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**Culture Clash: Labor's Economic Agenda  
and Taft-Hartley Trustees' Interpretation of ERISA**

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### Abstract

In the context of the increased importance of pension fund assets in the economy since WWII, the labor movement has repeatedly tried to articulate an economic agenda for labor and encourage union pension funds to invest in accord with this agenda. While recent academic interest has focused on the behavior of the large, highly visible, public pension funds, little is known about the investment practices of smaller funds. In this paper we analyze the investment practices of two Taft-Hartley pension funds in order to discover the extent, impacts, and limits of investments targeted to produce labor-friendly collateral benefits. We find trustees hesitant to target investments to produce desirable collateral benefits. Yet, the economically targeted investments actually engaged in by the funds have clear beneficial impacts. Comparing the practices of the two funds reveals room for more economically targeted investment, but organizational and legal factors tend to discourage consideration of collateral benefits by trustees. The cultural perspective on law and organizations (Edelman and Suchman, 1997) provides a framework for understanding these findings and a guide to further research.

Culture Clash: Labor's Economic Agenda  
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Abstract

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## I. Introduction

### A. Pension Funds as "Labor's Capital."<sup>1</sup>

US pension assets are currently worth 5.8<sup>2</sup> trillion dollars. Pension funds own nearly 30% of all financial assets and control over 22% of all corporate equity. A small portion of this money is managed through Taft-Hartley pension plans and is therefore directly controlled by representatives of the workers and employers for whom the pension funds are created.<sup>3</sup> This money is, in a real sense, labor's capital as it is contributed to funds on behalf of unionized workers pursuant to collective bargaining agreements between unions and employers and is controlled jointly by union and management trustees. There is renewed interest by labor in mobilizing this capital. In the words of Richard Trumka, Secretary Treasurer of the AFL-CIO, it is time to "There is no more important strategy for the labor movement than harnessing our pension funds and developing

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<sup>1</sup> This term is taken from the title of Teresa Ghilarducci's book, *Labor's Capital: The Economics and Politics of Private Pensions*, the MIT Press, 1992.

<sup>2</sup> AFL-CIO Capital Stewardship Program, August 4, 1997; Underlying data are from the Federal Reserve Flow of Funds.

<sup>3</sup> Here we follow Ghilarducci's (1997) categorization of plans according to form of employee representation. Taft-Hartley funds, which are also referred to as multi-employer funds, are established by collective bargaining agreements between unions and employers. Contributions are made to the funds by employers pursuant to the collective bargaining agreements and the funds are jointly managed by union and management trustees pursuant to the requirements of ERISA, the Employee Retirement Income Security Act of 1974.

capital strategies as so we can stop our money from cutting our own throats.<sup>4</sup>"

The AFL-CIO in 1997 established the Center for Working Capital, a resource center for pension trustees and labor leaders. The buzz words from the Center are that labor will be the "capital stewards" of working people's retirement assets. The Center lays out its objectives in broad terms to "1. Safeguard workers' savings and the integrity of their retirement plans; 2. Ensure that the benefits of workers' accumulated wealth accrue to them and their families; 3. Align the attainment of retirement security with the promotion of economic prosperity."<sup>5</sup> The spin of "capital stewardship" is new, but the concept is old: the labor movement will recover its lost economic and political power by using its financial power, the power of pension capital.<sup>6</sup>

This case study of two Taft-Hartley funds explores the impact of these kinds of initiatives at the level of investment practices of small pension funds. We are interested in the extent to which trustees incorporate labor's economic agenda in their pension fund investment decisions. When they do pursue innovative investment or corporate governance strategies, we ask what impacts these initiatives have on the local and regional economy. Thus,

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<sup>4</sup> AFL-CIO Human Resources Development Institute (1998), p. 73

<sup>5</sup> AFL-CIO Center for Working Capital (1997)

we analyze and compare the extent, impact, and limits of economically targeted investment in the portfolios of two Taft-Hartley pension funds.

Pension trustees have the power to make choices about what investments to make, which professionals will manage these investments, and how they will engage with the fund investments as shareholders/owners (either by proxy voting or informal shareholder communication). We focus mostly on these trusts' economically targeted investments because we found virtually no activity with respect to proxy voting or shareholder resolutions in the two funds studied. Thus, we analyze and compare the extent, impact, and limits of economically targeted investment in the portfolios of two Taft-Hartley pension funds.

Our study suggests that Taft-Hartley trusts have a culture in which trustees ask a limited range of questions of their pension professionals and choose investments from within a limited range of investment vehicles. The trust fund culture is shaped by trustees' and pension professionals' understanding of the Employee Retirement Income Security Act (ERISA) and the internal dynamics of the Boards of Trustees.

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<sup>6</sup> Perhaps the most comprehensive plan of this sort put forward yet is that developed by Rifkin and Barber and presented in their book *The North Will Rise Again* (Rifkin and Barber, 1978).

## **B. Literature Review**

Since the 1950s scholars have tried to define the role of pension funds in the economy (Harbrecht, 1959; Dorsey, 1987; Drucker, 1976; Rifkin and Barber, 1978). Drucker (1976) provocatively claimed that pension funds had brought socialism to the United States, because workers owned pension funds and the funds, in turn, owned controlling shares of most major corporations. Drucker concluded that the workers owned the companies, thus American capitalism had given way to pension fund socialism. Rifkin and Barber (1978) argued that pension fund assets were neither "private" nor "public," but a new form of wealth. They called for state and local governments to ally with pension funds to rejuvenate declining industrial regions of the United States. Hawley (1995) argues that the newly active role of large public pension funds as shareholders influencing corporate governance and bottom line economic issues has resulted in a partial "re-marriage" of ownership and control in American capitalism.

Some authors have suspected that among pension funds, union funds act differently. Early scholarship tended to assume that union pension funds were invariably used for political purposes by union "bosses." Greenough and King (1976) argued that in Taft-Hartley pension funds "the unions have tended to become the dominant partners" (p. 49). Dorsey and Turner (1990) begin their analysis of pension



fund investments and earnings with an exhaustive enumeration of reasons we would expect pension funds involving unions to engage in "social investing" of various types, including economically targeted investing. They argue further that Taft-Hartley funds should be more likely than other union funds to use pension fund assets to further economic goals of the labor movement, because these funds might be more likely to be controlled by the union.<sup>7</sup>

Rather than assume that labor side trustees always wear their union hats, Ghilarducci and colleagues have analyzed the conflicts inherent in the labor-side trustees' position of being both shareholder and union representative (Ghilarducci et al., 1997; Ghilarducci et al., 1995). They argue that unions have traditional interests in promoting "firm-specific employee interests," while shareholders have "an interest in pursuing technological change and innovation although it may be both job displacing and job creating" (Ghilarducci et al., 1997, p. 27). Based on their study of the Operating Engineers Central Pension Fund Ghilarducci and colleagues (1995) argue that the Employee Retirement Security Act of 1974 enshrined the principles of modern portfolio theory, which limits the goals of investment to maximizing risk-adjusted return. Thus ERISA encourages

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<sup>7</sup> Dorsey and Turner (1990) found lower earnings for union funds prior to 1980 but no differences between multi-employer and other kinds of pension funds in risk-adjusted rates of return after 1980. They suggest that the impact of ERISA may account for the performance improvement. As Ghilarducci

labor-side trustees to resolve potential conflicts between union and shareholder interests in favor of focusing only on risk-adjusted rates of return and ignoring collateral impacts of investment decisions.

Hawley's (1995) study of public pension funds offers an explanation for why trustees might begin to involve themselves in issues beyond simple rates of investment return. Following Hirschman (1970; 1986), he suggests that trustees "exit" investments, remain "loyal" to investments or exercise their "voice" in the form of corporate governance initiatives investment performance is not satisfactory. In the public sector funds, Hawley argues that these choices are governed by market constraints. Because of their large size, public pensions cannot quickly divest themselves of particular investments without disturbing the market too much. Because of widespread indexing practices and the sheer size of these large, public funds, they have trouble finding buyers when poor performance in a specific firm or sector might warrant selling. The big public funds are therefore more likely to develop relationships with their holdings and exercise "voice" in the governance of the corporations they own.

There are very few studies of the investment practices of union pension funds from the "ground's eye" level of the

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and colleagues (1995) explain, ERISA encouraged Taft-Hartley trusts to focus on keeping investment returns up to levels generally being achieved in the market, rather than merely making safe investments.

trust boards. Existing case studies are of very large public and private pension funds (O'Barr and Conley, 1992) and a large and influential Taft-Hartley fund (Ghilarducci et al., 1995; Petersen, 1994). To our knowledge there are no case studies of how the trust boards of relatively small Taft-Hartley funds define their general investment strategies and the role of economically targeted investments within these.

The sheer magnitude of force concentrated in large pension funds naturally draws attention to them as key actors in the stock market today. However, from the point of view of labor's economic agenda, it is equally important to be able to influence and coordinate the investment practices of the myriad of smaller funds. Although small funds on their own may have little impact on the stock market, together they owned 296 billion dollars worth of the stock market in 1996. Moreover, economically targeted investments may have important impacts on the funds themselves or on local economies and are therefore of interest both to the labor movement and to scholars interested in understanding the role of pension funds in the economy.

Unfortunately, Hawley's (1995) compelling argument for why large, public sector funds are forced to consider factors beyond investment returns does not apply to the

Taft-Hartley funds studied here. Since the funds make investment decisions independently from one another, divestment of a particular holding will not likely upset the market. Trustees do not have strong incentives to try to improve underperforming firms or to consider factors beyond investment returns; Taft-Hartley funds are free to "exit." Nonetheless, the decisions of trustees to invest or divest appear to be governed as much by the dynamics between the trustees, their labor and employer constituencies and their pension professionals as by bottom-line outcomes for the funds. Thus, we propose that the cultural perspective on law and organizational behavior being developed by Edelman and others provides a way to understand the impact of ERISA on Taft-Hartley fund investment practices.

### ***C. Methods***

This case study was sponsored by the Ford Foundation as part of a multi-faceted project, High Performance Pensions: Multi-Employer Plans and the Challenges of Falling Pension Coverage and Retirement Insecurity. The companion pieces to the case study included a survey of multi-employer pension trustees conducted by Teresa Ghilarducci and Michael Reich, an analysis of fiduciary responsibility under ERISA by Kirsten Snow Spalding and Matthew Kramer and a study which identified the pension professionals serving the largest

West Coast multi-employer pension funds by Ghilarducci and Reich.

The research agenda was set by the researchers with the assistance of the Pension Practitioners Consortium, a group of West Coast pension trustees and pension professionals. The draft findings from these papers were presented to trustees and professionals at a conference held at UC Berkeley on September 4-5, 1997.

This case study focuses on two small pension funds. Both funds are sponsored by building trades unions on the west coast. One of the funds, which we refer to as the Craft Local Fund, is sponsored by a single local union and an employer association of construction contractors. The other fund, which we refer to as the West Coast Fund, is sponsored by several local unions of a single international union and has multi- employer contributors pursuant to a master collective bargaining agreement. The funds were chosen because of their local reputation for engaging in innovative investment practices. The data for this study were gathered through a series of interviews with union and management trustees, some (but not all) of the funds' investment managers, the Executive Officer of the Local Building and Construction Trades Council, and officials from the City Housing Authority. The analysis of the funds' investment holdings was based on the funds' reports to the

Department of Labor. The most recent data available from the DOL is 1995. Public opinion reports of the Funds' investment activities were gathered from local press reports.

It is notable that the Administrator is the same for both funds. The administrator refused to give the researchers an interview, refused to provide any of the funds' governing documents, including documents which were ultimately obtained through the Department of Labor. Likewise the trustees interviewed were unable to provide the researchers with fund governing documents because all copies are kept by the Administrator at their offices.

In accordance with sociological convention, the interviewees, the funds and the investment projects are referred to in this case study by pseudonyms. However, Investment Managers and vehicles are referred to by their real names.

This study examines investment practices; it does not provide investment advice. We assume that all investment decisions were prudent for the funds at the time they were made. We make no recommendation as to what other investment decisions these or other funds should make in the future. Nothing in this study should be understood as a legal opinion on the prudence of any particular investment or investment strategy.

## **II. Investment Practices on Two Taft-Hartley Trusts**

### ***A. Introduction to the Taft-Hartley World***

In 1947, the Taft-Hartley amendment to the National Labor Relations Act established that pension funds could no longer be managed solely by unions and required that they be jointly managed by union and employer trustees. The multi-employer funds established after this amendment are referred to as "Taft-Hartley" pension funds. They are created by collective bargaining agreements between unions and employers. By the terms of the collective bargaining agreement, employers make hourly contributions to the pension funds on behalf of all employees covered by the collective bargaining agreement. Taft-Hartley funds are established jointly by one or more local unions and employers who have collective bargaining relationships with these local unions. Some large Taft-Hartley funds are established by a single International Union and cover all employees of the employers in a given region. The decisions about which employers and which unions will be included in the fund are the subject of collective bargaining. The decisions about the rate of employer contributions to the funds and the level of benefits provided to employees are made by the Taft-Hartley Boards of Trustees. But the decisions made by the Board of Trustees impact the bargaining negotiations between the employers and unions and likewise the bargaining negotiations impact the decisions of

fund trustees. In many cases the same individuals will be both bargaining representatives for contract negotiations and trustees for the purposes of managing the pension funds.

Taft-Hartley Funds, like all employee health and pension plans (with the exceptions of government plans and church plans) are governed by the Employee Retirement Income Security Act, ERISA. For all covered plans, ERISA establishes disclosure and reporting requirements, participation and vesting requirements, minimum funding requirements, fiduciary responsibility rules for plan professionals and trustees, and plan administration and enforcement regulations. For the purposes of this study, we refer primarily to the ERISA fiduciary responsibility and reporting requirements. The five ERISA fiduciary requirements are: 1) the fiduciary must discharge his duties solely in the interests of the plan participants and beneficiaries. (ERISA 404(a)(1)(A)); 2) the fiduciary must discharge his duties for the exclusive purpose of providing benefits to participants and their beneficiaries; 3) the fiduciary must act with the care, skill and diligence of a prudent man acting in like capacity; 4) a fiduciary must diversify the plan investments so as to minimize the risk of large losses; and 5) the fiduciary must discharge his duties in accordance with the documents and instruments governing the plan. The interpretation of these provisions will be



discussed in reference to specific investment decisions below, but most controversial from the trustees' perspective is the question of whether the sole interest, exclusive benefit and prudent man requirements prohibit trustees from investing in economically targeted investments (ETI).

We define ETI's as investments which are "prudent and responsible," and which provide financial return commensurate with inherent risk, but which also have collateral benefits, which other, equally "prudent and responsible," investments do not have.<sup>8</sup> Examples of ETI are investments in low income housing developments which create union construction jobs and provide low income housing,<sup>9</sup> or investments in industrial construction projects which condition the investment on the use of union service or production workers.<sup>10</sup>

A companion strategy to economically targeted investment is for the labor movement to exercise its capital power through corporate governance initiatives. The pension funds exercise their influence as shareowners of corporation. Examples of these initiatives have included

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<sup>8</sup> This is our definition of ETI. Trustees and investment professionals offer alternative definitions, for example some will consider an investment economically targeted only if the collateral benefits accrue directly to the participants in their fund, other will consider the investment an ETI only if the investor has some level of control over the collateral benefit.

<sup>9</sup> This is the project of the AFL-CIO Housing Investment Trust discussed at length below.

<sup>10</sup> This is the project of the Union Labor Life Insurance Co.'s J for Jobs program. *Union Pension Funds Moving to Support Projects that Hire Only Organized Labor*, 18 Pens. Rep. (BNA) 577 (Mr. 25, 1991).

proxy votes to establish independent boards of directors,<sup>11</sup> requests for information on workplace practices or lawsuits under Securities and Exchange Commission laws guaranteeing disclosure of information to shareholders. Trustees acting as shareowners may directly affect workplace practices--for example by influencing the management decision to "downsize" a workforce, or may more indirectly affect practices, for example by prohibiting "poison pills" or other incentives for merger or acquisitions.

As the cases which follow illustrate, these strategies (ETI's or corporate governance) championed by the AFL-CIO or the International Unions do not automatically become the policies or practices of the Taft-Hartley funds.

### ***B. The "Craft Local Fund"***

#### **Plans, Assets, Investments**

The Craft Local Fund has two pension plans.<sup>12</sup> Part A is a defined benefit plan, part B is a defined contribution plan. Both pension plans were established January 1, 1972. In 1994, Part A, the defined benefit plan had 1,141 active

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<sup>11</sup> The AFL-CIO Office of Investment's Center for Working Capital regularly publish lists of Labor Shareholder Resolutions to encourage pension trustees to vote their proxies as a concerted effort to advance labor interests.

<sup>12</sup> A defined benefit plan is one which promises to pay a fixed monthly payment (or an amount based on the employee's salary) at the time of retirement. A defined contribution plan will pay a monthly annuity based on the amount in the employee's account at the time of retirement. The amount in the account is determined by employer and employee contributions tot he account and the investment returns on those amounts.

participants and 1,085 retired or separated participants receiving or entitled to future benefits and beneficiaries of deceased participants. In the same year, Part B, the defined contribution plan, had 1,140 active participants and a total of 3, 125 participants with account balances.<sup>13</sup> The trustees interviewed in 1997 and 1998 reported that the plans together had about 1400 active members plus a few hundred "travelers" from other locals and between 400 and 600 retirees.<sup>14</sup>

The Craft Local Fund has been doing a very good job providing good, secure pension benefits for union members. Currently members are retiring with defined benefit payments of approximately \$3,000/month in addition to having amassed up to 200-300,000 dollars in their defined contribution accounts. The policy of the Craft Local Fund is "no unfunded liabilities."

[Table 1 about here]

At the end of 1994 both plans together invested \$288,412,193.<sup>15</sup> Table 1 shows the management and allocation of the Local Fund's investment assets for Parts A and B together. The table shows a trend away from investments with insurance companies to reliance on investment managers. In 1989 less than half of Part A's investment assets were

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<sup>13</sup> Source: DOL Form 5500s, Auditor's reports.

<sup>14</sup> The number of "travelers" is due to a current construction boom. Contributions to pension funds earned by travelers are sent to their local funds.

managed by Frank Russell. This percentage increased steadily between 1989 and 1994, when Frank Russell managed more than three quarters of the plan's assets. Similarly, before 1990 Part B's assets were distributed among insurance companies and various brokers; after 1990 most of the assets were turned over to the investment management firm, McMorgan & Company. In 1994 McMorgan & Company managed more than 90% of Part B's assets (see Table 3 in the appendix).

There is also a trend of increasing numbers of investment managers. In 1994, Part B added two new investment vehicles: the Frank Russell Trust Company's "Small Capitalization Fund," and Miller, Anderson and Sherrerd's "International Equity Fund." Part A added the AFL-CIO's HIT and BIT to its investment portfolio. According to the trustees interviewed in 1997 and 1998, this trend has continued with the additions of the investment managers Ferguson, Wellman, Rudd, Purdy and Van Winkle, Inc. (Portland, OR); Montgomery (San Francisco, CA); and ULLICO's J for Jobs.

Most of the investment managers used by the Craft Local Fund are "conventional" investment managers. The conventional managers each have their own style of investment and may specialize in an asset class. They are not focused on economically targeted investments, nor are

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<sup>15</sup> Source: DOL Form 5500s, Auditor's reports.

they known for their activism in corporate governance once they have holdings in companies. Within the fund's investment guidelines, the individual money managers seek the highest possible risk-adjusted return and exclude other criteria of investment benefits.

Only a small amount of the Local Fund's investments can be considered "ETI." Table 1 shows the distribution of the Local Fund's assets for Plans A and B together; highlighted entries may be considered "ETI." These are investments in the AFL-CIO's Housing and Building investment trusts, the Union Labor Life Insurance Company's Mortgage Pooled Account and mortgages bought as part of McMorgan & Company's construction program. These are all investments which promote union-only construction. ULLICO's mortgage account and the AFL-CIO's Housing and Building investment trusts were founded to provide union-friendly investment vehicles for union health and welfare benefit funds. McMorgan & Company's construction program also ties investment to union guarantees.

In 1995 (our most recent data point), 1% was allocated to the AFL-CIO's HIT and BIT, 2.34% was invested in McMorgan construction program mortgages and 1.93% was invested in ULLICO's Mortgage Pooled Account. Chart 1 shows that the total percent ETI per year engaged in by the Craft Local

Fund ranged from less than 5% in 1993 to a little over 7% in 1990.

[Chart 1 about here]

[Diagram A About Here]

### Power and Influence on the Craft Local Fund Trust Board

Diagram A shows the complex organizational web within which the Craft Local Trust board makes investment decisions. The solid lines in the diagram indicate direct influence on investment practices. The dotted lines represent indirect influence. In theory, the agency chain of investment decision making runs from union members (plan participants) to the board of trustees; in fact the decision making about investments is most influenced by professional advisors. The trustees' understandings of their holdings in relations to the economy--including any aspect of labor's economic agenda as articulated by the AFL-CIO affiliated international unions or even by local unions--is profoundly shaped by the trust professionals. Specific investment choices are delegated to another set of professionals, the investment managers.

Investment decisions are made in the broader context of two interacting environments: the stock market and

investment practices, and the legal framework of ERISA and the regulations of the Department of Labor. The members of the Trust Board rely on professionals to interpret both the economic and legal/regulatory environments. Investment consultants help the board set guidelines for asset allocation and choice of investment managers. Consultants also act as independent monitors of the performance of the investment managers. The trust lawyer and the International Foundation of Employee Benefit Plans are the primary interpreters of the legal requirements for trustee fiduciary responsibility. The International Foundation is probably the most important source of education and training for trustees; Craft Local Fund trustees attend annual International Foundation conferences.

At the center of the process is the actual trust board, composed of 4 management side trustees and 4 union trustees. One of the management trustees is essentially a professional trustee because he is the staff director of the Contractors' Association. The President of the Board of Directors of the Contractors' Association appoints the other 3 management trustees. The Association avoids unnecessary turnover on the board because training a new trustee is costly in time and money. The Craft Local's Business Manager/Financial Secretary is a trustee because he is the Local's principal officer. The President of the

Local appoints the other 3 trustees. Labor side trustees are also appointed for indefinite terms and generally stay on the Board for about 10 years.

The relationships among trustees are also among individuals who face each other across the bargaining table regularly. We believe it is important to recognize that the bargaining and trustee relationships are not isolated from each other and there is the potential for "issue trading" where a bargaining party agrees not to press an issue on the trust in exchange for winning an issue in the collective bargaining arena. On this fund, one informant did suggest that employer associations have become much more interested in investment practices than they used to be, because investment returns affect contribution levels i.e. higher investment returns might mean lower contribution levels.

Decision making on the board of trustees seems to function smoothly. Voting is according to majority rule and the trustees interviewed only remembered one case of a deadlock between the four labor side and four management side trustees. At issue was the method of funding an early retirement benefit. This was actually resolved in the parties' collective bargaining.

Investment management issues are not delegated to a subcommittee, but handled by the full trust board. However, the Craft Local Fund's trust board does not make specific



investment choices. Instead, the Board chooses investment managers, who are given the authority to make specific investment choices and vote the Trust's proxies. Thus the points at which the trust board has the most direct influence on how the trust's money is used are (1) in the choice of investment managers and (2) in the guidelines regarding investments and proxy voting given to the investment managers.

The investment consultant helps the trust board choose investment managers by advising on what kinds of managers are desirable as well as by suggesting which investment managers should be allowed to bid to the Trust Board at all. Decisions about hiring and firing investment managers are made once a year at three day sessions in which the entire investment strategy is discussed. The agenda for these discussions is set primarily by the investment consultant. Five or six firms suggested by the consultant have a chance to address the board. Any firm considered seriously will be interviewed a second time as well. The trustees generally agree to add a new investment vehicle or a new money manager only when this can be done without re-allocating assets from one manager or vehicle to another.

In choosing investment managers, the trustees consider past performance and fee structures. The managers are not asked about their union-friendliness or awareness of labor

issues. They are not asked about their activism in terms of willingness to engage in ETI or monitoring and encouragement of union friendly policies within companies they own. Generally, however, the trustees only consider money managers with experience managing Taft-Hartley benefit funds.

As noted above (see Chart 1 and Table 1), the Craft Local Fund has most of its assets with conventional investment managers. These include Frank Russell; Miller, Anderson, Sherrerd; Ferguson, Wellman, Rudd, Purdy, and Van Winkle; Aetna Capital Management; and Montgomery. McMorgan & Company could also be considered a conventional investment manager. With the exception of the construction program, which accounts for a very small portion of the Plan's assets with the firm, McMorgan seems to invest conventionally. However, the aggressive program undertaken by the firm to promote union-only construction is definitely a form of ETI, thus marking McMorgan as very different from the other investment managers.

The Craft Local Fund seems to have chosen a different investment philosophy for their defined benefit plan and their defined contribution plan. While the defined benefit assets (Plan A) are divided up among different investment managers, each with their own investment style, the defined contribution assets (Plan B) are virtually all invested with

a single manager, McMorgan & Co. (Tables presenting the distribution of investment assets for Parts A and B separately are presented in the Appendix.)

Craft Local Fund trustees suggested that the form of the benefit changes the plan participants' view of investment practices and this influences trustees' investment decisions. According to the trustees interviewed, because the benefits from the defined contribution plan (Plan B) are determined by the investment returns, beneficiaries watch over returns very carefully. If they do not like how the investment returns look, they complain to the union trustees or directly to the investment manager. Thus, from the point of view of the trust board, it is not desirable to take a longer term view of investment with these funds; these funds need to show steady, positive quarterly returns. One trustee implied they are satisfied with McMorgan & Co. for the defined contribution funds because McMorgan & Co. deals well with beneficiaries who may talk to them as well as doing a good job investing these funds. McMorgan & Co. also has a vehicle for rolling the retiree benefits into individual retirement accounts when the participant retires..

Having chosen the money managers, the trust board delegates authority for all specific investment decisions. The managers are bound by the guidelines on asset allocation

determined by the trust board and by a quarterly review of the investment returns. The Craft Local Fund's board sets asset allocation guidelines in conjunction with their investment consultants. These guidelines do not consider collateral benefits or consequences of investment beyond the prudent risk adjusted rate of return. Proxy voting is also delegated.

Upon request by the trustees the managers may report on a particular proxy vote after it has occurred; however, this almost never happens. The International Union of this Craft has encouraged the local to take advantage of the services of the Marco Consulting Group, a labor friendly multi-employer pension consulting firm, which has a proxy voting service. However, the proposal was rejected because the fees were considered too high.

The roles of fund administrators, actuaries, and auditors were not identified as important influences on investment practices by our informants. However, it is likely that administrators screen information which reaches trustees. Actuaries produce information crucial in investment planning. The influences of these actors is beyond the scope of this paper, but should be noted as an area for further investigation.

**Union "Voice" in Investment Practices**

As Diagram A indicates, most of the direct influence on investment decision-making comes from professional advisors and consultants. However, the union Local and its membership could potentially exercise direct influence on the actions of the union trustees. The Local could advise trustees to consider collateral benefits of investment decisions, for example. The principal officer is elected, so he is open to some kinds of pressure. In practice, however, the Union International is the only union body which tries to get Craft Local Fund trustees to consider labor's economic agenda as part of their investment practices. The International has an investment monitoring program by which the International union attempts to track the holdings of all of its local and regional pension funds. This fund does not participate in this program. The International has also encouraged Locals to use the services of the Marco Consulting Group to determine how proxies should be voted; this has been rejected by the board as "too expensive." The International reportedly also informs union trustees about union-friendly investment vehicles.

Trends in the management of the defined contribution funds have opened up space for individual union members to have a more direct say in how the funds in their defined contribution accounts are invested. Craft Local members may actually direct the investment of portions of this account

rather than leaving it all in the hands of the trust board. Without advice from the local union or even a clearly articulated investment strategy coming from the International leadership, this form of participation actually bypasses both the trust board and the union. It is individualizing, rather than contributing to the articulation of a collective "voice" representing labor's collective economic agenda.

Open conflicts between labor and management interests do not play an important role on the trust board; however, slight differences in focus are apparent. Although both labor and management trustees seemed uninterested in activist ownership issues, the union side is more sensitive to these issues. Both sides acknowledge shared interests in protecting market share for union construction, but most of the ETI considered is put on the board's agenda by labor trustees.

Management trustees reported that labor side trustees are "pressured" by their international to push particular ETIs. For example, one trustee reported an incident in which the board decided that such an ETI was not "prudent and responsible." The management trustees agreed to "take the blame" for not investing in it, but the Local's principal officer was ostracized at the next meeting of the International Union. However, management trustees stated

they were open to ETIs promoting union construction as long as these were otherwise good investments.

The Craft Local Fund has investments with several vehicles clearly identified as ETI because they promote union construction. These are investments with the AFL-CIO's Housing and Building investment trusts, ULLICO's Mortgage Pooled Account, and McMorgan & Company's construction program. (See Table 1.) However, the trustees interviewed tended to take the view that these investments did not necessarily differ in impact from traditional investments. The AFL-CIO's HIT and BIT, for example, have only recently begun to finance projects in the Local's region, so they provide no immediate, tangible benefits to the Craft Local Fund's participants. The union-side trustee even went so far as to claim the Craft Local Fund does not engage in economically targeted investing. In his view "economically targeted" investing would mean that the trust's money was invested in firms or projects carried out by contractors signatory to the Fund's agreements.

Management side trustees stated that collateral benefits of any particular investment are not considered relevant by the trust board; however, it seems likely that that this is not completely true. In response to our question about consideration of collateral benefits, one management trustee responded, "well, young lady, as a good

ERISA lawyer, you should know I can't do 'social investing,' so you didn't ask me that."<sup>16</sup> Similarly, discussions with Morgan & Co., one of the Craft Local Fund's investment managers, revealed an array of practices designed to promote union construction, which, however, had not been mentioned by any of the trustees interviewed. According to Morgan, their "construction program" is "understood," it is not based on explicit agreements, written or oral. Morgan's business is 99% Taft-Hartley funds, and, according to Dan O'Donnell, VP for Construction, "the funds know we understand their needs, we don't have to say it."

### **C. West Coast Fund**

#### **Plans, Assets, Investments**

The "West Coast Fund" pension plan is a defined benefit plan established in 1960. It involves 7 craft locals and their respective contractor associations. At the end of 1994, the Plan had 2,473 active participants and 1,310 participants (and dependents) receiving benefits, as well as 898 people entitled to future benefits. At the end of 1994 the West Coast Fund reported total assets worth \$221,992,236

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<sup>16</sup> See Spalding, Kirsten Snow and Matthew Kramer, "What Trustees Can Do Under ERISA: A Study of Permissible Trustee Activism", presented at the High Performance Pensions Conference September 1997, University of California at Berkeley and Jeffrey S. Petersen, PhD. And Peter Phillips, PhD., "The Effect of 'Union Only' Provisions on Construction Labor Costs and Pension Benefits," paper prepared for "High Performance Pensions." In fact, ERISA does not prohibit consideration of collateral benefits, as long as the investment is otherwise "prudent and responsible."



and investment assets valued at \$219, 591,551.<sup>17</sup> The fund both invests its assets and purchases benefits insurance. Table 4 shows the distribution of the West Coast Fund's investment assets. As can be seen in Table 4, this fund, like the Craft Local Fund, has followed the trend away from investments with insurance companies towards reliance on investment managers.

Otherwise, the investment practices of this fund differ from those of the Craft Local Fund. First, rather than diversifying their investments by choosing several different managers, the West Coast Fund employs only one investment manager, McMorgan & Company. In 1995 McMorgan managed over 80% of the Fund's assets; remaining assets were invested with insurance companies or in ETI vehicles. Second, the West Coast Fund invests directly in real estate. Third, the West Coast Fund has engaged in more different forms of ETI than the Craft Local Fund as well as allocating a much higher percentage of assets to ETI vehicles.

Moreover, the investment manager chosen by the West Coast Fund does not act for this fund as a "conventional" investment manager interchangeable with managers like Frank Russell or Montgomery. At first glance, McMorgan seems to be a conventional investment manager, which has successfully wooed Taft-Hartley business. However, according to an

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<sup>17</sup> 1994 DOL Form 5500 and 1994 Auditor's Report

independent observer, "McMorgan is probably the biggest purveyor of union-friendly construction type investment around."<sup>18</sup>

According to Daniel O'Donnell, McMorgan's Real Estate Officer and Bob Hirsch, McMorgan's General Counsel, McMorgan and an influential West Coast labor-side law firm began putting together ETI's in the form of union-only construction in the early 1970s. The McMorgan construction program now consists of various methods of financing made contingent on union-only labor restrictions, including forward loan commitments, construction financing, permanent financing and equity involvement. Representing Taft-Hartley funds as owners, McMorgan stipulates that buildings are maintained and rehabilitated by union labor.<sup>19</sup> McMorgan has also been involved in precedent setting lawsuits establishing the legality of such practices.<sup>20</sup>

[Table 2 about here]

Table 2 shows the distribution of the West Coast Fund's investment assets and highlights the entries we consider "ETI." These are the AFL-CIO's Housing and Building Investment Trusts (HIT and BIT), investments with Union Labor Life (only 1989), ULLICO's J for Jobs, the Multi-employer Property Trust (MEPT), direct investments in

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<sup>18</sup> Interview with Jeffrey Petersen, PhD, Post-doctoral Fellow, National Institute of Aging, November 1997.

<sup>19</sup> Interviews with Daniel O'Donnell and Bob Hirsch, February 9, 1998.

Real Estate, and mortgages bought as part of the McMorgan construction program. Thus the table shows that ETI has accounted for at least 8% of the fund's total investment assets since at least 1989. Furthermore, the fund developed and implemented a compensating balance "Rehabilitation Program" together with a local bank, which directly promoted the employment of pension plan participants by making the fund's money available as loans for home improvement work done by signatory contractors. (This program cannot be tracked with the information available in the DOL Form 5500, therefore it does not appear in Table 2.)

[Diagram B About Here]

### Power and Influence on the West Coast Fund Board

Diagram B shows the organizational context in which the West Coast trustees manage their investments. The solid lines represent direct influence on investment practices; the dotted lines represent indirect influence. As is the case with the Craft Local Fund, professional advisors exercise the most direct influence on the West Coast trustees. Another set of professionals, the investment managers make the specific investment decisions and vote the fund's proxies. However, West Coast trustees have taken a more active role in articulating a labor-friendly economic

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<sup>20</sup> Chernoff, Joel, "Judge Clears Fund in Antitrust Case," *Pensions & Investment Age* v13, n26, December 9, 1985

agenda for their fund, as well as in choosing investment managers and investment vehicles in line with their agenda of promoting union construction.

The West Coast trustees work in the same broad context as the Craft Local Fund and similarly rely on professionals to interpret the stock market and investment practices, the legal framework of ERISA, and the regulations of the Department of Labor. In both cases the International Foundation of Employee Benefit Plans appears to be the most important source of trustee education and training. In both cases investment consultants help trustees set asset allocation guidelines and monitor investment performance. The trustees exercise the most control over investment decisions at the point of choosing investment managers and vehicles.

The West Coast Fund board is made up of 7 management side and 7 labor side trustees, one from each local involved. This represents the geographic diversity of the region. The union side trustee interviewed is a trustee because he is Business Representative for his local; however, the President may appoint someone else or sit on the trust board himself and other locals may appoint trustees differently. Management trustees are chosen by the signatory contractor association; one of them is the association director, an employee of the association.

Virtually all the decision-making power regarding investments resides with the benefits subcommittee of the West Coast Fund, which has four members appointed by the chair of the fund board. The benefits subcommittee makes all the investment-related recommendations and these are generally adopted by the full board.

Because the West Coast Fund involves several locals, the members of the benefits subcommittee may or may not face each other across the bargaining table. Thus, for this fund, it may be possible to isolate the trustee relationship from the primary bargaining relationship. Again, we do not have evidence on how this affects investment practices, but it should be noted that the complex of relationships among trustees is probably very important.

The benefits subcommittee reviews bids by investment managers. Managers are evaluated according to a mix of traditional and union-sensitive criteria. First a manager's history, associated risks, the markets s/he performs best in, general reputation, and familiarity with Taft-Hartley funds are investigated. Finally, the benefits subcommittee asks, "how would this investment benefit us?" Thus the investment managers' knowledge of the labor agenda and familiarity with labor friendly investment is explicitly considered by the West Coast trustees.

Once having chosen an investment manager, however, the West Coast fund delegates authority for specific investment decisions and proxy voting to the managers. Conventional investment guidelines merely stipulating asset allocation are developed with the consultants. The fund board does not provide investment guidelines which promote labor's economic agenda.

Investigation of how the fund administrator, actuary and auditor influence investment practices is beyond the current scope of this investigation. However, these actors play potentially important roles. It is likely that the administrator screens information. And, obviously, the knowledge produced by the actuaries is relevant to investment planning.

### Union "Voice" in Investment Practices

Conflicts between labor and management do not play a big role in the investment practices of the West Coast Fund; however, labor's greater interest in developing ETI in the form of promoting union-only construction was reported. The labor side trustee interviewed is very actively engaged in seeking prudent and responsible ETI opportunities. In his view the management trustees are not opposed to this, they are just less interested in dealing with these issues and the inevitable work involved in doing something non-traditional. In contrast to the Craft Local Fund, the

international of this craft was not reported to encourage investment in ETI or proxy vote monitoring. (Thus, the question mark in the relevant box on Diagram B.)

As in the case of the Craft Local Fund, the potential for plan participants/union members to influence investment practices is limited. The only official mechanism for such input would be for members to vote the Business Representative or the Local's President out of office. The International of this craft does not seem to have much influence either. In contrast to findings about the Craft Local Fund, the West Coast trustee interviewed did not report the International encouraging the use of proxy voting services or promoting any particular investment vehicles. The local union does not have any particular policy encouraging trustees to consider collateral benefits of investment decisions. Indeed, the labor side trustee interviewed suggested that a trustee's personal fiduciary responsibility might actually prohibit him from receiving investment guidelines from either his international or local union.<sup>21</sup>

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<sup>21</sup> We can assume the trustee is informed in general about the US Supreme Court's Amax Coal decision which held that under ERISA a situation in which a trustee has "dual loyalties, and, therefore, he cannot act exclusively for the benefit of a plan's participants and beneficiaries" is prohibited. (453 US 322, 334 (1981)) However, the interpretation that this general rule prohibits trustees from considering union proxy voting guidelines is most conservative and one that the Department of Labor does not accept in its interpretive bulletins or advice memoranda. In fact the Joint Statement Of The Responsibilities Of Pension Plan Fiduciaries In Tender Offers And Mergers, issued January 31, 1989 by the Departments of Labor and Treasury provide the very basis for the AFL-CIO Proxy Voting Guidelines.

Proxy voting issues are not discussed often on the West Coast Fund board. However, occasionally investment advisors may inform the trustees of how they are planning to vote proxies. Neither the local nor the international union provides proxy voting guidelines in any form to the trustees. However, the West Coast Fund does exercise a small amount of "activist ownership," through direct ownership of real estate. Buildings owned by the fund are built, rehabilitated, and sometimes serviced exclusively by union labor.

Compared to the Craft Local Fund, the West Coast Fund has invested a relatively large percentage of its assets in various vehicles which may be considered ETI because they promote union construction. The fund has not merely invested in existing ETI vehicles such as the Multi-Employer Property Trust, but has also developed its own ETI program. As Table 4 shows, West Coast Fund's investment in ETI's increased from 8% in 1989 to 15% in 1994 and dropped back to 14% in 1995. In addition, during some of this time, a further 1% of investment assets were in certificates of deposit with a local bank, providing "compensating balance," for loans for home improvements done by signatory contractors. At the time of the interview in 1997, one trustee reported the Board might consider investing in the



MFS Union Standard Equity Fund, a mutual fund which invests only in "union-friendly" companies.

With regard to ETI, the West Coast Fund trustees ultimately DO ask, "how can this investment benefit us?" Thus they are actively engaged in considering the collateral impacts of various investment strategies. They have clearly articulated an agenda in favor of promoting union construction, when it is "prudent and responsible" to do so. Nonetheless, trustees have little information about the collateral benefits of the investments once they hold them. They are not actively monitoring collateral benefits nor are they demanding "voice" in corporate governance through concerted proxy voting, shareholder resolutions or suits or even in active monitoring of corporate Boards of Directors.

#### ***D. The collateral benefits of economically targeted investing***

Our case study of two craft pension funds turned up several instances of ETI. We found ETI vehicles explicitly labeled and marketed as "union-friendly," such as ULLICO's J for Jobs as well as one relatively low profile form of ETI, McMorgan's construction program. In what follows we briefly examine these ETIs and their potential for collateral benefits. We are interested in how effective these vehicles really are in promoting an economic agenda for labor. Thus we examine traditional categories of risk

and return in conjunction with other indicators of economic benefit such as job creation, fund contributions, units of low-income housing built and qualitative benefits such as the potential for strengthening community-labor alliances.

We find that the ETI practices of the trusts studied are providing prudent, responsible investments with potential for collateral benefits of two main types. First, an investment may provide both good investment returns and direct financial benefits for plan participants in terms of job creation and thus increased fund contributions. Second, collateral benefits might include difficult to quantify factors such as the potential for strengthening labor-community ties and creating positive visibility for labor.

Before describing the ETIs found in the trusts studied, we would like to enter the caveat that we are not comparing these investment vehicles in terms of their ability to produce returns on investment. Based on publicly available information we conclude that each of these investment options is suitable for *consideration* by union pension funds. We are not providing investment advice. Instead, we argue that after establishing prudent and responsible rates of return, union pension funds should *consider* the collateral impacts of their investments. Collateral impacts may be negative or positive. For example, one investment may finance downsizing and de-skilling of a workforce, while

another, equally profitable, investment may finance creation of new, "high road" jobs. To this end we examine the ETI practices of the Craft Local Fund and the West Coast Trust more closely for their potential for collateral benefits.

### Real Estate Investment Trusts: J for Jobs, MEPT, HIT & BIT

a. ULLICO's J for Jobs, the AFL-CIO's Housing and Building Investment Trusts and the Multi-Employer Property Fund are all pooled real estate investment trusts. Each is structured somewhat differently, however, they all contribute to the creation of union construction jobs. When a union pension fund invests in real estate through these vehicles, trustees know their money is financing high quality construction, high wage jobs, and contributions to union health, welfare, and pension funds. These investment vehicles pool assets, experience and information. Thus they may be better equipped to make good real estate investments than small individual pension funds.

ULLICO's J for Jobs account is a pooled mortgage account organized in 1977. It invests in private, union built construction and has provided good returns. It's annualized rate of return of 9.75% for the period ending June 30, 1994 made it one of the best performing real estate funds available for pension plan investment, according to a

report in *Pension & Investments*.<sup>22</sup> ULLICO estimates that 32,000 hours of construction work are created for every one million dollars invested by the J for Jobs program.<sup>23</sup>

b. The Multi-Employer Property Trust founded in 1982 is a pooled real estate equity fund investing in commercial and multi-family residential construction. The MEPT was designed as an investment vehicle for multi-employer and public employee pension plans. As of April 1997, 107 pension plans were participating and the net asset value of the MEPT was 1.15 billion dollars.<sup>24</sup> The Marco Consulting Group has compared MEPT's performance to the ASB Capital Management "Employee Benefit Real Estate Fund" for the years 1992-1989, finding the MEPT's performance better. The MEPT also performed better than Evaluation Associates' Inc. Open End Equity Funds Index for the 10 year period 1992-1982.<sup>25</sup> The MEPT estimates that projects financed by the MEPT have created "over 12 million hours of new work for Building Trades members across the country" in 15 years.<sup>26</sup>

c. The AFL-CIO's Housing and Building Investment Trusts are designed to provide secure retirement income and promote union construction. The Building Investment Trust (BIT) does both real estate equity and mortgage investing

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<sup>22</sup> See Williams, Terry (1993) "Union Realty Funds Make Successful Showing," *Pension and Investments*, August 23, 1993.

<sup>23</sup> As reported by Zanglein (1995), p. 70.

<sup>24</sup> *MEPT Report* of April 1997

<sup>25</sup> As reported in *AFL-CIO Pensions in Changing Capital Markets*, p. 60

and the Housing Investment Trust invests only in mortgages and mortgage-backed securities. The BIT was founded to offer union pension funds "a medium for pooling their funds for long term investment primarily in interests in, or interests secured by, real property." However, BIT is managed independently of the AFL-CIO. At the end of 1996 the BIT held assets worth more than \$429 million.<sup>27</sup>

The AFL-CIO's Housing Investment Trust is perhaps the oldest ETI developed by labor. It was established in 1964 "under the sponsorship of the AFL-CIO as an instrumentality of the United States labor union movement."<sup>28</sup> The investment objective of the HIT is "to provide current income through investment in construction and long-term mortgage loans and mortgage-backed securities carrying competitive market yields." Moreover, the HIT "will limit investments ... to those in which such new construction or rehabilitation work is done by union labor."<sup>29</sup> Investment participation is restricted to unions, union pension plans and public retirement systems. At the end of 1996, the HIT had 395 investor participants and net assets worth \$1,383,000,000.

According to SEC filings, both the Housing and Building Investment Trusts provide good returns. The BIT has earned

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<sup>26</sup> Multi-Employer Property Trust, *1996 Year in Review*, p. 9, "Annualized Gross Returns

<sup>27</sup> AFL-CIO Building Investment Trust, *Investment Memorandum and 1996 Annual Report*

<sup>28</sup> AFL-CIO Housing Investment Trust, *Prospectus*, p. 7

an annualized return of 7.8% since its founding.<sup>30</sup> The HIT has also done well, outperforming both the Salomon Brothers Mortgage Index and the Lehman Brothers Aggregate Bond Index for the last 1 year, 3 years, 5 years, and 10 years.<sup>31</sup>

### The West Coast Fund's Rehabilitation Program

The West Coast Fund's Rehabilitation Program is a "targeted CD" program. The trust agreed to keep a certain amount of its funds in a local bank in CDs. The bank agreed to make loans for home improvements up to the value of the Trust's CD holdings in the bank, whereby the loans were conditioned on work being performed by signatory contractors. The trust's primary investment manager, Morgan & Company had full responsibility for monitoring the fund's participation in this program and evaluating the advisability of continuing or suspending the program. This ETI let the trust funnel pension fund money directly back into the community, putting plan participants and signatory contractors to work. The trust both earned the interest on the CDs and garnered new contributions for the pension plan. Morgan & Company's involvement in this program is consonant with the firm's commitment to promoting union construction work, described below.

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<sup>29</sup> AFL-CIO Housing Investment Trust, *Prospectus*, p. 8

<sup>30</sup> Reported in Zanglein (1995), p. 69

<sup>31</sup> AFL-CIO Housing Investment Trust, *Annual Report 1996*, p. 3

### "Hidden" ETI: the McMorgan construction program

We call the McMorgan construction program "hidden" ETI because it does not exist anywhere on paper. Instead there seems to be an implicit understanding between the firm and its Taft-Hartley clients that health and welfare benefit fund assets are not invested in non-union construction and are used to promote union-only construction, when this is a feasible and prudent component of an overall investment portfolio. Furthermore, the "ETI" aspect of McMorgan's mortgage, land, and real estate investments cannot be tracked in DOL Forms 5500. This contrasts with programs like the AFL-CIO's Housing and Building Investment Trusts, the Multi-Employer Property Trust, and ULLICO's J for Jobs which are clearly identified and marketed as promoting union construction as a collateral benefit.

According to Bob Hirsch, General Counsel for McMorgan, the firm together with an influential Bay Area labor-side law firm began putting together ETIs in the form of union-only construction by the early 1970s. Hirsch suggests that the McMorgan program began "hidden," or "implicit," because legal boundaries were initially very unclear.<sup>32</sup> The

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<sup>32</sup> Indeed, Joel Chernoff (1985) identifies a lawsuit in which McMorgan and Company was a party as the first court decision on the issue of linking pension fund financing to a union-only stipulation when the project was only partly financed by the union pension fund.

McMorgan construction program involves various methods of financing real estate development made contingent on union-only labor restrictions.<sup>33</sup> This includes everything from forward loan commitments to requiring land owned by a client to be developed with, and buildings owned by a client to be serviced by, all union labor. McMorgan estimates that real estate projects financed by McMorgan clients generated over 232 million man-hours of union employment between 1981 and 1996.<sup>34</sup>

While McMorgan and Company appears at first glance to be a traditional investment management firm which has successfully wooed Taft-Hartley business, a closer look suggests the company was at least in part founded to provide a vehicle for the consolidation and coordinated investment of regional Taft-Hartley funds. First, the firm's business is 99% Taft-Hartley funds. Second, a study of the top 30 multi-employer funds found that McMorgan works with twice as many funds as the nearest competitor.<sup>35</sup> This is also suggested by McMorgan's aggressive promotion of union-only construction and the close ties between McMorgan and an influential Bay Area labor-side law firm.

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<sup>33</sup> Interviews with Daniel E. O'Donnell and Bob Hirsch, February 9, 1998

<sup>34</sup> O'Donnell, Daniel E., McMorgan & Company, E.V.P. "Building Local Economies: Economic Activity and Employment Generated by Construction Activity," conference paper presented at "High Performance Pensions: Multi-Employer Plans and the challenges of Falling Pension Coverage & Retirement Insecurity," September 4-5, 1997, U.C. Berkeley

<sup>35</sup> "Who Manages the Big Money?: Profile of the Top Multi-Employer Pension Funds in the Western States," *Labor Center Reporter*, 303, Spring 1998



Our discovery of McMorgan's "hidden" ETI, raises the question of whether and to what extent the firm actually does consolidate and coordinate Taft-Hartley fund investment with the objective of promoting labor's economic agenda. If so, the question is raised of whether similar approaches and firms do or could exist in other regions to promote consolidation and coordination of Taft-Hartley fund investment practices.

#### **Collateral Benefits: contributions, market share, labor-community alliances**

Trustees are required by ERISA to make "prudent and responsible" investments. In practice, most trustees seek the highest possible risk-adjusted investment returns. Any impact of an investment other than this narrowly defined accounting for investment returns is considered "collateral." When a construction union pension fund invests in a construction project which puts its members to work, job creation and the man-hours of contributions to the plan's funds generated by this investment are considered "collateral" benefits.

The potential for increasing employment and therefore contributions to multi-employer pension funds is an important collateral benefit because it may help maintain the appropriate balance of active participants to retirees

in the building and construction pension funds.<sup>36</sup> These are the kinds of collateral benefits produced by the West Coast Fund's Rehabilitation Program. This program funneled fund money directly back into the community putting union members to work, thus generating both employment and contributions to the trust fund. Some parts of McMorgan's construction program also have these kinds of collateral benefits. The pooled real estate investment trusts also have the potential for generating jobs for plan participants and contributions for the Taft-Hartley funds invested in them. However, the pooled real estate investment vehicles are less specifically targeted. The West Coast Trust's investment in ULLICO's J for Jobs, for example, might generate work for locals outside of the west coast region. Nonetheless, the summed impact of promoting these kinds of investments might indirectly help maintain or increase union contractors' share of the construction market. This is potentially a very significant potential collateral benefit of this kind of investment.

Similarly, an investment vehicle's effort to find profitable ways to promote a social good might be construed as a collateral benefit. For example, the AFL-CIO Housing Investment Trust's effort to seek profitable ways of promoting the social good of affordable housing might be

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<sup>36</sup> Petersen and Phillips (1997).

construed as a potential collateral benefit accruing to pension plan participants and beneficiaries, insofar as the HIT's effort has a positive impact on communities.

President Clinton implied this possibility in a speech to the residents of Dade County, Florida in the aftermath of hurricane Andrew.<sup>37</sup> The President stated, "I am proud of the work that has been done by the Department of Housing and Urban Development and the AFL-CIO in creating a partnership to invest in our communities...all across the country, the AFL-CIO, supported by...Fannie Mae and Freddie Mac, are going to establish a housing investment trust fund that will provide an additional \$600 million to rebuild and create affordable housing across this country..."<sup>38</sup>

The third kind of collateral benefit we discovered is the potential for certain kinds of ETIs to promote community-labor alliances and to provide labor with positive visibility. We interviewed several different parties involved in one particular affordable housing project, partly financed by the AFL-CIO's HIT, and concluded that the collateral benefits of the HIT's involvement in the project lie primarily in the potential for creating union jobs,

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<sup>37</sup> "Remarks to the community in Cutler Ridge, Florida," speech on September 6, 1993, *Weekly Compilation of Presidential Documents* v29, n36, September 13, 1993: 1698, Transcript.

<sup>38</sup> "Fannie Mae" is the Federal National Mortgage Association (FNMA). It started out as a federal agency but was privatized as a government chartered entity in 1968. Fannie Mae purchases loans on the secondary market, pools them and sells them. Fannie Mae deals in FHA, VA, and conventional loans. "Freddie Mac" is the Federal Home Loan Mortgage Corporation. It is like Fannie Mae but deals mostly with conventional loans. Both entities are supposed to encourage a secondary market for mortgages, in order to promote mortgage lending.

generating positive visibility for labor, and the chance to strengthen ties between labor and the community inherent in such a project.

## Los Lirios

a. Los Lirios: promoting labor's positive role in local communities

"Los Lirios," is a large, affordable housing complex located in northern California, comprising 246 housing units, most of which are "affordable," i.e., rented at below market rates pegged to household income to families with "moderate income," "low income," and "very low income."<sup>39</sup> Los Lirios was financed in part by the AFL-CIO's Housing Investment Trust, in return for a guarantee of 100% union labor on the project. This was the first time the union trust had done so in California and the union involvement was reported quite positively in the local paper.

The financing arrangements for Los Lirios were complex and multi-layered. The City contributed 7.76 million dollars in loans for land acquisition and pre-development costs, construction and permanent financing. The Bank of America contributed construction financing. SAMCO, a consortium of California lenders, issued a 9.96 million

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<sup>39</sup> "Los Lirios" is a pseudonym. Information on units and rental restrictions are based on a City Memorandum, April 21, 1993.

dollar mortgage loan.<sup>40</sup> Permanent financing of approximately \$12 million was contributed by the Low Income Housing Tax Credit investor-limited partners. Low income housing tax credits total \$11.69 million. The local non-profit developer of the project contributed equity.<sup>41</sup>

The AFL-CIO Housing Investment Trust was involved in the project as the buyer of the SAMCO mortgage. According to Marci Cohen, the HIT's Director of Development, HIT's role in financing Los Lirios was crucial. The local non-profit developer of the project approached the HIT about financing and the HIT was able to offer attractive terms and thus make the deal possible.<sup>42</sup> The secondary market for mortgage loans strongly influences the availability of mortgage loans.<sup>43</sup> Thus, as is usual in these kinds of multi-layered deals, SAMCO did not agree to issue the loan until Fannie Mae had agreed to insure it and the HIT had agreed to buy it.<sup>44</sup>

Representatives of the City's Department of Housing, however, saw the HIT as just one of several possible lenders for Los Lirios. In their view, the affordable housing market is driven by developers chasing Low Income Housing

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<sup>40</sup> SAMCO stands for Savings Association Mortgage Company.

<sup>41</sup> Financing information comes from City Memorandum, April 14, 1993 and October 28, 1992 and AFL-CIO Housing Investment Trust documents.

<sup>42</sup> Interview with Marcie Cohen, June 4, 1997.

<sup>43</sup> Interviews with Sarah Bland, Economist with the Office of Housing and Urban Development, and Jens Hillmer, Office of Housing and Neighborhood Development, City of Oakland.

Tax Credits and thus there was no shortage of capital for affordable housing. They did not remember that the HIT brought any special expertise to the Los Lirios deal.<sup>45</sup> Cohen disagrees strongly with this view. She argues that at *the time* financing was being sought for Los Lirios, the HIT was able to offer both forward commitments and fixed rates and few other organizations could have done that.<sup>46</sup> She also argues that the HIT can provide expertise in helping to structure the complicated financing arrangements in some kinds of affordable housing projects.

b. Los Lirios and Job Creation

Los Lirios generated jobs for building trades union members at a time when a lot of people were out of work. Because the HIT was involved in financing, the project was guaranteed to be 100% union built. The President of the County Building Trades Council informed us that between 1989 and 1992 the building trades trust funds had seen a 44.9% drop in man-hours. Thus the 275-300 construction jobs, which he estimated on the Los Lirios project, were extremely welcome at the time.<sup>47</sup> From another point of view, the HIT estimates that a project like Los Lirios would create at

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<sup>44</sup> "Fannie Mae" is the Federal National Mortgage Association or FNMA, a government sponsored entity which insures mortgage investments and creates and sells mortgage-backed securities. Fannie Mae's purpose is to expand the secondary market for mortgage loans to encourage mortgage financing.

<sup>45</sup> The City Department of Housing is not directly involved in raising capital, however. Instead developers must find their own financing, although the city may provide information about possible sources to developers.

<sup>46</sup> Cohen's emphasis on the time period in which Los Lirios was built is important. The role and efficacy of any given vehicle for economically targeted investment depends on the economic context.

least 544,000 man-hours for the \$34 million investment. These 544,000 man-hours would result in over a million dollars of contributions into various construction union pension funds.<sup>48</sup>

Since the HIT invests only in 100% union built projects, pension funds investing with the HIT can be sure that their money is putting union members to work rather than undercutting hard-won union wage and benefit standards. However, this is not the same thing as saying that the HIT actually creates union jobs. Officials in the City's Department of Housing pointed out that since federal funding and city funding were part of the Los Lirios deal, the project was subject to prevailing wage laws. They argued these laws together with the size of the Los Lirios project pretty much guaranteed that it would be built 100% union.<sup>49</sup>

c. Los Lirios as Affordable Housing

There is a pressing need for affordable housing in this area. Los Lirios contributed to increasing the city's stock of affordable housing and to improving the image of subsidized housing. According to reports in the local paper, Los Lirios is attractive and safe and has attracted desirable tenants, while providing rents significantly below

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<sup>47</sup> Interview with County Building Trades President, June 16, 1997

<sup>48</sup> Contributions per worker per hour vary by local and sometimes within locals as well. However, if we assume an average contribution of \$2.50 per man-hour, then 544,000 man-hours of union work produces \$1.36 million in contributions into pension trust funds.

<sup>49</sup> Meeting with Tom MacRostie, Housing and Development Administrator, Thomas M. Cook, Department of Housing, and Ronald E. Schreck, Development Specialist, City Department of Housing.

market rate. Tenants and neighbors of the project like it for these reasons. The local paper's editorial page carried an editorial in support of a neighboring city council's decision to build a similar project, holding up the success of "Los Lirios" as a positive model.

The success of Los Lirios may, in part, reflect union involvement via the HIT, in the project. According to Marcie Cohen, the HIT aims to invest only in high quality properties which will survive and produce returns over the long term. She points out that from the perspective of owning a 30 year mortgage, this is an important consideration. City representatives, in contrast, did not believe the impact of the HIT's involvement was different from other financing sources. In their view, HIT's involvement in the housing complex is at "arm's length," because they only hold the mortgage, thus having no impact on the quality and success of the project.

d. Los Lirios: strengthening alliances and showcasing labor

In the view of City Department of Housing representatives, the most distinctive feature of the HIT financial involvement in Los Lirios was its political appeal to elected officials. The HIT's labor connections were attractive to the mayor and some members of the board of supervisors who have been strongly backed by the labor constituencies in the City. The Housing officials agreed



that Los Lirios was a showcase project and that using union pension money to build low income housing with union labor has public appeal. Thus the role of the HIT's financing of Los Lirios helped to strengthen or establish relationships between elected officials and labor constituencies.

The public appeal of making good investments in affordable housing with union pension funds was also mentioned by several interviewees. While this may not seem especially important from the point of view of the Department of Housing, it might be considered an important collateral benefit from the point of view of union pension plan participants. The President of the County Building Trades Council remembered that Los Lirios and another prominent project in which the AFL-CIO's Building Investment Trust was involved came at a time when the economy was just beginning to improve again in the city. The public involvement of the AFL-CIO's investment trusts in these prominent construction projects helped put unions in a positive light at that time, creating union jobs and showing union money going into community development.

From the perspective of the West Coast Trust and Craft Local Fund, investing in the HIT works as part of a diversified investment strategy. The HIT provides good, secure investments in real estate. Moreover, as was shown in the case of "Los Lirios," the fact that the HIT targets

100% union construction and seeks to invest in communities results in collateral benefits above and beyond the investment returns. These include generating jobs and fund contributions, promoting affordable housing, strengthening labor's political alliances and showcasing labor's positive role in the community.

[Chart 2 near here]

### **III. Conclusion**

#### ***A. Accounting for different levels of ETI in the two funds.***

The Craft Local and West Coast Funds through their limited economically targeted investments have advanced a labor agenda, including job creation, low income housing development, political good will toward labor the development of labor/community alliances. But the funds have mobilized a very small percentage of their assets to achieve these goals. Over the last six years, the West Coast Fund has put an average of 12% of its assets into ETI and has also utilized the McMorgan construction program and the rehabilitation program to invest in construction jobs in the local area. The Craft Local Fund has put an average of 5% of its assets into ETI and has not engaged in any corporate governance activity. What accounts for the difference? How has the West Coast Fund managed to increase the percentage of its assets in ETI and engage more actively in a labor agenda?

The parameters within which the trustees of these two funds make investment decisions are broadly similar. Both funds serve building trades members. Both funds have informal communication with members about investment decisions, but neither has a formal mechanism for communicating with members or with their affiliated international union. Both funds delegate specific investment decisions to their investment managers. Neither the union locals nor the trustees attempt to set guidelines beyond the ERISA requirements for investment decision making. In both cases the only explicit investment guidelines followed by the investment managers are those set by the investment consultants regarding appropriate asset allocation according to conventional investment criteria.<sup>50</sup>

The union locals do not attempt to set guidelines for proxy voting by the trustees. The boards themselves do not have proxy voting guidelines governing their investment managers. Although the International Union of the Craft Local Fund has an investment tracking program, neither this Fund nor the West Coast Fund engages in consistent investment tracking. With the exception of McMorgan's construction program, in which the West Coast Fund participates, none of the trustees interviewed reported any

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<sup>50</sup> This is in contrast to situations where trustees have set investment guidelines to address corporate practices such as grossly high executive compensation, golden parachutes, election of corporate directors, director perks, director diversity, insider trading, downsizing supplier standards, corporate environmental

informal corporate governance initiatives or shareowner actions with respect to the funds' investment holdings.

Despite these broadly similar investment climates and practices, the West Coast Fund has consistently engaged in more ETI than the Craft Local Fund. Our comparison suggests that this may be due to the consistent activism of one of the union trustees on the West Coast Fund board. Further, we suggest that the organizational structure and culture of the West Coast Board facilitates the activism of this trustee. Compared to the Craft Local Fund, the West Coast Fund has delegated investment decision-making to a smaller subcommittee, has fewer different investment managers, and has a more liberal interpretation of ERISA's requirement of fiduciary responsibility—an interpretation which allows consideration of collateral impacts of investment.

As Diagram A illustrates, the network of agents between the worker/participants in the Craft Local Fund and their investments, is much more complicated than for the West Coast Fund (Diagram B). The Craft Local Fund has two plans with different investment strategies. Investment decision-making responsibility is spread among nine investment managers; no single manager has authority for a majority of the combined holdings of the two plans. Of these nine managers, three specialize in ETI type investments: ULLICO,

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and human rights conduct, high performance workplaces, fair lending practices for financial companies and environmental standards.

AFL-CIO's HIT/BIT and McMorgan. In contrast, the West Coast Fund has consolidated its investment decision making in McMorgan and Co., giving McMorgan 86.49% of its total assets to manage with the balance of its assets spread almost exclusively among investment managers who specialize in ETI.

The Craft Local Fund as a matter of policy chose to diversify its investments by diversifying its pool of investment managers. As one trustee noted, the managers were chosen *because* they have different styles of investing. By having a greater number of investment managers, the trustees made it inherently more difficult to coordinate investment in line with any non-conventional criteria. While the nine investment managers could conceivably pursue a concerted agenda, they are hired to pursue different types of investment opportunities. With 86% of its investments managed by McMorgan and Co. it is easier for the West Coast Fund trustees to put forward a labor agenda by communicating with McMorgan. Through McMorgan's construction program, the West Coast fund has both an economically targeted investment and can communicate directly with the Boards of Directors of the companies that West coast Fund owns. Acting as owners, West Coast Fund communications can be coordinated with other Taft-Hartley investors through McMorgan.

The West Coast Fund also streamlined the communication with McMorgan by consolidating the trustees' monitoring

function in the Benefits Subcommittee. The four member Subcommittee reviews investment decisions more closely and often than the full board could. As part of this monitoring, the West Coast Fund's Benefits Subcommittee consistently raises the issue of whether or not an investment vehicle or manager might provide collateral benefits to participants, beneficiaries or signatory contractors. The collateral benefits issues are raised both in the Benefits Subcommittee's initial decision to choose an investment manager and also in reviewing the investment performance of the existing managers.

While the streamlined agency chain from union trustee to the investment manager with control over the majority of the fund assets does not explain why the West Coast Fund made particular investment decisions, it does appear to provide an avenue for the activist West Coast fund trustee to pursue innovative initiatives that forward his labor agenda. For example, the activist trustee decided to explore the Rehabilitation program, he convinced the Benefits Subcommittee co-chair to permit him to explore this possibility and then simply directed McMorgan to pursue this type of fixed income investment. McMorgan proposed the investment strategy after they had negotiated the terms of the investment and the collateral benefits with the local bank. The labor chair was able to make the case for the

Rehabilitation program to the rest of the Subcommittee with the assistance of McMorgan.

Why does the Craft Local Fund have a more complicated network of fund professionals? Possibly the Craft Local trustees believe that diversification of investment advisors decreases the risk to the fund's assets and better serves the interests of the participants. This would be consistent with O'Barr and Conley's (1992) characterization of funds which choose a variety of investment philosophies as being particularly concerned with meeting legal requirements for "prudent" investing. These authors found that proponents of using a variety of investment approaches justified this in legal terms as a "demonstration" of prudence and in economic terms as ensuring that the fund is prepared for a variety of market conditions. Craft Local trustees emphasized that professional advisors help them meet legal fiduciary responsibility requirements.

While the West Coast trustees also articulated reservations about the boundaries of ERISA, the Craft Local Fund took these restrictions to the extreme position and interpreted ERISA as prohibiting trustees from even *considering* the collateral impacts of any particular investment. Craft Local Fund trustees therefore do not consider collateral impacts in the normal course of evaluating investment managers. They have not directed

their managers to engage in any concerted proxy voting campaigns or in any other corporate governance initiatives. Thus, both the proliferation of investment managers and the culture of the Craft Local board tend to inhibit engagement in economically targeted investments.

In sum, elements of the organizational structure and culture of the West Coast fund facilitate the efforts of the activist labor-side trustee to promote ETI. The board interprets ERISA as allowing inquiry about the collateral impacts of investments and development of alternative investment strategies (such as the Rehabilitation program). The relationship between the Benefits Subcommittee, the full trust board, and the primary investment manager allow the trustee to pursue ETI through relatively direct communication with the primary investment manager. In contrast, elements of the organizational structure and culture of the Craft Local Fund tend to discourage engaging in ETI. The Craft Local Fund trustees are relatively disinterested in pursuing a labor agenda. The Craft Local trustees interpret ERISA as restricting their ability to ask about collateral benefits of their investments. Furthermore, the Craft Local Fund's network of investment professionals makes it more difficult for a trustee to communicate a concerted agenda.



In both cases, the communications between the International union, the Board of trustees and the investment managers led to a common understanding of the boundaries of ERISA fiduciary responsibility and the potential for investment practices that would forward a union agenda. But on the West Coast Fund, that common understanding empowered the trustees and their investment managers to pursue economically targeted investments whereas on the Craft Local Fund, those common understandings bound the trustees and kept them from pursuing innovative investment strategies with their multiplicity of investment managers.

***B. Contributions of the Cultural Perspective on Law and Organizations to Explaining Trustee Disinterest in Pursuing Labor's Economic Agenda through Pension Fund Investment***

This study of the extent, impacts, and limits of ETI in the investment practices of two Taft-Hartley funds shows that despite the labor movement's efforts to encourage trustees to consider collateral impacts of investments, trustees tend to view investments purely in terms of risk-adjusted returns. Overall, we found a small amount of economically targeted investment in the portfolios of each fund studied; however, the difference between the two funds suggests there is room for more ETI when ERISA is interpreted as allowing trustees to consider collateral impacts and trustees take an active interest in promoting

beneficial collateral impacts of investment. Our examination of the Los Lirios experience from various points of view suggests that the labor movement could benefit if both investment professionals and trustees put some effort into thinking creatively and broadly about less measurable impacts of ETI, such as the impact of showcasing labor's positive role in the community.

Comparing the two funds studied suggests several factors which may inhibit or promote trustee activism for investment with beneficial collateral impacts. These are: 1) clear communication of a labor agenda from trustees to the investment managers; 2) more information about the collateral effects of investments flowing to the trustees; 3) a less restrictive understanding of the fiduciary responsibility requirements of ERISA; 4) a broader definition of "exclusive benefit to participants" which includes collateral effects of investments; 5) consideration of the hard to measure benefits such as "good will toward labor" when making investment choices.

The finding that trusts of relatively similar size with relatively similar organization constraints make different choices about economically targeted investments suggests that multi-employer funds do not make decisions purely based on market considerations. The Hawley exit-voice-loyalty model for public pension fund investment decision making

clearly does not apply to small funds which can divest and invest without broader market repercussions. The West Coast Fund's use of the McMorgan union-only real estate program suggests that multi-employer funds may exercise "voice" by concerted investment strategies with other funds. This option is not mandated by market conditions, but is instead motivated by the labor agenda of trustees. Our findings suggest that interpretations of ERISA are a critical factor in determining trustees' views on economically targeted investing. Thus, we conclude by proposing that the cultural perspective on law and organizational behavior being developed by Edelman and others provides a framework for understanding our findings and a useful guide to further research.

According to Edelman and Suchman (1997), the cultural perspective sees law as "a pervasive belief system that permeates the most fundamental morals and meanings of organizational life: Law constructs and legitimates organizational forms, inspires and shapes organizational norms and ideals, and even helps to constitute the identities and capacities of organizational actors" (p. 493). This perspective may help uncover the points where trustees' approach to economically targeted investing could be influenced. This approach also provides a conceptual framework for understanding the impact of law on society by

pointing to the actions of intermediate organizations, In this case, trust boards interpret ERISA in certain ways that shape their investment practices. These investment practices have societal impacts.

Edelman (1992) argues that organizational response to the law is a critical step in the mediation of law's impact on society. Our findings are consistent with this view. The fiduciary responsibility requirements of ERISA which were set out to advance the interests of workers and retirees who participate in the fund have been recast as restrictions on the behavior of fund trustees and other fiduciaries. Trustees commonly articulate this fear, "If I even consider collateral benefits in my investment decisions the Department of Labor will take my house."<sup>51</sup> Indeed, 37% of funds surveyed by the Institute for Fiduciary Education in 1993 state that the principal reason they did not invest in ETIs is because it conflicts with fiduciary duty.<sup>52</sup> Ghilarducci et al.'s (1995) study of the Operating Engineers Central Pension Fund also found that ERISA encouraged trustees to view "prudent and responsible" investing purely in terms of risk-adjusted rates of return.

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<sup>51</sup> Quote of trustee speaking in an open forum at the High Performance Pension Fund Conference, UC Berkeley, September 4-5, 1997.

<sup>52</sup> Institute for Fiduciary Education, *Economically Targeted Investments: A reference for Public Pension Funds* (1993).

Our findings suggest that trust fund culture is determined by the relationships among pension professionals and the labor community. For example Mc Morgan's relationship with the union-side labor law firm which represents the local unions in both the Craft Local Fund and the West Coast Fund creates a basis for unspoken understandings between McMorgan and the union-side trustees. Likewise the relationship between the AFL-CIO and its investment management companies, the AFL-CIO HIT and BIT at least symbolizes a common understanding between trustees and the investment managers. How ERISA attorneys, investment consultants and investment managers articulate fiduciary responsibility may open opportunities for greater trustee activism or pose barriers to new investment options. Likewise, the level of trustee education about ERISA fiduciary responsibility may shape the Fund culture into which pension professionals are hired and serve.

Edelman, Abraham, and Erlanger (1992) studied how personnel and legal professionals constructed the threat of wrongful discharge suits based on implied contract theory. They found that personnel professionals constructed the threat as pervasive and large, while legal professionals emphasized this threat was exceptional and small. Their study demonstrates that the "law" does not change organizational behavior in a simple and direct manner;

instead, it is interpreted by particular groups of professionals in particular ways and these interpretations condition organizational response. The different situations of legal and personnel professionals studied by Edelman et al. with respect to the consequences of wrongful discharge suits might help explain their differing constructions of this threat; in contrast, the case of ERISA's impact on trust board behavior points to the importance of autonomous developments within professional fields.

According to Ghilarducci et al. (1995), modern portfolio theory developed within the world of professional finance and was then enshrined in ERISA's definitions of "prudent" and "responsible" investment practices. Thus, "prudent and responsible" came to mean diversification in investment styles as well as in investment assets. Ghilarducci et al.'s (1995) finding that ERISA encouraged Taft-Hartley trusts to focus on keeping investment returns up to levels generally being achieved in the market, rather than merely making safe investments, is consistent with this view. The professional investment consultants and advisors hired by the two funds studied here clearly have a strong influence on the investment practices of these funds. But, perhaps more importantly, these individuals are merely representatives of the financial world, whose goals and perspectives differ greatly from those of the labor

movement. Thus the financial environment and the requirements of ERISA are interpreted for trustees from these points of view, rather than from points of view articulated by the labor movement.

Edelman's (1992) study of organizational response to EEO/AA law argues that organizations respond to the law by testing its limits, therefore, in fact defining the law through their actions. We found this to be the case as well. McMorgan and Company, has been engaged in attempts to expand the legal definition of investing in the "best interests of participants" for years. Ambiguity about the legality of linking construction investments to requirements of union labor has resulted in McMorgan's efforts being neither marketed nor labeled as economically targeted investment. McMorgan has also been forced to defend some of its practices in court, thus contributing to definition of the legal boundaries of such investment practices.<sup>53</sup>

Our discovery of McMorgan's "hidden" program of economically targeted investments raises the question of whether and to what extent an investment management firm like McMorgan actually manages to coordinate and consolidate the impact of Taft-Hartley fund investment. Does McMorgan's construction program actually promote increased market share for union contractors in the region? If so, could this

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<sup>53</sup>See discussion in Chernoff (1985).

model of low-profile, regionally-based coordination of some aspects of union pension fund investment practices be replicated in other regions?

Thus, our study shows the key role of professionals and suggests a few simple ways in which a change in professional practice could influence investment practices. First, clearly more and less labor-friendly investment professionals exist. Labor-friendly investment professionals could be prepared to offer more information to trustees about the collateral effects of investments and their corporate governance initiatives with the fund's holdings. As McMorgan's actions and the AFL-CIO investment vehicles ULLICO and HIT/BIT and the union-friendly proxy voting services of Marco Consulting demonstrate, professional investment managers and consultants can be encouraged to develop and implement labor-friendly investment practices. Given the complexity of the modern financial world, reliance on professionals will continue, so the question should be how can trustees influence these professionals to understand and implement a labor-friendly economic agenda?

While the important economic impacts of very large pension funds have been recognized in recent years, the potential impact of relatively small funds has not been studied. With this case study we hope to point out the



important role that little funds have in promoting retirement security for workers and could have in local and regional economies. The investment practices of these smaller funds should be of interest both to the labor movement and to scholars who are interested in understanding the role of pension fund capital in the economy.

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## **Appendix: Charts and Tables**