United States Senate

Republican Policy Committee

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September 9, 2003

Updated Form Will Protect Union Members from Financial Abuse

Needed: Real Financial Transparency for Labor Unions

Executive Summary

- Union members are the victims of financial mismanagement, fraud, and embezzlement when those in control of a union's funds take advantage of their positions for personal gain. Over the past five years, *an average of 11 union officials per month have been convicted* for financial mismanagement, fraud, and embezzlement of union funds.

- The purpose of the Labor-Management Reporting and Disclosure Act of 1959 (LMRDA) is to protect union members from such abuses by requiring all labor unions to file annual financial statements with the Department of Labor (DOL).

- Unfortunately, the law's financial disclosure form has remained substantially unchanged for 44 years and now reflects an outdated financial environment. The result is that the reporting by many unions is insufficient to allow DOL to protect union members.

- DOL is proposing to correct this problem through the rulemaking process by updating the financial statement form required of the largest labor unions, known as the LM-2 form, so that it provides more detailed financial information.

- Democrats oppose the proposed rule to update the LM-2 form and have threatened to offer an amendment to the Senate's FY 2004 Labor, Health and Human Services, and Education appropriations bill to prevent the rule from going forward.

- This paper will demonstrate why Senate Republicans should support DOL's proposed rule change and defeat any Democrat efforts to stop it.

Introduction

In response to labor union financial mismanagement, fraud, and embezzlement, Congress passed the Labor-Management Reporting and Disclosure Act (LMRDA) 44 years ago. This law required unions to publicly disclose certain financial information.[1] The LMRDA is no longer as effective as it should be in preventing these abuses; and the Department of Labor (DOL) has identified some reasons for this. The primary reason is the annual financial disclosure statements required by the law have not been updated to reflect the modern financial circumstances and methodology of labor unions. Therefore, it is very easy for unions to hide evidence of financial mismanagement, fraud, and embezzlement. Additionally, DOL does not have the resources it needs to adequately enforce the law, nor does it have the authority to punish those who fail to file reporting forms on a timely basis.

DOL has proposed a rule to update the annual financial disclosure statement, known as the LM-2 form, and is seeking legislative action to address the resource and penalty issues. However, Democrats and organized labor leaders are opposing DOL's proposed rule and have threatened to block it through an amendment to the Senate's Labor, Health and Human Services and Education Appropriations bill for fiscal year 2004. Their claims that changes to the LM-2 form would be burdensome and costly are overstated, and the position that current-law protections are sufficient is disproved by the facts. The campaign against the proposed rule to update the LM-2 contradicts the very purpose of a labor union – to benefit its members.

Federal and State Law Benefits Unions . . .
So Unions Must Be Held Accountable to Their Members

Organized labor unions are given preferential status under federal and state law because of the public policy assumption that they exist for the sole purpose of helping their members: unions do not pay taxes and are exempt from anti-trust laws and federal whistle-blower laws. Additionally, unions are allowed to compel dues from non-union employees in the 29 states which have not passed right-to-work laws. Right-to-work laws bar the practice of making union membership or dues mandatory in unionized workplaces.

Unions are funded by dues from members (and in the 29 states mentioned above, by the dues of non-union-member employees). Average union members' dues are no small investment, and members expect their unions to be good stewards of those funds. Though DOL does not tally union assets, others have calculated, based on current reporting, that union receipts in 2000

[1]Congress passed the Labor-Management Reporting and Disclosure Act (LMRDA) in 1959. This bill passed the Senate by a vote of 95-2, and passed the House by a vote of 352-52.

totaled $15 billion.[2] The same report estimated that $6.75 billion of the 2000 receipts came out of union members' paychecks as dues. The other income would be from return on investments made with union dues. The average dues collected per employee in 2000 was $675.[3] This amount is equivalent to one-third of the Federal Insurance Contributions Act (FICA) tax withheld from workers whose annual earnings are $30,000.

Abuse of Union Funds Violates Union Members Trust

Although all unions benefit from their advantageous status under federal and state law, not all unions live up to the purpose of protecting union members. Over the last five fiscal years, an average of 11 union leaders a month have been convicted of financial fraud – a total of 639 convictions.[4] Union officials have stolen from their members' hard-earned paychecks,[5] misused union-member dues for personal gain,[6] and abused their power over workers' earnings and work schedule to silence union members who question a union's use of funds.[7] Convicted parties have been ordered to pay over $15 million in restitution to the union members they robbed – but even that sum does not cover the full extent of lost funds.[8]

When union leaders put their own interests first, they do more than steal from members' paychecks – they abuse both their members' and the public's trust. With the record recited above, union members cannot be sure they are being represented effectively. Evidence of such disregard for the interests of union members themselves was delivered at a Senate Committee on Health, Education, Labor, and Pensions (HELP) hearing reviewing the recently exposed scandal within the United Teachers of Dade, Florida (UTD). One witness testified that union officials raised their own pay and benefits while failing to obtain raises or improved benefit packages for

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[2]National Institute for Labor Relations Research, "Big Labor is Still Big Business," February 1, 2002.

[3]National Institute for Labor Relations Research.

[4]Larry Yud, Deputy Director of the Office of Labor-Management Standards, Employment Standards Administrator, U.S. Department of Labor, in testimony to Health, Education, Labor and Pensions Committee (H.E.L.P.) June 19, 2003.

[5]*Baltimore Sun*, "D.C. Teachers Group Seized Under Allegations of Misuse of Dues," March 1, 2003.

[6]*Associated Press*, "Secret Stock Program, Special Bonuses Enrich ULLICO Executives," June 22, 2003.

[7]International Association of Ironworkers - Local 387 Atlanta. Just this year, one union assessed $10,000 fines on two members who hired a lawyer to obtain the union's financial records. Organized Labor Accountability Project, *Union Corruption Update*, April 28, 2003.

[8]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67, No. 249, December 27, 2002.

teachers, and waived the right to counsel for every member of the union.[9] In another recent example, officials of the Washington Teachers Union have been charged with embezzling directly from teachers' paychecks.[10] The theft came to light when the perpetrators took $160 from a teacher's paycheck instead of the $16 to which they were entitled.[11]

Financial Disclosure Law Is Outdated and Ineffectual

Although the LMRDA seeks to ensure financial integrity and transparency within labor unions, union members are not receiving the protections the law was designed to provide. The Department of Labor has determined that it lacks the information and resources it needs to more effectively prevent and detect cases of financial mismanagement, fraud, and embezzlement. A major source of the problem is the outdated LM-2 form, which does not reflect the complex financial world in which today's unions operate. The proposed update of the LM-2 form would better protect union members from financial mismanagement, fraud, and embezzlement.

Current-Law Disclosure Requirements on Unions

The LMRDA applies to all unions representing any non-governmental employees, including those that are mostly government workers, but have a mere handful of non-government workers. These unions are required to submit an annual report to the Department of Labor, known as LM-2, LM-3 or LM-4, depending on the size of the union.[12] The LM-2 – the only form significantly affected by DOL's proposed rule – is required of the largest labor unions, those that collect annual receipts of $200,000 or more; this is the form required of about 20 percent of all unions. To encourage good financial stewardship of union members' resources, the LMRDA requires unions to annually detail income, assets, and liabilities. The form requires a variety of information, such as rate of dues, number of members, losses or shortages of funds, loans payable, and payment to employees. LM-2 forms are intended to detail the union's financial picture both so that members may identify any financial mismanagement, fraud or embezzlement of union members' dues, and to deter such abuses in the first place.

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[9]Damaris Daugherty, Teacher Rights Advocacy Coalition, in testimony to HELP Committee, June 19, 2003.

[10]Two WTU employees were charged and pleaded guilty to stealing more than $1.5 million. The WTU President, Treasurer and other officials have not yet been charged, but have resigned their positions and the investigation is ongoing. WTU's own audit indicated that $5 million had been stolen. See, *Washington Post*, "Another Guilty Plea In D.C. Union Probe," April 12, 2003.

[11]*Baltimore Sun*, March 1, 2003.

[12]The proposed rule only significantly affects LM-2 forms.

Outdated Form and Reporting Requirements

As previously noted, the LM-2 form has remained substantially unchanged for 44 years,[13] and now reflects an outdated financial environment. As a demonstration of the problem of expenditures being reported in lump sums within vague categories – which the form now permits – the following listings from actual LM-2 filings show what a union member who wanted to review how his union was representing him would be able to learn:

- $7.8 million for "civic organizations"
- $3.9 million for "sundry expenses"
- $7.8 million for "political education"
- $68.7 million for "grants to joint projects with state and local affiliates"
- $23 million for "financial assistance to state and local lodges"
- $19.3 million for "organizing and servicing."[14]

DOL has proposed to restructure the LM-2 form to require that significantly past due or forgiven loans and obligations be listed, allowing union members to determine if the union is collecting its debs and paying its obligations. Additionally, each expenditure over $2,000[15] would be itemized and designated within one of eight categories: "contract negotiation and administration," "organizing," "political activities," "lobbying," "contributions, gifts and grants," "benefits," "general overhead," and "other disbursements."

The LM-2 form also fails to require reporting of joint ventures or any assets not owned wholly by the individual union. In a time when joint ventures are extremely common, such a broad loophole invites abuse. A union that shelters assets in joint ventures may be able to hide financial mismanagement, fraud, and embezzlement even if the current LM-2 forms are closely examined by members or the Department of Labor. The proposed rule would create a new form, T-1, on which unions would be required to disclose joint ventures, trusts, and subsidiaries, so that union members may have a more complete understanding of how union officials are spending their dues and union assets.

Until recently, union members could not easily gain access to LM2 form filings. This significantly hindered their ability to see how their dues were being spent. This information is now provided on the Internet by DOL for filings after 2000. In many cases, obtaining copies of these filings through DOL may be the only way union members can learn how their union is spending their dues money. The proposed rule would require that LM-2 forms be filed

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[13]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67, No. 249, December 27, 2002.

[14]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67, No. 249, December 27, 2002.

[15]The proposed rule suggests that the threshold for itemization of expenses on the revised LM-2 form would be from $2000 to $5,000, and invited comments on what number would be the most reasonable threshold.

electronically. DOL is developing software to facilitate this, and it will be provided free to all labor unions required to file.

Lack of Investigative Resources

Within DOL, the Office of Labor Management Standards (OLMS) is the agency that monitors basic standards of financial integrity of labor organizations, and administers the Labor-Management Reporting and Disclosure Act (LMRDA). Throughout the 1990s, the ability of OLMS to perform its mission was greatly handicapped by diminished resources.

From 1990 to 2002, the budget for OLMS declined by 40 percent in relation to other government spending. The impact of this dearth of resources was severe. Audits of all unions have declined – dropping from 800 in 1992 to only 269 in 2002.[16] Many large unions have never been audited.[17]

As part of the overall effort to protect the resources of union members from financial mismanagement, fraud and embezzlement, President Bush has requested a 15-percent increase in the OLMS budget for FY04 – an increase from $34 million in FY03 to $40.6 million for FY04. The House-passed bill exceeded that request, while the Senate appropriations bill as reported (S. 1356) would meet half of the request. Reasonable increases in resources for this enforcement agency are a crucial component in achieving the strong financial accountability the President seeks.

Insufficient Civil Penalties

The law does provide penalties for violation,[18] but does not impose a penalty for filing an LM-2 late; so it is no wonder over 40 percent of unions file their LM-2s late.[19] DOL cannot impose such a penalty without Congressional action. Therefore, DOL has requested that Congress enact civil financial penalties for late filing of LM-2 forms. President Bush recommended legislative action to correct this deficiency in his FY04 budget, and a bill has been introduced in the House of Representatives to allow the Secretary of Labor to establish and implement fines for late filing.[20] Related legislation in the House would require unions to notify

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[16]Office of Labor Management Standards.

[17]Larry Yud, June 19, 2003.

[18]Criminal penalties exist for filing a false report or failing to file, for which the LMRDA authorizes a fine of more than $100,000, imprisonment for not more than one year, or both.

[19]Larry Yud. The penalty for complete failure to file or knowingly filing false information is a $100,000 fine or imprisonment for up to one year, or both.

[20]The Union Members Right to Know Act (H.R. 992), the Labor Management Accountability Act (H.R. 993), and the Union Member Information Enforcement Act (H.R. 994) were introduced by Congressman Sam Johnson (R-TX) and have been the subject of hearings within the Education and Workforce Subcommittee to which they were referred.

members of their rights under LMRDA, and provide for strong enforcement of that right. Similar legislation is expected to be introduced in the Senate during this Congress.

DOL's Proposed Rule Would Create Effective LM-2 Form

On December 27, 2002, after holding nine "stakeholder meetings" with representatives of over 40 unions who file LM-2 forms, DOL issued the proposed rule to rewrite the LM-2 form and invited public comment.[21] The public comment period ended on March 27, 2003. Although the final rule was scheduled to be issued this month, DOL has indicated that in light of the thousands of public comments received, it likely will postpone the final rule date so that all comments may be considered.

Specifically, the proposed rule would:
– restructure the LM-2 form by requiring that expenditures over $2,000 be itemized and designated within eight prescribed categories;
– require general estimation of how much time individuals on the union payroll spend on each of the eight categories referenced above;
– require listing of loans which are 90 days past due or have been written off;
– require listing of debts which are 90 days past due or have been written off;
– close a major loophole in the current LM-2 form by requiring unions to report joint ventures and trusts;
– report the number of union members and status (i.e., retired, active, or apprentice); and
– require that LM-2 forms be filed electronically, which will make it easier to assure union members and the public access to the information via the Internet.

In July, Democrats in the House of Representatives threatened to offer an amendment designed to prevent the Department from moving forward with its proposed rule to update the LM-2 as that chamber prepared to consider its FY 2004 Labor, Health and Human Services, and Education appropriations bill, but no amendment was offered. As the Senate considers its version of the FY 2004 funding bill for the Department of Labor, efforts to thwart the rule may be renewed. The Office of Management and Budget issued a statement on September 2 that the President's senior advisors would recommend he veto the bill if DOL is prevented from moving forward with the rule.

A Response to Union Officials' Objections to the Proposed Rule

The labor unions' opposition to the proposed rule to update the LM-2 form is based on assertions of their leaders that the new LM-2 form would take significantly more resources to complete, and that the current LMRDA, along with the unions' own internal oversight, is sufficient to prevent financial mismanagement, fraud, and embezzlement.

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[21]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67, No. 249, December 27, 2002.

Argument That Compliance Will Be Burdensome is Overstated

The primary objection raised by unions is that compliance will be time-consuming and costly. As stated above, the additional activities that would be required by the proposed rule include record-keeping of major disbursements and receipts over $2,000, designation of the disbursements within eight designated categories, and a similar accounting for the major disbursements and receipts of any trust in which the union is interested. Reporting would continue to be made on a annual basis, as it is currently, but would be submitted through the Internet. Again, the proposed changes to the LM-2 form only affect the largest labor unions, which already deal with large balance sheets with at least $200,000 in annual receipts.

The AFL-CIO and DOL disagree on the costs of implementing the proposed rule. The AFL-CIO has estimated that it would cost unions who are obligated to file LM-2 forms a total of $1.2 billion annually.[22] Their analysis rests on an estimated average cost of $1.2 million per national union and $217,509 per local union. The AFL-CIO did not specify if it determined whether annual compliance costs would decline in future years.

In contrast, DOL has estimated the same costs at $14 million overall in the first year, $3.3 million in the second year, and $454,000 in the third.[23] The AFL-CIO attributes the $1.19 billion discrepancy to the following costs: obtaining computer, legal, and accounting expertise; training employees; and adapting existing software and "hardware." However, 40 percent of unions already are preparing and filing LM-2 forms electronically.[24] Furthermore, DOL is providing the necessary software to complete and file LM-2s online free of charge.

Argument that Internal Oversight is Adequate is Faulted by the Facts

Some unions tout their own internal auditing systems as adequate for oversight.[25] This is analogous to the fox guarding the henhouse. The track record of 639 convictions over five years indicates that internal oversight simply cannot be counted on to protect the assets of union members. The Washington Teachers Union, a local of the American Federation of Teachers (AFT), whose former leaders have been charged with embezzling as much as $5 million from its own members, was subject to so-called internal oversight. Although the local union was supposed to file financial statements with the national union annually, it had not actually filed one since 1997 – not surprisingly, the national parent union did not uncover the embezzlement. In

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[22]Jonathon P. Hiatt, AFL-CIO, before the Labor, HHS Appropriations Subcommittee hearing, July 30, 2003.

[23]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67 No. 249, December 27, 2002.

[24]Labor Organization Annual Financial Reports, *Federal Register*, Vol. 67 No. 249, December 27, 2002.

[25]Thomas Donahue**,** AFL-CIO, before HELP Committee, June 18, 2003.

another case, a union had its own auditor, but over $350,000 of embezzlement went undetected until OLMS conducted an audit.[26]

Conclusion

The OLMS statistics on convictions show that too many union members are not being well served. Like shareholders, pensioners, and the voting public, union members deserve to be able to monitor use of their hard-earned dues. Taxpayers, too, should have access to such information since they effectively subsidize union activities. The updating of the LM-2 form proposed by DOL will help ensure financial integrity within labor unions and deter financial mismanagement, fraud, and embezzlement. Any effort to thwart DOL efforts through the appropriations process must be defeated in the Senate. Further, DOL needs the ability to enforce the LMRDA through increased resources for investigation by the overseeing agency (OLMS). Finally, Congress should update the law itself by giving the Secretary authority to impose penalties for unions which do not file by the law's deadline.

[26]Larry Yud, June 19, 2003.