SENATE COMMITTEE ON LABOR

May 3, 1991 Hearing Room 50 03:00 p.m. Tapes 85 - 86
MEMBERS PRESENT:SEN. GRATTAN KERANS, CHAIR SEN. LARRY HILL, VICE-CHAIR SEN. PETER BROCKMAN SEN. BOB KINTIGH MEMBER EXCUSED: SEN. BOB SHOEMAKER STAFF PRESENT: ANNETTE TALBOTT, COMMITTEE COUNSEL ROBERTA WHITE, COMMITTEE ASSISTANT MEASURES CONSIDERED: SB 791- LEVERAGED BUYOUTS - PUBLIC HEARING

. These minutes contain materials which paraphrase and/or summarize statements made during this session. Onlv text enclosed in quotation marks report a speaker's exact words. For complete contents of the proceedings, please refer to the tapes.

TAPE 85, SIDE A

001 CHAIR KERANS calls the meeting to order at 3:16 p.m. and opens the public hearing on SB 791.

SB 791- LEVERAGED BUYOUTS - PUBLIC HEARING Witnesses: Cheryl Perrin, Fred Meyer Inc. Gerry Drummond, Oregon Investment Council. Irvin Fletcher, AFL-CIO. Brad Witt, Union Representative, Local 555 .

The Preliminary Staff Measure Summary is hereby made a part of these minutes (EXHIBIT A).

006 IRVIN FLETCHER, Oregon AFL-CIO: The Oregon AFL-CIO supports passage of SB 791 as written. As we understand the intent of the bill, the Legislature would establish an interim committee on state investment policy and direct the committee to study the impact of leverage buyouts and corporations and also to determine whether state investment in such corporations is good public policy. > 0regon AFL-CIO requested a similar bill in the 1989 session. >Believes the issue of whether it is good public policy to invest Oregon's public monies in leverage buy-outs of corporations which too frequently discharge thousands of workers as a consequence of buy-outs, is still with us. Senate Committee on Labor May 3, 1991- Page 2

Mr. Fletcher submits a Wall Street Journal article of May 16, 1990 (EXHIBll B).

035 BRADLEY WITT, Union Representative for United Food and Commercial Workers Union, Local 555, submits and reads a prepared statement in support of SB 791 (EXHIBIT C).

177 SENATOR KINTIGH: What happened (to wages) in Oregon?

180 MR. WITT: Oregon did not have the same experience because the membership was covered by a labor agreement. > There is no anticipation of wage reductions. · > There are demands on members which have created problems in the labor relations sector. The strike was in large part due to the question of whether or not the company would continue to fund health insurance. There are a number of other problems with the company since the leverage buyout. >We find Safeway trying to cut corners on its labor agreement and on a number of state and federal regulations. > Safeway is an entirely different company since the buyout. Issues discussed: > 0regon Investment Council invested in the RJR Nabisco buy-out which has created a best seller called "Barbarians at the Gate, the Fall of RJR Nabisco." > Profitability of Safeway stores

prior to buy-out. 270  GERALD K. DRUMMOND, Chairman, Oregon Investment Council, submits his biographical, professional and civic data and a prepared statement in opposition to SB 791 (EXHIBIT D) and calls the committee's attention to a letter sent to the committee by former Oregon Governor and State Treasurer Robert Straub, and the first chairman of the Oregon Investment Council, local businessman and former State Senator (EXHIBIT E).

MR. DRUMMOND reads his prepared statement and reviews the chart attached to his testimony of PERS investments with KKR (EXHIBIT D).

TAPE 86, SIDE A

015  MR. DRUMMOND continues reading his prepared statement.

A Wall Street Journal article, "Nostalgia for the 80's" and a paper prepared by Merton H. Miller were submitted by Mr. Drummond are hereby made a part of these minutes (EXHIBIT F).

128     CHERYL PERRIN, Vice President, Public Affairs, Fred Meyer, Inc.: Fred Meyer doesn't have a position on this bill. I am here today to give you some information about Fred Meyer and what has happened to our company since the LBO by KKR in 1981. At the time of the LBO in 1981, Fred Meyer was attracting unsolicited inquiries from potential acquirers. Following the death of Mr. Meyer in 1978, his controlling stock went into a trust designated in his will to be used as the basis for a charitable foundation. Something had to be done to convert the stock into assets suitable for use by the trust. Many inquiries were received from outside companies, including foreign companies, interested in acquiring that large block of stock. At the time KKR was making inquiries, there was a company from France that was prepared to come forward.



The only thing that stopped Fred Meyer at that time from being acquired by the French company was the fact that the president at the time froze the assets. The continuity of management because of the LBO allowed the company to continue its unique approach to one-stop shopping and to stay headquartered in Portland. Fred Meyer had many shareholders in 1981 who received a very solid return on their investments at the LBO price of $55 per share. Since the 1981 LBO, there have been no major asset dispositions and Fred Meyer has more than doubled in sized with growth primarily financed through the cash flow, proceeds from a public offering in 1986 and carefully managed bank debt.

·       When the LBO occurred at the end of 1981, Fred Meyer had 64 stores in four states totalling 6,123,000 square feet. Today the company has, as of June 1990, a total of 120  stores in seven states with a total of more than 12,200,000 square feet. This amounts to a 98 percent increase in store square footage. The company entered new markets with the acquisition in 1984 of Grand Central Stores from Salt Lake City, Utah. Between 1984 and 1986 Fred Meyer remodeled 17 of the 21 stores acquired. Since the 1981 LBO, Fred Meyer has completed 65 remodels of existing stores.

Capital expenditures through the 1990 year end for the corporation were $779 million since the 1981 buy-out. Oregon capital expenditures since 1981 were $389 million. Washington's were $248 million.

Fred Meyer sales have more than doubled from slightly over $1 billion in 198 1 to $2.476 billion in 1990. Revenue growth has exceeded 10 percent on a compounded annual basis. Earnings improved through 1990 going from $5.161 million for the full year of 1982 to $33.583 million in 1990. That is an increase of 551 percent and a compound annual growth rate of 26.4 percent per year.

Equity has increased from $51.9 million at the time of the buyout to $285 million at the end of 1990. During this period the company completed an initial public offering in October 1986 which generated equity proceeds of slightly over $63 million.

In 1981 the Fred Meyer total employment base was 10,739 employees in the four states. That included 6,904 Oregon employee. Today there are over 21,000 Fred Meyer employees with almost 12,000 in Oregon. Fifty-three percent of our total employment base is represented by 200 organized labor union contracts. In Oregon, 35 percent of Fred Meyer employees are represented by 13 local unions. There are 53 contracts. Union representation of the work force was 74 percent in 1988, compared to 60 percent in 1986. Our labor union members are in our main office, accounting department, sales promotion, bakery, dairy, distribution centers, plants, truck drivers and many others. Fred Meyer is represented by UFCW 555 in nearly all our nonfood departments. This sets us apart from some of our well known competitors--Payless, Target, LaMonts and most notably Wal-Mart.

A chart showing the history and result of leverage buyouts of Oregon companies was submitted by an unknown witness and is hereby made a part of these minutes (EXHIBIT G). A letter addressed to Mr. Irvin H. Fletcher from Anthony Meeker, State Treasurer dated April 30, 1991 is hereby made a part of these minutes (EXHIBIT H).



217 CHAIR KERANS: Why has the Investment Council put up with so many of the practices of KKR? He quotes from an article "After the Feast" written by Ellen Spriggins from the Publication Investment Division, April-May 1991, "For many of KKR's limited partners, the firm's hefty fees are a necessary evil---." Are you familiar with the HillSB oro example in the KKR portfolio which went bankrupt after being leveraged?
258 MR. DRUMMOND: There have been several unsuccessful investments in the KKR portfolio. 260 CHAIR KERANS: Because it is now in Chapter 11, the jury is still out on how well KKR's investment ultimately will do. Issues discussed: > KKR's fees charged Oregon Investment Council and profit for KKR. > 0regon Investment Council is a limited partner in the KKR fund. > The limited partnership agreement presented to the Council sets forth explicitly the types of compensation that KKR can earn. > The judgment of the Council was that even with the fee structure, the returns to the State far outweigh the risks and the aggregate returns would be superior to alternate investments. > There are relatively few losers in the KKR portfolio. > KKR selects the investments; the Council commits to the limited partnership fund. 432 CHAIR KERANS: It would

seem to me that a fit question to ask is how we are doing, what sort of things occur, what happens in LBOs and their impacts. I think it is worthy of investigation.

TAPE 85, SIDE B

035 CHAIR KERANS: KKR has it arranged in a way where they always stand to win and we stand to lose.

GERRY DRUMMOND: The record speaks for itself. We have been extremely successful. They are a highly reputable outfit. We pay them for the expertise and due diligence in these transactions. The formula for compensation is designed to compensate them for doing the kind of job they have been doing.

042 CHAIR KERANS: Do you think it is okay for them to not aggregate profit and loss.

MR. DRUMMOND: I think you can do it both ways. I not only think it is okay to continue to do business with KKR, the Council recently committed additional funds to KKR.

070 SEN. KERANS: Do you think a worthy subject for us to look at is whether it is prudent policy to invest in a company that does not aggregate?

072 MR. DRUMMOND: I don't.

074 SEN. KERANS: Another book that has just come out is called A Money Machine. How KKR Manufactured Power and Profits by Sarah Bartlett. He quotes from the book and asked if there is anything mentioned in the book worthy of legislative oversite of the Investment Council, the .


practice of LBOs and its partner, KKR?

162 MR. DRUMMOND: I don't know anything of the facts behind the quotes from the book, but if you're implying that perhaps an individual took advantage of a situation because of his position on the Council and usurped an opportunity from the Council, that might give rise to a civil liability, which I presume would be in the purview of the Attorney General to pursue. I don't see how this may or may not have been an ethical practice. I don't see how what happened, if it did happen, bears upon the performance of the Oregon fund. It happened following Mr. Meiers leaving the Council and there is no intimation from what the Chair has read that somehow his activities impoverished or diminished in any way the PERS fund.

179 CHAIR KERANS: Do you have any knowledge, or have you ever been told or been given any information that would lead you to understanding that anything of this nature ever occurred?

MR. DRUMMOND: I have no independent knowledge.

182 CHAIR KERANS: Do you think it is worthy of pursuit to find out whether PERS baneficiaries have been injured?

184  MR. DRUMMOND: I think if there is aufficient evidence of that kind, that might be a matter for a civil proceeding.

192  CHAIR KERANS: Ms. Bartlett has a chapter in her book, The Money Machine. How KKR Manufactured Power and Profits (published by Warner Books) on page 271, called "Fraud." He quotes from the chapter.
222     CHAIR KERANS: We have provided the money from our Investment Council funds to pose for KKR to LBO firms which they recapitalize themselves at distressed prices at a time they are about to gain their biggest return giving them the payday. Is that something that state government ought to be interested in? 240       MR. DRUMMOND: I believe that those allegations were filed by a man against his former partners. At that time I requested of the State Treasury of fice that the Attorney General monitor the process of that proceeding to see whether there had been any fraud on the part of KKR visa via the limited partners. To the best of my knowledge, no finding was made. 251  CHAIR KERANS: The settlement was sealed and we don't know. 251    MR. DRUMMOND: I would assume that the Attorney General would have pursued this- if there had been a reasonable suspicion that a fraud had been committed. The settlement is unknown to us. 258CHAIR KERANS: Do you think there is anything for the state to be worried about concerning Michael Milliken, etc.? 294       MR. DRUMMOND: I can't say that I know that no one was injured. 296    CHAIR KERANS: Has the Investment Council done anything about it? . . These minutes contain materials which paraphrase ant/or eurnmarize stl ements made during thir session. Only text enclosed in quotation rnarh report a speaker's exact words. For complete contents of the proceed ~gs, please refer to the taper. - Senate Committee on Labor May 3, 1991- Page 6

297  MR. DRUMMOND: No, we haven'".

296  CHAIR KERANS: Why haven't you done anything about it?

MR. DRUMMOND: No information has come to us.

CHAIR KERANS: Have you sought any information?

MR. DRUMMOND: No, we haven't.

CHAIR KERANS: That is exactly why this bill is in front of us.
303     CHAIR KERANS: I am deeply disturbed. If we discount by half everything that Ms. Bartlett, Ms. Spriggins, and the Pulitzer Prize winning Wall Street Journal author says, I believe there is something to be investigated. Do you still hold that there is nothing for us to be concerned with and this measure is not needed? 318      MR. DRUMMOND: That is my testimony. 319    CHAIR KERANS: Is that the position of the Investment Council? MR. DRUMMOND: That is my position. 338      CHAIR KERANS: I am not directing this at you individually, personally. We are at the tail end of the LBO binge. We find ourselves in partnership with people who are still positioning us with unaggregated deals, still taking us for director's fees, bankers fees, equity management fees, their 20 percent of every win and letting us stand on every loss with little or no money of their own even when they have a deal go straight to Chapter 11. I haven't even addressed the questions of the proponents of the bill. 362CHAIR KERANS: I am convinced we have a problem and I hope we do something about it. I would ask that you suggest to us, if you can, if this measure were to be adopted by the Legislature, how we might direct it so the Legislature, which serves as the Board of Directors of state government and oversees the work of the Investment

Council by virtue of creation of the Council, might discharge its responsibilities in relationship to these matters and how we might fruitfully use our time and resources. 380 MR. DRUMMOND: If the bill is passed by the Legislature and enacted into law, you can be assured that the Investment Council will cooperate fully with the investigatory committee and help guide your activities. The purpose of my testimony is that I think it is an unnecessary activity given the studies that have gone on in the past. And, I think it is a waste of state money. That is my opinion. You make policy; I don't. 44.0 CHAIR KERANS: Should the State be concerned that there could be possible antitrust issues involved with KKR owning both Fred Meyer and Safeway in the state of Oregon?



TAPE 86, SIDE B

022 MR. DRUMMOND: Both the state and federal government have antitrust laws and if they were viloated, I presume the Justice Department would be involved in seeking an answer to that question. 025 CHAIR KERANS: Has the question come up before the Investment Council?

MR. DRUMMOND: No, it has not.

037 CHAIR KERANS: Do the KKR people go back and forth between Safeway and Fred Meyer?

038 MS. PERRIN: We have three KKR people on our board. I don't believe any of those three are on the board of Safeway. 061 CHAIR KERANS declares the meeting adjourned at 4:42 p.m. Transcribed and respectfully
Reviewed by: submitted by: Annetta Mullins
Annette Talbott Assistant
Committee Counsel EXHIBIT SUMMARY A- SB 791, Preliminary Staff Measure Summary, staff B- SB 791, Wall Street Journal article, May 16, 1990, Irv Fletcher C- SB 791, prepared statement, Bradley Witt D- SB 791, biographical, professional and civic data and prepared statement, Gerald Drummond E- SB 791, letter received from Robert W. Straub F- SB 791, Wall Street Journal article, April 25, 1991 and report by Merton H. Miller, Gerald Drummond G- SB 791, history and results of leverage buyouts of Oregon companies, unknown. H- SB 791, letter from Anthony Meeker to Irvin Fletcher, unknown