TESTIMONY of Cheryl Moss Herman Regarding
SB 0475, Workgroup on the Maryland 529 Prepaid College Trust Program
Before the Maryland Senate Education, Energy, and the Environment Committee
February 22, 2023

Good Afternoon, Chair Feldman, Vice Chair Kagan, and Members of the Committee. My name is Cheryl Moss Herman. I am a resident of District 15, represented by Senator Feldman, but live close enough to the district line that my children attended elementary, middle, and high schools that were in Senator Kagan's District.

I am here today to share my views on SB 0475, which I support, but with significant amendment towards an equitable and timely solution to the harm caused to Account Holders from across Maryland by the missteps, mistakes and mismanagement of the Maryland Prepaid College Trust.

I purchased Prepaid accounts for both of my daughters, now young adults, in 2001 and 2004 and paid off each account over a number of years. I assure you that I understood the terms of what I purchased, including the actuarial projections of Trust investment earnings and of future college tuition costs used for price setting.

I also understood the changes proposed in 2021 and spent a great deal of time trying to understand the value of my younger daughter's account as she was selecting colleges in Spring, 2022. The difference between the Minimum Benefits estimate provided to me in May, 2022 and the recently received "Manual Report" is over $50,000, or a decline in benefits of almost $6,000 per semester. That is why I am here today.

The recent chapter for the Maryland Prepaid College Trust (MPCT) began on June 25, 2021, when the Maryland 529 Board approved the rate of return for minimum benefits, rollovers and refunds to be the Trust's since-inception rate of return as of June 30, 2021 -- 6% -- for balances held PRIOR to November 1, 2021. Contributions received on/after November 1, 2021 would receive the 10-year Treasury Note rate. These rates and calculation changes would go into effect on November 1, 2021.

The November 1, 2021, date of the change coincided with the transition from self-management of the MPCT to management by a third-party Program Manager, Intuition.

Prior to this change, the calculation used for a rollover or refund used MPCT's since inception rate of return to attribute earnings to the balances in an account. According to Maryland 529, this has been between 5% and 6% in the seven years prior to 2022. However, those account holders who were requesting Minimum Benefits, had their benefits calculated as contributions made under their contract plus a rate of return equal to a monthly rate of return of a U.S. Government Security with a constant maturity of one year minus 1.2%, with a floor of 0%. From

November 2008 to June 2017, the rate of return associated with the Minimum Benefit calculation was 0%.

A driver for the change was consistency and fairness -- for MPCT to align calculations for Minimum Benefit with calculations for rollovers and refunds so that an account was not worth more when it was rolled over or refunded than it was when it was used as intended.

In August 2021, MPCT announced to Account Holders the transition of operations to Intuition and provided Account Holders with a supplement that amended the prior December 2020 Disclosure Statement that had also been amended in April 2021. The changes, as noted above, would become effective on November 1, 2021.

The amended Disclosure language for says:

> "For Accounts in existence on October 31, 2021, contributions in your Account prior to October 31, 2021 will earn 6% on balances, compounded monthly, until Benefits are withdrawn, or your Contract is terminated.
>
> Contributions made on or after November 1, 2021, will accrue regular interest each year, compounded monthly, at a rate equal to the 10-year Treasury note rate. The Treasury note yield applicable to the Account contributions will be updated annual with the June 30th number."

For seven semesters, I successfully used my in-state benefits for my older daughter, a 2022 graduate of the University of Maryland - College Park. However, after the August 2021 changes to the disclosure went into effect on November 1, 2021, I realized we had value in the account above what would be needed for the final tuition payment. I called Maryland 529 to find out how to preserve that value and was told three different things – from the value will disappear when the final (8th) semester is paid to it will be available for an additional ten years. I was also advised each time that the most secure way to preserve the value would be to roll it over to the Maryland College Investment Plan(MCIP). Instead of rolling the dice on the what would preserve the value, I executed a rollover to MCIP.

The MPCT initiated the rollover as I requested and canceled my account on February 25, 2023. By mid-March, concerned that the money had not appeared in my MCIP, I began daily calls to both MPCT and MCIP to find the money. One day, the check from MPCT with my funds arrived at my home by mail, with a note from MCIP that the check was made out improperly and therefore rejected.

That's right. The MCIP rejected the check from MPCT – both are part of the same organization, Maryland 529.

I did not see anything improper about the check. After a number of phone calls, I returned the check to MCIP and it was deposited into my daughter's MCIP account. I was told that the “documentation” for the check was the issue. When I received the paperwork from the Prepaid, I could see why: the rollover of about $14,000 had earnings of over $29,000 reported for it. That. Can’t. Be.

It seems that my first account may have been one of the “canary in the coal mine” accounts. I was told that Maryland 529 staff was noticing discrepancies in the application of interest that required a programming fix. It was shared that the new earnings calculation was not only being applied to monies that remained in the account, but also to historical balances that had been distributed. That seems consistent with the account statement I was provided at the time of the rollover.

Additionally, a background document provided by Maryland 529 to the General Assembly in summer 2022 corroborates this error. It describes the calculation issue (page 4), “…the new earnings calculation, which increased the interest rate payable under the Minimum Benefit calculation, was not being applied to just the balances held in an account as of the transition date, as called for by the disclosure Statement, but rather to historical account balances that had long-since been distributed. As such, funds were being distributed with earnings calculations that were attributable not to the basis portion of that same distribution, but on past balances no longer held by the Trust.”

Upon discovery of the programming error, MPCT froze the application of earnings on accounts in April, 2022 while they investigated and attempted to correct what they described as a “technical error” that occurred during the November 2021 transition to a third-party program manager, Intuition. The freeze also resulted in all FAFSA (Federal application for financial aid) values now being displayed in an account’s online portal at the level of contributions only.

During the Spring of 2022, many Account Holders, myself included, relied on the balances shown on the end-of-year 2021 statement and estimated calculations done for them by MPCT upon request when making financial choices related to their student’s college education. For many, including me, this information played directly into their affordability calculations and the choice of in-state versus out-of-state colleges.

My second account, for my then high school senior, showed a FAFSA value of more than $85,000 with the added earnings per the 2021 policy change. I reached out to the Prepaid Trust multiple times from December, 2021 through February, 2022 to try to ensure I knew the balance of monies I saved for my daughter’s college education. I received confirmation of the end of year FAFSA value and its relationship to the Minimum Benefit multiple times in that timeframe.

But by the end of April, 2022, with college decisions looming, the MPCT representatives refused to share the value of the Minimum Benefit for my own Prepaid account with me. This information was key to learn before my daughter had to make her college section by May 1. This is when I reached out to my legislative delegation for help.

The availability of these funds were a critical part of our discussions that resulted in her deciding to attend an out-of-state university.

Thanks to intervention from Senator Feldman's office, I was provided a phone estimate on April 21, 2022 by Ms. Traci Ornella of Intuition -- in time to consider the financial implications as my daughter selected a college. The estimate was for over $87, 000 with a semester Minimum Benefit of almost $11,000 per semester. During that phone call, and subsequent calls, we also talked about the methodology for calculating the Minimum Benefit, with the 6% interest applied to contributions from the time they were made until the monies were withdrawn. During the April 21 call, I asked for the estimates in writing.

On May 18, 2022, I received a phone call from the then MPCT Executive Director, Erin Layton, during which the Minimum Benefit estimate was confirmed. We also discussed the 6% since contribution methodology for calculating earnings. Ms. Layton shared that she was approving a letter to be sent to me with my requested Minimum Benefit estimates. [That letter also addressed new calculations for the rollover of my older daughter's account that was completed in Feb/March 2022 that initially had an incorrect interest calculation.]

On May 19, 2023, I received the letter from Ms. Ornella, as approved by Ms. Layton and discussed with me the day prior. Both of the phone calls (Ornella and Layton) included estimates that calculated interest from the time of contribution as well as specific discussions of how the earnings were calculated at 6% on contributions from the time of contribution until dispersed. The May 19, 2022 estimated amount is similar to the end of calendar year 2021 statement FAFSA value. As noted above, it included an estimated Semester Minimum Benefit of almost $11,000 per semester - a <u>significant amount</u> above the approx. $5300 per semester weighted average tuition benefit.

It is important to note that neither the freezing of interest application or the change in the online FAFSA account value were shared broadly with Account Holders for months. Maryland 529 notified Account Holders of the April, 2022 suspension of interest earnings on August 29, 2022 – a full four months after that suspension was initiated and as Account Holders were filing for benefits for Fall 2022 tuition and qualified education expenses. Unless an Account Holder reached out specifically for an estimate of benefits or a rollover or refund, or inquired about the change in the online FAFSA value (long after most had filed the FAFSA form), the interest calculation freeze was not widely known.

I was not yet concerned about the 'technical issue' for my younger daughter's account because it was described as only affecting accounts that had prior distributions and each and every call I had included a discussion of the earnings methodology that was to be applied to my account.

The initial target for the recalculations to be completed was June, 2022. However, MPCT hired auditors in that timeframe and elected to have the recalculations reviewed by the auditors, pushing the new deadline to August, 2022. That was later revised to September, 2022.

For those Account Holders with students attending out-state-colleges in Fall 2022, this meant that Account Holders were only able to access the weighted average tuition (WAT), not the greater of WAT or Minimum Benefit, as described in the Disclosure. It also posed issues for Account Holders who counted on their excess benefits for other qualified education expenses and those whose students were graduating and will not have costs against which to take future distributions.

In September, 2022, Mr. Savia became the new Executive Director (the third in as many months) and during a Board meeting and a Townhall, acknowledged that the interest calculation issues were on-going and promised an update by October 31, 2022. He also established a process for identifying and prioritizing manual calculations of accounts thought an Account Support Request form.

On November 7, 2022, Maryland 529 informed Account Holders that on October 27, 2022, the Board voted on “a number of initiatives” aimed at providing accurate account values. The communication specifically noted a change from a “net contribution” method to a ledger balance method. Account Holders do not know what other “initiatives” were discussed and voted on at that meeting.

The November 7, 2022 Maryland 529 update also provided a projected timeline, which had the manual recalculations 100 % complete by the third week of December. This timeline should have allowed Account Holders to access their semester Minimum Benefit for Fall 2022 before the end of tax year 2022.

A December 12, 2022 Update from Maryland 529 said, in part, “The manual calculation process is underway and work remains ongoing to test and validate an automated process for the calculation across all Accounts. Our next step is to contact each Account Holder who submitted an Account support request form to advise on next steps.” The update directs Account Holders to FAQs on the Maryland 529 website, which included the prior timeline with the third week of December as the target completion date for manual calculations.

As far as we are aware, no manual calculations were completed and earned interest made available in 2022. This means that Minimum Benefits for Fall 2022 were not available in calendar year 2022, which would have enabled the matching of expenses and distributions in the same calendar year for tax purposes.

On January 6, 2023, an MPCT update introduced a new implementation approach where the 6% earnings are only applied to balances in your account on Oct 31, 2021. That update says, in part, "In the process of distributing these additional earnings (which ironically stem from an increase to percentage of attributable earnings effective November 1, 2021), the calculation was inaccurately reported and had to be corrected in compliance with the Board approved Disclosure Statement (which has always been publicly posted on our website at: https://maryland529.com/Portals/0/Files/MPCT_Disclosure_Statement.pdf).”

Additional explanation is provided via a slide deck linked to the update: Prepaid College Trust Public Update_1.6.23.pdf (maryland529.com). Page 12 indicates that for contributions made prior to Nov 1, 2021, the interest rate at the time (which was effectively zero from November, 2008 to June 2017) would be applied and the 6 % would be applied to balances in place on Oct 31, 2021 and, for these accounts – those that were in existence on October 31, 2021 -- thereafter.

This January 6, 2023 methodology change yields drastically different account values for Account Holders than shown on the 2021 end-of-year statements. Each Account Holder will not realize tens of thousands of dollars of earnings that they were previously expecting and counting upon. I also believe it is not consistent with the intent of the Board in June 2021 as it decreased the value for rollovers and refunds, which may not be allowed by the contract.

Based on discussions many Account Holders, including me, had with MPCT leadership and contractors and estimates received along the way, this change in approach is an unwelcome surprise. It is also surprising given the reference to interest calculations described in the Actuarial Soundness report included in the Maryland 529 2022 Annual report [2022_MD529_AnnualReport_FINAL.pdf (maryland529.com)]. On page 18, the actuaries who reviewed the actuarial soundness of the MPCT say the following (italics added for emphasis):

> "Beginning November 1, 2021, the same interest crediting will be used in calculations performed for the Minimum Benefit, rollovers and refunds. *Interest will be credited on contract payments made to the Trust prior to November 1, 2021 at the since inception rate of return as of June 30, 2021 (6.00 percent) for periods both before and after November 1, 2021.*"

The actuaries conducting the soundness report understood that the 6% was to be applied to contract payments before and after Nov 2021 – and – the assumptions in their report were included in the Annual Report and not disputed by comment or footnote.

Importantly, the actuaries determined that MPCT is actuarially sound if the 6 % interest is applied to contributions made prior to November 1, 2021 from the time of the contribution.

The January 6 update has confused matters considerably. I and hundreds of Marylanders relied on the 2021 information to make financial decisions related to our students' college education.

For me, the difference between the greater than $87,000 estimate I received by phone on April 21, 2022 as my family was making college choice, which was confirmed by Ms. Layton on May 18, and as approved by Ms. Layton, in writing by Intuition, on May 19, 2022 and the manual calculation reports I received on January 23, 2023 (and inexplicably again on January 31 and February 8) is over $50,000. That is, the Minimum Benefits calculated by the January 6, 2023 methodology is over $50,000 less than the estimate previously provided – or about $6,000 per semester less. College decisions were made on the initial estimate, causing us to have to find $6,000 per semester elsewhere.

Changing the rules retroactively in the “middle of the game” presents significant hardships related to college funding that are contrary to the objective of the Maryland 529.

This is unacceptable to me -- and should be unacceptable to you. As a State-legislature backed program, both transparency and accuracy should be paramount.

Account holders relied on this Maryland state agency to help them plan for college. This state agency failed me and thousands of others from across the state. Our families and our students deserve better. We need your full engagement soonest to make this right.

Those principles of consistency and fairness that were the basis for the June 2021 change in the interest rate calculation should carry forward to discussions about current status and future actions and solutions this legislative session.

I stand ready and willing to sit down with you, the Governor’s office, and the Maryland 529, to forge a fair and whole solution that helps the Maryland 529 meet its intended objectives immediately.

Thank you for allowing me to share my views.

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