

VEBAs moving into fast lane

Union contracts with automakers may put other industries on road to creating trusts

By **Mark Bruno**

Posted: October 15, 2007, 6:01 AM EST

The new multibillion-dollar pre-funded retiree medical trusts being spawned by General Motors Corp. and Chrysler LLC could prompt auto suppliers and steel companies to follow their lead.

"VEBAs (voluntary employees' beneficiary associations) haven't been talked about or thought about that much before, but now it's definitely on the table for a lot of reasons," said Jack Marco, chairman of Marco Consulting Group, a Chicago investment consultant to union pension funds. "If it makes sense for companies like GM and Chrysler, then other companies with strong unions will also give it a good look."

That could lead to rapid growth in VEBA assets. At the end of last year, 100 of the largest corporations in the U.S. had funded a total of \$83.7 billion toward retiree medical obligations, according to a survey by actuarial and consulting firm Milliman Inc., Seattle.

Just with the addition of GM and Chrysler, that dollar total would increase more than 50%. After GM agreed late last month to give the United Auto Workers about \$35 billion to fund a VEBA, Chrysler and the union reached an accord on Oct. 10 that reportedly includes \$11 billion from the company to fund another UAW-managed VEBA.

Gradual funding GM already has agreed to make a \$24.1 billion contribution to the UAW-sponsored VEBA and is expected to gradually fund the remainder over time. Details of the VEBA Chrysler will form for the UAW, which was part of a tentative labor agreement with the union last week, were not made public at press time.

Plus, Ford Motor Co. could pump up to an estimated \$18 billion into a VEBA to help fund its retiree medical costs. David Cole, chairman of the Center for Automotive Research in Ann Arbor, Mich., expects Ford and the UAW to carve out a pact with a similar "spirit" to those of GM and Chrysler.

Marcey Evans, Ford spokes-woman, declined to comment.

"Once someone sets the precedent, momentum can take over," said Mr. Cole. "And the Big Three have the potential to redefine how companies operate, even in other industries."

Next up in the VEBA queue likely will be either steel companies or auto suppliers.

The steel companies in the Rust Belt, for one, often tend to mirror the auto companies when it comes to labor issues, said Dale Yamamoto, chief health-care actuary for Hewitt Associates LLC, Lincolnshire, Ill.

Both industries have strong unions, offer generous benefits and have heavy pension and health-care obligations to their retirees — obligations that could inhibit these companies financially, he added.

At least one steel company formed a VEBA since the GM-UAW accord was reached. AK Steel Corp., West Chester, Ohio, struck a deal to create a \$663 million VEBA for 4,600 retirees from its Middletown, Ohio, production facility.

Other steel companies might soon follow, said Thomas Conway, international vice president at the United Steelworkers, Pittsburgh, a union organization that is no stranger to VEBAs.

Several years ago, a number of steel companies formed smaller VEBAs as part of broad restructurings related to bankruptcies throughout the industry, Mr. Conway said. The use of VEBAs now would be different, he explained, but still should be attractive to steel companies.

"It will have appeal to a lot of companies," he added. "It's not a complete solution to the health-care issue, but it is better than the possibility of employees and retirees winding up with nothing."

Deal with Goodyear

Last year, the USW negotiated with the Goodyear Tire & Rubber Co., Akron, Ohio, to create a \$1.7 billion, union-run VEBA to cover the current and future health-care liabilities of the company's unionized work force. Goodyear was looking to cut costs, and the USW was looking to secure benefits for its work force, Mr. Conway said.

Separately, a number of "tier one" auto parts suppliers also are interested in creating VEBAs for the same reason, said Robert Stevenson, attorney at Stevenson Keppelman Associates, an employee benefits law firm in Ann Arbor that has helped companies throughout the auto industry form VEBAs.

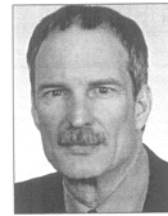
One supplier in particular, ArvinMeritor Inc., is said to be considering such a move, but Lin Cummins, spokeswoman for the Troy, Mich.-based company, did not return a call seeking comment.

Meanwhile, one auto supply company already agreed with the UAW earlier this year to create a VEBA to offload its employees' and retirees' health-care and long-term disability obligations. Dana Corp., a Toledo, Ohio-based supplier agreed in July to fund a VEBA for the UAW using \$704 million in cash and \$80 million in company stock.

Mr. Stevenson said he has been contacted by several other such supply companies since the GM-UAW agreement was announced last month. "The companies would be off the hook from large obligations, and the unions would get something tangible: something worth much more than just a naked promise to cover those obligations."

The largest VEBAs, however, are run by the auto manufacturers and two telecommunications companies: AT&T Corp. and Verizon Communications Inc., according to Milliman, based on company reports.

Well more than half of \$83.7 billion in total VEBA assets were in four company's funds at the end of last year: AT&T had the largest, with \$17.1 billion, followed by GM which had \$16.9 billion in a preexisting VEBA run by the company; Ford, \$4.9 billion in a company-run VEBA; and Verizon, \$4.3 billion.



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Executives in the investment management community, meanwhile, are gearing up to try to win business from the VEBAs.

Mr. Marco, for one, said that while he does not now provide investment consulting services to any VEBAs, he has begun to make it a priority: "With such large dollar amounts materializing, it's at the top of my list."

For money managers and consultants, working with VEBAs would not be much of a stretch from working with their pension fund clients. That's because pre-funded retiree medical trusts tend to be invested much like defined benefit plans. They differ, however, in that VEBAs need to consider shortterm liabilities more, and must also account for unpredictable medical inflation.

In some cases, a company's VEBA can be invested more aggressively than its pension plans.

AT&T, for example, had 73% of its VEBA assets, or roughly \$12.5 billion, invested in equities at the end of last year, according to the San Antonio-based company's 2006 annual report. Meanwhile, only 57%, or \$39.5 billion, of the company's \$69.3 billion in pension assets were in equities.

McCall Butler, spokesman for AT&T, could not say by press time whether the VEBA assets are managed internally, or by outside money management firms.