

The 2010 Union Pension Bailout Bills

By F. Vincent Vernuccio

Summary: Get ready to give some of your hard-earned cash – again – to the cronies of Congress who are pushing for yet another bailout. Two bills in Congress propose using taxpayer dollars to bailout private union pension funds. If either one becomes law, Congress for the first time will allow the Pension Benefit Guaranty Corporation (PBGC) to use public funds – the money you earn and pay to the government – to shore up horribly mismanaged union pension plans. Estimates for the current shortfall go as high as \$165 billion. Aside from the taxpayers’ gift to the unions, the bills could also bailout the deficit-ridden PBGC.



Rep. Earl Pomeroy (D-ND)

This March Sen. Robert Casey (D-PA) introduced S. 3157, the Create Jobs and Save Benefits Act of 2010. It complements H.R.3936, the Preserve Benefits and Jobs Act, introduced last year by Reps. Earl Pomeroy (D-ND) and Pat Tibiri (R-OH). By the time you read this you’ll know whether Pomeroy will still be a member of Congress in January. (North Dakota is a right-to-work state and only six percent of its workforce is unionized. Yet twelve of Pomeroy’s top twenty donors are unions.) But the bill he and others cosponsored could live on, paying back the unions for their political support.

Over the August recess the bailout bills received a big boost when Senate Majority Whip Dick Durbin (D-Ill.) signed on as a

cosponsor. Connie Hair of *Human Events* reports, “With nine Republican co-sponsors of the House bill, Big Labor is pushing for passage during a lame duck session after the November elections.”

The public is increasingly aware that state government and union pensions are essentially a giant pyramid or Ponzi scheme: The system, which promises benefits to retirees, cannot be sustained unless new members are enrolled in order to pay for the pensions of retiring workers. Think of the promises Bernie Madoff made to his clients—or the promises Social Security makes to retirees. Government and union pensions are

on a collision course with disaster that is bound to accelerate over the next decade. However, unlike government pensions and Social Security, union pensions aren’t open

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to political fixes or backstopped by U.S. taxpayer dollars—for now.

However, all this may change if Big Labor persuades some Democrats and Republicans in Congress to see things their way.

Pensions and the Concept of Risk

Most people know that there are two main types of pension system in use today—defined contribution (DC) and defined benefit (DB) pensions. DC plans are what most nonunion workers have today. These are the 401(k), IRA, and similar vehicles that allow employees and employers to contribute to retirement accounts invested for the employees' retirement. Employee stock ownership or profit sharing plans have similar characteristics. The DC account is in the employee's name and can be transferred from job to job. Employees can contribute to their DC plans by making scheduled contributions from their paychecks as well as by receiving annual contributions from their employer. Employees are "vested" over time in the employer's contribution to their DC account, and they are entitled to the entire amount when they retire, usually after age 59 ½.

DC plans are beneficial to employees be-

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cause their features provide them with personal control and the accounts are portable. The money in the plan is legally the employee's, and the employee controls the pace and placement of the investments. When an employee makes regular contributions that are diversified into sound investments over a lifetime of work the likelihood is that the pension yield will be considerably higher than what is promised by defined benefit (DB) plans.

Employers are also fans of DC plans because they are not held liable for the future success or failure of the employee's investment decisions. Unions, on the other hand, oppose DC plans, claiming that because the value of the investments can fluctuate they do not provide workers with a secure retirement benefit that in theory will add up to an annual pension for the rest of the retiree's life.

Single employer DB plans—the kind controlled by one company—are quickly being phased out in the non-union private sector. Only one in four employees and retirees in the private sector is now covered by a DB plan. In the 1980s there were over 100,000 DB plans insured by the PBCG. That's down to about 30,000 plans now. But DB plans prevail in the public sector even though their financial health is in poor and even desperate condition. Currently state and municipal DB plans are underfunded by an estimated three trillion dollars. California's pensions are underfunded by \$535 billion, which is greater than the gross domestic product of Saudi Arabia, Switzerland, or Poland.

How Unions Control Multiemployer Defined Benefit Pensions

The Casey and Pomeroy bills up for consideration focus on what are called multi-employer plans. These are DB plans created by a collective bargaining contract between a union and multiple employers.

There are about 1,500 multiemployer plans, which cover more than 10.4 million workers and retirees. These plans were developed for an understandable reason. Because union members often work for many different employers within a unionized industry the plan lets them switch jobs without losing their pension benefits. However, multiemployer DB pension plans are not nearly as portable as DC plans. That's because while a carpenter, say, can switch jobs within the construction industry and still retain his pension, he must always work for companies organized by the Carpenters Union in order to receive the maximum benefit of the pension plan upon his retirement. (Unfortunately, for the carpenter, 75 percent of multiemployer pension plans in the construction industry are facing funding shortfalls this year.)

In single employer defined benefit (DB) plans the employer is liable for making all the payments as well as the investment decisions that eventually provide retirees with their pension benefits. No wonder these plans are rapidly losing popularity. By contrast, in multiemployer DB plans, all the participating companies make pension contributions to union members who have occasion to work for them. Here's the rub. In a multiemployer defined benefit pension plan every company is liable for every worker in the plan, but if one employer goes bankrupt all the others must still pay benefits to the bankrupt company's employees.

In addition, control over investment of the pension funds is effectively held by the union! Multiemployer plans are controlled by a board of trustees. Multiemployer plans governed by the Labor Management Relations Act of 1947 and are "jointly administered labor-management pension plans." All the employers together appoint only half the board. The union appoints the other half, and in most cases the union trustees vote as a block. If the union can pick off a single employer's trustee, it wins.

It's increasingly recognized that DB pension plans don't benefit a modern workforce. They require an employee to work for the same company or union for decades to receive the pension's maximum benefit. If an employer makes poor investment decisions or puts off making pensions payments during a worker's tenure workers risk losing their pensions.

If an employer becomes insolvent and cannot fund its retirees' pensions the PBGC provides some degree of protection. PBGC insures single employer DB plans for up to \$54,000 a year per worker who retires at the age of 65. However, PBGC insurance is much less for a worker who is part of a multiemployer plan. If that plan becomes insolvent, the PBGC will pay a retiree no more than \$12,780 per year. The PBGC argues that because risk is pooled among multiple employers it is less likely that multiemployer plans will become insolvent.

Union Pensions Underfunded by \$165 billion

Moody's Investor Services estimates that multiemployer plans were underfunded by \$165 billion in 2009. Because of the economic downturn, Congress enacted a law in 2008—the Worker, Retiree, and Employee Recovery Act—that let pension funds avoid reporting their actual funding levels by freezing their funding status at 2007 levels. But this year the independent Financial Accounting Standards Board (FASB) made life harder for multiemployer pension managers when it announced that companies must report their pension liabilities on their balance sheets. The change means that because the disclosure of information about pension underfunding cannot be put off it will have immediate consequences. The FASB rule increases the pressure on pension sponsors to keep their plans healthy by pushing them to comply with the 2006 Pension Protection Act (PPA).

The PPA requires that all pension funds tell their participants, beneficiaries and the Department of Labor (DOL) whenever their pensions become “endangered” or “critical.” An endangered pension plan is one that is below 80 percent of being fully funded. A critical pension plan is below 65 percent of being fully-funded. The PPA also mandates remedial measures to bring pensions back to health.

When Sen. Casey introduced his bill earlier this spring, representatives from the International Brotherhood of Teamsters, YRC Transportation and ABF Freight Systems flanked him. The Teamsters are likely the first beneficiaries of his proposed bailout.

The Teamsters' Central States Pension Plan for the South East and South West Areas was funded at an anemic 57% in 2008. This reflects an upswing from 2007 when the plan only had 47 cents on every dollar owed to its members. The reason? United Parcel Service (UPS) realized that it had a large ticking time on its hands. In 2007 UPS paid out \$6.1 billion in order to withdraw from the multiemployer plan it administered with the Teamsters and other companies. UPS still must pay pensions to 44,000 Teamsters working for them but at least it avoids the liability of having to pay for employees who never worked for it.

DOL lists 12 Teamsters' pension plans as in critical status and another eight in endangered status. The Teamsters have been lobbying for the bailout since Rep. Pomeroy introduced his bill last year. They consistently blame everyone but themselves for the problem.

Last October Teamsters president James P. Hoffa Jr. even sent *The Washington Times* a letter to the editor defending the bailout bill. Hoffa blamed union underfunding on the stock market crash even though the Teamsters pension fund was funded at 47%

in 2007 well before the financial meltdown. He even claimed unions are not responsible for their pensions, despite the fact that in almost all cases they control half the board of trustee. Hoffa wrote, “The pension crisis isn't just about unions or certain employers. It's about living up to the responsibility to provide the retirement security promised to employees.” What Hoffa conveniently forgets is that the U.S. taxpayer did not promise Teamster members a pension; their unions did.

This year Hudson Institute economist Diana Furchgott-Roth published a report *Union Pensions at Risk*. She noted that only 18 percent of multiemployer plans were fully funded in 2007, the last year for which full data is available. PBGC data show that multiemployer plans, in aggregate, have not been fully funded since 2000 when the assets in all plans were sufficient to cover 105 percent of pension benefits. By 2006, that number plummeted to 66 percent. The drop in funding is even more shocking because it occurred before the current recession, which undoubtedly has worsened the stability of these plans.

DOL has reported that 640 union pension plans were funded below 80 percent (“endangered”) or had applied for relief from reporting requirement in 2009, up from 230 the previous year. (Citing the recession as an excuse, Congress cut the unions some slack and passed a law in 2008 that let unions apply for relief from reporting [i.e. not report] the extent of their underfunding.)

In 2009 almost half of the top union pensions were underfunded. In *The Washington Examiner* reporter Kevin Mooney noted the Service Employees International Union (SEIU), the United Food and Commercial Workers (UFCW), the International Brotherhood of Electrical Workers, the Laborers International Union

of Northern America, the International Association of Machinists, the United Brotherhood of Carpenters, the International Union of Operating Engineers, and the National Plumbers Union all had underfunded pension plans (July 2009).

Furchgott-Roth's report shows that multiemployer plans fare much worse than other non-union pensions. She writes that 89 percent of non-union plans were above the endangered level while only 64 percent of union funds met that threshold. Only 1.5 percent of non-union pensions were in critical status compared to 12 percent of union plans.

By contrast, union officer and staff pensions are in great shape. According to Furchgott-Roth, the average funding for the 28 officer plans in the largest 46 union pensions was 96 percent. The rank-and-file plans were only funded at 80 percent. Well compensated union officials clearly know how to manage their own retirements.

How a Taxpayer Union Pension Bailout Would Work

On May 27, 2010 President Obama's Assistant Secretary of Labor for the Employee Benefits Security Administration testified before the Senate Committee on Health, Education, Labor and Pensions. Assistant secretary Phyllis Borzi admitted that Senator Casey's legislation "ultimately makes the taxpayers liable for paying the benefits of [insolvent union pension] plan[s]." She admitted that his bill would increase the Pension Benefit Guaranty Corporation's funding liability, saying "Currently, no other benefit obligations assumed by PBGC are subject to the full faith and credit of the U.S. government."

That will change if Sen. Casey's bill is adopted during the lame duck session. As previously noted, multiemployer plans are

made up of multiple companies and the union that represents their workers. The language in both the House and Senate union pension bailout bills creates what's called a "Fifth Fund" in PBGC. It would allow PBGC to split an underfunded union pension plan into two parts.

One part would consist of workers whose employers still contribute to the plan. The second "partitioned plan" would consist of "orphans" of the original plan—the employees of companies that no longer contribute to the plan.

Both bills limit partitions to pension plans in critical or endangered status that PBGC concludes are apt to become insolvent. However, even though PBGC picks up the tab, it is not given the authority to administer a partitioned plan. Both the Casey and Pomeroy bills give authority back to the original trustees who ran the plan into the ground. They continue to administer the new plan for the orphaned employees—only now with taxpayer dollars. Casey's office admits, "PBGC [would] not provide notices, calculate benefits or in any other form administer the plan."

In addition, under the terms of the bailout bills orphaned employees will receive their promised pension without the limits of PBGC's cap (which the bills increased from \$12,870 to \$21,000).

PBGC Joins Fannie Mae and Freddie Mac

PBGC likes to boast that it "receives no funds from general tax revenues." It is, like Fannie Mae and Freddie Mac, a quasigovernmental agency that describes itself as a federal corporation. The sponsors of DB plans pay insurance premiums to finance PBGC operations. But because the premium rates are set by politicians elected to Con-

gress, they are generally too low to cover the potential liabilities they insure against.

Besides giving PBGC tax dollars to sustain underfunded union pensions the legislation also lets PBGC use tax dollars to support other financial transactions it makes. The bills state that PBGC may "invest amounts of the [fifth] fund in such obligations as the corporation considers appropriate"—a camel's nose under the tent for bailing out all of PBGC.

According to PBGC Pension Insurance Data Book 2009 the Pension Benefit Guaranty Corporation expects to spend on multiemployer benefit programs five times as much in the next 10 years as it has over the last 30 years. PBGC already has a severe funding shortfall. In 2009, it had only \$72 billion in assets to cover \$90 billion in liabilities. The shortfall is expected to balloon to \$34 billion in the next decade.

Royal S. Dellinger, PBGC's Principal Deputy Executive Director from 1984 to 1989, confirms the potential for an agency bailout. He notes that "as the agency heads toward inevitable failure this provision seems to allow it to use funds held in the single-employer trusts and the new "fifth fund" to mask the shortage in multi-employers plans." It could allow PBGC to "defer ugly decisions and could very well violate the trusts of extant terminated single-employer plans." Dellinger suspects PBGC will "use the [fifth] fund to mask deficiencies wherever they can" including using it to shore up their single employer fund.

Looking for Answers

There are no easy answers to the multiemployer pension crisis. Aggressive unions and compliant companies have run up a huge tab and someone must pay the bill when it comes due. The companies and unions have

promised retirement benefits in collective bargaining agreements but failed to fund them adequately. The unions were happy to tell their members they scored increased concessions in contract negotiations and the employers were happy to put off pension costs to another day. Neither side saw any advantage of setting aside enough money to ensure adequate funding.

The multiemployer model for providing pension benefits must be reexamined. The funding and disclosure standards of the Pension Protection Act and FASB are the first steps toward reform but more needs to be done.

* Unions that recruit members with the promise of large and secure pensions should be required to tell prospective union members if their retirement plans are currently in endangered or critical status.

* Any mention of government insurance or guarantees should be accompanied by the caveat that multiemployer plans are only insured up to \$12,870.

* No worker should be forced into an underfunded pension fund in “critical” status. New workers did not make pension promises to current employees and retirees and they should not be forced to pay into a pension system that is broken.

* Union members need the pension control and portability enjoyed by three out of four workers who participate in pension plans or receive pension benefits in America. New workers should be able to join 401k, IRA and other DC plans. Older union members should have the option to opt-out of failing pension plans and transfer pension assets to a DC plan.

* Federal law should be revised so that a multiemployer plan may be terminated if all contributing employers or a majority of

beneficiaries agree whenever the ratio of employees to retirees reaches 1 to 1. In 2007 the Teamsters Central States Plan covered the pensions of 451,000 workers even though there were only 155,000 workers currently employed. Despite the enormous cost UPS withdrew from the pension system because it understood that whenever one worker supports three retirees the system is doomed to failure. Rather than face decades of future liabilities, employers should be have the option to buy out of failing union pensions.

Multiemployer plans, in their current form, have underperformed most other types of pension plans. Yet unions insist that their benefits provide the most secure retirement. They don’t. Declining union membership, inadequate financial contributions, and poor investment decisions are the cause of pension failures. A pension bailout will solve none of these issues.

Even Obama administration officials don’t think the legislation will work. During her testimony, Borzi commented, “These larger problems [the declining number of active participants and a significant drop in the number of employers who contribute to the plan] facing plans in troubled industries won’t be solved by the kind of temporary short-term funding relief Congress is currently working on.”

The *Wall Street Journal* agreed but noted that unions still have major incentives to back the bailout bills. An August 15 editorial said: “If Democrats could shift orphan company pensions to the taxpayer, the liabilities for the remaining companies would fall dramatically, and the multi-employer scheme could continue. Unions and employers could keep promising current workers fabulous pay and benefits, without which they have little chance of stemming their continuing decline in membership.”

Sen. Casey predicts his bill will cost only

\$10 billion, but the *Wall Street Journal* estimates that the cost could be as high as \$165 billion overall—and that doesn’t include the cost to taxpayers of bailing out PBGC. Casey’s bill would set a dangerous precedent: PBGC has never before used taxpayer dollars to fund the pensions it insures. Moreover, using public dollars to bailout private union pension plans is unfair to taxpayers, who have seen their own 401(k), IRA, and retirement savings shrink to pay for the retirement of others. The proposed bailout is another example of cronyism in Congress. Big Labor contributed to members of Congress, and now expect payback for its support.

Big Labor spent \$450 million during the 2008 presidential election. This year the AFL-CIO and Service Employees International Union (SEIU) pledged to spend another \$100 million. But that’s chump change compared to the benefits they hope to receive.

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Many thanks,

**Terrence Scanlon
President**

LaborNotes

The Great Unemployment continues: In September, the U.S. economy lost jobs for the fourth consecutive month. According to the **Labor Department**, 95,000 jobs were lost, and the unemployment rate held steady at a dismal 9.6 percent. In addition, as reported by *Reuters*, “The government revised data for July and August to show 15,000 more jobs lost than previously reported.” Those are the official numbers; the real picture may be even worse. As **Gallup** reported on October 7: “Unemployment, as measured by Gallup without seasonal adjustment, increased to 10.1% in September — up sharply from 9.3% in August and 8.9% in July.” Whoever is doing the measuring, it’s clear that millions of American families continue to struggle in a depressed labor market, as the “Summer of Recovery” gives way to the Autumn of Despair.

The **Kellogg School of Management at Northwestern University** and the **University of Rochester** have produced a new analysis of the public pension crisis. The message: It’s bad. Specifically, large cities and their counties face a gargantuan public pension funding gap (more like a gulf) of possibly \$574 billion. As if that wasn’t bad enough, that hole is in addition, as Nicole Bullock of the *Financial Times* puts it, “to \$3,000 billion in unfunded liabilities already estimated for state-run pensions...” Lavish pensions, negotiated by public-sector unions, combined with plummeting state and municipal tax revenues due to the economic downturn, have conspired to paint this dire fiscal picture. **Joshua Rauh** of the Kellogg School drolly sums up the situation: “What is yet to be seen is how this burden will be distributed between state and local governments and whether the federal government will be called upon for bail-outs.” Whether? Gee, I wonder....

A **General Motors** stamping factory in Indianapolis, Indiana - and its jobs – are as good as gone since the **United Auto Workers Local 23** voted 456-96 against accepting the pay cuts necessary to save the plant. As a result, according to the *Detroit News*, “Addison, Ill.-based JD Norman Industries said Tuesday it is dropping its effort to buy the factory, which means the 80-year-old plant will close next year.” Unions exist allegedly to look out for the interests of its members. That there actually be a factory open to employ people would seem to be one of those interests, but hey, what do we know?

Another gem for the “you couldn’t make this up” file: According to the *New York Post*, a 2,300-member union of city accountants “had no idea how much money was in its bank accounts.” *The Post* obtained a June 22, 2009 report from the **American Federation of State, County and Municipal Employees**, which admitted, “The local is not up to date on its financial reporting, bank reconciliations, and entering its checks into its accounting system.” Is it just me, or is *The Onion* becoming less necessary by the hour?

Yet another story proving the increasing irrelevance of *The Onion*: The internal election of the **American Postal Workers Union** has been thrown into chaos because thousands of members did not receive their ballots – yup, they seem to have been lost in the mail. According to FOXNews.com: “The union’s election committee was supposed to be counting those ballots this week in downtown Washington, D.C., following a traditional mail-in election. But the union announced that only about 39,000 ballots were turned in — and that ‘a large number of union members had not received their ballots.’” We have now moved beyond “you couldn’t make this up” and officially crossed into “too stupid to not be true.” Somewhere, Ben Franklin weeps.