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Thrift Savings Plan: Investment Issues

The Thrift Savings Plan (TSP) was created under the Federal Employees' Retirement System Act (FERSA; P.L. 99-335; June 6, 1986). TSP is a defined contribution retirement plan for the civilian federal workforce and the uniformed services, similar to the 401(k) plans sponsored by many private-sector employers. TSP provides individual accounts that serve as a source of income in retirement to participants and their beneficiaries. As of March 2022, there were more than 6.5 million total participants in TSP and $817.7 billion in total assets.

The Federal Retirement Thrift Investment Board (FRTIB) administers TSP. FRTIB is an independent agency that receives no appropriations from Congress. Instead, administrative expenses for FRTIB are paid through TSP loan fees, 1% agency automatic contributions forfeited by certain employees who leave federal service before they have vested, and administrative charges against participant accounts. FRTIB is composed of five board members chosen by the President and confirmed by the Senate. The Board also selects an Executive Director who manages daily operations. Under current law, members of the FRTIB and the Executive Director serve as fiduciaries, legally obligated to act "solely in the interest of the [TSP] participants and beneficiaries … and for the exclusive purpose of providing benefits to participants and their beneficiaries" (5 U.S.C. §8477(b)(1)).

All TSP investment options are set out under current law (5 U.S.C. §8438). In order to offer these investment options to participants, FRTIB develops specific investment policies—for example, selecting benchmarks for the index fund investment options—that provide for "prudent investments suitable for accumulating funds for payment of retirement income; and low administrative costs" (5 U.S.C. §8475). Thus, in addition to its fiduciary responsibilities, FRTIB must adhere to their statutory mandates to keep administrative costs low and prudently manage returns for TSP account holders.

Legislative History of TSP Investment Options

At its creation in 1986, the TSP was designed to be passively managed in order to avoid political manipulation—in particular, using the large pool of assets managed by FRTIB for political purposes. Thus, TSP index funds are all passively managed by professional fund managers, each with an investment objective of matching the performance of a specific, benchmark index fund. TSP fund managers do not actively select a fund's portfolio assets. Currently, BlackRock and State Street Global Advisors both hold fund manager contracts for all TSP index funds.

Three investment options—the "C" Fund (a common stock index fund), the "F" Fund (a fixed income index fund), and the "G" Fund (a government security fund)—were authorized at TSP's creation under FERSA. Two additional index funds, the "S" Fund (a small cap stock index fund) and the "I" Fund (an international stock index fund) were added in 2001 in accordance with the Thrift Savings Plan Act of 1996 (P.L. 104-208; September 30, 1996).

In 2005, FRTIB introduced "Lifecycle Funds" (L Funds), which are invested in various combinations of the five existing TSP funds with allocations based on the year that the participant expects to begin withdrawing money from the TSP. The Smart Savings Act (P.L. 113-255; December 18, 2014) changed the default investment option for automatic contributions to TSP. Prior to P.L. 113-255, TSP default contributions were automatically invested in the "G" Fund of the TSP. (The default contribution rate for most employees is 5% if enrolled in TSP after October 1, 2020, or 3% if enrolled between August 1, 2010, and September 30, 2020.) P.L. 113-255 changed the default investment option to the age-appropriate Lifecycle Fund.

Title I of Division B of P.L. 111-31, the Thrift Savings Plan Enhancement Act (June 22, 2009), provided FRTIB with the authority to set up a mutual fund window (MFW) "if the Board determines that such addition would be in the best interests of participants" (5 U.S.C. §8438(b)(5)(A)).

Current TSP Investment Options

Participants in the TSP may currently choose among five funds in which they can invest their TSP contributions:

- The "C" Fund replicates the Standard and Poor's 500 Index of 500 large to medium-sized U.S. companies.
- The "F" Fund invests in bonds in the same proportion as they are represented by the Barclays Capital U.S. Aggregate Bond Index.
- The "G" Fund invests in U.S. government securities and pays interest equal to the average rate of return on government securities with maturities of four years or more.
- The "S" Fund tracks the Dow Jones U.S. Completion Total Stock Market Index of small to medium-sized U.S. companies not included in the "C" Fund.
- The "I" Fund replicates the Morgan Stanley Capital International EAFE (Europe, Australasia, Far East) Index.

Finally, the L Funds are composed of the five existing TSP funds and consist of L2025 through L2065 in five-year increments and the L Income Fund, which is a low-risk option designed to achieve asset preservation for participants making withdrawals or nearing retirement. As the participant approaches retirement, the proportion of contributions invested in the C, I, and S funds—which invest in stocks—is reduced. The proportion invested in the G and F funds—which invest in bonds—is increased. This helps to protect participants who are nearing retirement from investment losses that would occur from a sharp decline in stock prices.

Recent Policy Interest Related to TSP Investments

Recent policy interest in TSP investment has focused on two issues. First, I Fund investment practices have drawn attention from policymakers—specifically, the deliberation surrounding whether to change the I Fund benchmark. In November 2017, after consulting with experts, FRTIB made the decision to move from the current I Fund benchmark—the Morgan Stanley Capital International (MSCI) EAFE (Europe, Australasia, Far East) Index—to a new benchmark: the MSCI ACWI ex. U.S. IMI (All Country World ex USA Investable Market Index). FRTIB justified this decision using the following arguments: (1) the MSCI ACWI ex USA represents 99% of the international equity market (vs. the MSCI EAFE Index, which represents only 58%) and, thus, is a more representative benchmark that better fulfills the statutory requirement of a complete representation of the international equity markets; and (2) the MSCI ACWI ex USA would be more in line with the investment policies of other large retirement plans in the private and public sectors, which offer the ability to invest in Canada and emerging markets.

Before the change to the I Fund benchmark could be implemented, however, this FRTIB decision received attention from policymakers. This interest focused on issues raised by investments in certain Chinese companies. For example, in August 2019, Senators Rubio and Shaheen sent a letter to FRTIB outlining concerns with the proposed I Fund benchmark change as “a decision to invest in China-based companies, including many firms that are involved in the Chinese government’s military, espionage, human rights abuses and ‘Made in China 2025’ industrial policy, and therefore poses fundamental questions about the board’s statutory and fiduciary responsibilities to American public servants who invest in federal retirement plans.” In November 2019, FRTIB reviewed its decision and announced that it was moving ahead to finalize the I Fund benchmark change. In May 2020, however, FRTIB announced that it was deferring any action on the I Fund benchmark due to (1) the “meaningfully different economic environment related in large part to the impact of the global COVID-19 pandemic” and (2) the nominations of new FRTIB members. Since May 2020, there have been no further plans or announcements by FRTIB related to the I Fund benchmark. Congress is currently considering a slate of FRTIB nominations. Additionally, several pieces of legislation have been introduced in the 117th Congress that would prohibit any TSP investment in Chinese firms (thus, preventing the I Fund benchmark change to the MSCI ACWI ex USA)—for example, S. 1665, S. 1742, S. 1993, H.R. 3295, H.R. 3553, and H.R. 4792.

Second, there has been interest in environmental, social, and governmental (ESG) issues with regard to TSP investments. In a May 2021 report, the Government Accountability Office recommended that FRTIB evaluate TSP investment risks with regard to climate change. There has also been legislation introduced in the 117th Congress related to TSP investments, fossil fuels, and climate change (e.g., S. 606 and H.R. 1618); TSP divestment from Russia, although none of the TSP funds have any Russian holdings currently (e.g., H.R. 7113); and the use of diverse asset managers by federal institutional investors, including FRTIB (e.g., S. 4097 and H.R. 7594). As explained below, the upcoming mutual fund window will provide ESG investment options to TSP participants.

Upcoming TSP Mutual Fund Window

The FRTIB has announced that it will exercise the optional authority provided by P.L. 111-31 to offer a new MFW to TSP participants. FRTIB has stated that the implementation date for the MFW will be summer 2022 and provided the following additional details: “Of the more than 5,000 mutual funds available through the MFW, there will be funds that are designed for ESG [environmental, social, and governance] investment (however a participant may define that), as well as commodity specific funds, actively managed funds, and emerging manager funds.” (Emerging manager funds generally refer to newer, smaller funds or funds with diverse asset managers.)

In a final rule for the MFW, released on May 10, 2022, FRTIB sets out terms and conditions of MFW participation: (1) a minimum initial transfer of $10,000 into the MFW; (2) a limit of no more than 25% of a TSP account holder’s balance into the MFW (thus, a minimum balance of $40,000 is required); and (3) inclusion of transfers to and from the MFW in the overall limit on interfund transfers (two per month). FRTIB also specified fees for TSP participants who choose to invest in the MFW: an annual $55 administrative fee, an annual $95 maintenance fee, a per-trade fee of $28.75, and any fees and expenses imposed by the specific mutual fund(s).

Additional Resources

For more information on the TSP investment options, see “TSP Fund Information,” March 2022, https://www.tsp.gov/publications/tsplf14.pdf.

For FRTIB discussions and decisions, see https://www.frtib.gov/meeting-minutes/.

FRTIB, “Mutual Fund Window,” 87 *Federal Register* 27917-27923, May 10, 2022, https://www.govinfo.gov/content/pkg/FR-2022-05-10/pdf/2022-09972.pdf.

For background on ESG, see CRS In Focus IF11716, *Introduction to Financial Services: Environmental, Social, and Governance (ESG) Issues*.

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