We Need Investor Education, Not A "Public Option"

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I write about how technology shapes society, and vice versa. In addition to blogging for *Forbes*, I cover tech policy for *Ars Technica.* I'm an adjunct scholar at the Cato Institute and have a master's degree in computer science from Princeton. I live in Philadelphia with my wife and our two cats. There's more information about me on my website, including a comprehensive disclosure statement. Please follow me on Twitter. You can email me at contact@timothyblee.com.

The author is a Forbes contributor. The opinions expressed are those of the writer.

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Matt Yglesias endorses a “public option” for retirement savings, a proposal originally made by Dean Baker. The proposal doesn’t make much sense to me. Baker points out that private mutual funds, on average, charge much higher fees (as a percentage of assets under management) than the costs of the Thrift Savings Plan the federal government makes available to federal employees. So, he says, why not open the TSP up to anyone?

This is a case where averages are extremely misleading. I’m an investor in a Vanguard fund that invests in the large, publicly traded companies in the S&P 500. The fund’s “expense ratio” is 0.06 percent, significantly below the TSP’s cost of 0.15 percent of assets under management. My wife invests in Vanguard’s “life cycle” fund for people planning to retire in the 2040s. Its expense ratio is 0.19 percent, much lower than the private sector average and only slightly higher than the TSP.

Anyone who wants to invest in these low-cost funds (or the many others Vanguard offers) is free to do so. And thanks to IRAs, they can get tax benefits similar to those available under employer-sponsored 401(k) plans. And employers themselves can offer Vanguard funds under their 401(k) plans if they so choose. The problem isn’t that the private sector isn’t offering low-cost mutual funds, it’s that widespread financial illiteracy (combined with the fact that high-fee firms spend a lot on advertising) has caused a lot of people to squander their retirement savings on high fees. A public option does nothing to solve this problem.

And of course, expanding the TSP isn’t without risk. The TSP appears to be run efficiently today, but there’s no guarantee that will continue to be true in the future. If the option became popular, we could wind up with the federal government being a major shareholder in thousands of American companies. Government meddling in the governance of private companies seems like a bad idea. There’s also the risk of corruption: as the TSP gets larger, there will be increased lobbying to affect the government’s pattern of investment.

One thing Congress might want to do is to change tax law so that to qualify for the 401(k) tax break, a retirement plan must offer at least one low-cost option. But beyond that, this is fundamentally a problem of investor education. Low-cost plans are readily available. People just aren’t investing in them.

So let me do my small part in the education effort: if you are a mutual fund investor (and if you’re between 25 and 70, you should be) you should know your fund’s expense ratio and/or fees. If they are more than 0.25 percent, then you’re needlessly subsidizing the lavish lifestyle of some Wall Street fund manager. If possible, you should transfer your money to a fund with lower costs. If you’re in a 401(k) plan that only offers high-cost mutual funds, you should lobby your HR person to offer a lower-cost option.

And in case anyone’s wondering, my only relationship with Vanguard is as a satisfied customer. As always, readers should check my disclosure page for information about potential conflicts of interest.