to 403(b) plans.* Morningstar, Inc.

2 This assumes that half of the $1.26 trillion in nonprofit retirement assets are transferred from mutual funds to CITs, and the average cost of these assets falls 4 basis points. (A basis point is one-hundredth of a percentage point.)

Vanguard urges support for bipartisan efforts in Congress to address this inequity and let educational and nonprofit workers choose among a broader range of high-quality, low-cost products. We applaud Congress for passing the SECURE 2.0 Act of 2022, a bipartisan law that includes tax changes to expand access to CITs. However, securities law changes to make 403(b) plans eligible to invest in CITs were not included in the law, and as a result, further legislation is required to create parity for 403(b) plan savers. For this reason, Vanguard urges support and cosponsorship of the Retirement Fairness for Charities and Educational Institutions Act sponsored by Reps. Frank Lucas (R-OK), Bill Foster (D-IL), Andy Barr (R-KY), and Josh Gottheimer (D-NJ).

If 403(b) plans have the same opportunity to offer CITs as 401(k) plans, retirement plans in the nonprofit sector will have more investment choices to help meet the diverse needs of their participants, ultimately helping to improve the chances of a secure retirement for these workers.

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As one of the world's leading asset managers, Vanguard is committed to ensuring that financial products—and the regulations governing them—work in the best interests of investors everywhere, regardless of their level of investable assets.

We summarize this commitment in Vanguard's core purpose: To take a stand for all investors, to treat them fairly, and to give them the best chance for investment success.

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