RESEARCH NOTE

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Proposed GM/UAW VEBA: A House of Cards?

My initial assessment of the Proposed GM/UAW VEBA (Legal Implications of Proposed GM/UAW VEBA, Research Note, 10/02/2007) concentrated on the implications of the proposed sale of the Convertible Note to the VEBA. I have now had the opportunity to assess more fully the Memorandum of Understanding covering the VEBA that the UAW has made available to its members in advance of the contract ratification vote. This MOU makes clear that the entire VEBA structure fails to secure future health care obligations from the potential risk of GM bankruptcy. To put it succinctly, the VEBA structure can be said to balance like a house of cards completely subject to the ups and downs of GM's financial future. If GM collapses into bankruptcy it is very likely that the VEBA will also collapse.

The basis of this conclusion is simple: according to the MOU GM retains unilateral power to make up to $7 billion of its potential contributions to the VEBA in cash over a twelve to twenty year period through annual payments. Since these payments are to be made in cash they depend entirely on the availability of that cash from GM. But if GM declares bankruptcy there is no means to guarantee now that the cash will be available or that GM will not use the bankruptcy process to shield itself from these future payment obligations. This compounds the problems associated with the Convertible Note whose value rises and falls with GM stock and whose annual interest payment and return of principal could be blocked in bankruptcy.

Let me describe this process more fully. The new VEBA will take over health care obligations from GM on January 1, 2008. In theory, the new VEBA will have assets on hand on that date from several sources:

- The Convertible Note ($4.4 billion)
- Current assets of smaller existing GM VEBA's (value unknown)
- Diversion of promised wage and COLA increases to the new VEBA ($3.8 billion)
- A base payment ($1.8 billion)
- A "contingent cash payment" (amount unknown) and
- Annual Shortfall payments to be made if the VEBA does not have adequate funding to meet its obligations (currently valued at $1.6 billion)

However, GM can *at its discretion* stage up to $7 billion of this amount (including the Wages/COLA payment, the Base payment and the Shortfall payments) as far into the future as 2027. As an example, if GM elects to pay its obligations in those three categories in cash annually, it is projected in the MOU that in Year Five of the VEBA (2013) GM will owe an annual payment to the VEBA of $631 million, assuming a Shortfall payment is required. If GM in that same year wanted to pay down its entire future obligation to the VEBA it would have to pay $7.3 billion.

Since those future payments are to be made in cash they are subject to GM having the cash on hand to make the payments. In addition, as liabilities of GM they could potentially be cancelled if GM declares bankruptcy, thus leaving the VEBA on its own without sufficient assets to meet the health care needs of UAW retirees.

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