The Regulatory Studies Program (RSP) of the Mercatus Center at George Mason University is dedicated to advancing knowledge of the impact of regulation on society. As part of its mission, RSP conducts careful and independent analyses employing contemporary economic scholarship to assess rulemaking proposals from the perspective of the public interest. Thus, this comment on the Department of Labor’s proposed rule, *Labor Organization Annual Financial Disclosure Reports*, does not represent the views of any particular affected party or special interest group, but is designed to evaluate the effect of the Department’s proposals on overall consumer welfare.

This comment is organized such that Section I provides a brief introduction to the proposed rule. Section II provides some economic background to the rule and our analysis of it. Section III reviews the main benefits ascribed to the proposed rule. Section IV discusses the cost estimates developed by the Department, while Section V provides an alternative estimate of rule-associated costs. Section VI provides various benchmarks against which the cost estimates can be compared and placed into a larger context.

I. Introduction

Under the *Labor-Management Reporting and Disclosure Act of 1959* (or, the “Landrum-Griffin Act”), the Employment Standards Administration (ESA) within the Department of Labor is seeking to reform the financial disclosure requirements applicable to organized labor. The Department’s purpose in reforming the reporting requirements applicable to labor organizations is “to improve the transparency and accountability of labor organizations to their members, the public, and the government; to increase the information available to members of labor organizations, and to make the data disclosed in such reports more understandable and accessible.”

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1 Prepared by Jay Cochran, Research Fellow, Regulatory Studies Program. This comment is one in a series of Public Interest Comments from Mercatus Center’s Regulatory Studies Program and does not represent an official position of George Mason University.


3 *ibid.*, p. 79280.
More than forty years have passed since enactment of the Landrum-Griffin Act, and only once in that time have the reporting procedures applicable to organized labor undergone any appreciable change. The Department suggests it may once again be time to reform reporting requirements, especially in light of the myriad technological changes affecting both organized labor in general and financial reporting in particular.

Some of the reforms the Department seeks under the proposed rule include: (a) an electronic filing requirement for labor organizations reporting financial disclosures using Form LM-2; (b) identification of “major” receipts and disbursements; and (c) reporting of assets, liabilities, receipts, and disbursements of organizations with annual receipts of $200,000 or more that meet the statutory definition of a “trust in which a labor organization is interested.”

Before discussing the specific benefits and costs of the Department’s proposed rules, we provide some basic background on the economics of organized labor. Doing so will establish an important contextual foundation for the remainder of our comment on the proposed rule.

II. Economic Background

Normally, when an executive branch agency considers the implementation of a new regulation, our first question asks whether a significant market failure exists that merits federal regulatory attention. Clearly, such an argument cannot be advanced in the present case. The most one can claim is that a regulatory or government failure exists, and that the present regulation is an attempt to remedy part of that failure. This conclusion rests on and results from the basic political economy of organized labor.

Unions are customarily treated in microeconomic theory as monopoly suppliers of labor in a particular industry or trade, with the attendant reduction in labor supply and increase in wage rates characteristic of a typical industrial monopoly. The precise combination of wage rate increases and labor supply reductions remains a function of union goals (e.g., maximized union employment, capture of economic rents, or maximization of total union wage

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4 Late in 1992, changes to union reporting requirements were implemented that increased the classification detail of disbursements. This rule, however, was rescinded in December 1993.

5 According to the Department, Form LM-2 currently applies to labor organizations with $200,000 or more in annual receipts (p. 79290). The Department estimates that Form LM-2, therefore, applies to 5,514 labor organizations. An additional 21,398 other labor organizations fall below this $200,000 threshold and will have to file the simpler LM-3 or LM-4 forms. Another 3,551 “trusts” or organizations or funds held by multiple labor organizations will be required to file a modified form T-1. (See also Table 2, p. 79297.)

6 ibid., p. 79280.

7 See the Mercatus Center Regulatory Checklist, where we ask whether (i) a market failure has been identified by the regulating agency; (ii) a federal role has been appropriately established; (iii) the agency examined alternative approaches; (iv) the agency attempted to maximize net benefits; (v) there is a strong scientific or technical basis for the regulation; (vi) the distributional effects are clearly understood; and (vii) individual choices and property impacts are clearly understood. The checklist has been applied to the present rule, and the results of that evaluation are attached in an Appendix to this comment.
It is crucial to recall, however, that the monopoly position enjoyed by organized labor in the United States today is not a “natural” monopoly in the economic sense of that term, but rather arises from the various privileges and immunities awarded and protected by the federal government since about the time of the New Deal.

It is therefore difficult to make the case that the labor market has failed in any substantive sense with respect to organized labor given that it has not been allowed to function without impediment. Rather what we are presented with in the current set of regulations is an effort to curb the more egregious financial practices of some unions—practices that have emerged, in part, by virtue of their specially protected status. In other words, the present set of regulations attempts to correct and control abuses stemming from a previous set of laws and regulations that distorted the operation of the labor market and in effect opened the door to such abuses in the first place.

It is perhaps unreasonable, therefore, to expect this set of regulations for enhanced financial disclosure to achieve its intended aim, since the problem is not with financial disclosure per se, but rather with the market distortions created by government interference in the labor market. Nevertheless, this should not be taken as disparaging the effort entirely; inasmuch as if the latter path (i.e., restoration of free contract in labor) is not currently a viable option, then curbing the more egregious abuses attendant with monopoly labor supply may be a second-best course of action.

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9 See, for example, Morgan Reynolds (1987), Making America Poorer: The Cost of Labor Law, Washington, D.C.: Cato Institute, pp. 15-25. Reynolds draws a useful distinction between privileges (i.e., special rights conferred on organized labor that are unavailable to other members of U.S. society), and immunities (i.e., actual exemptions from law that are similarly unavailable to others in the U.S.). The National Labor Relations Act of 1935 (“Wagner Act”), for example, provides that employers must bargain in “good faith” with “duly elected” union representatives. Union representatives, in turn, may require compulsory dues payments from non-members, and may provide collective representation to those who wish no such representation. The Wagner Act in effect gives unions the privilege of representing both those who wish to be so represented as well as those who do not wish such representation and to collect dues from both parties.

By contrast, the Clayton Act of 1914 and the Anti-Injunction Act of 1932 (“Norris-LaGuardia Act”) exempt unions from antitrust laws, immunize them against federal court injunctions, and grant immunity from private civil damage suits. In addition, the Anti-Racketeering Act of 1934 specifically exempted unions from anti-racketeering laws. (The Hobbs Amendment attempted to overcome this exemption, but was unsuccessful on subsequent Court challenge, when the US Supreme Court upheld the use of union violence to achieve legitimate labor goals, saying, “the [Hobbs] Act does not apply to the use of force to achieve legitimate labor ends”—as quoted in Reynolds [1987, p. 23].)

Lastly, to curtail some of the unintended consequences of pro-labor legislation, Congress sought to reign in organized labor through the Labor-Management Relations Act of 1947 (“Taft-Hartley Act”) and the Labor-Management Reporting and Disclosure Act of 1959 (“Landrum-Griffin Act”). As Reynolds (1987, p. 21) points out, shortly after the passage of the Wagner Act, “Government regulation expanded to deal with some of the effects of union power, largely created by privileges and immunities.” Expansion of the regulatory requirements on organized labor under the Landrum-Griffin Act, in fact, is the subject of the present set of regulations.
The specific problem the present regulation attempts to remedy is a variant of the principal–agent problem: in particular, an information asymmetry between the principal (labor) and his/her agent (union officials). This asymmetry emerges largely because the usual set of market checks and balances has been attenuated in the case of organized labor. Under present disclosure standards, it is difficult, and in some cases impossible, for the principals to know the applications to which union funds and other resources have been put, due to the opaque and infrequent nature of union financial disclosure statements.

Without meaningful external checks on an agent’s financial decisions afforded by vigorous market competition for resources (including membership), it becomes easier to understand the increased frequency of self-dealing, embezzlement, or other problems that have checkered the history of organized labor. Such undesirable behavior need not, however, be the case. Controls to prevent or uncover financial abuses can arise out of the natural operation of market competition for resources or, failing that course, can be brought about through the deliberate design and application of regulations.

III. Benefits Attributed to the Rule

The Department lists three main benefits from the reform of union financial disclosures:

- Better reporting will allow union members to make better decisions about the governance of their unions.
- More-detailed financial reporting will make it more difficult to hide fraud.
- More-detailed reporting will provide an effective deterrent to financial mismanagement.

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10 That is, because of the privileges granted by US labor laws, such as compulsory collective bargaining and representation, a union does not have to compete for its membership or income stream. Because of the immunities that unions enjoy, organized labor does not have to rise to the same standards of conduct as other members and institutions of US society.

11 This is not to suggest either that such temptations do not occur when competition is vigorous. They do. The point, however, is that such problems tend to be caught more quickly, and the damages that result are contained more efficiently under competition than without it.

12 The regulatory approach is necessarily a second-best alternative since it is impossible to design a regulatory apparatus that foresees every eventuality, and because those subject to regulation innovate along non-regulated dimensions as well as in the necessarily “grey areas” of any rule.

13 The Department and ESA suggest that increasing the volume of financial disclosures made by labor organizations will provide “union members with useful data that will enable them to be responsible and effective participants in the democratic governance of their unions.” (p. 79281)

14 The Department suggests “the broad aggregated categories on the existing forms made it possible to hide embezzlements, self-dealing, overspending, and financial mismanagement.” (p. 79282)

15 “…detailed reporting can be an effective deterrent, and that more detail throughout the form LM-2 would further discourage malfeasance.” (p. 79282)
A. More-Informed Governance Decisions

To be sure, more disclosure has the potential for union members to make more informed decisions about their union. However, the Department may be making an overly strong benefit claim when it states, “If the members of labor organizations had more complete, understandable information about their union’s financial transactions, investments, and solvency, they would be in a much better position than they are today to protect their personal financial interests and exercise their democratic rights of self-governance.”\(^\text{16}\)

This unqualified statement can be incorrect if union members suffer from other impediments to effective action beyond a simple lack of information. Indeed, just having more information may not necessarily be beneficial by itself if individuals, for example, bear concentrated costs of taking action arising from their evaluation of financial information, while the benefits accruing from such action remain dispersed among the union membership as a whole.\(^\text{17}\) If concentrated personal costs and dispersed benefits exist, then it does not follow that individual union members will automatically be in any better position today from increased disclosure.

It is important to stress, however, that this line of reasoning does not argue against increased disclosure and improved transparency. Increased disclosure is more likely than less disclosure to bring about improved transparency; however, it will not automatically do so, and overly strong benefit claims may not advance the case for improved disclosure in any event.

B. More-detailed financial reporting will make it more difficult to hide fraud

We concur with the Department’s assessment that in comparison to the current reporting requirements on labor organizations, more detailed financial reporting will tend to raise the cost of hiding fraud. By increasing the number of classification categories, lowering the dollar level of disclosures, and by potentially increasing the number of people who must participate in a potential fraud, the revised reports sought by ESA and the Department should make committing fraud more costly than it is under current disclosure rules.

\(^{\text{16}}\) Proposed Rule, pp. 79280-79281.

\(^{\text{17}}\) It is possible, for example, to imagine a case where a union member—through her own analysis of union finances, made possible by the proposed regulation—uncovers financial mismanagement. However, because of intimidation (physical violence or threats of same), she has to bear substantial personal costs unless she remains quiet. If, on the other hand, she successfully pursues her discovery, the benefits of better union management will be bestowed not just on her, but also on all the members of her union.

This example should not be taken as arguing that union members should or should not pursue discoveries of mismanagement as and when they find them, nor that enhanced disclosure should not be in place to facilitate such potential discoveries. Rather its purpose is merely to illustrate the concept of concentrated costs and dispersed benefits, and how such a situation can present a barrier to acting on information that will not always be solved by the provision of more information.
C. More-detailed reporting will provide an effective deterrent to financial mismanagement

Since more-detailed financial reporting is likely to raise the cost of committing fraud, less financial mismanagement can be a likely outcome, other things being equal. This result occurs because the potentially dishonest respond to incentives just as the honest do, and therefore by raising the cost of committing fraud, one can reasonably expect to see less of it. Despite this basic economic relationship, however, we would hasten to add that deterrence per se, is not simply a matter of increased or more-detailed disclosures. Rather, it can be argued that disclosure is instead a necessary but insufficient precondition for effective discovery and deterrence of financial mismanagement.

The Department seems implicitly to understand that a more involved process of deterrence operates than simply more-detailed reporting. In the proposed rule, it cites a recent case in which “the lack of supporting detail [on expenditures] enabled [union] officials to hide in excess of $1.5 million in personal dining, drinking and entertainment expenses from 1992 to 1999.”18 The important attribute to consider in this case, though, is not that certain officials hid their misappropriation of funds, but rather that it was a Departmental investigation that uncovered the fraud, and that this discovery, moreover, occurred within the current environment of comparatively poor disclosure.

In other words, actual deterrence of financial mismanagement is more difficult in an organized labor setting than in a comparable competitive setting for reasons outlined earlier, and because fewer checks on the financial performance of unions occur on a regular basis. This means improved financial disclosure is an important component of the overall deterrent process, but it is not all. We would add that examinations of financial data by interested parties (union members, journalists, citizens, etc.); regular audits by disinterested accounting professionals; and periodic investigations by appropriate Department personnel are other important tools that complement and complete any enhanced disclosure process aimed at deterring financial mismanagement.

1. Disclosure Thresholds

To enhance the disclosure process and to deter mismanagement, the Department establishes minimum disclosure standards for various balance sheet and income statement items.19 At several places throughout the proposed rule, the Department asks for comment on whether

18 Proposed Rule, p. 79282.

19 The new LM-2 for example, requires attachment of an accounts receivable aging schedule recording any individual or entity from which more than $1,000 is due. A similar schedule (and threshold) is applied to accounts payable. All investments with a market value of at least $5,000 (or representing more than 5% of the total market value of all investments) must be reported on a separate schedule to the LM-2. Similarly, disbursements to employees totaling more than $10,000 in a reporting period, and all disbursement to officers must be documented in attachments to the required filings. Receipts and disbursements to any individual or entity totaling more than $5,000 during the reporting must also be separately reported. See the Proposed Rule, p. 79285–79289.
these specifically proposed dollar thresholds of disclosure are set at appropriate levels. Given the operational peculiarities of individual unions as well as their wide disparity in sizes, it is probably impossible to determine an appropriate level of disclosure for all unions under all circumstances.

To resolve the threshold issue while still recognizing the likelihood of important differences among the various unions, we suggest that the Department may wish to consider implementing a disclosure standard based on whether an outside observer (i.e., a reasonable person unconnected with the union) would consider a given disclosure material to an accurate understanding of a labor organization’s financial position. Implementing a materiality standard (similar to the standard that exists with regard to corporate disclosure and auditing standards) helps to resolve the Department’s issues with respect to absolute disclosure levels.

Admittedly, a materiality standard introduces an element of judgment in the reporting process and has the potential to complicate the investigative process. However, such tradeoffs seem no worse than establishing what are in fact arbitrary reporting thresholds and then applying those thresholds in a one-size-fits-all fashion to every labor organization.20

IV. Department Cost Estimates of the Proposed Rule

The Department estimates that the proposed changes to the four financial disclosure forms (LM-2, LM-3, LM-4, and T-1) will be $17.8 million in the first year, $5.8 million in year two, and $5.3 million in year three.21 These costs result from increased recordkeeping and reporting burdens, software changes, training and so on, that the unions will incur in order to comply with the proposed rule. In addition, the Department estimates that the Federal government will incur incremental equipment, personnel, and overhead expenses of $7.2 million per year in connection with implementing and overseeing the new rule.22 Below we offer comments on the Department’s estimates.

A. Very Precise Burden-Hour Estimates

We congratulate the Department for being able to make such precise burden-hour estimates for over 26,000 unions and over 3,000 trusts. However, precision carried out to two decimal

20 It is possible also to address (at least partly) a one-size-fits-all criticism to disclosure thresholds by assigning differing thresholds based on union size (using assets, receipts, membership, or other appropriate measures). Doing so lifts the judgment burden regarding disclosures that exists under a materiality standard from the unions and places it on the Department. In addition, a disclosure threshold that varies with union size reflects an acknowledgment that there are likely to be important differences among unions as to what constitutes a material disbursement, investment, accounts receivable and so on.

In sum, an explicit regulatory threshold places an ex ante judgment burden on the regulators to establish appropriate thresholds that are neither too rigid nor too lax. A materiality threshold, by contrast, places an ex post judgment burden on the disclosing union and its auditors.

21 Proposed Rule, p. 79293.

22 Loc. cit.
places does lead one to wonder whether it is reasonable to assume that the 8,108 unions filing form LM-4, for example, will incur precisely 0.03 hours (or 1.8 minutes) of on-going recordkeeping burden in connection with the rule.\textsuperscript{23}

We would suggest in the alternative that if the actual incremental burden is negligible, then zero should be used. If, however, there is expected to be some non-trivial increase in on-going recordkeeping burden, more defensible estimates would consider making allowances for error and correction, for personnel time to recall proper classifications, and so on. In other words, additional recordkeeping rules mean that those responsible for implementing such rules may be likely to incur additional, non-trivial amounts of time in on-going recordkeeping procedures if such recording is to be undertaken accurately.

Perhaps just as important in this connection is the recognition that on-going recordkeeping functions with respect to the new requirements are likely to exist beyond the confines of a union’s accounting department. Thus, for example, when a union organizer hosts an educational program and then seeks reimbursement for her expenses, she will have to consider and follow the rule’s requirements pertaining to documentation, record retention, appropriate expense classification, and so on (and the new rules are likely to be different from and more complicated than the rules she has been accustomed to observing).\textsuperscript{24} Such burdens, though perhaps small for any given accounting event, and likely to be dispersed across many people throughout an organization, nevertheless seem unlikely to be as small in the aggregate as the Department suggests in its recordkeeping burden estimates for the various forms.

In the alternative estimates we provide below, we have used small (though non-trivial) hourly estimates for on-going recordkeeping burdens. With respect to burden estimates more generally, we have chosen to provide round figures (typically rounded to nearest half working day) rather than very precise estimates. The rationale for such an approach is to produce cost estimates that are defensible in general magnitude rather than in particular exactitude.

\textbf{B. Inconsistent Cost/Burden Hour Applied}

Laying aside the issue of burden-hour estimate precision, and taking the total burden hours estimated by the department at face value, we are still left with the application of inconsistent dollar costs per hour to the burden-hour estimates themselves. For example, the Department estimates that the new LM-2 form will entail total reporting and recordkeeping burdens of 579,135 hours. Dividing this figure into the Department’s total cost estimate for the LM-2 form ($14.618 million) yields an hourly cost of $25.24. Similar calculations for the LM-3,

\textsuperscript{23} Proposed Rule, Table 2, p. 79297.

\textsuperscript{24} The new rules might suggest that such costs are learning curve related and thus unlikely to recur once the learning is completed. While there is, no doubt, some truth to that assertion, it also seems equally likely that a changed institutional environment is likely to involve changes of permanent nature.
LM-4, and T-1 forms yield per hour cost estimates of $20.36, $24.79, and $26.61 respectively.\textsuperscript{25}

In its description of the burden estimates, the Department suggests that little beyond incremental labor will be required by the unions to comply with the new disclosure requirements.\textsuperscript{26} If this is true, then the hourly rates used to monetize the hourly burden estimates, arguably, should be more consistent. In our cost estimates, presented below, we have applied instead an hourly labor rate of $27.80, which represents the fully loaded hourly wage rate of union employees in the United States.\textsuperscript{27}

C. Little Documentation Of The Government’s Own Incremental Costs

The Department estimates that incremental costs to the federal government of changing the reporting requirements for unions are $7.187 million per year. It suggests that this estimate “includes operational expenses such as equipment, overhead, and printing, as well as salaries and benefits for the OLMS staff in the National Office and field offices that are involved with reporting and disclosure activities. The estimate also includes the annualized cost for redesigning the forms, developing and implementing the electronic software, and implementing digital signature capability.”\textsuperscript{28} Without any supporting documentation or detail of the data included in the Department’s estimate, it is impossible to validate this figure, or to offer an alternative estimate. In our alternative estimates (see below), we have simply adopted the Department’s estimates of incremental governmental expenses related to the rule.

D. No Capitalization of Cost Estimates Provided

Although the Department displays a high level of precision in developing its compliance burden estimates, nowhere does it capitalize the cost estimates that it does generate. The sum of the discounted present value of all the cost streams is important so that the proposed rule can be evaluated against other alternatives with potentially different time dimensions as well as to give policymakers an indication of the total lifetime costs of a particular rule.

\textsuperscript{25} The hourly rates also change without explanation for subsequent year estimates for forms LM-2 and T-1.

\textsuperscript{26} In calculating the burden for form LM-2, for example, “the Department carefully considered the amount of time it takes to: (a) Read the reporting instructions; (b) gather the books and records to respond to various reporting requirements; (c) organize the books and records to respond to various reporting requirements; (d) complete the form; and (e) check the responses.” (Proposed Rule, p. 79294) This suggests the burden-hour estimates consist almost entirely of labor hours. This perception is further reinforced when the Department states, “…any capital investment including computers and software that are usual and customary expenses incurred by persons in the normal course of their business are excluded from the regulatory definition of burden.” (Proposed Rule, p. 79294)

\textsuperscript{27} This figure includes wage and salary payments, fringe benefits, as well as Social Security, unemployment insurance, and workers compensation payment paid on behalf of a union employee. \textit{Source:} Statistical Abstract of the United States (2001), Table 626, “Employer Costs for Employee Compensation per Hour Worked: 2001, p. 406. Union data taken from column 6 of Table 626.

\textsuperscript{28} Proposed Rule, p. 79296.
Capitalizing the Department’s annual cost estimates, using the OMB-suggested discount rate of seven percent, produces an estimated lifetime cost of the rule of $212.5 million. About $103 million of this figure represents capitalized government-incurred costs of the rule, while the remaining $110 million represents the long-run compliance costs incurred by the labor organizations themselves.

V. Alternative Cost Estimates of the Proposed Rule

Appendix I details the sources and methods used to estimate the costs of the Labor Department’s enhanced financial disclosure regulation. In short, however, it is estimated that the lifetime cost of the rule will be roughly $298 million, including the incremental costs to the government to administer and enforce the new standards. Capitalizing the up-front and annually recurring costs using OMB’s recommended 7 percent discount rate produced this estimate.

In the first year of application, the revised form LM-2, LM-3, LM-4, and T-1 are estimated to result in compliance costs of $63.3 million for the more than 26,000 affected labor unions and 3,500 labor-related trusts in the United States. In the second year, estimated total compliance costs are expected to decline to $19.9 million, while costs in the third and succeeding years are expected to total $9.0 million each year. With respect to incremental cost of administration and enforcement for the federal government, we adopted the estimates made by the Department of $7.2 million per year.

A. Differences Explained

The two main areas that account for the difference between our estimates and the Department’s are (1) the number of hours for reporting and record keeping expected to be incurred by the average union organization, and (2) the application of a consistent (and higher) labor rate per hour. The change in the number of hours estimated for reporting and recording keeping (mostly in form of rounding and more generous allowances for initial compliance) accounted for roughly three-fourths of the deviation between our estimate and the Department’s. The remaining one-quarter of the difference can be accounted for by the application of a standardized labor-hour rate. We believe these adjustments provide a more generous estimate of both burden hours and costs likely to be incurred by the affected labor organizations.

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29 We applied the 7 percent discount rate assuming that the first year’s compliance costs would be back-end loaded; that is, incurred mostly toward the end of the first year in which the rule was applicable. Thus, the first year’s costs are not discounted, while the second year’s costs are discounted one period. Third and subsequent year’s costs were then assumed to recur. To arrive at a capitalized cost for these out-year estimates, the recurring costs were first annuitized back to the third year, and then the annuitized sum was discounted back for two periods at the seven percent rate.
B. Average Cost per Union

The Department estimates that 26,912 unions and 3,551 labor trusts will be affected by the changed financial disclosure regulations. Based on our estimates of lifetime costs to the unions (and ignoring incremental costs to the federal government), the average union will bear a cost of approximately $4,715 to comply with the new disclosure requirements, while the average labor-related trust will bear a long-run cost of $19,035 to comply.

Averages can be misleading since they can obscure large variances among the different organizations. This suggests costs may be disproportionately higher for larger unions. However, averages are supplied so that some standardized comparisons can be made to other organizations that disclose financial information on a regular basis.

VI. Cost Estimate Context

This section provides several different ways to put the various compliance cost estimates of the rule into context.

A. Comparison to Union Estimates

The long-run cost estimates provided in this comment were about 40 percent higher than a capitalized version of the Department’s estimates. Our estimates, however, remain at the low end of published reports of cost estimates made by union representatives. Laurence Gold, associate general counsel to the AFL-CIO suggested, for example, in a recent Associated Press story “the accounting and recordkeeping changes could cost unions $250 million to $1 billion.”

Observing that there are 26,912 unions and 3,551 trusts covered by the new rule, the average compliance cost—using the AFL-CIO’s estimates—ranges from about $8,200 to just under $33,000 per covered labor organization.

B. Comparisons to Corporate Disclosure Costs

Comparing the unions’ disclosure costs to the costs incurred by other agents as they report to their principals provides another means of putting the rule’s compliance costs into context. U.S. corporate managers (agents), for instance, regularly disclose their financial performances to shareholders (principals) through corporate annual reports, among other means. In calendar year 2001, it is estimated that the 12,000 public corporations in the U.S. communicated with their shareholders through corporate annual reports at a cost of slightly

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30 Leigh Strope, “Proposed Regulations Would Require Unions To Open Books, Report More Financial Detail,” Associated Press, Washington, December 21, 2002. It was unclear from the AP story whether Mr. Gold was referring to annually recurring costs or lifetime costs of the rule. Given the context of the other estimates herein, the latter case seems more likely.

31 See Table 2, Proposed Rule, p. 79297.
more than $9.0 billion. These annual report production and distribution costs represented an average disclosure cost per corporation of slightly more than $750,000 in 2001, or about 23 times more than the AFL-CIO’s own worst-case cost estimate.

C. Cost per Union Member of Enhanced Disclosure

The capitalized Department-estimated cost of the detailed financial disclosure (or $110 million, which excludes the additional $103 million of federal government costs for implementation and enforcement) represents an average cost of $6.15 per union member. By comparison, our cost estimates yield an average long-run cost of $10.88 per member. Even using the AFL-CIO’s high-end estimate of $1.0 billion produces a cost estimate for more detailed disclosure of $55.94 per union member (while its low-end estimate works out to an average cost per member of $13.99).

Regardless of which estimate proves closest to being correct, the decision of whether or not this cost provides a positive value to individual union members is a question only individual members can answer. However, we can say that given our estimate of lifetime costs for enhanced disclosure represents about 24 minutes of the average US union member’s hourly pay rate, many may consider it bargain—but only if the new rules deliver the benefits the Department suggests they will.

D. Compliance Costs in Relation to Union Receipts

A sampling of union receipts (from dues, services, etc.) per union member can also help to put the rule’s estimated compliance in perspective. Consider, for instance, that the Auto Workers Union (AFL-CIO) as of December 2001 reported on its LM-2 form that it had 701,818 members and total receipts of $328.7 million, or roughly $468 in receipts per member that year. Even if the worst case prevailed and compliance costs totaled one billion dollars, resulting in average compliance costs of $55.44 per union member, that would still represent about 12 percent of one year’s UAW average, per-member receipts. On the other hand, if our estimates or the Department’s are closer to the mark, the lifetime costs of

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32 Glenn Hasek (1997), “Adding Art to Numbers: Corporate Annual Reports,” *Industry Week* 246: 21, p. 122. In this article Hasek cites Sid Cato, publisher of the *Newsletter on Annual Reports*, who states “more than 12,000 U.S. companies generated an average 232,000 copies of annual reports for 1996 at a cost of approximately $3 per copy.” Mr. Cato updated his estimate for 2001 in a news release stating that average per-copy investment in 2001 annual [reports] was $3.24...” From a news release dated November 1, 2002, taken from [http://www.sidcato.com/news/2002/rel11102.html](http://www.sidcato.com/news/2002/rel11102.html). These per-copy figures include printing and distribution costs, but not other costs such as executive and employee preparation time, related capital investments, etc.

33 As stated above, the Department did not capitalize its cost estimates. Therefore, we capitalized their estimates by applying OMB’s suggested 7 percent discount rate to the various estimates of annual costs. Estimates of third year costs were treated as subsequently recurring into the indefinite future. The bulk of first year costs were treated as having been incurred near the end of first year in which the rule was applicable; therefore, year one’s costs were not discounted.

34 Data taken from the Department’s financial reporting database, at the Office of Labor-Management Standards, at [http://www.union-reports.dol.gov](http://www.union-reports.dol.gov). The search criteria were for national/international unions with total receipts greater than $200,000 per year for the latest reported data.
the rule would equate to roughly 2 percent of average per member receipts for the Auto Workers’ Union in 2001.35

35 The Auto Workers have neither the highest nor the lowest per member receipt totals, based on our search criteria of the Department’s database. The Air Line Pilots Association (AFL-CIO), for example, reported total receipts as of December 2001 of $274.0 million and 54,513 members, yielding average per member receipts of $5,026. By contrast, the Catholic School Teachers Association (an independent union) reported total receipts of $307,149 as of August 2001 and 4,762 members, giving it average per member receipts of just $65. Even in the case of Catholic schoolteachers, our compliance cost estimate amounts to roughly 14 percent of their reported 2001 receipts. These compliance cost estimates, moreover, reflect lifetime costs of the rule and thus represent costs that would not be borne in any one year, but rather represent costs that would be spread out over several years.
APPENDIX I
COST ESTIMATES OF THE DEPARTMENT OF LABOR’S
PROPOSED LABOR ORGANIZATION FINANCIAL DISCLOSURE RULE

I. Compliance Burden Estimates

Form LM-2 involved the most significant changes and increases in supporting data to be provided. In the estimates that follow, our general procedure was to opt for burden estimates rounded to the nearest half working day, under the assumption that general orders of magnitude rather than precision are the best estimating outcome that one can hope to achieve. In addition, our estimates do not include any burden or cost estimates for legal oversight such as legal review of the regulation’s applicability or subsequent compliance assurance before filing.

A. First Year Compliance Burden Estimates

1. Install New Software

We allocated one-half working day (i.e., four hours) for software installation. Though the software installation itself should be fairly rapid and uncomplicated, additional time is allotted to allow for unanticipated bugs, incompatibilities, or to installation of additional software utilities and/or hardware as may be required to make a fully functional system.

2. Design/Adjust Report Forms and Format Structures to Comport with Regulatory Requirements

Electronic data processing systems simply store and facilitate the manipulation of basic accounting data, and though such systems greatly ease reporting in comparison to manual systems, one cannot necessarily conclude from this that little or no incremental effort is involved to comport with new or modified regulatory reporting requirements. That is, new or significantly modified reports are likely to be necessary in order to reflect the changed regulatory requirements.

We estimate that because of the detail involved in the seven new schedules on the LM-2, for example, each additional report will require at least one working day to design new output reports that follow the regulatory forms’ requirements. This new burden is in addition to the 15.25 hours the Department estimates that it already takes to complete the forms, as they exist currently. In addition, although the new LM-2 also saw a net reduction in the number of questions asked by the Department, those reductions nevertheless represent changes to existing procedures that will have to be incorporated into new reporting practices. Therefore, we retain the Department’s original estimate of 15.25 hours (rounded up to an even 16 hours, or two working days) and add to it the allowances described above for the new supporting schedules, resulting in an estimated total of 72 hours to design and reformat output reports.
3. **Modify Existing Accounting Systems and Interfaces**

Beyond reconfiguring and adding new accounting output reports, adjustments will also likely be required to the accounting systems themselves. Such adjustments may include addition of or modification to audit trails (to track why data were changed or accessed and when), time to adjust accounting procedures to reflect new regulatory thresholds (such as the changed minimum levels for disbursement tracking, investments, and so on), and time to implement data exporting features into the Department-provided software (e.g., e.LORS) or into similar reporting systems from the existing accounting programs. Additional time should also be allowed to accommodate the adjustment of any documentation retention policies and to communicate these policies to appropriate union personnel. We assumed these tasks could be completed, on average, in four working days, or 32 hours.

4. **Incorporate Electronic Signatures**

We assumed that two working days at a minimum would be required to incorporate electronic signatures into the reporting documents filed with the Department. This time includes not only incorporation of the signatures themselves, but also time to test and verify the security features of this application. As with any new technology, time estimates are only rough approximations. Substantially more time may be required to implement this new and unusual feature successfully and to ensure its overall integrity as part of the reporting system.

5. **Validate and Reconcile Reported Output; Systems Testing**

Reports, supporting schedules, and other output will have to be compared to known-good data sources in order to validate that the reports are producing reliable and accurate output. Inevitable discrepancies will have to be reconciled and corrective procedures implemented. In addition, the overall system will need to be tested to ensure smooth integration and functioning of all subcomponents. We allotted three working days to complete the validation processes for the new reports. Although this procedure is classified as a reporting function, it can also result in increased recordkeeping costs if records have to be revised as a result of errors uncovered during a reconciliation process.

6. **Employee Training**

We assumed that, on average, four accounting and/or regulatory compliance staff members would require training for two full working days (i.e., at 8 hours per day per person). Large unions are likely to incur proportionately more training costs in order to ensure that enough personnel are proficient in the new reporting requirements. Conversely, smaller unions are likely to see proportionately smaller training requirements.

**B. Second Year Reporting**

We made a simplifying assumption that, on the average, LM-2 report filers would be able to ascend 80% of the learning curve toward their final and best efficiency, with best efficiency being achieved in year three. In other words, although filers are expected to be much more efficient in year two than in year one, they will not reach peak efficiency until year three.
Subsequent years beyond year three are assumed to see reporting burdens similar to those occurring in year three.

C. Third Year Reporting

By year three, we expect that unions filing form LM-2 will have become proficient at doing so and will require approximately 24 staff hours to complete the reporting required by the revised form. This figure represents an augmentation to the time estimated to complete existing forms. The Department estimates that it currently takes 15.25 hours to complete the LM-2 including its 15 supporting schedules. By adding 7 new and schedules, the Department has increased the simple volume of schedules by nearly 50 percent. In a few cases, moreover, the new schedules have the potential to be quite lengthy (e.g., the accounts receivable aging schedule, as well as the investments, receipts, and disbursements detail schedules). While it is true that the Department has shortened some of the existing up-front questions and data classification requirements, the largest incremental increase in reporting and record keeping seems likely to occur as a result of these new schedules.

We have, therefore, conservatively added one hour per new schedule to the existing estimate of 15.25 hours giving a total slightly less than 23 hours, on average, to complete LM-2 (once the institutional learning curve has been ascended). We then rounded our estimate up to the nearest whole working day, or 24 hours, consistent with our view that precision is not as important as general orders of magnitude.

D. LM-2 On-going Recordkeeping Estimates

We estimated that incremental changes to record keeping requirements would total approximately one additional working day on average. These estimates reflect our belief that on-going recordkeeping functions with respect to the new requirements are likely to exist beyond the confines of the union’s accounting department—e.g., for anyone disbursing or receiving funds for example, who now must keep more-accurate records regarding where such funds were disbursed to or from whom such funds were received. These additional burdens, though probably small for any given accounting event, and likely to be dispersed across many people throughout a labor organization, nevertheless seem equally likely to sum to non-trivial amounts in the aggregate. This on-going recordkeeping burden is expected to persist at one working day, moreover, for years two, three, and beyond.

II. Form LM-3 Burden Estimates

The changes to the LM-3 form are minor. The requirements as to who must file a Form LM-3 have been changed, as has the requirement for increased disclosure if an LM-3 filer had an interest in a trust to which the filer contributed more than $10,000 in a given year. Since these changes are minor, we assumed that initial reporting burdens (software changes, report adjustments, training, and so on) would amount to one additional working day per union filing the LM-3. As the LM-3 union became more proficient in year two, this burden would be expected to drop to 2 hours, and then to one-half hour by year three and beyond.
On-going record keeping requirements may be expected to total one hour in the first year and at most an additional half an hour in succeeding years.

III. Form LM-4 Burden Estimates

The changes to form LM-4 are as minor as for LM-3. Therefore, we assumed that initial reporting burdens (software changes, report adjustments, training, and so on) would amount to at most one additional working day per union filing the LM-4. Moreover, as the union became more proficient in year two, this burden would be expected to drop to 2 hours, and then to one-half hour by year three and beyond.

On-going record keeping requirements may be expected to total one hour in the first year and at most an additional half an hour in succeeding years.

IV. Form T-1 Burden Estimates

In estimating the burden for filers of the T-1 form, we used the same estimates of reporting and record keeping burdens used for the revised LM-2 form. The justification for this approach is suggested by the Department itself, when it states, “The new T-1 is structured similarly to the LM-2.”

V. Summary Tables

The following tables summarize the cost estimates based on the preceding sources and methods. Table A.1 summarizes the estimated hourly compliance burden and resulting cost estimates, while Table A.2 summarizes the capitalized estimates of the data in Table A.1.

<table>
<thead>
<tr>
<th>Form</th>
<th>First Year</th>
<th>Second Year</th>
<th>Third Year &amp; Beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Hours</td>
<td>Cost</td>
<td>Hours</td>
</tr>
<tr>
<td>LM-2</td>
<td>1,305,040</td>
<td>$36,280.1</td>
<td>415,240</td>
</tr>
<tr>
<td>LM-3</td>
<td>116,266</td>
<td>$3,232.2</td>
<td>32,389</td>
</tr>
<tr>
<td>LM-4</td>
<td>72,972</td>
<td>$2,028.6</td>
<td>20,270</td>
</tr>
<tr>
<td>T-1</td>
<td>781,220</td>
<td>$21,717.9</td>
<td>248,570</td>
</tr>
<tr>
<td>TOTAL</td>
<td>2,275,498</td>
<td>$63,258.8</td>
<td>716,469</td>
</tr>
</tbody>
</table>

| Cost to Federal Government | $7,187.0 | $7,187.0 | $7,187.0 |

36 Proposed Rule, p. 79295.
### Table A.2
**Summary of Capitalized Cost Estimates**

<table>
<thead>
<tr>
<th></th>
<th>First Year</th>
<th>Second Year</th>
<th>Third Year &amp; Beyond</th>
<th>Discounted Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unions</td>
<td>$41,540.9</td>
<td>$12,156.6</td>
<td>$73,196.2</td>
<td>$126,893.7</td>
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<tr>
<td>Labor Trusts</td>
<td>$21,717.9</td>
<td>$6,458.2</td>
<td>$39,416.7</td>
<td>$67,592.8</td>
</tr>
<tr>
<td>Federal Govt.</td>
<td>$7,187.0</td>
<td>$6,716.8</td>
<td>$89,677.2</td>
<td>$103,581.0</td>
</tr>
<tr>
<td><strong>Total Capitalized Costs</strong></td>
<td><strong>$70,445.8</strong></td>
<td><strong>$25,331.6</strong></td>
<td><strong>$202,290.0</strong></td>
<td><strong>$298,067.5</strong></td>
</tr>
</tbody>
</table>
Appendix II  
RSP Checklist

Labor Organization Annual Financial Disclosure Reports; Proposed Rule

<table>
<thead>
<tr>
<th>Element</th>
<th>Agency Approach</th>
<th>RSP Comments and Grades</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Has the agency identified a significant market failure?</td>
<td>Although not clearly articulated, there is an implicit information asymmetry argument made throughout the proposed rule.</td>
<td>There can be no market failure if the market is not allowed to function. The unionized labor market in the U.S. has been thoroughly impeded by previous federal legislation and regulations. These previous impediments opened the door to the abuses that the present rule attempts to correct. Thus the present rule is in fact an attempt to remedy a government not a market failure.</td>
</tr>
<tr>
<td><strong>Grade: N/A</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Has the agency identified an appropriate federal role?</td>
<td>The Department cites the 1959 Landrum Griffin Act as the basis for its action.</td>
<td>Given the way unions have been organized since at least the New Deal, the federal role cited by the Department seems correct.</td>
</tr>
<tr>
<td><strong>Grade: A</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Has the agency examined alternative approaches?</td>
<td>The Department explores some alternatives with the context of the 1959 Act.</td>
<td>Within the confines of the legislation and within the proposed rule itself, the Department has identified some alternative approaches to, and thresholds within, the present rule. The Department could have been more thorough however in recognizing that deterrence of financial mismanagement is not simply a matter of better reporting, but is instead also a function of periodic audits and investigations. Regular validation of reported data, in other words, should be made part of the rule.</td>
</tr>
<tr>
<td><strong>Grade: B</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Element</td>
<td>Agency Approach</td>
<td>RSP Comments and Grades</td>
</tr>
<tr>
<td>---------</td>
<td>-----------------</td>
<td>-------------------------</td>
</tr>
</tbody>
</table>
| 4. Does the agency attempt to maximize net benefits? | The Department does not attempt to value the benefits attributed to the rule. It does however assign a dollar value to compliance costs. | Although we do not place a dollar value on the benefits either, we do attempt to put the costs of compliance into a variety of different contexts so that some evaluation can be attempted.  
**Grade: C** |
| 5. Does the proposal have a strong scientific or technical basis? | The rule has the potential for some scientific basis through the application of Generally Accepted Accounting Principles (GAAP). | It is possible that the Department’s job could be greatly simplified by drawing upon disclosure procedures already established under GAAP. Adjusting GAAP to the peculiarities on union finance might then constitute the Department’s marginal contribution to enhancing the disclosure process.  
**Grade: C** |
| 6. Are distributional effects clearly understood? | The Department seems to ignore distributional consequences among unions themselves. | By establishing single disclosure thresholds, the Department ignores potentially important differences among unions based on size. Thus, disbursements of less than $5,000, for example, may be material for small unions, but are not material for larger unions until a much higher dollar figure is disbursed. A uniform disclosure threshold for all unions glosses over these differences.  
**Grade: D** |
| 7. Are individual choices and property impacts understood? | The Department recognizes that the union members themselves are the owners (principals) and therefore have a right to know how the agents are performing on the owners’ behalf. | By recognizing that members who own the unions, and the public who confers the special privileges and immunities on them have a right to know the financial status of these organizations, the current rule is step in the direction of reasserting proper control over these organizations.  
**Grade: A** |