Obscure Health-Benefit Scheme Is Central Issue in Auto Talks

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Saturday, September 22, 2007

General Motors and the United Auto Workers have put back on the table a giant health-care trust fund that has been at the heart of their contract talks, a source close to the discussions said Friday night.

A voluntary employees' beneficiary association, or VEBA, has become the sticking point of the union's negotiations with the three major U.S. automakers, as the companies attempt to use it to shift the enormous task of administering retirees' health-care costs to the union.

The plan for creating a union-controlled tax-exempt trust fund to pay for retiree health benefits had been put on hold Tuesday. The parties may have agreed to a tentative framework for VEBA on Friday, a full week after the contract deadline, said the source, who spoke on condition of anonymity. The source was not authorized to speak publicly on the matter.

The most controversial details of the VEBA, such as how much money GM would put into the union-controlled trust, remain unclear. As the VEBA discussions appear to be progressing, analysts and union leaders around the country say there is still widespread confusion among workers about how the VEBA would work.

"I don't think a lot of them understand what the funding is and all that," said Chris Sherwood, president of Local 652 in Lansing, Mich. "They're calling and saying, 'What the hell is a VEBA anyway?' "

While VEBAs have been in the tax code since the 1920s, these tax-exempt trust vehicles for providing employee benefits are relatively obscure, even to the accounting and actuarial professions. The number of VEBAs nationwide has dropped slightly over the past few years, to 12,206 in 2006, according to the Internal Revenue Service. Analysts say, though, that changes to accounting standards and skyrocketing health-care costs over the past decade will soon make VEBAs much more common.

"These companies have been making promises they can't keep for a long time," said Lee Sheppard, a tax attorney and contributing editor for Tax Notes. "Everybody's creating

VEBAs now for the same reason: They realize these expenses are going to eat them alive."

Because of a change ordered by the Financial Accounting Standards Board, all companies will soon have to include their unfunded post-employment benefit obligations on their balance sheets. This is intended to more accurately reflect a company's liabilities, and it can greatly reduce the value of a company because health-care costs are rising so quickly. So, just as companies are switching from traditional defined-benefit pension plans to defined contribution plans such as 401(k)s, they are also changing the promises they make about future benefits. Putting money into VEBAs takes the liability off their books, making the companies more attractive to lenders and stock analysts.

Typically, a company will put about 5 percent of its total liability into a VEBA up front and then make regular deposits, said Dale Yamamoto, a Hewitt Associates actuary. The company, sometimes with labor representatives, appoints trustees to manage the money in the VEBA.

GM wants to deviate from the traditional setup, people close to the talks said. The company reportedly wants to put one large lump sum into a VEBA, which the union alone would control, and does not want to regularly replenish the fund. The people spoke on the condition of anonymity because the negotiations are supposed to be private.

How much GM should put into the trust is contentious. According to news reports, GM appears to be offering to pay 50 to 70 percent of its liability, estimated to be around $55 billion.

The right level of funding is critical. A VEBA created by Caterpillar in 1998 went dry six years later, leaving retirees to pay for health-care benefits they had been promised.

"We heard at the end of our careers that we were not going to get what was promised all the years we were coming into work every day," said Larry Solomon, former president of UAW Local 751 in Decatur, Ill. "We felt betrayed."

The form of funding is also important. A VEBA funded with cash is less risky than one funded with stock in a shaky company.

Because VEBAs are so complicated, vigorously educating employees on how they work is key to their success, said Lance Wallach, a VEBA consultant. "A few years ago, a lot of the casinos in Atlantic City started calling me about setting up a VEBA for them," he said. "I told them it wouldn't work because a lot of the workforce were not English-speaking. Part of making this work should be communicating to workers."

Some of the more successful VEBAs, analysts say, are run by states and municipalities, which can raise taxes if their VEBAs run low on money. Government entities in California, Idaho, Indiana, Montana, Oregon and Washington have created VEBAs, and many more expect to do so in the next few years because the Governmental Accounting

Standards Board recently began requiring disclosure of post-employment benefit obligations.

"They now have to do a 30-year projection on what the health costs will be, causing their financial statements to not look nearly as good as they did in the past," said Mark R. Wilkerson, a senior consultant at HRA Consultants, which manages Washington state's VEBA.

The model for GM appears to be the VEBA that Goodyear Tire & Rubber and the United Steelworkers union created last year, said John Russo, a labor professor at Youngstown State University in Ohio. Goodyear paid 77 percent of its estimated $1.3 billion liability up front, Russo said.

Wayne Ranick, a United Steelworkers spokesman, said Goodyear initially offered to fund just 50 percent of the liability and only changed its mind after a three-month strike. "Goodyear had to go through major losses before agreeing to fund the trust at what we thought was an appropriate level," Ranick said.