

DATE: NOVEMBER 18, 2004

TO: ALL LOCAL UNIONS PARTICIPATING IN THE CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND

RE: NEW YORK TIMES ARTICLE

An article printed in the New York Times on November 15, 2004 about the Pension Fund is filled with biased and incorrect information apparently provided to the reporter by two dissident members of the Teamsters Union with an obvious political agenda. This letter corrects the errors in the article and we would appreciate you posting it for your members. We will also address the article in the upcoming TeamWork magazine.

At the outset the article correctly notes that the Pension Fund has suffered financial distress, along with the vast majority of other pension funds, as a result of the 2000–2002 downturn in the financial markets. The article also correctly notes that the Pension Fund's assets are required to be managed by independent professional investment managers known as "Named Fiduciaries" (currently Goldman Sachs and J.P. Morgan) pursuant to a 1982 Consent Decree. However, the reporter's suggestion that the assets of the Pension Fund were imprudently invested by the investment managers which resulted in the Pension Fund's current financial difficulties is wrong. In particular, after acknowledging that the Pension Fund's asset-allocation strategy mirrored that of a majority of other professionally managed pension funds, the reporter concludes that the Pension Funds' assets should have been invested primarily in fixed income instruments (i.e., corporate and government bonds) rather than equities (stocks).

Reflecting on this theory, let's compare the long-term performance of the Pension Fund's investments against fixed-income securities. For the 20-year period from 1984 through 2003, the Pension Fund's portfolio contained a diversified mix of domestic and foreign stocks, fixed income securities, real estate and other investments which produced a cumulative return of 717%. (For the record, such a diversified investment strategy is mandated by the provisions of ERISA, the federal law which governs pension funds, a point overlooked by the reporter.) For the same 20-year period the Lehman Brothers Aggregate Bond Index (a key benchmark for domestic fixed-income investment returns) produced a cumulative return of 498%. Thus for the 20-year period, the Pension Fund's diversified portfolio of investments outperformed the reporter's suggested undiversified fixed-income portfolio by 219%. Putting this into perspective, had the Pension Fund earned the Lehman Brothers Fixed-Income Index return of 498% rather than the Pension Fund's actual return of 717%, the Pension Fund's net assets today would be roughly \$7 billion less than its current value of \$18 billion. With a 100% fixed-income portfolio the Pension Fund would now have \$11 billion in net assets and be about 37% funded (or alternatively the benefit levels would be much, much lower.) While it is true that the Pension Fund is currently about 63% funded, the Pension Fund's financial difficulties are not the result of its investment allocation strategy or mismanagement. Rather, the Pension Fund's financial problems are due to (1) a decline in active participants, (2) an increasing number of retirees with longer life-spans, and (3) three consecutive years of poor investment markets resulting in returns well below the actuarially expected return of 8%.

The New York Times reporter also suggests that the driving force behind the decision to diversify into stocks is that the investment managers (the Fund's Named Fiduciaries) would realize greater fees. This is not true, and in fact such an arrangement would amount to self-dealing by the Named Fiduciaries and violate ERISA. Rather, the Pension Fund pays fees to the Named Fiduciaries based upon a percentage of the assets that they control. There is no difference in the Named Fiduciary fees whether the assets are invested in stocks or bonds; instead the Named Fiduciaries earn greater fees only if the assets grow. Unbeknownst to the reporter, she is correct that the Pension Fund's investment fees would be lower with a 100% fixed-income portfolio for a different reason – but only because the Pension Fund's assets would be \$7 billion lower with this investment strategy, the investment fees which are based upon a percentage of assets would be lower.

Finally, on the issue of diversified investments, the New York Times reporter also notes that the Western Conference of Teamsters Pension Fund has historically followed an investment strategy more heavily slanted towards fixed income securities (bonds) than has the Central States Pension Fund. However, the reporter has failed to note that the Western Conference Pension Fund also experienced significant investment losses during 2000-2002, and was also required to reduce benefit accruals and is not immune from financial hardships. Also not discussed in the article is the fact that over the years the Central States Pension Fund has been hit harder than the Western Conference Fund by declines in the number of active participants. Due to this crucial difference in the demographics (actives versus retirees, average age and service of participants, etc.), a difference completely overlooked in the New York Times article, it is not possible to draw simplistic comparisons between the Central States Pension Fund and the Western Conference Fund. Certainly it would be irresponsible (and potentially catastrophic) for the Central States Pension Fund to try to mimic an investment strategy designed for a fund with significantly different demographics

Another particularly misleading statement presented as fact by the reporter comes from a UPS driver in North Carolina known for his politically charged and extremist views of Teamster Union leaders. This driver claims he researched the Pension Fund's annual report and discovered that the Pension Fund lost \$77 million due to ownership of risky shares of a stock in a Russian company. Possibly a good story – if it was true. Had the reporter actually read the Pension Fund's annual report herself or questioned Fund executives, she would have learned that the supposed \$77 million in Russian stock was actually a \$27 investment (dollars not millions of dollars!) in a bond from a Russian bank which was in default of its interest payments; the Pension Fund's total loss was \$9.

The Trustees of the Pension Fund take great pride in the honesty with which we have communicated the Pension Fund's problems to you and your members. Certainly the Pension Fund's financial problems are not unique as many pension plans across the country have struggled to deal with the problems associated with the market downturn. The truth is that one can hardly pick up a paper without reading about another major corporation terminating its pension plan and jettisoning its retirees to the Pension Benefit Guaranty Corporation (PBGC), the federal agency charged with insuring pension plans. An avalanche of once strong companies - Bethlehem Steel, US Air, LTV Steel, TWA, Polaroid, and Outboard Marine to name a few - have all terminated their pension plans and a host of others such as United Airlines are seriously considering termination. In 2002 the PBGC received more pension claims than the total sum in all previous years. During 2003 alone, a record 152 companies terminated their pension plans shifting more than 206,000 retirees to the PBGC roles. The liabilities of the PBGC have now ballooned to the point that it is facing record deficits of \$23 billion more than double its 2002 year-end deficit.

Compounding the investment losses which fueled much of the current crisis, the Pension Fund has lost 12% of its active participants since the end of 2000. A large portion of this drop in active participants resulted from recent bankruptcies, including Consolidated Freightways in September 2002 and Fleming Foods in October 2003. Unlike the pension plans of Consolidated Freightways and Fleming Foods which covered non-union employees and which were terminated with corresponding benefit reductions, Central States continues to provide benefits to its participants who had worked for those companies. These costs, combined with the market losses has put significant pressure on the funding status of the plan which must be dealt with responsibly. Putting a majority of our assets into fixed income instruments at a time when interest rates are at historic lows is frankly a nonsensical and irresponsible method of dealing with the problem.

The Pension Fund's problems will not be solved by irresponsible political groups trying to gather support or reporters concerned with selling newspapers and unaware of the true facts. The Trustees of the Pension Fund will continue to communicate the truth to you and your members as they work diligently towards a long-term solution for the Pension Fund's financial difficulties.

Sincerely,

Thomas C. Nyhan
Executive Director