

## When fixing Social Security, we should pay heed to 401(k) industry

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By most projections, the “pay as you go” Social Security System stops paying for itself in 2018 and runs out of money altogether by 2042.

The debate is heating up over how to “fix” Social Security, with the Bush administration preparing to announce its plan in coming weeks.

What we know so far is that Bush’s plan will allow for private accounts, giving workers limited control over a portion of the funds being contributed to Social Security from their paychecks.

Without speculating on the details or arguing the pros and cons of the yet-to-be-announced proposal from the White House, I suggest policy-makers thoroughly investigate the 20-plus year experience of 401(k) plans before deciding on the best course of action for Social Security.

What have we learned from 401(k) plan participation that could be applicable to a new Social Security system?

The good news is that we know, when given the opportunity, most (+70%) American workers will choose to fund a personal retirement account.

Private Social Security investment accounts likely are to be embraced by the majority of American workers, especially if they can be shown how doing so will benefit them. I also believe that many would take some comfort building a tangible Social Security account balance vs. the current benefit, which is simply a promise to pay with dollars that many - especially younger workers - believe won’t be there when it comes time to collect.

The not-so-good news is that the majority of workers who go to the trouble of funding a 401(k) account have

demonstrated a colossal lack of interest, time and sometimes aptitude for managing these assets.

Therefore, a plan to fix Social Security that assumes the American worker will embrace taking control over the investment decisions for a portion of their Social Security benefit seems misplaced. Yet shares of publicly traded mutual fund companies rallied recently on hopes that a revamped Social Security System will funnel billions of dollars their way.

An alternative to allowing participant control over the assets in private Social Security accounts is the creation of an agency that would be charged with investing the assets of these accounts. Is it possible that a team of highly trained investment experts, a Social Security Investment Board, could deliver superior results to the vast majority of individual 401(k) investors? I think so.

A good model to follow is that of two of the most sophisticated large pools of assets in the country, the Yale and Harvard endowment funds. These multibillion-dollar pools of assets are managed by teams that are staffed by some of the brightest and best-trained investment minds in the world. By following a well-diversified investment strategy, these funds have delivered consistently superior results.

Of course to attract the brightest minds, the compensation would have to be commensurate with the responsibility. I suspect the thought of a government employee earning \$40 million a year would be pretty hard for many to swallow, but perhaps not so difficult to justify if their compensation were primarily performance-based.

The public understands that Social Security as we know it is in dire trouble. The time to act is now. Like corporate executives responsible for their employees’ 401(k) benefits, federal policy-makers must develop a plan that is focused on what is best for all the participants in the Social Security system.

While instituting a system of private Social Security investment accounts for a portion of future Social Security contributions may prove to be the most viable solution to our current problem, it should not be assumed that these accounts need to be self-directed.

It is time for the financial services industry and the policy-makers in Washington to carefully evaluate the evidence before them and put the interests of Social Security recipients ahead of their own. They both have a great model to learn from, the 401(k) industry. Let’s hope they have been paying attention.

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