The End of Retirement

The Motley Fool

By Robert Brokamp

Tired of reading about America's retirement woes? Then I have an alternative for you: Watch a TV show about them. Heck, you don't even have to move to your TV - you can watch it on your computer, from the comfort of your own desk chair. The particular program I'm talking about is an episode of the PBS series *Frontline* titled "Can You Afford to Retire?"

Of course, since you've clicked on this article, you can't be *too* tired of reading about all of the impending retirement woes out there, so let me sum up the program's main points and then explain how *you* can be an extraordinary American by actually being able to retire.

Goodbye, pensions ... unless you're the CEO

We all know that thousands of pensions are underfunded. We've heard the tales of people who dedicated their lives to a company only to see it slip into bankruptcy and take all of its retiree benefits with it. The *Frontline* program rightly started off by discussing the demise of the traditional pension - it focused on current and former employees of **UAL** 's United Airlines, which filed for Chapter 11 bankruptcy protection in 2002 and dumped its pension plans on the Pension Benefit Guaranty Corp. When the government-sponsored PBGC takes over your plan, you'll still receive pension benefits, but possibly only a fraction of what you would have received if your company had stayed in business. (The PBGC itself, by the way, is $23 billion underfunded.)

But the real shocker in the *Frontline* program was the revelation of how such ba nkruptcies are becoming an acceptable way for companies to get out of their pension obligations. Check out what United Airlines' lead bankruptcy lawyer, James H.A. Sprayregen, told *Frontline*: "I would say that Chapter 11 has become somewhat of a more accepted strategic tool than just companies filing who are about to go out of business or something like that. As a result, there's more use of Chapter 11 now than probably 20 years ago."

So should you be worried if your pension is underfunded? Well, according to a recent report from Standard & Poor's, corporate America doesn't seem to be taking pension funding too seriously. From the 2005 "Pensions & Other Post-Employment Benefits Report," I found the following statement: "While corporate operating earnings post 16 consecutive quarters of double-digit growth, corporate pension plans remain in the red with minimal contributions continuing to be made. ... S&P 500 defined-benefit plans as a group were $140.4 billion underfunded for 2005."

According to the report, here are some of the companies with the biggest deficits:

Goodyear (NYSE: GT) **Alcoa** (NYSE: AA) **DuPont** (NYSE: DD) **Motorola** (NYSE: MOT) **Electronic Data Systems** (NYSE: EDS)

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It should be noted that bankruptcy might be the only way for some companies to survive, and sometimes employees have to give up something just to keep their jobs. United was certainly in dire straits. But I suspect that it's harder for the folks in the rank-and-file to accept their reduced pension benefits when, according to *Frontline*, executives were given $400 million in stock grants *and* CEO Glenn Tilton's $4.5 million retirement package was put in a special trust so that he'll still get his full benefit. Very nice.

Hello, 401(k)s ... unless you don't participate

Next, *Frontline* discussed the shift from defined-benefit plans to defined-contribution plans - i.e., the shift from companies being responsible for funding retirement to the employees having to do it themselves. For instance, **Hewlett-Packard** and **Sears Holdings** (Nasdaq: SHLD) cut back their defined-benefit plans at the beginning of 2006, opting to instead focus their efforts on 401(k) plans.

Unfortunately, employees don't seem to be doing a good job of taking the reins. After all, they have to answer several important questions:

"Should I participate?" The answer, of course, is yes! But since 30% of workers choose not to, some folks aren't making the right choice. And we're not even talking about the 50% of workers who don't have access to an employer-sponsored plan. *"How much should I save?"* The best answer is "as much as you're allowed," but, says Alicia Munnell of the Boston College Center for Retirement Research, fewer than 10% of participants contribute the maximum. *"How should I invest it?"* The move to defined-contribution plans requires that every employee becomes his or her own money manager. We at The Motley Fool believe you can do it, but clearly, as we'll see later, many people aren't up to the task. *"How should I take the money out?" Frontline* profiled a fellow who cashed out his entire 401(k) when he retired, resulting in a huge tax bill. Ouch. The better move: Transfer the money to an IRA, and take money out only when you need it, leaving the rest to grow tax-deferred.

One of the most interesting tidbits from the *Frontline* episode came from benefits consultant Brooks Hamilton, who oversees 15 large 401(k) plans. At one point, he calculated the investment return for each participant in each of the plans. Here's what he found:

"Say the bottom 20% had an investment return for the year of 4%. The top 20% would be anywhere between five and seven times that number. ... In every case, the 20% at the top not only had the highest investment income, they also had the highest average annual pay. Whereas the bottom 20% not only had the lowest investment income, they had the lowest average annual pay."

Frontline characterized the situation this way: "The richest people are getting richer, and the middle-class workers are falling further behind." This is certainly true, but not in the same way as Glenn Tilton getting to keep his pension while everyone else's is reduced; the 401(k) system isn't rigged. We

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do have to recognize, however, that the average American isn't prepared to be an investment expert. Most schools don't teach personal finance, and neither do most parents. And clearly, most Americans aren't doing enough to teach themselves.

Now, we at The Motley Fool - being the do-it-yourself, control-your-own-destiny types - are big fans of self-directed retirement accounts. And believe me, traditional pensions aren't the answer. They benefit people who stay with the same employer for decades, not the typical job-hopping American. My wife and I worked a combined 10 years at the same elementary school, and from those jobs we'll receive a combined $108 a month in retirement - *not* adjusted for inflation. I would have gladly taken the 6% of my salary that the school contributed to the pension fund in the form of matched contributions to our 403(b) plans.

But the reality is that as retirement becomes the sole responsibility of the individual, many people - because of bad decisions, bad health, bad education, or bad luck - will have to work forever.

It's all up to you

Frontline interviewed Notre Dame economics professor Teresa Ghilarducci, who said, "What is the meaning of retirement if the only way you can live is to work? The answer is, there is no meaning to retirement anymore. We are now shifting from lifetime pensions to lifetime work. It's the end of retirement."

For millions of Americans, Ghilarducci is absolutely right. But it doesn't have to be that way for *you*. You don't have to be among the people who don't save enough, who don't invest wisely, and who don't make smart decisions about 401(k) withdrawals. If you need to learn the basics, read about the easiest retirement plan ever. For more detailed information, give our *Rule Your Retirement* service a 30-day free trial. You'll get access to all of our past issues and special reports, as well as our online financial-planning tool and professionally staffed discussion boards.

But whatever you do, just promise me you'll do *something.* The choice between working and retiring is entirely up to you.

This article was originally published June 22, 2006. It has been updated.

Robert Brokamp is the advisor of Motley Fool Rule Your Retirement. *Robert will rule his retirement by not paying $800 a year for basic cable. And with shows like* Frontline, *who needs cable? Robert doesn't own shares of any companies mentioned in this article. The Motley Fool has a disclosure policy.*