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THE RETIREMENT SYSTEM IN THE UNITED STATES – AN EXAMINATION OF THE SYSTEMIC DYSFUNCTION AND MACRO CONSEQUENCES

Summary. Retirement signifies the transition from a position of active employment to a non-employee status usually triggered by age or other significant life event. The underlying principle of retirement continues to be a necessary event to sustain the American economy. In the post-depression era, the idea of retirement and more recently the idea of encouraging individuals to retire became a popular notion. Benefits from retirement include job openings for younger workers who graduate from college or university or are ready to start a trade or other employment. Recently government and private workers have been enticed into retirement with a myriad of buy-out arrangements. Even when Americans make a good faith effort to save for retirement, it is possible to end up with inadequate resources due to corrupt business practices and investment decisions that do not generate adequate returns.

Keywords: Investments, Pension, Private Sector, Retirement

SYSTEM EMERYTALNY W STANACH ZJEDNOCZONYCH – OCENA DYSFUNKCJI SYSTEMOWYCH ORAZ KONSEKWENCJI GLOBALNYCH

Streszczenie. Emerytura oznacza przejście z pozycji aktywnego zatrudnienia do statusu osoby niepracującej zwykle z powodu wieku lub inych istotnych wydarzeń życiowych. Podstawowe zasady przechodzenia na emeryturę w dalszym ciągu są niezbędne dla utrzymania amerykańskiej gospodarki. W okresie pokryzysowym, zachęcanie osób do przejścia na emeryturę stało się popularnym zjawiskiem. Korzyści z przejścia w status emerytalny osób uwzględniają otwarcie rynku pracy dla młodszych pracowników kończących szkoły i uczelnie lub gotowych do podjęcia działalności handlowej lub innego zatrudnienia. W ostatnim czasie pracownicy sektora administracyjnego i prywatnego zachęcani byli do przejścia na emeryturę za pomocą licznych ofert wykupu. Nawet jeśli Amerykanie w dobrej wierze oszczędzają na emerytury, istnieje możliwość, że pozostaną z niewystarczającymi środkami za sprawą praktyk korupcyjnych w biznesie i decyzji inwestycyjnych, które nie przynoszą odpowiednich zwrotów.

Słowa kluczowe: inwestycje, wypłata emerytalna, sektor prywatny, przejście na emeryturę

1. Incentives to retire[1] young

In 2002 New York State Governor George Pataki signed into law an Early Retirement Incentive Program (ERI) at the urging of the AFL-CIO Pension Task Force. Chapter 69 of the Laws of 2002 allowed eligible members to take advantage of ERIs.

The ERI provided New York State employees who were age 55 or more with a minimum of 25 years of service the opportunity to retire with an extra three years of employment credited to the calculation of their pension.[2] For example, an employee with 26 years would have their pension benefits calculated as if they had 29 years of service to the State.

The type of ERI offered to state employees was a targeted incentive for employees with seniority to retire. This ERI provided several opportunities such as allowing New York State to reduce its workforce, trim its payroll, and hire new junior level employees where appropriate. Senior employees typically make the most money because of State incremental increases in pay designed to reward longevity. The program also worked well for employees/retirees who chose to partake as well as workers looking for employment, the State Government, and ultimately the taxpayers.

These ERI programs have become commonplace in state government and even private sector employment. From a positive perspective, they provide some workers a desired opportunity to retire at a comparatively young age. These workers can embark on another career or entrepreneurial venture or to completely withdraw from the labor market. Public sector ERIs are generally viewed positively in that they cannot usually be forced as a result of due process rights to their position unlike in the private sector where employment is at will.

[1] www.freedictionary.org/index.php, last verified March 23, 2006.
[2] www.nysut.org/legislation/2002earlyretirement.html, last verified March 24, 2006.

Thus, in some circumstances, usually private enterprise employment, early retirement can be forced, feared, and are often viewed as a threat to a workers livelihood, ability to care for family, assist children with college expenses, etc.

Recently workers at General Motors (GM) are mulling over their options due to the financially stressful times at the manufacturing giant.

One news story, states,

"After 34 years at General Motors Corp. and Delphi Corp., the endgame of Tim Krzeszewski's working life and future retirement comes down to this: Where will he place his bets? Ever since a union steward stopped the sheet metal worker at his Saginaw, Mich., plant this week to deliver details of a sweeping buyout offer, Krzeszewski has been mulling the decision before him, trying to divine its many unknowns. 'To me, it's like a gambling issue. Are you going to keep the hands that were dealt to you ... or throw the cards in and ask for a re-deal and hope you get a better hand,' says Krzeszewski, who is 52 and leaning heavily toward taking early retirement. Then you could lose it all." [3]

Similar to Mr. Krzeszewski's internal debate, many employees are faced with the question of whether to retire younger than they had planned. The question is important in that many American workers are aware that they have not saved enough for retirement.

Majority started saving very late in life and need time to secure a nest egg of retirement funds for their nonworking years. This is why the U.S. Internal Revenue Service (IRS) allows an additional $5000 retirement contribution for those aged 50 years and older. It is estimated that the average net worth of the typical American household is less than $15,000 excluding home equity. A non equity position is reached if automobiles and other possessions are factored out. Additionally less than 25 percent own any stocks, bonds or even a money market account and most are unable to cover monthly operating expenses without a paycheck. Furthermore about fifty percent of the elderly over 65 would live in poverty without their meager Social Security payments.[4]

It is estimated by **American Consumer Credit Counseling** that the total U.S. credit card debt in the first quarter of 2002 was approximately $60 billion. The average credit card interest rate at about 18.9% on the average.[5] Estimates show that approximately half of all credit card holders only pay the minimum each month with a total of 1.2 billion credit and retail cards in North America.[6]

Similar to GM workers described earlier, many workers, blue collar or otherwise face a real dilemma. The employers claim they can no longer afford to keep them although the employee has done the same job (developed a skill) over their entire career and in many

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[3] http://news.moneycentral.msn.com/ticker/article.asp?Symbol=US:GM&Feed=AP&Date=20060324&ID=5595889, last verified March 24, 2006.
[4] www.freerepublic.com/forum/a38356912243a.htm, last verified March 20, 2006.
[5] http://ask.yahoo.com/20040209.html, last verified March 25, 2006.
[6] Ibidem.

cases, lack the time, stamina, and/or ability to retrain for or start a new career. There is the additional defacto age barrier of entry for a new profession. Workers at GM and similar firms often earned a substantial income due to longevity and a strong union. These salaries cannot be replaced by other work which they are qualified to perform. Krzeszewski for example earned yearly wages averaging close to $90,000 including substantial overtime pay.[7] One of the biggest fears of these employees is that they may no longer have health insurance after retirement. We should also not be misled by the syntax chosen. Although programs are often referred to as “buyout offer” or “early retirement incentive” they very often do not provide the employee much choice. As Krzeszewski stated, “If he stays, Delphi may well try to terminate its pension plan and turn it over to the federal government, resulting in the capping of retirement benefits. The company could in addition eliminate health insurance and has already signaled its intention to sharply reduce hourly wages of workers for those who do not opt for the buyout offer.[8]

From a global perspective a recent BBC article reported that the Church of England is also concerned about its’ employees ability to have enough funds for retirement.[9]

2. A new societal problem

The generation dubbed “Babyboomer” those born between 1940 and early 1960s are the first to face this problem on large scale unlike previous generations. Historically, companies provided pension plans for their employees that paid retired employees a percentage of their working income. In other words, companies were obligated to pay a certain pension, regardless of how the stock market performed. These types of plans were sometimes referred to as pension or defined benefit plans.

The covenant between corporations and employees is undergoing a fundamental overhaul regarding pensions. Industry Leaders historically would not have considered the option of canceling pension plans due to the notion of corporate responsibility. There was a covenant so to speak between the employer and employee that was bonded by mutual loyalty.

Pension and defined benefit plans still exist today, but many are now closed to new employees. Additionally, when finances get tight or it seems a better corporate decision in the minds of current management, many companies feel no sense of loyalty or obligation to deliver what they had for years promised their employees would be available at retirement.

[7] http://news.moneycentral.msn.com/ticker/article.asp?Symbol=US:GM&Feed=AP&Date=20060324&ID=5595889, last verified March 24, 2006.
[8] Ibidem.
[9] http://news.billinge.com/1/hi/business/1310604.stm, last verified March 24, 2006.

3. The employer breaks their end of the bargain

The headline reads, **US Air To Axe Pensions**.[10] "Feds clear bankrupt airline's proposal to create a new, cheaper pension plan for its pilots. Bankrupt US Airways Group Inc. cleared its last big hurdle in restructuring when the government said it had approved the carrier's proposal to terminate its pilots' pension plan and replace it with a cheaper one. The action by Pension Benefit Guaranty Corp., a federal corporation, clears the way for the No. 7 U.S. airline to receive final bankruptcy court approval."[11]

In the late 1990s, a number of business enterprises decided to adopt defined contribution pension plans in order to reduce the expense and the risk of paying set-amount pensions. Granted, the expense and risk for employers has increased dramatically as people have been living longer and the cost of health benefits, especially for retirees because they are older have risen quickly and exponentially. However, there has been other market as well as psychological factors at work.

4. Scandal

Enron – "As the scandal unfolded, Enron's employees lost their jobs and their pensions. Its stockholders lost their shirts. Its accounting firm lost its credibility and its ability to operate as an auditor. About the only ones to walk away from Enron's fall intact were a number of executives who pocketed millions of dollars in compensation despite the company's collapse." [12]

"The rise of corporate scandals over the past two years, which caused a significant drop in stock prices, also cost New York State's economy $2.9 billion, cut State tax revenues by $1 billion and decreased the State pension fund value by $9 billion according to **a report issued today** by State Comptroller Alan G. Hevesi. The report noted that corporate scandals cost New York City approximately $260 million in tax revenues, and cost the New York City pension fund almost $7 billion in value." [13]

Consider the Corporate Scandal Sheet.

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[10] www.webprowire.com/summaries/446274.html, last verified March 24, 2006.
[11] Ibidem.
[12] http://levin.senate.gov/newsroom/release.cfm?id=210071, last verified March 24, 2006.
[13] www.osc.state.ny.us/press/releases/aug03/082003.htm, last verified March 24, 2006.

5. The Corporate Scandal Sheet

Penelope Patsuris, 08.26.02, 5:30 PM ET

NEW YORK – With the avalanche of corporate accounting scandals that have rocked the markets recently, it's getting hard to keep track of them all – but our Corporate Scandal Sheet does the job. Here we'll follow accounting imbroglios only – avoiding insider-trading allegations like those plaguing ImClone, since chronicling every corporate transgression would be impractical – and our timeline starts with the Enron debacle.

Table 1

Company	When Scandal Went Public	Allegations	Investigating Agencies	Latest Developments	Company Comment
Adelphia Communications (otc: ADELA - news - people)	April 2002	Founding Rigas family collected $3.1 billion in off-balance-sheet loans backed by Adelphia; overstated results by inflating capital expenses and hiding debt.	SEC; Pennsylvania and New York federal grand juries	Three Rigas family members and two other ex-executives have been arrested for fraud. The company is suing the entire Rigas family for $1 billion for breach of fiduciary duties, among other things.	Did not return repeated calls for comment.
AOL Time Warner (nyse: AOL - news - people)	July 2002	As the ad market faltered and AOL's purchase of Time Warner loomed, AOL inflated sales by booking barter deals and ads it sold on behalf of others as revenue to keep its growth rate up and seal the deal. AOL also boosted sales via "round-trip" deals with advertisers and suppliers.	SEC; DOJ	Fears about the inquiry intensified when the DOJ ordered the company to preserve its documents. AOL said it may have overstated revenue by $49 million. New concerns are afoot that the company may take another goodwill writedown, after it took a $54 billion charge in April.	No comment.
Arthur Andersen	November 2001	Shredding documents related to audit client Enron after the SEC launched an inquiry into Enron	SEC; DOJ	Andersen was convicted of obstruction of justice in June and will cease auditing public firms by Aug. 31. Andersen lost hundreds of clients and has seen massive employee defections.	Did not return repeated calls for comment.

con. tab. 1

Bristol-Myers Squibb (nyse: BMY - news - people)	July 2002	Inflated its 2001 revenue by $1.5 billion by "channel stuffing," or forcing wholesalers to accept more inventory than they can sell to get it off the manufacturer's books	SEC	Efforts to get inventory back to acceptable size will reduce earnings by 61 cents per share through 2003.	Bristol will continue to cooperate fully with the SEC. We believe that the accounting treatment of the domestic wholesaler inventory buildup has been completely appropriate.
CMS Energy (nyse: CMS - news - people)	May 2002	Executing "round-trip" trades to artificially boost energy trading volume	SEC; CFTC; Houston U.S. attorney's office; U.S. Attorney's Office for the Southern District of New York	Appointed Thomas J. Webb, a former Kellogg's CFO, as its new chief financial officer, effective in August.	No comment.
Duke Energy (nyse: DUK - news - people)	July 2002	Engaged in 23 "round-trip" trades to boost trading volumes and revenue.	SEC; CFTC; Houston U.S. attorney's office; Federal Energy Regulatory Commission	The company says an internal investigation concluded that its round-trip trades had "no material impact on current or prior" financial periods.	Although the effect [of these trades] on the company's financial statements was immaterial, we consider improper trades in conflict with the company's policies. To address this we have made changes to our organization, personnel and procedures.
Dynegy (nyse: DYN - news - people)	May 2002	Executing "round-trip" trades to artificially boost energy trading volume and cash flow	SEC; CFTC; Houston U.S. attorney's office	Currently conducting a re-audit. Standard & Poor's cut its credit rating to "junk," and the company said it expects to fall as much as $400 million short of the $1 billion in cash flow it originally projected for 2002.	Dynegy believes that it has not executed any simultaneous buy-and-sell trades for the purpose of artificially increasing its trading volume or revenue.

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El Paso (nyse: EP - news - people)	May 2002	Executing "round-trip" trades to artificially boost energy trading volume	SEC; Houston U.S. attorney's office	Oscar Wyatt, a major shareholder and renowned wildcatter, may be engineering a management shakeup.	There have been no allegations or accusations, only requests for information. The company has confirmed in multiple affidavits that it did not engage in "round-trip" trades to artificially inflate volume or revenue.
Enron (otc: ENRNQ - news - people)	October 2001	Boosted profits and hid debts totaling over $1 billion by improperly using off-the-books partnerships; manipulated the Texas power market; bribed foreign governments to win contracts abroad; manipulated California energy market	DOJ; SEC; FERC; various congressional committees; Public Utility Commission of Texas	Ex-Enron executive Michael Kopper pled guilty to two felony charges; acting CEO Stephen Cooper said Enron may face $100 billion in claims and liabilities; company filed Chapter 11; its auditor Andersen was convicted of obstruction of justice for destroying Enron documents.	No comment.
Global Crossing (otc: GBLXQ - news - people)	February 2002	Engaged in network capacity "swaps" with other carriers to inflate revenue; shredded documents related to accounting practices	DOJ; SEC; various congressional committees	Company filed Chapter 11; Hutchison Telecommunications Limited and Singapore Technologies Telemedia will pay $250 million for a 61.5% majority interest in the firm when it emerges from bankruptcy; Congress is examining the role that company's accounting firms played in its bankruptcy.	No comment.

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Halliburton (nyse: HAL - news - people)	May 2002	Improperly booked $100 million in annual construction cost overruns before customers agreed to pay for them.	SEC	Legal watchdog group Judicial Watch filed an accounting fraud lawsuit against Halliburton and its former CEO, Vice President Dick Cheney, among others.	Halliburton follows the guidelines set by experts, including GAAP (generally accepted accounting principles).
Homestore.com (nasdaq: HOMS - news - people)	January 2002	Inflating sales by booking barter transactions as revenue.	SEC	The California State Teachers' Retirement pension fund, which lost $9 million on a Homestore investment, has filed suit against the company.	No comment.
Kmart (nyse: KM - news - people)	January 2002	Anonymous letters from people claiming to be Kmart employees allege that the company's accounting practices intended to mislead investors about its financial health.	SEC; House Energy and Commerce Committee; U.S. Attorney for the Eastern District of Michigan	The company, which is in bankruptcy, said the "stewardship review" it promised to complete by Labor Day won't be done until the end of the year.	Did not return repeated calls for comment.
Merck (nyse: MRK - news - people)	July 2002	Recorded $12.4 billion in consumer-to-pharmacy co-payments that Merck never collected.	None	The SEC approved Medco's IPO registration, including its sales accounting. The company has since withdrawn the registration for the IPO, which was expected to raise $1 billion.	Our accounting practices accurately reflect the results of Medco's business and are in accordance with GAAP. Recognizing retail co-payments has no impact on Merck's net income or earnings per share.
Mirant (nyse: MIR - news - people)	July 2002	The company said it may have overstated various assets and liabilities.	SEC	An internal review revealed errors that may have inflated revenue by $1.1 billion.	This is an informal inquiry, and we will cooperate fully with this request for information.

con. tab. 1

Nicor Energy, LLC, a joint venture between **Nicor** (nyse: GAS - news - people) and **Dynegy** (nyse: DYN - news - people)	July 2002	Independent audit uncovered accounting problems that boosted revenue and underestimated expenses.	None	Nicor restated results to reflect proper accounting in the first half of this year.	Our focus now is to stabilize this venture and put some certainty to its financial results. The company is evaluating its continued involvement in this venture.
Peregrine Systems (nasdaq: PRGNE - news - people)	May 2002	Overstated $100 million in sales by improperly recognizing revenue from third-party resellers	SEC; various congressional committees	Said it will restate results dating back to 2000; slashed nearly 50% of its workforce to cut costs; is on its third auditor in three months and has yet to file its 2001 10-K and so, consequently, is in danger of being delisted from the Nasdaq.	We have been and will continue to cooperate with the SEC and the Congressional committee.
Qwest Communications International (nyse: Q - news - people)	February 2002	Inflated revenue using network capacity "swaps" and improper accounting for long-term deals.	DOJ; SEC; FBI; Denver U.S. attorney's office	Qwest admitted that an internal review found that it incorrectly accounted for $1.16 billion in sales. It will restate results for 2000, 2001 and 2002. To raise funds, Qwest says it is selling its phone-directory unit for $7.05 billion.	We are continuing to cooperate fully with the investigations.
Reliant Energy (nyse: REI - news - people)	May 2002	Engaging in "round-trip" trades to boost trading volumes and revenue.	SEC; CFTC	Recently replaced Chief Financial Officer Steve Naeve with Mark M. Jacobs, a managing director of Goldman Sachs and a Reliant adviser.	We're cooperating with the investigations.

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Tyco (nyse: TYC - news - people)	May 2002	Ex-CEO L. Dennis Kozlowski indicted for tax evasion. SEC investigating whether the company was aware of his actions, possible improper use of company funds and related-party transactions, as well as improper merger accounting practices.	Manhattan district attorney; SEC	Said it will not certify its financial results until after an internal investigation is completed. The Bermuda-based company is not required to meet the SEC's Aug. 14 deadline. Investors looking to unseat all board members who served under Kozlowski may launch a proxy fight to do so.	The company is conducting an internal investigation and we cannot comment on its specifics, but we will file an 8-K on the initial results around Sept. 15.
WorldCom (nasdaq: WCOEQ - news - people)	March 2002	Overstated cash flow by booking $3.8 billion in operating expenses as capital expenses; gave founder Bernard Ebbers $400 million in off-the-books loans.	DOJ; SEC; U.S. Attorney's Office for the Southern District of New York; various congressional committees	The company stunned the Street when it found another $3.3 billion in improperly booked funds, which will bring its total restatement up to $7.2 billion, and that it may have to take a goodwill charge of $50 billion. Former CFO Scott Sullivan and ex-controller David Myers have been arrested and criminally charged, while rumors of Bernie Ebbers' impending indictment persist.	WorldCom is continuing to cooperate with all ongoing investigations.
Xerox (nyse: XRX - news - people)	June 2000	Falsifying financial results for five years, boosting income by $1.5 billion	SEC	Xerox agreed to pay a $10 million and to restate its financials dating back to 1997.	We chose to settle with the SEC in April so we can put the matter behind us. We have restated our financials and certified our financials for the new SEC requirements.

Editor's Note: The Corporate Scandal Sheet ceased being updated as of September 2002.[14]
SEC: Securities and Exchange Commission. CFTC: Commodity Futures Trading Commission. DOJ: U.S. Department of Justice

The Scandal Sheet raises a number of important questions. One, such a list has not existed in prior times and secondly, the "transgressions" are bold, intentional, and calculated.

[14] www.forbes.com/2002/07/25/accountingtracker.html, last verified March 24, 2006.

It is hardly believable that there is a lack of accountability amongst a mass of employers, managers, and executives. It is also noteworthy that members of Board of Directors operate in such a state of ignorance or incompetence that they allow such gross mismanagement and conduct to take place. It is of course recognized that not all business enterprises are poorly managed.

6. A few spoil it for the rest

Of all of the business enterprises in operation in the United States of America the above list represents a small number. But the above small group controlled, influenced and made a huge mark on the economy. Most business enterprises are probably making a good faith effort to serve their customers, employees, and stockholders. The result of the outrageous behavior uncovered in the large scandals and the resulting long-term negative ramification on Americans' pensions and the market in general triggered new regulations. New government regulation and oversight is a common response mechanism to an injustice followed by mass public outcry. Compliance with government regulation can be time consuming, onerous, and costly.

The Sarbanes-Oxley Act of 2002 was signed into law by President George W. Bush on July 30, 2002.[15] "There are two sections of the Act that require CEO/CFO certification of periodic reports filed with the SEC. Pursuant to Section 302 of the Act, the SEC has recently promulgated rules under which CEOs and CFOs must certify annual and quarterly reports filed with the SEC. Section 906 of the Act is self-executing and provides that a company's CEO and CFO must certify that each periodic report containing financial statements filed with the SEC "fully complies" with the reporting requirements of the Securities Exchange Act of 1934 and that the information contained in the periodic report "fairly presents, in all material respects, the financial condition and results of the operations" of the company. Any CEO or CFO who files a certification knowing that the report did not comply or was false is subject to criminal fines and imprisonment." [16]

7. Conclusion

Given that employees are now aware of the potential danger of relying on the employer in their retirement years, or indeed relying on having their respective job until retirement, the burden has shifted from employer to employee. Some may argue that the market is at work

[15] U.S.C.A. § 7263.
[16] http://ceb.com/newsletterv4/business_law1.htm, last verified March 24, 2006.

whereas we live and work in a capitalist society and it is the responsibility of the individual to shoulder the responsibility for the retirement years.

Workers certainly should be saving and managing their own alternative retirement accounts in addition to employer pension and the government social security. Numerous investment vehicles such as traditional IRA accounts, ROTH IRA accounts, private banking accounts, bonds, real estate, or commodities are readily available.

The problem with the recommendation above is that most employees have no idea about investments or retirement planning; do not even know who to ask or what questions to ask. Other employees are so busy that they do not make time to monitor their pension fund or to learn how to read a financial statement. Further, after recent headline stories about business corruption, can the financial statements be trusted for accuracy and completeness by those who can understand them?

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