



STATE OF NEW YORK
COMMISSION OF INVESTIGATION

**A TRUST BETRAYED:
FRAUD, BREACH OF FIDUCIARY DUTY,
AND WASTE AT THE TEAMSTERS LOCAL 237 WELFARE FUND**

MARCH, 1981

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NEW YORK, NEW YORK 10007

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TEMPORARY COMMISSION OF INVESTIGATION
OF
THE STATE OF NEW YORK

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AND WASTE AT THE TEAMSTERS LOCAL 237 WELFARE FUND

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I. INTRODUCTION

Teamsters Local 237 represents over fourteen thousand men and women working for the City of New York. It is the Nation's largest Teamsters public-employee union.

Each year, New York City, pursuant to collective bargaining agreements with Local 237, contributes approximately \$5 million to a welfare fund established and managed by officers of Local 237. The Fund exists to provide important health and life insurance benefits to the workers represented by the Union.

In 1967, Barry Feinstein ("Feinstein") became President of the Union and Chairman of the Fund's Board of Trustees. As Chairman of the Board of Trustees, Feinstein selected William Wallach ("Wallach"), a long-time friend and relative by marriage, as the Fund's insurance broker and consultant.

Together with Calvin Winick ("Winick"), another insurance broker, Wallach defrauded the Fund of over \$3 million from 1972 through 1980. This could not have happened if the Trustees of the Fund had properly exercised their fiduciary obligations to preserve the Fund's assets.

This Report will describe how Wallach and Winick defrauded the Fund by obtaining illegal commissions from the Fund's insurer, Trans World Life Insurance Company of New York ("Trans World"), in return for placing the Fund's business with Trans World. These commissions, which were concealed from the Fund, were passed on as premium charges to the Fund.

The Report will describe the efforts Feinstein made to assure that Wallach and Winick would continue to receive exorbitant payments even after he knew of their fraud, including his efforts to influence the progress of an audit by the New York City Comptroller's Office and a later investigation by the New York State Insurance Department. The Report also will detail the failure of those entrusted with the preservation of the Fund's assets, including Feinstein, the Trustees, and the Fund's counsel, to prevent the Fund from being victimized. Finally, the Report will describe how the City of New York annually provides over \$140 million to various union welfare funds which are almost entirely unregulated.

II. SUMMARY OF REPORT

In April, 1980, the New York State Insurance Department ("Insurance Department") announced that it had recovered \$2.27 million for the benefit of thirteen union welfare funds with over 47,000 beneficiaries. These moneys were paid to the Insurance Department by Trans World, by insurance brokers, and by others associated with Trans World. The payments were made following a lengthy investigation by the Insurance Department which revealed that Trans World and the brokers had grossly overcharged the union welfare funds. The total amounts paid to the Insurance Department for the benefit of the welfare funds represented the largest recovery from an insurer in New York State history.

The principal beneficiary of the Insurance Department recovery was the Local 237 Fund, established by Teamsters Local 237 for the benefit of over 14,000 New York City employees. The Fund, like welfare funds maintained by more than 100 other City unions, provides its members with a variety of life and health insurance benefits. Of the \$2.27 million recovered by the Insurance Department, the Fund received \$1.3 million, the balance going to twelve other union welfare funds. The amounts repaid to the welfare funds were about one-half of the total amounts the Insurance Department found the welfare funds were overcharged.

From 1972 through 1978, the Local 237 Fund was insured by Trans World. The Fund had placed its insurance with Trans World at the suggestion of Wallach and Winick, the Fund's insurance brokers, advisors, and consultants.

Although the Insurance Department conducted a vigorous investigation of Trans World and the insurance brokers, the Department did not have jurisdiction to investigate the Fund. The Commission, therefore, undertook to determine who was responsible for the Fund's having paid out millions of dollars in excessive fees and commissions, and whether any criminal acts were committed.

The Commission heard testimony at public hearings from Barry Feinstein and other Trustees, and from attorneys, administrators, consultants, and other persons associated with the Fund. Wallach and Winick refused to testify in reliance upon their constitutional rights. The Commission also heard testimony from New York City Comptroller Harrison J. Goldin and persons from his office, who had been involved in an audit of the Fund.

The Commission's investigation and hearings have demonstrated that Wallach and Winick, assisted by Trans World, systematically defrauded the Fund. However, this fraud would not have been successful if Fein-

stein had not protected Wallach and Winick, and if the Trustees of the Fund had properly exercised their fiduciary and managerial duties to protect the Fund from such exploitation. The Commission's specific findings can be summarized as follows.

A. The criminal violations

The Fund's brokers and advisors, Wallach and Winick, assisted by Trans World, defrauded the Fund of almost \$3 million from 1972 through 1980. Specifically, Wallach and Winick assured the Fund that, after exploring other companies, they were placing the Fund's insurance with Trans World because Trans World would provide good insurance coverage at the lowest available cost. In fact, there was no competitive bidding, and they placed the insurance with Trans World because the carrier was willing to pay them concealed and illegal commissions, pursuant to sham "service" and "promotional" contracts. Moreover, the charges for administration, commissions, and fees, made by Trans World to the Fund, were more than twice as high as charges made by other carriers to comparable welfare funds.

Wallach and Winick assured the Fund that all of Trans World's premiums, and the commissions and fees paid by Trans World to Wallach and Winick, had been

filed with and approved by the Insurance Department. In fact, the fees and commissions had been concealed from the Insurance Department and from other regulatory agencies.

As a result of this fraud, the Fund paid grossly excessive premiums for insurance coverage which could have been obtained at a much lower cost. These premiums were inflated by the illegal commissions Trans World paid to Wallach and Winick as well as by other improper charges made by Trans World. The Commission estimates that the total loss to the Fund as a result of these practices was over \$3.5 million.

In the Commission's view, these practices constituted violations of both federal and state criminal fraud statutes.

B. Breaches of fiduciary duty

Feinstein and the Trustees have fiduciary responsibilities in managing the Fund. While it is clear that the Trustees were defrauded by Wallach and Winick, the Commission also finds that Feinstein and the Trustees did not properly exercise their fiduciary obligations.

Feinstein totally dominates the Board of Trustees of the Fund. It was at Feinstein's urging that Wallach, a close personal friend, was retained as the

Fund's insurance broker. When evidence was brought to his attention that Trans World, Wallach, and Winick were overcharging the Fund, Feinstein used his political influence in an attempt to prevent such facts from being publicly exposed. At the same time, he used his influence over the Trustees to perpetuate the arrangements which enabled Wallach and Winick to enrich themselves at the Fund's expense.

There is no doubt that Feinstein knew that Wallach and Winick were being grossly overpaid at the Fund's expense. Feinstein concealed this from the Fund and insisted on continuing Wallach and Winick as the Fund's consultants in spite of the clear evidence of their fraud. If this Commission had not held public hearings which revealed the facts, we believe that Wallach and Winick would still be acting as the Fund's paid advisors.

The other Trustees also bear responsibility for the losses suffered by the Fund. Despite their fiduciary obligations, the Trustees relied entirely on Wallach and Winick in the administration of the Fund. Year after year, the Trustees approved payments of exorbitant premiums to Trans World solely on the recommendation of Wallach and Winick. At no time did the Trustees make independent efforts to determine whether less costly insurance could be obtained elsewhere, or whether

Wallach and Winick were placing the insurance with Trans World solely to maximize their commissions and fees.

When facts were brought to their attention indicating that the Fund had been victimized, the Trustees did not question Feinstein's desire to continue using Wallach and Winick as the Fund's consultants. It was only after this Commission's public hearings that the Trustees finally took action to discontinue the Fund's contractual relationships with Wallach. Winick's company still provides administrative services to the Fund today; although the Fund claims it is looking for a replacement.

C. The lack of controls by regulatory authorities

Welfare benefits to public employees have become larger and more important in recent years. New York City alone contributes more than \$140 million annually to union welfare funds, which are largely self-administered. Union welfare funds established by local government are not subject to the jurisdiction of the United States Department of Labor under the Employee Retirement Income Security Act ("ERISA"). New York State has no program equivalent to that created by ERISA for control of these welfare funds.

In reliance upon an opinion of the Attorney General of New York State, the Insurance Department has taken the position that it has no jurisdiction over self-administered insured welfare funds such as the Local 237 Fund. Moreover, any funds which are self-insured clearly are not subject to the Insurance Department's jurisdiction and are totally unregulated.

All funds receiving money from New York City are required to file reports with the office of the City Comptroller and are subject to audit. The Comptroller, however, has no independent enforcement powers with respect to abuses uncovered by an audit. The Comptroller's office has placed the audit of welfare funds low on its priority list.

In short, a welfare fund such as that established by Local 237, has control of large sums of money which constitute a trust for the benefit of the members. These funds are frequently administered by Trustees who have no particular experience or training. As demonstrated by this Report, the Trustees of the 237 Fund, for example, have mismanaged the Fund. From 1972 through 1980, only about 65 cents of every dollar the Fund received from the City went to the Fund's members as benefits. A substantial portion of the remainder was lost due to fraud and wasteful administrative practices.

While Trustees are liable to suit by the beneficiaries of the welfare funds for any abuses in the funds' management, such suits are rare. The funds are at the mercy of their Trustees.

III. THE FRAUD PERPETRATED BY WINICK AND WALLACH

A. The Fund's insurance program from 1967-1972

Local 237 represents over 14,000 City employees, most of whom work for the New York Housing Authority and the New York City Health and Hospitals Corporation. Pursuant to collective bargaining agreements with these authorities, Local 237 has established a trust fund to receive contributions from the City which are used to provide supplemental welfare benefits to the Union's members. The trust fund is administered by seven Trustees, all of whom are officers of Local 237. In fact, all of these Trustees are hand-picked by Feinstein.

Feinstein became President of Local 237 and Chairman of the Board of Trustees of the Fund in 1967. According to Feinstein, when he became Chairman, the Fund was in "very, very dire condition"* and had not paid its premium to the insurance carrier for several months. Faced with this situation, Feinstein called Wallach, an insurance broker who was a close friend, a relative by marriage, and someone Feinstein viewed as "family." For the next 13 years, Wallach acted as the

* Quotations to testimony come from sworn testimony given at public and private hearings conducted by the Commission or in the course of an investigation by the Insurance Department, except where otherwise noted.

Fund's chief advisor and insurance broker. Wallach misused his position to enrich himself at the Fund's expense and used the proceeds to acquire and build insurance businesses, including The Lion Insurance Company of New York, the Eagle Insurance Company of New York, and the Robert Plan Corporation.

Wallach had twenty years of insurance experience, mostly in the automobile casualty field, but no group insurance experience or experience with welfare funds. As he testified before the Insurance Department:*

I never handled group insurance before Mr. Feinstein . . . came to me. What the hell did I know? I learned.

Despite this lack of experience, Wallach was chosen to be the Fund's insurance broker and consultant. In addition to receiving commissions and service fees from insurance companies with whom the Fund did business, he was paid \$9,999 a year in consulting fees by the Fund in 1969 and 1970. Feinstein testified about Wallach's role:

Mr. Wallach between the years of 1967 and 1972 had functioned as our expert in this area. He was the

* All testimony of Wallach and Winick cited in this Report was given before the Insurance Department.

fellow that was responsible for finding carriers to continue to write risk for us, was responsible for the maintenance of our benefit structure levels, to ensure that what we did during that period of time wasn't biting off more than we could chew.

The same year in which Wallach became the Fund's broker, he asked Feinstein to be a member of the Board of Directors of The Lion Insurance Company ("Lion"), which Wallach owned. Lion was in the business of providing automobile liability insurance. Feinstein served on the Board of Lion from 1967 to 1975 and was paid small Director's fees.

Wallach obtained insurance for the Fund from several companies, including Thomas Jefferson Insurance Company ("Thomas Jefferson"), where he dealt with Winick, who was an officer in the Group Department of Thomas Jefferson.

The Fund's life, accidental death and dismemberment, and hospital and surgical benefits were insured by Thomas Jefferson from June 30, 1967 to October 1, 1969, at which time Winick left Thomas Jefferson and established Winick Associates, Inc. ("WAI"), a New York corporation of which he was the sole stockholder, officer, and employee. Wallach wanted to continue using Winick's "expertise." As Winick told the Insurance Department:

I was familiar with the business. I knew everything. He thought that I was very necessary to him, because of the knowledge I had, and when I left the company because they went out of the group insurance business, he wanted to continue using me because of my knowledge and expertise.

Wallach authorized Winick to place the Fund's insurance through WAI:

Q. And some of the business that you were paid for as a general agent [were] the Teamsters 237 contracts, policy?

A. Sure, correct.

Q. Who brought it to you, or what?

A. When Winick Associates [was] first incorporated, these cases were brought to Winick Associates by Mr. Wallach as, I believe, W.V. Brokerage Corp.*

Winick found new carriers for the Fund: Eastern Life Insurance Co. ("Eastern"), Beneficial National Life Insurance ("Beneficial"), and American Medical Insurance Company ("American Medical"). As Winick testified:

* W.V. Brokerage Corp. ("WVB") is a shell corporation owned by Wallach.

The time that the group business left and I left, Mr. Wallach indicated that he would like me to find another company where the business could be placed that had been in Thomas Jefferson, and I found Eastern Life Insurance Company, and I placed that part of the coverage in Eastern Life as general agent.

Thus, upon Winick's leaving Thomas Jefferson, the Fund's business was placed with Eastern, Beneficial, and American Medical. Until January 1, 1972, Winick and Wallach received commissions and service fees as a result of placing the Fund's business with these carriers.

In the fall of 1971, Winick and Wallach entered into negotiations with Beneficial, ostensibly on behalf of the Fund, looking toward the possibility of Beneficial insuring all the benefits provided by the Fund. Beneficial offered to provide such coverage. However, as a price for placing the business with Beneficial, Winick and Wallach demanded that they be paid fees and commissions greater than Beneficial could pay in accordance with its filings with the Insurance Department.*

* Sections 204(4) and 221(7) of the Insurance Law provide that no insurance company may pay commissions or fees which are not on file with the Insurance Department. Moreover, the Department refuses to accept for filings the commissions or fees it determines to be excessive.

David Schultz, an officer of Beneficial, testified:

[Winick] called me in November, 1971 to say that he was acting as a consultant to Wallach, and what could we do to increase the allowances. I went over the figures with him in detail and he agreed that we could not legally pay more than we offered and would so advise Wallach. [Emphasis added]

On November 8, 1971, Winick proposed to Schultz that Beneficial take over the full insurance program. Winick brought with him an underwriting package with several exhibits, one of which projected that in 1972 a total of 6.72 percent in commission and service fees would be paid to Wallach. Beneficial reviewed Winick's proposal and retained a consulting actuary to examine the proposal. The actuary reported that:

a) The compensation arrangement requested by Mr. Winick for the broker and general agent appears to be excessive.; b) It is questionable whether the compensation arrangement requested by Mr. Winick will be approved by the New York State Insurance Department.; c) The retention of approximately 24% on a group case of this size is quite uncompetitive.

In noting that a retention rate of 24 percent was "uncompetitive," the actuary referred to the fact that, as the Insurance Department later established,

ordinary "retention charges"* for a large union welfare fund were between 6 and 10 percent of the Fund's premiums. Thus, Wallach and Winick were proposing an arrangement which eventually resulted in the Fund paying retention charges which were two to three times what they should have paid.

On December 14, 1971, Schultz met with Wallach, and "explained that we were entirely satisfied with the overall underwriting . . . , but it is quite likely that we would not be able to file for a total of 6.72 percent overall general agency commission and allowances." Schultz summarized his negotiations with Winick and Wallach for the Commission as follows:

Q. And Mr. Winick was acting on behalf of Mr. William Wallach?

A. So he told me.

* * *

Q. Did Mr. Winick make certain requests of you concerning the size of the fees paid to Mr. Wallach?

A. Yes, he did . . .

* Under the arrangements between the Fund and Trans World, the Fund paid premiums every year from which Trans World paid claims. After paying claims, Trans World retained moneys, for "retention charges" which included commissions, fees, taxes, charges for risks or contingencies, and Trans World's profits.

Essentially Mr. Winick wanted us to increase the total of allowances paid to W. V. Brokerage.

Q. Could you so increase the allowances paid to W.V. Brokerage?

A. No . . .

Because they would have been in excess of the allowances we were allowed to pay under our filings with the Insurance Department.

Schultz explained to the Commission that after Beneficial was unwilling to pay the unlawful commission sought by Winick and Wallach, his company lost the business:

The second matter that came under discussion was the matter of commissions payable on the entire package of coverages.

Mr. Winick estimated for me that the overall allowable commissions and fees to W.V. Brokerage would be a total of 6.72 percent.

He had given me that figure earlier. I worked with our own filings and with schedules that I knew were used by the Insurance Department and I told him that my best estimate was that the maximum total for W.V. Brokerage would be between five and six percent.

So at that point, which was then probably the end of November or early December of 1971, I told Winick that we were agreeable to writing the package of coverages

subject to the retention of the dividend and subject to filing of commissions and allowances.

Q. As a result of all this, I take it that your company was taken out of the picture; is that correct?

A. We did not hear anything further, sir, until we learned that we were no longer the insurance company, that's correct.

B. The Fund places its insurance with Trans World

Because Beneficial did not accede to their demands, Winick and Wallach approached Trans World, which was then a small insurance firm with virtually no group insurance business.

Following discussions between Trans World, Wallach, and Winick, Trans World agreed to pay the illegal commissions sought by the brokers, in return for being selected as the Fund's insurer.

Since Trans World had no group insurance department, it was agreed that the insurance program would be administered by Serv-Co Administrators Inc. ("Serv-Co"), a corporation which was in the process of being established by Winick and two of his former associates, Arno Talesnik and Stanley Mandel.*

* Another company, Pre-Paid Prescription Plans, doing business as U. S. Administrators, ("PPP") contracted with Trans World to pay claims on Trans World's drug and dental group insurance.

These illegal payments were passed on, dollar for dollar, to the Fund as part of the premiums which the Fund was charged by Trans World. Thus, it was the Fund, and not the insurance carrier, which bore the costs of these illegal payments to Winick and Wallach.

On January 1, 1972, Trans World entered into a contract with Serv-Co, pursuant to which Serv-Co was to pay claims and to provide administrative and consulting services in connection with Trans World's group business.

It should be emphasized that the great bulk of the work necessary to administer the Fund's insurance program was done internally by the Fund, at a yearly cost exceeding \$400,000, which employed a large staff, directed by the Fund's administrator, Robert Groom, for that purpose. The staff, for example, kept records concerning the Fund's members, prepared all claims, issued bills, distributed booklets, explained benefits to members, and performed other extensive services. Serv-Co was paid large sums by Trans World -- money which was ultimately paid by the Fund -- to perform services, many of which were already being performed by the Fund's staff. Thus, the Fund's insurance premiums were inflated to the benefit of Winick, Mandel, and Talesnik, the principals of Serv-Co.

The illegal commissions which Winick and Wallach were to receive were disguised as "service fees" and "promotional fees," to be paid under sham agreements between Trans World, on the one hand, and shell corporations owned by Winick and Wallach on the other hand. These fees were apart from and in addition to the legal commissions paid to Winick and Wallach as brokers on the Fund's insurance placed at Trans World.

On January 1, 1972, Trans World also entered into a "Group Service Agreement" with WAI, pursuant to which Trans World was to pay WAI five percent of all premiums received by Trans World from the Fund. In turn, WAI agreed to pass on these payments, and more, to WVB. Between 1972 and 1978, Trans World paid WAI \$1,135,924 under this Agreement.

These payments allegedly were to compensate WAI for rendering administrative services with respect to the Fund. In fact, WAI and Winick did nothing for the money. The Group Service Agreement was simply a vehicle for paying illegal commissions to Wallach (passed to him by Winick) for bringing the Fund's business to Trans World.

In order to pay Winick illegal commissions, Trans World entered into a "Special Group Representative Agreement" with WAI. Trans World agreed to pay to WAI \$7,600 a month (later increased to \$13,000), ostensibly

for generating other group insurance business for Trans World. The payments under this Agreement were no more and no less than illegal commissions paid to Winick for bringing in the Fund's business.

C. WAI's Service Agreement with Trans World

As mentioned above, WAI received about \$1.13 million from Trans World under the Group Service Agreement, from 1972 through 1978. These "service fees" were directly charged to the Fund as part of the premiums the Fund paid Trans World.

It is clear that Winick performed no bona fide services pursuant to this Agreement. Most of the services listed in the Agreement were performed by the Fund's staff under the direction of Robert Groom. For these internal services, the Fund allocated over \$400,000 a year. To the limited extent that Groom's staff did not perform the listed services, they were performed by Serv-Co. Some of the charges for "services" listed in the WAI Agreement could not properly be charged to a welfare fund.

The Group Service Agreement was a sham. It listed eight "services" which Winick purportedly was to perform. In fact, Winick was not expected to perform these services which were largely performed by the Fund's staff. The eight listed "services," the fees

Winick received from Trans World under the Agreement, and the reasons why such payments were fraudulent are as follows:

<u>Service</u>	<u>Fees (1972-1978)*</u>	<u>Comment</u>
1. Issuance of certificates	\$113,592	Performed by Fund
2. Preparation of premium billing	\$113,592	Performed by Fund
3. Maintenance of enrollment cards	\$56,796	Performed by Fund
4. Education of agents	\$170,388	Not a proper charge
5. Assistance in distribution of booklets	\$56,796	Performed by Fund
6. Assistance in explaining new benefits	\$113,592	A broker's function, already compensated by regular commissions
7. Assistance in preparation of master policies	\$56,796	A broker's function, already compensated by regular commissions
8. Installation and resolicitation fee	<u>\$454,372</u>	A broker's function and an improper charge
	\$1,135,924	

* The fees Winick received under the Group Service Agreement were expressed in percentages of premium totalling 5 percent. The amounts in the table were arrived at by applying the applicable percentage to the total premiums from 1972 through 1978.

The first listed service, "Issuance of Certificates," for which Winick received \$113,592, was performed by the Fund. Groom testified before the Commission:

Q. ... For example, you issue the certificates, don't you?

A. A booklet.

Q. You issue the booklet which is a certificate of enrollment to your member.

A. Yes.

Similarly Gerald Lener, Senior Examiner for the Insurance Department, who conducted a triennial examination of Trans World, testified before the Commission:

Serv-Co, under its contract was to perform issuance of certificates under a contract where they would receive a five percent commission and was also being paid a certain amount to issue certificates.

In fact, these certificates were issued by neither one of the two.

It was issued by Mr. Groom's office.

The second listed service, "Preparation of Premium Billing," for which Winick received \$113,592, was performed by the Fund. The Fund itself collected

the premium due, made up its own bill, and paid it on time.

The third listed service, "Maintenance of Enrollment Cards," for which Winick received \$56,796, was also performed by the Fund. At most, Winick appeared at the Fund once a year to flip through the cards to be sure "they were being kept up to date." As Groom testified before the Commission:

Q. And you maintained all the enrollment cards. Is that correct?

A. ... Yes.

Q. I think you said that Mr. Winick came once a year [to the Fund] and looked through the enrollment cards to see that they were being kept up to date.

A. Yes.

* * *

Q. How much time would he [Winick] spend with the 15,000 cards, a full day [per year]?

A. No.

Q. A couple of hours?

A. A few hours, two, three hours.

The fourth listed service, "Education of Agents," for which Winick received \$170,384, was a patently improper charge. Winick testified before the Insurance Department:

Q. Will you tell us one agent that you ever spoke to in this respect?

A. William Wallach.

* * *

... William Wallach was the only agent.

* * *

In other words, the Fund paid \$170,388, to Winick, one of its brokers, to "educate" Wallach, the Fund's principal broker, advisor, and consultant, who was himself the ultimate recipient of these very same payments.

The fifth listed service, "Assistance in Distribution of Booklets," for which Winick received \$56,796, was performed by the Fund. Groom testified:

Q. Let's talk about the distribution of the booklets which is what the contracts referred to. Who distributed the booklets?

A. Our office distributed the booklets.

The sixth listed service, "Assistance in Explaining New Benefits," for which Winick received \$113,592, was not a service for which a fee, other than the basic broker's commission, could properly be charged. As Lener testified before the Commission:

A. . . . explaining the benefits .
. . . that is also a general agent's
function. That is the way a general
agent produces benefits or obtains
business.

Q. Are you saying, therefore, that
there would be no reason to pay Mr.
Winick these fees since he was re-
quired by other contracts he had
with Trans World to render the same
service?

A. That is correct.

The seventh listed service, "Assistance in
Preparation of Master Policies," for which Winick re-
ceived \$56,796, did not have to be performed by anyone,
since the policy with the Fund was adopted from prior
policies. Lener testified:

Q. I take it what you are saying is
that there was no need to prepare
any kind of a policy because it was
simply an adaptation of a prior
policy that had existed with anothe-
r insurer?

A. That is correct.

Q. And a policy that remained in
effect without any substantial
modifications for seven years?

A. That is correct.

Further, even if the policy had been prepared
by WAI, there was no reason why WAI should have been
paid a fee every year for a task that would have been
done only once.

The eighth listed service, "Installation and Resolicitation Fee," for which Winick received \$454,372, also was not a legitimate service charge. It was a payment to Winick for "resoliciting" the Fund's policy each year. In other words, the Fund paid Winick \$454,372 over and above the normal broker's commission, for the privilege of having its business solicited by him. Lener testified:

Q. Would you take us to the last item?

A. The last item is "Installation and Resolicitation Fee," which is also the type of service which a general agent would perform in order to earn his commissions.

Q. Now, to the extent that Mr. Winick would have done any such thing, he would have received a commission as a general agent of the company; is that correct?

A. That is correct.

In summary, the Group Service Agreement between Trans World and WAI authorized payment to WAI of \$1,135,000 for eight alleged "services." Four of these services were performed by the Fund itself or by Serv-Co; one of the services was patently improper; and three of the services were duplicative of services for which Wallach and Winick received broker's commissions.

Moreover, WAI, the recipient of the \$1.13-million, could not have performed any such "services" since it was merely a shell corporation. WAI had no employees, other than Winick, and no office. Its "office" was merely an address at Serv-Co's office. The company's tax returns and books show that almost all of its revenues consisted of moneys from Trans World paid in connection with the Fund's insurance program, and that WAI had no significant expenses or payroll.

D. WAI's Special Group Representative Agreement with Trans World

The second contract executed by Trans World and WAI on January 1, 1972 was a "Special Group Representative Agreement," whereby WAI received \$7,600 a month increasing to \$13,000 a month, (\$156,000 a year) by 1976. The ostensible purpose of these payments was to reward Winick for bringing new group business to Trans World. But the payments were required to be made regardless of how much added business Winick produced and in advance of any such business being produced. Actually, Winick brought no substantial business to Trans World, except for the Fund's business, for which he was paid a legitimate commission of over \$20,000 a year.

Murray Simon, an Insurance Department Examiner who conducted an examination of Trans World, told

the Commission that the payments made to Winick under this Agreement, which totaled \$931,200 from 1972 through 1978, were disguised commissions for bringing in the Fund's business:

Q. Are you saying, in effect, that they, Trans World paid Winick excessive commissions and in order to do so concealed them under the rubric of a group representative agreement or under the cover, I should say, of a group representative agreement?

A. That is correct. . . . During the testimony there was nothing to demonstrate that they rendered any substantial services that could remotely require the payment of \$1,000,000 for the service they rendered.

* * *

Q. Was Mr. Winick able to identify any substantial business that he generated for this company, Trans World, which would even remotely justify the payment from a business, moral or legal or ethical point of view of a million dollars?

A. He claimed the company's worth of business as of 1976 had greatly increased.

It was true, but it had nothing to do with his efforts.*

* Winick told the Insurance Department that he had earned these fees by "creating an environment" which allowed Trans World's group business to grow. But he could not specify any additional group business which he brought in.

Under the Group Service Agreement and the Group Representative Agreement, discussed above, WAI received a total of \$2.06 million from 1972 through 1978. Of these amounts, approximately \$1.3 million was passed on to Wallach by Winick, pursuant to a separate agreement between WAI and WVB. Winick thereby acted as a conduit for the payment by Trans World to Wallach of illegal commissions disguised as "service fees" and "promotional fees."

E. WVB's Group Insurance Sales Agreement with Trans World

In January, 1972, WAI and WVB entered into an agreement called a "Group Insurance Sales Agreement" under which WVB was to receive 5.82 percent (later 5.35 percent) of the Fund's premium, in return for Wallach's allegedly performing four of the eight "services" which were listed in Winick's Group Service Agreement with Trans World. The following chart lists the "services," the fees Wallach received, and the reason why such payments were fraudulent:

<u>Service</u>	<u>Fees (Total)*</u>	<u>Comments</u>
(1) Review and check master contract		A broker's function, compensated by regular commissions
(2) Install group program including distribution of master policy and certificates		A broker's function, also performed by Fund
(3) Furnish enrollment cards to the Insurance Company		Performed by Fund
(4) Assist in collection of delinquent premiums		Fund not delinquent
(5) Participate in the resolution of administrative problems with the policyholder		A broker's function
	<u>\$1,305,057</u>	

The first listed service, "Review and Check Master Contract," was duplicative of Serv-Co's contract with Trans World. In addition, this task needs to be performed only when the policy is issued and is one of the tasks a broker normally performs on behalf of his client without compensation above his commission.

* Payments under this Agreement were not broken down for each alleged "service."

The second listed service, "Install group program, including distribution of master policy and certificates" -- another service performed only when the policy is put into effect -- was performed by the Fund. As Wallach admitted to the Insurance Department:

Q. And distribution of certificates, which are the booklet certificates, did you do anything about that? What did you specifically do under that category?

A. Only in that I explained it to the trustees, I explained it to the fund, I took those portions of the booklet which were of information to the people that were to be involved in receiving the claims, to alert them to the requirements of it and also instruct the fund as to the proper payment of the premiums.

Q. But you did not physically distribute the booklets to the individual members, did you?

A. No.

The third listed service, "Furnish Enrollment cards to the Insurance Company," also was performed by the Fund. Wallach testified before the Insurance Department:

Q. And there are enrollment cards in your office?

A. No.

Q. You do not prepare them or handle them?

A. No.

Groom likewise told the Insurance Department:

Q. Now, were any enrollment cards duplicated and furnished to Trans World? Were there any other sets of enrollment cards anywhere other than what we just discussed?

A. No.

Q. In other words, Winick didn't have his own set of enrollment cards?

A. No.

Q. And Wallach didn't?

A. No.

The fourth listed service, "Assist in collection of delinquent premiums," did not have to be performed by anyone, because the Fund was not delinquent. Even if it had been delinquent, Serv-Co was contractually obligated to collect premiums. Groom testified:

Q. Did your office participate in the preparation of premium billing?

A. You mean the monthly report for producing the check that went to Trans World?

Q. That's correct.

A. Yes.

Q. That was done internally, so to speak, isn't that so?

A. It had to be. I have the figures in my office.

* * *

Q. Were you aware Mr. Winick was getting paid for delinquent premiums and being charged to your funds? How often are you delinquent?

* * *

A. I don't really consider we are ever delinquent.

The fifth listed service, "Participate in the resolution of administrative problems with the policyholder," was not a legitimate charge, since an insurance broker performs those services to keep the business and would receive no compensation above his basic commissions for doing so.

Between January, 1972 and December, 1978, WAI paid WVB \$1,305,057* pursuant to the Group Insurance Sales Agreement. In addition, WAI paid WVB a legitimate commission of \$93,512. All these payments were listed as commissions on WVB's books. The payments Wallach re-

* The \$1.3 million figure was obtained by applying the contract percentages against total premiums paid by the Fund from 1972 through 1975; and from a review of WVB's books covering 1976 through 1978. WVB's books show that Wallach received about 5.75 percent of premium, more than the 5.35 percent his contract called for, during 1976 through 1978.

ceived under the Agreement were not fees for performing the listed services. They constituted illegal commissions, disguised as fees for services under a sham agreement.

F. The Fund's self-insurance arrangements with Wallach and Serv-Co

In late 1978, Wallach recommended that the Fund become self-insured, purportedly in order to reduce its expenses. This recommendation was accepted, and the Fund terminated its contract with Trans World as of December 21, 1978.

As of January 1, 1979, the Fund entered into agreements directly with Serv-Co, Wallach, and PPP after negotiations between Wallach and Feinstein. The Agreement with Wallach provided that he was to act as a "coordinator" for the Fund's benefits and, in particular, that he would coordinate and review the performance of Serv-Co. The Agreement also required him to consult with the Trustees concerning the Fund's benefit programs and to assist the Fund in the establishment of a "claims review procedure." For these services the Fund agreed to pay Wallach pursuant to a complex formula based upon the number of beneficiaries and the premiums that had been paid previously to Trans World. Under this formula Wallach received about \$178,000 a year.

The Fund also entered into a contract with Serv-Co under which Serv-Co received about \$99,000 a year, requiring Serv-Co to perform services similar to those it had performed in the past. PPP contracted to process drug and dental claims for about \$208,000 a year.

At the time the Fund entered into these agreements with Serv-Co and Wallach, Wallach entered into a side agreement with Winick pursuant to which Wallach was to pay Winick \$50,000 a year for Winick's "assistance." The Trustees did not know about this side agreement.

Testimony given by Groom made it clear that the Fund's self-insurance program did not result in any additional work for Wallach or Winick, and that they continued to receive large fees from the Fund for doing little other than attending quarterly Trustees' meetings and occasionally consulting on Fund matters.

Although the Trustees approved the contracts between the Fund, on the one hand, and Wallach and Serv-Co, on the other hand, they testified that they had no idea how much money Wallach and Serv-Co were to receive under these agreements. The Trustees were also unaware that Wallach was going to pass on to Winick \$50,000 a year of the moneys which Wallach was to receive under his contract.

Feinstein testified that he negotiated these agreements, and that he did know how much money Wallach and Serv-Co (but not Winick) were to receive. He stated that he was led to believe that the moneys Wallach and Serv-Co were to receive were consistent with what they had been paid between 1972 and 1978, and that such fees had been approved by the Insurance Department. But, as will be seen, the fees actually had been concealed from the Insurance Department. Moreover, the fees they had received in prior years were in fact, illegal commissions paid them, not for services performed, but for placing the business with Trans World.

The Fund paid Wallach and Serv-Co under these Agreements for two years until December, 1980, when, in light of this Commission's public hearings, the Trustees voted to discontinue Wallach's payments and to make arrangements to replace Serv-Co.

Several Trustees testified before the Commission that they approved Wallach's and Winick's contracts without knowledge of material facts. Among these facts were: (a) that Wallach and Feinstein were related by marriage; (b) that Feinstein had served as a director of a company controlled by Wallach; and (c) that Wallach and Winick had been receiving, out of the Local 237 premium, hundreds of thousands of dollars annually in illegal commissions and fees. These trustees further tes-

tified that if they had been advised of these facts, they would not have approved, or might not have approved, the Fund's 1979 contracts with Wallach and Serv-Co.

G. The Fund's losses from the fraudulent scheme

During its investigation of Trans World and the brokers, the Insurance Department determined that the Fund had, from 1972-1978, overpaid a minimum of \$2.6 million for insurance. The Insurance Department arrived at the \$2.6 million figure after conducting a survey of "retention charges" in the insurance industry.

The Insurance Department learned through its survey that total retentions, including the cost of administrative services under group insurance policies similar in size to Local 237 policy, ranged between 6 and 10 percent of premiums. In contrast, Trans World's retention charges to the Fund were 23 percent of premiums.

In determining that the Fund overpaid \$2.6 million for insurance, the Insurance Department took the difference between Trans World's 23 percent retention rate and an 11 percent rate, the highest permissible rate in the Department's opinion. Twelve percent of the premiums which the Fund paid Trans World, or about \$2.6 million, was therefore calculated to be the total overcharge.

The \$2.6 million figure does not, however, take into account the interest obtainable in an action on the moneys fraudulently obtained from the Fund. If a six percent simple interest factor is applied to the moneys fraudulently taken from the Fund each year, the true loss is over \$3.5 million.*

H. The deception practiced by Trans World, Wallach, and Winick

(a) Misrepresentations to the Fund

As insurance brokers and consultants, Winick and Wallach had the obligation to obtain insurance for the Fund at the best possible price, and they led the Trustees of the Fund to believe they had done so.

Winick and Wallach defrauded the Fund by recommending insurance, not on the basis of what was in the interests of the Fund, but on the basis of what was in their personal interests and then concealing these facts from the Trustees. Specifically, they induced the Fund to place insurance with Trans World because Trans World was willing to pay them illegal commissions, and they concealed these commissions from the Fund, from the Fund's beneficiaries, and from the government.

* Six percent is the rate of interest generally recoverable under New York law. CPLR §5004. In actions at equity, however, the Court has the discretion to set a higher rate of interest.

Feinstein and the other trustees testified that the Fund placed its business with Trans World in reliance on assurances by Wallach and Winick that Trans World would provide the insurance at the lowest cost available. In this regard, they testified that Wallach and Winick led them to believe from the outset that many larger, more established insurance companies would not insure the Fund because of its poor financial condition and because it was a Teamsters fund. Feinstein testified:

During that period of time, we kept finding companies either leaving us, failing to continue to write the kind of business we had either because we were a municipal or we were a union . . . and Mr. Wallach found Trans World as a carrier that would continue to write the risk when the company previous to Trans World told us that they were no longer going to write that kind of business.

Contrary to the representations made by Wallach and Winick, there is no evidence that a major insurance company would have been unwilling to take on the Fund's business. It is clear that Beneficial was willing to provide insurance, and that Wallach and Winick broke off negotiations solely because Beneficial was unwilling to meet their demands for excessive commissions. Moreover, there is no evidence that Wallach

and Winick approached any insurance carriers besides Beneficial before the Fund's business was placed with Trans World. Even if Trans World had been the only available carrier, the Fund could have obtained insurance from Trans World at a cost which did not include the large illegal commissions paid to Wallach and Winick.

In 1976, the Fund came under the scrutiny of the Comptroller of the City of New York, which was then conducting an audit of the Fund. At that time, the Comptroller's auditors pointed out to the Fund that it was paying excessive fees and commissions for its insurance and that the insurance was too costly overall.

Normal procedure would have called for the Fund to submit to the Comptroller's Office a written response to the draft. A final draft would then be prepared incorporating the Fund's comments. In fact, the Fund's counsel had started to prepare a written response, and had contacted Winick, Mandel, and others to get their response to the auditors' concerns. The response made by Winick to counsel's inquiry graphically illustrates the means by which Winick and Wallach defrauded the Fund.

On or about November 23, 1976, Winick sent a letter to the Fund's counsel purporting to set forth information, "which we hope will be useful in your reply

to the City auditor who is currently auditing the Welfare Funds." In response to questions the auditors had raised as to the compensation received by the brokers, Winick's letter stated:

The General Agent (Winick Associates, Inc.) is paid commissions in accordance with a schedule filed with the N.Y. State Insurance Department. This schedule of commissions is competitive with what other Insurance Companies pay. In addition, where the General Agent (or Agent) performs services that are normally done by the Insurance Company, the General Agent (or Agent) are paid service fees in accordance with a schedule filed with the N.Y. State Insurance Department. The General Agent is paid the total commissions and service fees by the Insurance Company and in turn pays the Agent (W.V. Brokerage Corp.). These fees are also competitive with what other companies pay. (Emphasis added)

Winick's letter was false and misleading. Contrary to his representations, the commissions received by WAI had not been filed with the Insurance Department. Moreover, contrary to the letter, the service fees paid to WAI, and thereafter to WVB, had not been filed. Nor were these fees "competitive with what other companies pay." Indeed, the fees were impermissible.

Counsel for the Fund had also inquired of Winick as to whether competitive bids were sought for the Fund's insurance in 1972. Winick's letter answered this inquiry as follows:

You questioned also whether the policy was ever put out for bids. When we first came to Trans World in January 1972, W.V. Brokerage and myself went to various carriers to show them the various details of this risk. Beneficial National Life Insurance Company, who had been the carrier for the Drug Coverage only, was approached to take the whole risk and they refused. We also went to Nationwide Insurance, Prudential and Mutual Benefit Life and all had rejected us as they were not interested in writing municipal unions at that time. We went to Trans World and reached an agreement which was competitive with what was being charged other groups. (In fact, we were even lower.) [Emphasis added]

These statements also were false. As previously noted, Beneficial did not refuse to insure the Fund's benefits, but rather refused to pay unlawful commissions sought by Wallach and Winick. Winick's statement that Trans World's fees were "competitive with what was being charged other groups" was patently false, as demonstrated by the Insurance Department's later survey which revealed that Trans World's charges for administration were about two and one-half times the norm.

Winick responded to counsel's inquiry by presenting what purported to be invitations he had extended to four major insurance companies to bid on the Fund's business. Winick thereafter told the Fund that these insurance companies had declined to bid, and he gave the Fund letters to that effect from the insurance companies. However, Winick did not reveal that at least one of these insurance companies -- Mutual of Omaha ("Mutual") -- had indicated a serious interest in offering coverage. Mutual only declined to bid when Winick told an officer of Mutual that the price for placing the insurance would be illegal commissions payable to him of at least 9.5 percent, as well as additional fees. Another insurance company to which Winick had written did not even provide coverage for welfare funds.

Thus, Wallach and Winick misled the Fund in 1972 by telling the Fund that Trans World was the only insurer available. They misled the Fund again in 1976 by representing that they had made genuine but unproductive efforts to obtain less costly insurance, and they lied to the Fund's counsel about the fees and commission they were receiving.

(b) Concealment of fees from the Insurance Department

The New York State Insurance Law, §§204(4) and 221(7), requires that all payments made by an insurance

carrier for commissions, services, and administration on group insurance be in accordance with a schedule of fees filed by the carrier with the Department.* As a matter of practice, if the fees are too high the Department will not accept the schedule for filing. The Code of Ethical Practices ("Code")** sets forth the Department's policy that on union group insurance these payments can be made only for the reasonable value of four itemized services.*** (Code, §2(c)(1)).

Under its contracts with Trans World, Serv-Co was responsible for all filings with the Insurance Department. As stated above, Winick had been told by

* Every violation of the Insurance Law is a misdemeanor in addition to any other penalty provided by law (I.L. §5).

** The National Association of Insurance Commissioners ("NAIC") in addressing the corruption and depletion of welfare and pension fund assets at its convention on December 2-5, 1957, adopted the Code of Ethical Practices as a declaration of applicable principles on the proper conduct of insuring welfare and pension funds. The NAIC adopted the Code to serve as a complement to "... existing state insurance laws as require that insurance benefits be reasonable in relation to the premiums charged, and which prohibit unfair discrimination, rebates, misrepresentation, misleading or deceptive acts, and other unfair trade practices or unfair methods of competition, as being prejudicial to the interests of beneficiaries of insured welfare and pension funds." The New York State Insurance Department fully subscribed to the Code by circular letter dated December 19, 1957 and by adopting 11 NYCRR Part 202 (group life insurance).

*** These four itemized services are: (1) issuing certificates; (2) maintaining employee records; (3) billing premiums; (4) processing claims.

Beneficial that the commissions he and Wallach were seeking were excessive and would not be approved by the Insurance Department. After Trans World agreed to pay the commissions, Serv-Co did not disclose the fees to the Insurance Department, having been told by Beneficial that the Department would disapprove them. When questions were later raised about their fees, Winick and Wallach repeatedly assured the Trustees that the fees paid by Trans World had been duly filed with the Insurance Department. These representations were false.

Trans World's payments to WAI under the Group Service Agreement were concealed from the Insurance Department. They were not in accordance with the schedule of fees to be paid in connection with union welfare cases which Trans World had filed with the Insurance Department.* The payments by WAI to WVB also were not filed with or disclosed to the Insurance Department.**

* The schedule which WAI did have on file with the Department conformed with the Code. But the payments actually made to WAI under the Group Service Agreement did not conform with the schedule on file and did not conform with the Code. Serv-Co's officials told the Department that the wrong schedules had been filed "by mistake."

** Trans World has argued that the fees paid by WAI to WVB did not have to be filed because they were not paid by Trans World, the insurance company. In our view, this contention is absurd. If accepted, it would allow insurance companies to avoid the limitations on commissions merely by paying the excessive commissions indirectly through a third party, as happened here. Trans World also claims that it first learned about these payments to WVB in 1978.

Trans World's fees to WAI and to Serv-Co (and PPP, the administrator and payer of claims on dental and drug coverage) also were not in accordance with fee schedules filed by Trans World with the Department.* In short, the fees received by Wallach and Winick were concealed from the Insurance Department.

(c) Concealment of fees from the United States Department of Labor

The Welfare and Pension Plans Disclosure Act of 1958** required welfare plans to disclose certain insurance information to the United States Department of Labor on a "Form D-2." The Employee Retirement Income Security Act of 1974 ("ERISA"),*** effective January 1, 1975, superceded the Welfare and Pension Plans Disclosure Act, and required welfare plans to make comparable

* Trans World has argued that the Serv-Co contract did not have to be filed because Serv-Co was performing the functions of a group department for Trans World. But Serv-Co was not a division of Trans World. It was, by the terms of the Consulting and Administrative Agreement, an independent contractor (Agreement, §1, p. 1). Moreover, even if payments under consulting agreements may not have to be in accordance with filed schedules, payments under administrative agreements must be. Since this was an administrative agreement, combined with a consulting agreement, the payments to Serv-Co had to be in accordance with a filed schedule and they were not.

** 29 USC §1001, et seq, effective January 1, 1975.

*** 29 USC §301, et seq.

disclosures on a "Form 5500." A major purpose of these disclosure requirements is to make a matter of public record the total fees and commissions paid to insurance brokers and others in connection with union welfare fund insurance, in order to deter kickbacks and other illegal commissions.

Both Forms required reporting funds to disclose the names of each recipient of fees and commissions and the amounts paid to them. From 1968 through 1978, these Forms were annually submitted by the Fund to the United States Department of Labor.

The financial data concerning the fees and commissions paid by Trans World were prepared by Serv-Co, submitted for review to Trans World, and then delivered to the Fund. This information was then incorporated in the Forms, which were filed by the Fund with the Department of Labor. The data were also included in "Summary Annual Reports" which the Fund was required to, and did send annually to all of its 14,000 participants.

The fees and commissions paid to Wallach and Winick were not fully disclosed to the Department of Labor. Indeed, in all of the filings with the Department of Labor, Wallach was never listed as a recipient of commissions and fees of any kind. Trans World's "promotional" payments to WAI, under the Special Group Representative Agreement, also were not disclosed.

Rather, they were treated by Trans World as overhead costs and, on that theory, not revealed as commissions, even though, as shown above, they clearly were commissions to Winick.

Trans World's payments to Serv-Co (and to PPP) were not specifically identified either, but were included in the Forms, lumped together with other items, as a "charge for risks or contingency." A "charge for risk" is the profit margin of the insurance carrier for taking the risk; a "charge for contingency" is the amount the insurance carrier sets aside for protection against unforeseen events. By lumping the fees paid to Serv-Co and PPP with other charges, under the category "charge for risks or contingency," the total administrative charges to the Fund were concealed.

An examination of the filings with the Labor Department would not have revealed how much Trans World was paying to third parties, such as Wallach and Winick, for fees and commissions. Wallach received about \$1.3 million in commissions from Trans World from 1972 through 1978. Yet he was not identified as the recipient of any fees in the filings. WAI was identified as the recipient of "service" fees but no mention was made of its receipt of \$931,200 as a "Group Representative" of Trans World. Moreover, because Serv-Co was not identified, there was no way to tell from the filings

that Winick was being paid twice for performing the same illusory services--once through WAI and again as a shareholder in Serv-Co.

(d) Concealment of fees from the Fund's beneficiaries

Under its collective bargaining agreements, the Fund was required to send each of its participants Summary Annual Reports of the business and affairs of the Fund. These reports included certified financial statements showing the Fund's income, expenditures, and related matters. The Reports also included the financial data concerning the fees and commissions paid by Trans World.

In preparing the Summary Annual Reports, the Fund used data furnished by Trans World and prepared by Serv-Co concerning the fees and commissions Trans World had paid. This data consisted of nothing more than the information contained on the Form 5500's, which Trans World had submitted to the Fund for filing with the United States Department of Labor. Since, as mentioned above, the Form 5500's failed to properly disclose the payment of fees to Serv-Co and Wallach, the same omissions were repeated in the Summary Annual Reports.

As a result, the participants in the Fund could not determine from the Summary Annual Reports the total service fees paid by Trans World, at the Fund's

expense, to third parties associated with the Fund. Nor could they tell that large payments were being made to Wallach.

* * *

As brokers, Wallach and Winick were fiduciaries, and therefore, they had a duty to disclose to the Fund the amount of their compensation from Trans World. They also had a duty to assist the Fund in obtaining insurance at the most reasonable rate.* In blatant disregard of these obligations, Wallach and Winick sought to obtain insurance from the company which would provide them with the largest commissions--indeed illegal commissions--rather than the least costly insurance. To accomplish this, they hid the commissions they were receiving by disguising them as "service fees" and "promotional fees." Then, they concealed these payments from the Insurance Department, the Department of Labor, and the Fund.

* In Brink v. DaLesio, 82 F.R.D. 664 (D.C. Maryland, 1980), Alfred Bell provided consulting, administrative, and insurance brokerage services to Teamsters Local 311 welfare fund. The fund's administrative costs were twice the average cost for similar funds. Bell failed to inform the trustees that various of the fund's insurance carriers also paid him for certain administrative services charged to the fund. In holding Bell liable to the fund, the Court stated that a broker has: "a duty . . . under the common law to divulge the amount of compensation he is receiving from the insurer as well as a duty to assist the insured in obtaining insurance at the most reasonable rates."

In addition, they fraudulently led the Trustees to believe that they had placed the insurance on the basis of competitive bids with the least costly available carrier and that their fees had been approved by the Insurance Department. In our view this course of conduct constituted fraud, under applicable Federal and State law.*

* See Title 18 United States Code §1341 (Mail Fraud), and New York Penal Law §§155.05 and 155.35 (Grand Larceny Second Degree).

IV. THE INSURANCE DEPARTMENT'S INVESTIGATION

On September 20, 1978, the Insurance Department commenced a formal investigation of the premiums Trans World was charging the Fund and other union welfare funds. The existence of the excessive charges had been brought to the Insurance Department's attention by Robert Nuding, Chief of the Department's Policy Branch in Albany. Nuding had determined that the "retentions" Trans World was charging the Fund were averaging about 23 percent of premiums. He concluded, in a letter to the Department's counsel, that this was "a ripoff of massive proportions," and so advised the Department's General Counsel.

In 1978 and 1979, the Insurance Department conducted its investigation, which involved taking testimony from officials of Trans World, and from Wallach, Winick, Serv-Co, and others. This testimony revealed that Wallach and Winick were being paid large fees for services which were actually performed by the Fund's internal staff.

The investigation also incorporated a survey done by Nuding which established that the normal cost of insurance for large welfare funds is in the area of 6 to 10 percent of premiums.

By the fall of 1979, the Insurance Department had determined that Trans World had overcharged the

Fund by at least \$2.6 million between January 1, 1972 and December 31, 1978. The Department demanded that Trans World repay one-half of these overcharges to the Fund and admit violations of the Insurance Law. Trans World took the position that if it had to make restitution, so should Wallach and Winick, who had received a large part of the overcharges. As Sidney Glazer, Associate Counsel, of the Department, testified before the Commission:

Q. Did (Trans World) indicate that they felt if any restitution that would be made that they would want the third-party administrators to be included?

A. Yes. They also took the position that if retentions were excessive they were in large part based upon their payment of high fees of excessive fees and, therefore, the Department should include the demand we were making upon Trans World for return of monies, include the third-party administrators who had received these excessive service fees, include them as respondents in these demands, so they can contribute toward any restitution.

Negotiations followed involving the Insurance Department, Trans World, Winick, and Wallach. During the negotiations, Trans World proposed that the Settlement Agreement provide that the settlement was a "full, fair, and complete" recovery of all overcharges.

Glaser testified:

Q. I would like to call your attention to paragraph 6 of the proposed stipulation.

* * *

That contains language which Superintendent Lewis referred to, I believe, as follows.

"Having obtained a full, fair, and complete recovery of all charges of Trans World and the other Respondents deemed by it to be excessive, the Department will neither take nor initiate any further actions or proceedings ...".

Was that provision found objectionable by the Department?

A. Yes. The characterization of the recovery as full, fair, and complete was objectionable to us because, indeed, it was a fifty percent recovery, and we in no way wanted to characterize or obscure the fact that it was a fifty percent recovery, that it was not a full recovery.

The Insurance Department rejected this proposal:

Q. Did Mr. Jordan [counsel to Trans World] or any of the other participants in this settlement express apprehension or concern about the possibility of Trans World or its service providers being sued by the Fund?

A. Yes, they did.

Q. What was said in substance with respect to that?

A. The Department would not participate in any way in precluding the trustees of these funds or the beneficiaries from attempting, if they saw it to be their duty or their wish, to obtain any further monies in the matter.

By November of 1979, Trans World, Wallach, Winick, and the Insurance Department had agreed in principle to a settlement involving restitution of \$1.3 million to the Fund. However, Trans-World, Wallach, and Winick were apprehensive about making payment without assurances that they would not later be sued by the Fund for excessive charges not covered by the settlement.

V. FEINSTEIN'S RESPONSE TO THE INSURANCE DEPARTMENT'S
INVESTIGATION AND THE SETTLEMENT

Feinstein learned that the Insurance Department was conducting an investigation by no later than March, 1979. At a Trustees' meeting on March 16, 1979, he told the Board that the Insurance Department was "objecting to the amounts of money which Trans World retained for payment of administrative expenses, commissions, fees and other expenses beyond the payment of claims."* However, Feinstein went on to tell the Trustees that "all fees, commissions and charges were always on record with the Insurance Department, as well as our premiums and they were aware of them." As noted previously, this statement was false. The fees, commissions, and charges made by Trans World had not been duly filed with the Insurance Department.

Sometime later in 1979, Feinstein asked Harold L. Fisher, Esq., who was counsel to Local 237 (and not the Fund), to meet with Albert Lewis, Superintendent of Insurance, to discuss the investigation. Lewis testified that during a brief meeting Fisher told him he was representing Feinstein personally, and that one of the Insurance Department's attorneys allegedly was "out to get" Feinstein. Lewis

* The quotations are taken from the minutes of a meeting of the Trustees held on March 16, 1979.

replied that no such vendetta was being conducted by his office.

In his appearance before the Commission, Feinstein testified that he sent Fisher to the Insurance Department to learn what the investigation was about, so that the Trustees would be fully informed as to any overcharges that were being made by the Fund's insurance carrier. When asked why he sent Fisher, rather than the Fund's counsel, he said he did so because Fisher had a personal relationship with Superintendent Lewis. In fact, Lewis testified that Fisher made no inquiry as to the nature of the investigation, or Trans World's overcharges. He merely expressed to Lewis a concern that the Insurance Department not conduct a personal vendetta against Feinstein who, of course, was not the subject of the investigation.

Despite Fisher's visit to Lewis, the investigation went forward and reached a point of settlement by the end of 1979.

In November, 1979, officials of Trans-World, and its counsel, met with Feinstein, Wallach, and Harold Baer, Jr. of Guggenheimer & Untermyer, counsel to the Fund, to discuss the proposed settlement with the Insurance Department. At this meeting, the Fund was asked to provide releases as a condition of the settlement. Feinstein responded that the Fund could not give

releases without first determining whether the settlement was appropriate. Subsequent events raise serious doubts as to Feinstein's actual intentions in seeking such a determination.

Shortly thereafter, the Fund, through its counsel, retained William M. Mercer, Inc. ("Mercer"), a subsidiary of Marsh & McLennan, a large insurance broker, to analyze the proposed settlement. William Mackie, a vice-president of Mercer who was in charge of the matter, testified that on December 19, 1979, he was retained to:

. . . evaluate the [1.3] as to whether or not it was an acceptable offer and should they, the union, seek more money, should we, in our evaluation, determine that maybe it should have been something else other than [1.3], we should get back to them and tell them about that.

Mackie testified that at a meeting on December 14, 1979, he was told by Andrew Fisher, Esq. -- counsel not to the Fund but to Local 237 itself -- that if he was able to justify the settlement, and the Fund later received the proceeds, the Fund might hire Mercer to tell the Fund "what kind of benefits they could buy with the \$1.3." Mackie conceded that in saying this "counsel might have been whetting my appetite to take on the account." Mackie was also told that time was of the

essence and that he had to reach a conclusion as to the settlement in less than two weeks.

In mid-December, 1979, Mackie undertook to read twenty seven volumes of testimony given to the Insurance Department and other extensive material, and to render an opinion within two weeks. Mackie testified:

We were asked to evaluate all of the circumstances and to get back within fourteen days, given in Harold Baer's communication to me, in his letter, approval to go ahead with a stated rate and come back to him with a verbal report over a period, at the latest, within fourteen days, and that they may require at some time later a written report.

On January 30, 1980, Mackie met with Feinstein and Baer and reported his conclusion that the settlement was acceptable:

At 9:30 on January 30th [I] met at 216 West 14th Street on the third floor with Barry Feinstein [and Harold Baer] . . .

[I]t had to be [the 30th because] I couldn't make the verbal presentation to Harold Baer for one reason or another, and Harold put it off until I could make the presentation to him and Barry Feinstein at the same time.

The verbal presentation was nothing more than, we think, the settlement offer was a good one and you should grab the money and run.

Satisfied with the oral report, Feinstein told Mackie to write a written report. Then, Baer conveyed Mackie's opinion to Trans World's attorneys, and Feinstein conveyed it to Wallach. Armed with the knowledge that Mackie had reported the settlement was "acceptable," and that it was therefore unlikely that they would face a lawsuit by the Fund, Trans World, Wallach, and Winick entered into the settlement with the Department, which was formally executed on March 19, 1980.

Although Feinstein and Baer had conveyed Mackie's conclusions to Trans World and Winick, the Trustees of the Fund were totally unaware that Mercer had been retained, that he had orally reported to Feinstein and Baer, and that the results of his study had been communicated to Trans World and Wallach. It was not until March 21, 1980 that the Trustees were even informed that Mercer was being retained. The minutes of the Board Meeting of March 21 read, in part:

... the Fund has hired the consultant firm of Marsh McClennon to review the entire matter to determine the appropriateness of the settlement.

This will be a very involved study and will be fully reported so a decision can be made on agreement.

Thus, the Board was led to believe on March 21 that Mackie was about to embark on a "very involved study" of the settlement whereas, in fact, Mackie had already finished the "study." As Mackie testified, his work in evaluating the settlement was "98 to 99 percent" complete by March 21.

On April 24, 1980, Mackie submitted a written report setting forth the conclusions he had reached earlier as to the settlement. His report confirmed the Insurance Department's finding that Trans World's 23 percent retention charges were excessive, and concluded that "the retention charges should have averaged between 12-14% of annually-paid premiums for the benefits provided during the indicated period."

In testimony before the Commission, Mackie said that the 12-14 percent figure was a consensus of several persons in his firm who had experience with similar funds. However, further testimony established that the consensus was reached during an informal conversation, without the benefit of any relevant data. In effect, it was no more than a "guess estimate." Moreover, Mackie was unable to cite a single example of a fund whose retention rate was as high as 12-14 percent. The Insurance Department had concluded that a retention of 6-10 percent would be normal for a fund of this size.

Mackie subsequently testified to the Commission that had he been aware of certain facts which he claimed had not been brought to his attention, he would have concluded that the proper retention rate was lower than 12-14 percent.* For example, Mackie said he was totally unaware of the services performed by Groom's staff. In other words, he did not know that the Fund was largely self-administered.

Mackie's report went on to note that the settlement of 1.3-million had "effectively reduced retention charges to an average of 17%." Nevertheless, the report concluded that the settlement was "reasonable and justified," particularly in light of Mackie's understanding that, "Trans World did not attempt to conceal or gloss over any rates or administrative expenses maintained during the contract period.**" Emphasizing that the fees Trans World had been fully disclosed, Mackie's report stated:

* The Fund's counsel demonstrated to the Commission that much of the material which Mackie claimed he requested, and was not given, was in fact sent to him. Thus, it appears that Mackie rendered his opinion without reading many of the critical documents furnished him.

** Mackie also claimed that, if sued, Trans World could make certain arguments to justify even a 17 percent rate. On the other hand, his report also noted that there was outstanding interest due the Fund.

Their aggregate charges, premium rates and expenses were submitted and received by the State Insurance Department as required, and apparently not disputed until the recent investigation. As the industry watchdog and arbitrator of improprieties, we may assume that more drastic measures would have been imposed much sooner by the State Insurance Department if deemed necessary.

This critical statement in Mackie's report was false. In fact, the charges and expenses of Trans World had not been submitted to the Insurance Department, as required, and had never been approved by the Department.

In early March of 1980, Mackie and one of his associates met with Harold Baer, Jr. and one of his associates to discuss a draft of Mackie's report. Mackie and Baer have informed the Commission that during that meeting, and on at least one earlier occasion, Mackie specifically discussed with the Fund's counsel the statement in his report to the effect that Trans World's charges and expenses had been duly submitted to the Insurance Department. Nevertheless, Mackie's report was submitted to the Trustees in the form quoted above.

When the Commission asked Mackie to explain the basis for the statement in his report that the fees paid by Trans World had been disclosed, he informed the

Commission under oath that his report referred to the Form 5500's submitted by the Fund. However, the Form 5500's were not filed with the Insurance Department, but rather with the United States Department of Labor (as the Forms themselves indicate). Moreover, as noted earlier in this report, the Form 5500's filed by the Fund did not disclose the payment of fees to Serv-Co and to Wallach. Therefore, the Forms could not have revealed to the Insurance Department all the fees and commissions paid by Trans World even if, as Mackie claims to have believed, they had been filed with the Insurance Department.

Moreover, on or about April 2, 1980, before Mackie's report was completed, the Fund's counsel furnished Mackie a copy of the Settlement Agreement between Trans World and the Insurance Department. That Agreement contained an admission by Trans World that it had paid commissions and fees in connection with its group life and accident and health insurance that were not filed with the Insurance Department, in violation of §§204(4) and 221(7) of the Insurance Law. Mackie testified that he read the Settlement Agreement quickly but "probably didn't even realize what I was reading."

On June 25, 1980, Mackie's report was discussed at a meeting of the Board of Trustees. After reviewing the report, and a statement by counsel concerning

legal issues which would be involved in an action to recover the overcharges, the Trustees unanimously adopted a resolution "that the settlement be accepted" and the matter be "closed." At the time this resolution was adopted, the Insurance Department had already reached its settlement with Trans World, Wallach, and Winick three months earlier, and the Fund had accordingly been paid approximately half of the overcharges. For the Fund to "accept" the settlement, and "close" the matter was to surrender, without compensation, a valid, additional claim of at least \$1.3 million and, with interest, as much as \$2.3 million. Yet that is what the Trustees proceeded to do.

According to the minutes, the Trustees then directed the Fund's counsel to draw up "limited releases," which would release Trans World, Wallach, and Winick from liability for all matters covered by their settlement with the Insurance Department. In other words, the Trustees voted to release Trans World, Wallach, and Winick from liability for all the overcharges they had made to the Fund, even though the settlement had recovered only half of those overcharges, and Mackie's own report, as flawed as it was, had itself concluded that between \$600,000 and \$1.1 million, plus interest, was still owing to the Fund.

The minutes also state that before the

Trustees voted to release Trans World, Wallach, and Winick, Feinstein told them that all of the commissions and fees received by Wallach and Winick "had been filed with the State and not rejected." This was a vital statement. If Wallach's and Winick's fees had been properly filed, then the Trustees might reasonably have believed that the Fund had simply been overcharged. It was precisely the concealment and non-filing of the commissions and fees that proved that Wallach, Winick, and Trans World actively defrauded the Fund. In this case, had the Trustees known that the fees and commissions had not been filed, it would have been far less likely that the Trustees would seek no further recovery from Trans World, Wallach, and Winick. It might also have led to a termination of the existing contracts between the Fund, Wallach, and Serv-Co.

Feinstein, on behalf of Wallach and Winick, represented that all fees and commissions had properly been filed with the State. The statement was made to the Trustees in the presence of Mackie and Baer. Both knew or had cause to know that the representation was not true, yet neither made any effort to correct this grossly misleading statement.

In the spring of 1980, the Fund gave Mackie a second retainer. This was to analyze the administration of the Fund by Serv-Co and Wallach to whom the Fund's

programs had been entrusted after the Fund became self-insured on January 1, 1979. In the summer of 1980, Mackie reported that Serv-Co's operation was not professional, and he recommended that his firm replace Serv-Co. Mackie testified that Feinstein responded as follows:

Just keep in mind whatever we do has got to involve Billy Wallach because that man has saved the Fund countless thousands of dollars, and he may have said millions, . . . in everything he has done.

Mackie testified that Feinstein told him to take up with Wallach the possibility of Mercer's replacing Serv-Co:

A. [We] all had a meeting, myself, Mr. Feinstein, Mr. Baer, Mr. Fisher [in July, 1980] . . . During the meeting [Feinstein] called Billy Wallach . . .

His comment at the time, if I remember correctly, was Billy, I'm coming out to use your pool tomorrow . . .

And then he said . . . I've got your friend Bill Mackie here.

And then there was something said on the other side, and Feinstein laughed a little bit, and between the two of them they kind of arranged that I would meet with Billy Wallach during the following week.

Q. What was the purpose . . . in your getting together with Mr. Wallach?

A. The purpose was . . . to discuss Serv-Co . . . and how they could be replaced [by Mercer].

Q. And why would you be discussing that with Mr. Wallach?

A. My understanding is that Mr. Wallach is a consultant to the Fund, and that he was acting on the orders of Mr. Feinstein.

Mackie met three times with Wallach to discuss whether Mercer would replace Serv-Co. Wallach made it clear that he would not approve the substitution unless he, Wallach, was also going to be involved in the future administration of the Fund. Moreover, Wallach insisted that Winick would have to be involved too, even though Mackie's report had been highly critical of Serv-Co, which was to be replaced. As Mackie described his conversations with Wallach:

A. [O]ne thing that did come out in the conversations was . . . my personal feeling about the Serv-Co operation. And I told him, I think they are a shlock operation . . .

And we did talk about Winick in particular, and he was kind of pushing me, at one time he even asked me if Mercer would be interested in buying Serv-Co.

And I said, "Not in your fondest dreams," . . .

And then he asked me, he said something to the effect about having to have Winick with him because Winick was like a right-hand man to him.

* * *

Q. And did he indicate to you, did he urge you . . . to somehow include Mr. Winick in whatever arrangements were being discussed for the [F]und?

A. [Wallach said,] if Winick and I, meaning if I had any problems with Cal Winick, that Wallach and I would have some problems.

Q. What did that statement by him mean to you at the time?

A. That unless Winick and I and Wallach could see eye to eye, more than likely there would be no further business relationship with Mercer.

Mackie's discussions with Feinstein concerning changes in the Fund's administration apparently were suspended when it became known in the late summer of 1980, that this Commission was conducting its investigation. Public hearings were held in November of 1980, at which Mackie testified that Feinstein had insisted that Wallach continue as the Fund's advisor, despite Feinstein's knowledge of the results of the Insurance Department's investigation.

At the public hearings, Feinstein testified that the contracts between the Fund, on the one hand, and Wallach and Serv-Co, on the other hand, were being

reviewed and that no decision had been made as to whether they would continue as the Fund's consultants and administrators. Feinstein stated that he wanted to examine the matter in light of whatever findings the Commission would make. Thus, in November, 1980, a full year after he knew for certain that Trans World, Wallach, and Winick had made gross overcharges to the Fund, Feinstein told the Commission that the Fund might still continue to use the services of Wallach and Serv-Co.*

Subsequently, Feinstein informed the Commission that in December, 1980, the Trustees voted to discontinue Wallach's services as of January 1, 1981 and to replace Serv-Co when a substitute was found.

* Testimony at the Commission's hearing established that the Trustees were unaware of Feinstein's discussion with Mackie concerning Wallach's continued involvement.

VI. FEINSTEIN'S EARLIER EFFORTS TO PROTECT WALLACH AND WINICK - THE COMPTROLLER'S AUDIT

The Insurance Department's investigation was not the first occasion on which Feinstein attempted to protect Wallach and Winick at the expense of the Fund. Feinstein testified repeatedly and emphatically that he first learned that Wallach and Winick were receiving excessive fees in 1980 through the Insurance Department's investigation. The facts show he learned much earlier.

In late 1976, Feinstein learned that the Fund was being audited by the New York City Comptroller's Office, and that the auditors believed the Fund was paying grossly excessive amounts to Trans World for insurance. Feinstein did not tell the Board of Trustees about this but rather attempted to refute and block the audit. This incident casts light on Feinstein's attitude toward Wallach and Winick.

In 1975 Arthur Puchalsky, an accountant with the Comptroller's Office for twenty-five years, became chief of the division authorized to conduct welfare fund audits. Puchalsky believed that welfare fund audits had been unreasonably neglected, since New York City contributed great sums into welfare funds and had no direct control over their management. Moreover, welfare funds historically had been subject to fraudulent and incompetent management.

In late fall, 1976, Puchalsky ordered one of his auditors to begin an audit of the Fund. After completing the preliminary review of the Fund's records, Puchalsky and the field auditor, Robert Rosenfeld, focussed on five areas: the cost of insurance; the purchase and improvement of the Fund's building; the placement of Fund money in non-interest bearing accounts; the allocation of expenses between the Fund and the Local 237 union; and travel and entertainment expenses of the Trustees.

By early April, 1977, Puchalsky and Rosenfeld had completed a draft audit report on the Fund. According to Puchalsky, the draft was forwarded to Martin Ives, the First Deputy Comptroller, and sent to the Fund.

The draft, which was sent to the Fund and its counsel and was later discussed by Feinstein personally with the Comptroller's office, was highly critical of the Fund's management and its purchase of insurance. With respect to the Fund's insurance program, the draft made serious allegations of overcharges and excessive commissions. Thus, it stated on page one that: "The Fund is not purchasing the best benefit package at the lowest cost," and it unfavorably compared the Fund to the United Federation of Teachers' Welfare Fund, by stating that, "only 7.5% of the UFT's expenditures were

for insurance administration and claims handling as compared to 26% for the Fund." The draft also criticized the Fund for failing to "obtain bids and for failing to go to the large insurance carriers regularly writing insurance for union welfare funds." In addition, the draft was critical of other practices of the Fund, such as excessive travel and entertainment expenses for the Trustees and payment by the Fund to the Union of large sums for ostensible services to the Fund.

Although counsel to the Fund had been preparing a written response to the Comptroller's audit, the Fund did not produce a written response. As Puchalsky testified:

Q. With whom did you have [a] conference in order to attempt to obtain written responses to the audit?

A. I believe I spoke to Mr. Baer on a number of occasions, requesting the written response.

Q. What were his reasons for not sending written responses to you?

A. If my memory serves me correct, I believe he indicated that the response would be forthcoming shortly. However, I never received it. Subsequently, I was notified by the First Deputy [Ives] that he had been contacted and they wished to have an exit conference at the Comptroller's Office.

The meeting to which Puchalsky referred was held on April 22, 1977. It was arranged by Feinstein, through Richard Wells, the Comptroller's executive assistant from 1974 through 1980, whom Feinstein knew. Wells testified about his conversations with Feinstein as to the audit:

At some point, some years ago, Mr. Feinstein mentioned to me that the Comptroller's Office was performing an audit of his Union and that people in his organization disagreed with some of the thrusts or conclusions or whatever you would call them, of the Comptroller's Office.

And he inquired how his people, or he in fact might get in touch with the right people in the Comptroller's Office to pursue the matter to discuss their differences.

Q. What did you tell him?

A. . . . I probably told him what I told the hundreds of other people who called me with similar kinds of questions relating to different functions of our office.

I said, I'll look into it and get back to it.

Q. What steps if any did you subsequently take as a result of Mr. Feinstein's conversation with you?

A. I believe that I spoke to Mr. Ives, the First Deputy Comptroller and told him about the conversation.

Wells and Ives both testified that, following this call, they met Feinstein for lunch near Feinstein's office where, Ives recalls, they discussed the audit.* A few days later, Feinstein, Baer, and Wallach met with Ives, Puchalsky, and Rosenfeld for several hours, and discussed the draft report. The auditors recall that throughout the discussion of the Fund's insurance costs, Feinstein vigorously asserted that the Fund was getting the best protection at the least cost.

After the meeting, Ives asked Puchalsky and Rosenfeld to do some additional work on the insurance issue. According to Puchalsky, Ives was "concerned with standards. How can we make an allegation without having a standard of comparison . . ."

Puchalsky received no instructions to finalize the report because Ives had decided that, as he testified, "many of the significant audit comments and recommendations were not adequately supportive and were not adequately documented," and that he "needed to obtain the additional data concerning welfare funds to be able to establish whether charges like that are high."

Ives testified that because of the lack of documentation for his auditors' opinion that the Fund's charges were too high, he ordered the audit indefinitely

* Feinstein testified that he had no recollection of this luncheon. Wells recalls it but did not recall what was discussed.

suspended, and he promulgated "Directive No. 12"* to get such documentation.

* * *

On April 26, 1979, Charles L. Smith, Regional Administrator of the United States Department of Labor's Labor-Management Services, wrote Comptroller Goldin to inform him of an audit of the Fund which had been started by Smith's office. The Department of Labor ("DOL") concluded that it lacked jurisdiction over the Fund and discontinued the audit. Before doing so, however, the DOL reached conclusions about the Fund very similar to those reached earlier by the Comptroller's auditors. As Smith wrote the Comptroller:

In the course of our audit questions were raised regarding the fund's apparently high

* Directive No. 12 requires city employee welfare funds to provide the Comptroller's Office with:

- 1) an annual report prepared by a CPA;
- 2) two management letters, one prepared by a CPA and another, by the Board of Trustees;
- 3) the annual report distributed to a fund's membership; and
- 4) a copy of Federal Form 5500 with supporting schedules or a financial statement prepared according to a format copied by the Comptroller's Office from the Form 5500.

Much of the information sought by Directive 12 was already available. City employee welfare funds were required under collective bargaining agreements to submit a yearly audit performed by a CPA to the Comptroller. The Form 5500 is a public record on file with the Department of Labor. A welfare fund's annual report is widely distributed and can be simply obtained from the welfare fund on request.

administrative expenses, excessive insurance retention charges and improper allocation of union expenses to the fund . . . It is thought that your office would have an interest in this matter and if so, our file on this discontinued audit is available for your review. [Emphasis added]

After receipt of this letter, Comptroller Goldin ordered that the audit of the Fund be resumed, nothing having been done on the audit since its suspension by Ives two years earlier.*

In connection with the audit's resumption, the auditors obtained a copy of a "Report of Investigation" prepared by the DOL. The DOL Report raised issues and made findings similar to those in the Comptroller's 1977 draft audit report. The Report stated, for example, that there were "questionable practices with regard to the insurance policy purchased by the trustees to provide benefits. Also the ratio of expense to contributions is high." It also stated that "an analysis of retentions made by the New York Insurance Department for a similar group of policies with similar premium volumes showed that retentions ranged between 6% and 8%." As previously noted, Trans World's retention charges averaged about 23 percent of premiums from 1972 through 1978.

* The Comptroller testified that it "was possible that I would have made a copy of this letter, sent a copy of this letter to Mr. Feinstein; I don't know."

In November, 1980, the Comptroller's Office finally released its audit of the Fund. The audit report found that the Fund's internal administrative expenses averaged 15.3 percent of New York City's contributions to the Fund from 1975 through 1978, as compared to an average of 9.4 percent for other welfare funds of comparable size. The high expenses were attributed in part to the Fund's practice of paying Local 237 over \$200,000 annually to reimburse the Union for the alleged services of Union representatives in explaining benefits to Fund participants. The report was highly critical of this practice. The report was also very critical of excessive expenses incurred by the Trustees for travel and conferences, the under-charging of the Union for rent, the payment of fees to consultants for unspecified services, and similar acts.*

* The Comptroller's Audit noted that the Fund, and Local 237, had retained Walter Eisenberg, a Labor Arbitrator for the City, and John Zuccotti, former Deputy Mayor, as "independent fiduciaries" to review the Fund's payments to Local 237. The Report took strong issue with the findings of these fiduciaries and concluded that their findings were not documented.

The Audit also noted the payment of various fees to other consultants, including \$144,228 paid to Program Planners (a pension and administrative consulting firm run by Jack Bigel). The Audit criticized the Fund for making such payments without appropriate written agreements detailing the types of services to be provided by such consultants.

The Comptroller's audit supports the Commission's own determination that the Fund has wastefully managed its assets. From 1972 through 1980, the Fund's participants obtained only about 65 cents in benefits out of every dollar the Fund received from New York City.

With regard to the insurance costs, the audit merely cited the results of the Insurance Department's investigation and the refund of \$1.3 million to the Fund. It noted that Wallach and Serv-Co had continued to act as consultants to the Fund after it became self-insured and recommended that the Fund solicit bids upon the termination of Wallach's and Serv-Co's contracts.

The data derived from Directive 12, the need for which purportedly had delayed the audit for over two years, was not incorporated or used in the final audit. Ives testified that by the time the audit was done, the Insurance Department had completed its investigation and, therefore, the Comptroller made no independent findings about the insurance issues and merely referred to the results of the Insurance Department's investigation.* The audit made minimal reference to the Insurance Department's findings. Thus, it ignored entirely

* The data from Directive 12 was used in a report published by the Comptroller in February, 1980 which discussed the internal administrative expenses incurred by various funds.

the question of whether the settlement by Trans World, Wallach, and Winick had been in full satisfaction of the Fund's claims. The report therefore failed to note that at least \$1.3 million, plus interest, in excess charges were still unaccounted for.

In testimony before the Commission, Feinstein repeatedly asserted that he did not know until March, 1980, when the Insurance Department announced the results of its investigation, that Trans World, Winick, and Wallach had received excessive fees. Indeed, he castigated the Insurance Department for not bringing those facts to his attention earlier.

The facts surrounding the audit by the Comptroller's office belie Feinstein's testimony. It is clear that Feinstein knew as early as 1977 of claims by the Comptroller's Office that the Fund was paying too much for insurance, and that Trans World was making excessive payments for commissions and administrative charges.

As noted above, the Fund's counsel asked Winick to respond to these claims, whereupon Winick sent them a letter that included patently false representations to the effect that he and Wallach had obtained competitive bids for the Fund's insurance and that their fees and commissions were competitive and had been approved by the Insurance Department.

The fraud practiced by Wallach and Winick does not, however, excuse Feinstein's response to the questions raised by the Comptroller's office concerning the excessive fees and commissions. Feinstein clearly should have referred this matter to the Trustees for an inquiry as to exactly what fees Wallach and Winick were receiving and whether such fees were excessive. Taking Winick's word that the "the schedule of commissions is competitive with what other Insurance Companies pay" was to accept the self-serving statement of a person who was one of the very subjects of the auditor's accusations concerning excessive fees.

Instead of seeking independent opinion to determine the validity of the auditors' allegations, Feinstein called Wells, Comptroller Goldin's executive assistant and chief political aide, to complain about the auditors. Then he met with Ives and Wells at lunch, at which the audit was discussed. Finally he, Wallach, and Baer met with the auditors and aggressively defended the Fund's insurance program.

Feinstein's efforts to prevent release of the Comptroller's audit in 1977 bore fruit at that time. The Comptroller, Harrison J. Goldin, and the First Deputy Comptroller, Martin Ives, have asserted that the decision to suspend the 1977 audit was based purely on professional considerations. They have stated that they

could not responsibly have criticized the Fund's purchase of insurance, or any of its other management practices, without possessing comparable data on other funds. Directive 12, they state, was designed to provide the Comptroller's office with the data required to compare one fund to another.

However, the data played no important part in the Comptroller's final audit report on the Fund. Moreover, there were other ways in which the Comptroller's office could have obtained additional data concerning insurance costs without having to suspend the audit for, as it turned out, more than two years.

Comptroller Goldin has testified that he did not believe Ives was affected by his private discussions with Wells and Feinstein, although the Comptroller recognized that Feinstein's contacts with Wells and Ives might have had "an appearance that can be misconstrued":

Q. It certainly was not a usual practice, . . . for your executive assistant and your First Deputy Comptroller . . . to sit down during the course of an audit for lunch with the subject of that audit who might be highly embarrassed by its conclusions, and who happened to be

a major political figure whose support is very important at election time to the City of New York?

A. In retrospect, I can see why it is you are saying that given what we now know, there could be an appearance that could be misconstrued. I see your point.

Comptroller Goldin testified that he makes every effort to insulate himself from the audit process:

My audit program is kept wholly independent from my political activity. Mr. Ives is not involved in my political activity at all and certainly the people under him and the levels of administration and management that we have in the audit level operations are fully insulated and fully detached.

Therefore, they make decisions based on their own professional judgment. Those decisions are not cleared with me. Those decisions are not reviewed by me.

The Comptroller's philosophy, that audits should not be affected by political considerations, is commendable. But such a policy would require that the audit process be removed entirely from political contacts. In this case, that did not occur in the sense that Feinstein, a supporter of the Comptroller, was able to go outside ordinary channels to meet with Ives in the

presence of the Comptroller's chief political aide.* The Commission has no way of determining whether this contributed to Ives' decision to suspend the audit. But the fact remains that, after Feinstein's intervention, the audit was suspended for a considerable period of time. During that period of time, Trans World, Wallach, and Winick continued to defraud the Fund.

* Wells also testified that, in November, 1980, several months after leaving the Comptroller's office, he learned that the Audit Report was about to be released and immediately notified Feinstein. Feinstein expressed a concern about the tone of any press statement which might accompany the Audit's release. Wells then reviewed a draft of the press release and suggested changes in its wording to the Comptroller.

VII. THE FAILURE OF FEINSTEIN AND THE BOARD OF TRUSTEES
TO PROTECT THE FUND

Under Local 237's collective bargaining agreements, and as a matter of common law, the Trustees of the Fund had fiduciary obligations to preserve the Fund's assets and minimize its expenses. The record shows that Feinstein and the Trustees failed to meet these obligations.

The Fund has seven Trustees.* Each of them is an officer of Local 237 and each became a Trustee because he or she was an officer of the Union. They became officers of the Union after their nominations for Union office were approved by Feinstein.

It is clear that the Trustees merely rubber stamped decisions made by Feinstein as to the policies and management of the Fund. Indeed, the testimony revealed that there had never been a dissenting vote cast by a Trustee on any issue during the period from 1972 through 1978.

Wallach and Winick became the Fund's brokers

* The following are the persons who have served as Trustees during the period from 1972 through the present. (PRESENT BOARD MEMBERS): Barry Feinstein, 1964-Present; Edward Cervo, 1970-Present; Melanio Cuebas, 1975-Present; Pauline Dyer, 1967-Present; Carroll Haynes, 1978-Present; Frederick Kennedy, 1971-Present; Frank Scarpinato, 1972-Present. (PAST BOARD MEMBERS): Robert Beverly, 1964-1978; Arthur Foley, 1964-1975; John Koch, 1964-1973.

solely on the basis of Wallach's relationship with Feinstein and without any independent evaluation by the Trustees. Feinstein brought in Wallach in 1967 without advising the Board as to the nature of their relationship and without disclosing that he was a Director of Wallach's Lion Insurance Company.

The Trustees, including Feinstein, testified that they relied on the advice of Wallach and Winick in placing the Fund's insurance with Trans World. They also testified that they knew Wallach and Winick were being paid by Trans World, but they did not know how much they were being paid. In substance, the Trustees claimed that their main concern was with the amount of the Fund's premiums paid to Trans World, and that so long as the premiums were "competitive" they were not particularly concerned about the size of the fees and commissions received by Wallach and Winick. As Edward Cervo, one of the Trustees, stated:

Everything we talked about at Board meetings as I remember was total package. We talked in terms of premiums.

And all the information I ever been made aware of was that whatever bids were made were made in total packages, this would be the total cost. . .

The Trustees met with Wallach and Winick on a regular basis at quarterly Board meetings and occasionally at out-of-town seminars and conferences. They testified that Wallach and Winick also entertained them from time to time.* Yet the Trustees never inquired what fees Wallach and Winick were receiving. Moreover, they never reviewed, or had counsel review, any of the contracts between Trans World, Wallach, and Winick.

Groom testified that his staff performed such functions as issuing certificates, maintaining enrollment cards, preparing bills, distributing booklets and processing claims. The staff also spent a considerable amount of time answering questions from beneficiaries of the Fund and explaining their benefits to them. For these services, the Fund allocated over \$400,000 a year. In addition, the Fund paid Local 237 about \$200,000 annually, purportedly to reimburse the Local for time spent by its business agents and employees in explaining the Fund's benefits to the members.

If the Trustees had reviewed the contracts, it would have been evident that (a) Serv-Co, Wallach, and Winick were being paid ostensibly to do many of the things which were being done by Groom's staff and

* Wallach, for example, each year gave a party for the Trustees at a cost exceeding \$1,000.

(b) Wallach and Winick were being paid ostensibly to perform services for which Serv-Co was being paid. It also would have been evident that the brokers were being paid large fees for the performance of "services" such as "education of agents" or "installment and resolicitation", which could not properly be charged to the Fund.

In early 1979, the Trustees learned that the Insurance Department was investigating Trans World. The Trustees knew that the investigation involved claims that excessive fees were being charged by the insurance company to the Fund.* The Trustees were assured by Feinstein that the investigation was "routine." At no time did they make an independent inquiry to determine the nature of the investigation, or the validity of the allegations that the Fund's charges were excessive. Instead, the Trustees took the attitude that they should await the results of the Insurance Department's investigation before taking any action. As Carroll Haynes, a Trustee, put it:

We were waiting for the investigation to be completed. After the investigation is when . . . to analyze the situation.

* Groom testified as a witness before the Insurance Department on April 17, 1979, at which time he was accompanied by the Fund's counsel, Harold Baer, Jr., Esq.

You are asking me to say that a person was guilty and before the decision came out, you had had a good relationship with that particular person.

You are saying because of an investigation you should have done this.

The Trustees acted irresponsibly in failing to inquire about the facts underlying the Insurance Department's investigation. It may not have been the responsibility of the Trustees to determine whether its brokers, Wallach and Winick, or Trans World, had complied with all the requirements of the Insurance Law. But it was their job to assure that the Fund was not being charged excessive fees. That was a responsibility which the Trustees had at all times, regardless of whether an investigation was being conducted. Rather than giving the Trustees an excuse for deferring their own inquiries, the Insurance Department's investigation made it especially important for them to inquire fully into the relationships between Trans World, Wallach, and Winick.

In March of 1980, the Trustees learned that Trans World, Wallach, and Winick had agreed to pay \$1.3 million to reimburse the Fund for excessive charges. This settlement clearly put the Trustees on notice that the Fund had been grossly overcharged. Despite the Trustees' assertions that they had previously deferred

looking into the matter until the Insurance Department's investigation was over, the Trustees continued to refrain from taking any action with respect to Wallach and Winick.

The Trustees testified that when they learned about the settlement they hired Mercer to determine whether the settlement was reasonable. They apparently regarded this as an appropriate response to the payment by Trans World, Wallach, and Winick of the \$1.3 million.

This response was not satisfactory. Mercer was hired in order to determine whether the \$1.3 million was ample restitution, or whether additional moneys were due the Fund. But whether or not additional moneys were due, the Trustees knew that Trans World, Wallach, and Winick had received large sums of money from the Fund to which they were not entitled. In these circumstances, it was incumbent upon them to replace these unfaithful fiduciaries. That Wallach and Winick had paid back, under compulsion, some of the money they had improperly received, did not make them fit persons to continue handling the Fund's assets.

Mackie reported that a proper retention charge would have been 12-14 percent of premiums. Even accepting his figure, which he later admitted was too high, Trans World, Wallach, and Winick owed the Fund between \$680,000 and \$1.1 million, plus interest, above

the \$1.3 million which they had returned. Yet the Trustees unanimously voted not to sue.

The Trustees undoubtedly relied on counsel's advice, and on Mackie's report, in deciding not to sue. But whatever advice they may have received from counsel, it is hard to understand their decision not to sue, in light of the large sums still owing the Fund and the facts uncovered by the Insurance Department. Moreover, there is no conceivable justification for the Trustees' decision to continue to employ Wallach and Winick as the Fund's consultants in view of the results of the Insurance Department's investigation. In our opinion, the Trustees' actions can only be explained by Feinstein's total domination of the Board and his personal reluctance to sue Winick or Wallach, with whom he was so closely associated, or to discontinue the Fund's relationship with them.

There is little doubt that the Trustees were misled as to the practices engaged in by Wallach, Winick, and Trans World. For example, the Trustees were told that Wallach and Winick had sought competitive bids for the insurance. In fact, no genuine effort was made to seek competitive bids. The Trustees were also told that all of the fees and commissions had been duly filed and approved by the Insurance Department. In fact, such commissions and fees had been systematically concealed.

Moreover, the Trustees were provided with data and information by Trans World which purported to set forth the commissions and fees which were paid. In fact, those reports were incomplete and misleading.

The Trustees testified that they had no knowledge of the arrangements whereby Winick paid over to Wallach \$1.3 million in service fees which Winick received from Trans World. They also testified that they did not know that Winick was the beneficiary of duplicative contracts, whereby he was paid once through WAI for allegedly performing certain services and again through Serv-Co for allegedly performing the same, or substantially overlapping, services.

The Trustees testified that if they had known of these matters and other facts discussed in this Report, such as Feinstein's familial and business relationship with Wallach, they would have terminated the relationships between the Fund and Wallach and Winick. Thus it is clear that, in approving the relevant contracts, the Trustees were defrauded.

This does not excuse what the Commission believes was their failure to properly exercise their responsibilities to preserve the Fund's assets. The Trustees relied on Wallach and Winick in the administration of the Fund. Yet, when facts were brought to their attention indicating that the Fund had been the victim

of a "ripoff" by Wallach and Winick, Feinstein was willing to continue using them as consultants, and the Trustees did not question Feinstein's judgment. Indeed, it appears that Wallach and Winick would have continued indefinitely as the Fund's advisors -- with perhaps some cosmetic changes in their functions and fees -- if the full story concerning the practices engaged in by Trans World, Wallach, and Winick had not been brought out by this Commission.

VIII. THE ROLE OF COUNSEL

In December 1972, the Fund retained Guggenheimer and Untermyer, and Harold Baer, Jr. of that firm, as counsel. Guggenheimer & Untermyer represented the Fund and not any individual Trustee or group of Trustees. As counsel, Baer attended Trustee's meetings regularly, and he and the firm performed various tasks relating to the Fund's business including litigation, the preparation of opinions as to duties of Trustees, review of contracts, and like matters.

In late 1976, Guggenheimer and Untermyer learned that the Comptroller was doing an audit of the Fund. Counsel then asked Winick and Mandel about the auditors' allegations concerning the Fund's insurance costs. As mentioned previously, Winick responded to these inquiries by making deliberate misrepresentations to counsel concerning the fees and commissions he and Wallach were receiving, as well as other matters relating to the Fund's insurance costs.

Guggenheimer & Untermyer began a written response to the Comptroller's report, but their response never was finished. Instead, a meeting was held at the Comptroller's office, which Feinstein arranged through Wells, to discuss the auditors' draft report. At that meeting, Baer was present when Feinstein vigorously defended the Fund's insurance costs.

There is no reason to doubt that Guggenheimer & Untermyer was deceived by Winick when they made inquiry about the auditors' allegations. On the other hand, counsel did not see fit to tell the Trustees about the allegations of the auditors, or to recommend to the Trustees that an independent consultant be retained to determine the validity of the auditors' claims. Instead, counsel apparently thought it sufficient to rely upon Wallach and Winick who themselves were charged by the auditors with taking excessive fees.

If counsel had recommended that an independent consultant be retained, or if counsel had reviewed the various insurance contracts between Trans World and the brokers, the fraudulent scheme perpetuated by Wallach and Winick might have been uncovered.

In April, 1979, Baer represented Robert Groom when he testified as a witness in the Insurance Department investigation. The questioning of Groom by the Insurance Department made it evident that the Department believed the fees paid earlier to Trans World and Winick were excessive, that Winick had been paid for services which actually were rendered by Groom's staff, and that Winick had been paid for services which were not proper charges under the Code of Ethical Practices. Similar questions had, of course, been raised earlier by the Comptroller's auditors. Nevertheless, apparently

counsel again did not recommend to the Trustees that an independent consultant be retained to determine the validity of such changes. Rather, counsel appears to have adopted the same "wait and see" attitude concerning the Insurance Department investigation which the Trustees expressed to the Commission.

When the Insurance Department investigation was completed, Baer met with Morton Greenspan, Chief Counsel of the Insurance Department, to discuss a number of unrelated matters. During the course of their conversation, Greenspan suggested to Baer that the Fund consider suing Trans World and the brokers. Guggenheimer & Untermyer furnished the Commission with evidence that its attorneys did research as to legal theories that might be used as the predicate for a lawsuit. Yet, Baer advised the Trustees that a suit probably would not be productive.

The Commission is perplexed by counsel's opinion in light of the evidence that Trans World, Wallach, and Winick had systematically overcharged the Fund for years and made fraudulent misrepresentations to the effect that the insurance charges and fees had been filed with, and approved by, the Insurance Department.

As noted earlier in this Report, at the meeting of the Trustees on June 25, 1980, at which the Trustees voted not to sue Trans World, Wallach, or Winick,

the Trustees reviewed Mackie's Report, which stated:

Their aggregate charges, premium rates and expenses were submitted and received by the State Insurance Department as required, and apparently not disputed until the recent investigation. As the industry watchdog and arbitrator of improprieties, we may assume that more drastic measures would have been imposed much sooner by the State Insurance Department if deemed necessary.

At the Trustees meeting, and on prior occasions, Feinstein told the Trustees that Trans World's fees and charges had all been approved by the Insurance Department.

Baer informed the Commission, by letter dated February 27, 1981, that he and one of his associates had met with Mackie and reviewed a draft of Mackie's report. As already noted, they specifically discussed the statement in the report that Trans World had not concealed its rates and administrative expenses. Indeed, as a result of their discussions, a section in the draft of Mackie's report, referring to the alleged submission of the fees to the Insurance Department, was changed.*

* The draft stated that Trans World's "service charges, premium rates and expenses were filed." The final report dropped reference to "service charges" and referred instead to "aggregate charges" apparently with reference to the disclosures made in the Form 5500's. However, as previously noted the Form 5500's were not submitted to the Insurance Department, and they clearly did not fully reveal the fees paid by Trans World.

In late March, 1980, Guggenheimer and Untermyer received a copy of the Settlement Agreement between Trans World and the Insurance Department, which reflected Trans World's admission that the fees and commissions had not been duly filed.

Yet, when Mackie's report was discussed at the Trustees' meeting on June 25, 1980, Baer did not bring to the Trustees' attention the fact that Trans World's fees had not been filed. Nor did counsel correct Feinstein when he told the Trustees that the fees had been accepted by the Insurance Department. Thus, when the Trustees decided not to sue, it was without knowledge that Trans World, Winick, and Wallach had not only overcharged them but had lied to them and had concealed their fees from the Insurance Department.

IX. THE ABSENCE OF CONTROLS OVER THE EXPENDITURE
OF MONEYS BY THE FUND

In recent years, the payment of supplemental benefits to public employees has become an increasingly important part of their compensation. Currently, New York City alone contributes more than \$140 million annually to union welfare funds.

Prior to 1975, the Federal Government and the States had concurrent jurisdiction over welfare funds. Therefore, prior to 1975, the Insurance Department actively reviewed New York State's welfare funds through its Pension and Welfare Unit.

In 1975, the Employee Retirement Income Security Act ("ERISA") (29 USC §1001) became effective in 1975. ERISA preempted the states from regulating private welfare funds which thereafter fell under the jurisdiction of the United States Department of Labor and the Treasury Department. As a result, the Pension and Welfare Unit of the Insurance Department, which had consisted of about 60 persons, was disbanded.

Although ERISA preempted local regulation of welfare funds generally, it did not affect local jurisdiction over public employee welfare funds, which were

exempted from the coverage of ERISA.* In short, although it appears to be widely believed that the Federal government reviews the administration of all welfare funds under ERISA, the Federal government has no present authority to do so with respect to public employee welfare funds.**

New York State has no program equivalent to that created by ERISA for the control of public or private welfare funds. In the area where New York State has not been preempted, its statutory power to regulate such funds is found in Article III-A of the New York Insurance Law, which gives the Insurance Department power to examine into the affairs of employee welfare funds. However, the Insurance Department has taken the position, citing a 1956 opinion by the Attorney General (1956, Op. Atty. Gen. 187), that it does not have jurisdiction over unilaterally administered welfare funds

* Section 1003(b)(1) of ERISA explicitly exempts "governmental plans" from the statute's coverage. It has been held that since the Local 237 Fund was established by a government, i.e., the City of New York, its administration is not subject to the provisions of ERISA, Feinstein v. Lewis, 477 F.Supp. 1256 (S.D.N.Y. 1979).

** Even with respect to the welfare funds subject to ERISA, it has been reported that the DOL is unable to exercise close supervision since there are a very large number of funds which file reports under ERISA, and the Department of Labor has allocated only about 250 persons to enforce ERISA.

such as Local 237.*

Since public employee welfare funds are not subject to Federal regulation under ERISA, and unilaterally administered public welfare funds may not be subject to State jurisdiction under the Insurance Law, a fund such as the Local 237 Welfare Fund is totally unregulated by public authorities. Such funds are, as noted above, required to file reports with the City Comptroller's office and are subject to audit, but the Comptroller has no power to take remedial action with respect to abuses uncovered by an audit.

The Insurance Department's investigation, which resulted in the payments to the Fund by Trans World, Wallach, and Winick, arose under the Department's power to investigate insurance companies. As Superintendent of Insurance Albert Lewis testified, this restitution was achieved "in a somewhat fortuitous 'back door' manner in that an examination of the Trans World Insurance Company revealed inordinate services fees."

As Superintendent Lewis noted further, even this "indirect intervention" by the Insurance Depart-

* Section 37-A of the Insurance Law defines employee welfare fund as meaning funds "established or maintained jointly by one or more employers together with one or more labor organizations." Thus, the Attorney General's opinion seems inapplicable to a fund such as Local 237's since it was clearly "established" by contract between Local 237 and the City and is clearly "maintained" by the City's yearly contributions.

ment can be easily avoided by funds adopting self-insurance programs. In this case, the Local 237 Fund became self-insured in January, 1979, so that the Insurance Department had no power to seek recoveries of excessive fees paid thereafter by the Fund to Wallach and Serv-Co.* And, of course, the Insurance Department presently has no jurisdiction over the Fund.

In order to remedy some of the gaps which allow many welfare funds to go unregulated, the Insurance Department submitted a proposal in 1980 to the New York State Legislature for an amendment to the Insurance Law and Banking Laws which would have explicitly extended the authority of the Insurance and Banking Departments to cover unilaterally administered public welfare funds.

The proposed amendment would thus have eliminated the disparity in supervision between jointly administered and unilaterally administered funds. This amendment was not adopted.

* As previously noted, even after January 1, 1979 when the Fund became self-insured, Wallach and Serv-Co continued to receive large fees from the Fund.

X. FINDINGS

A. Criminal Violations

In the opinion of the Commission, the Fund was the victim of criminal fraud. From 1972 through 1978, Wallach and Winick together sought and obtained over \$2 million under sham contracts which they did not intend to perform and did not perform.

The Fund paid a premium to Trans World which was inflated by the illegal commissions Trans World paid to Wallach and Winick. The Fund paid the premium on the basis that the commissions and fees were necessary and proper compensation for services actually performed.

Wallach and Winick assured the Fund that the fees they received were proper, had been approved by the Insurance Department, and that the premium paid to Trans World was the lowest available. In fact, their fees were not for performing legitimate services but were illegal commissions given in return for placing the Fund business with Trans World. Moreover, the premium, far from being the lowest available, was grossly inflated because it included the illegal commissions and excessive fees paid to Winick, Wallach, and Serv-Co.

In addition, from 1979 through 1980, Wallach and Winick together received \$356,000 under a service

contract that was also procured by fraud. In entering into this contract, the Board of Trustees was not given material information that Wallach and Winick had defrauded the Fund for over six years; that Wallach was Feinstein's relative; that Feinstein had been a director of one of Wallach's insurance companies; that Wallach had agreed to pass on a substantial portion of his fees to Winick; and that Wallach was to be paid over \$177,000 a year.

The Fund was also defrauded by being deprived of the honest and loyal services of its brokers and the Fund's chance to bargain for the least costly insurance with all the relevant facts before it. As brokers and consultants to the Fund, Wallach and Winick had a fiduciary duty to seek insurance for the Fund at a fair and reasonable cost. They betrayed the trust which the Fund had in them. They obtained insurance so as to maximize their illegal commissions. They failed to disclose to the Fund the moneys they received. They fraudulently induced the Fund to purchase insurance from Trans World by asserting, and creating a false record, that no other insurance company would insure the Fund's benefits. All these facts were concealed from the Trustees by Trans World as well.

These acts constituted a scheme to defraud the

Fund in violation of Federal* and State law.**

B. Breaches of Fiduciary Duty

Mismanagement and abuses of welfare funds deprive workers of the benefits to which they are entitled. Labor officials, as administrators of these funds, and those affiliated with them, have fiduciary responsibilities in managing the funds. They are in a position of trust. When these officials fail to exercise their responsibilities working men and women suffer the loss.

Throughout this Commission's hearings, Fein-

* Title 18 of the United States Code §1314, makes it a federal offense to "devise any scheme or artifice to defraud" in which a mailing occurs. The elements of the offense of Mail Fraud are (1) the use of the mails in furtherance of (2) a scheme to defraud. U.S. v. Corey, 566 F.2d 429 (S.D.N.Y., 1977).

This statute was applied in U.S. v. George, 477 F.2d 508 (7th Cir., 1973), cert. den., 414 U.S. 827 (1974), in which the Court found that Zenith Corporation had been defrauded by a purchasing agent's placement of business with a supplier who paid kickbacks to the purchasing agent. The Court found that there was a scheme to defraud because Zenith was deprived of the purchasing agent's "honest and loyal services" in seeking suppliers for its products. The defendant's fraud consisted of his holding himself out to be a loyal employee of Zenith but actually not giving his honest and faithful services to the company by withholding from the company material knowledge concerning the moneys he was receiving from the supplier and the supplier's willingness to sell its product for less money.

** Penal Law §§155.05 and 155.35 make it a Class D felony to obtain property by "false pretenses."

stein and the Trustees repeatedly asserted that the Fund's benefits were superior to those offered by other public employee funds.

The Commission has seen no evidence that the benefits of the Fund were superior to those offered by comparable funds. In any event, those benefits could have been obtained from Trans World without paying illegal commissions to Wallach and Winick. The plain duty of the Trustees was to manage the Fund in such a manner that its assets not be dissipated by the payment of unlawful and excessive commissions and fees. This duty is owed by the Trustees to the public employees who are the beneficiaries of the Fund. In a broader sense, it is a duty which they owe to the taxpayers who provide New York City with the money it contributes to the Funds.

The Commission finds that the Trustees, and particularly Feinstein, breached this obligation. The Trustees clearly abrogated to Feinstein virtually all responsibility for decisions affecting the Fund's vital interests. They made no effort independently to determine whether the Fund's insurance program was economic or proper. Even when they learned of the Insurance Department's investigation, they declined to make inquiries, which a prudent man would make, to determine whether Trans World's charges, and Wallach's and

Winick's fees, were reasonable and proper. In the face of a settlement whereby Trans World, Wallach, and Winick were compelled to pay the Fund \$1.3 million, the Trustees declined to institute suit for excessive charges not repaid and continued the arrangements which were enriching Wallach and Winick at the Fund's expense. The Trustees would have continued to do so, we believe, if this Commission had not exposed the facts set forth in this Report, causing the Trustees belatedly to terminate the Fund's relationship with Wallach and Winick.

Feinstein's conduct is more egregious. He retained Wallach to handle the Fund's insurance, knowing that Wallach had no experience in group insurance, and he failed to disclose to the Trustees the nature of his relationship with Wallach and The Lion Insurance Company. In light of the close relationship between Wallach and Feinstein, it is highly unlikely that Feinstein did not know, at all times, the extent to which Wallach, at least, was profiting from the arrangements with Trans World. In any event, he clearly knew no later than January of 1979, the extent to which Wallach and Winick profited prior to that time.

Feinstein denied receiving any moneys from Wallach and Winick. But regardless of any payment, the fact is that Wallach and Winick could not have continued

their fraud without Feinstein's willingness to continue the Fund's relationship with them and his efforts to prevent disclosure of all the facts pertaining to them.

When questions were raised by the City Comptroller's office and the Insurance Department concerning the fees and charges which the Fund was paying for its insurance, Feinstein reacted by attempting to bury those inquiries instead of pursuing them. Even after it was a matter of public record that Trans World, Wallach, and Winick had "ripped off" the Fund, Feinstein insisted that Wallach continue as the Fund's paid advisor and consultant.

The Trustees' responsibility for the excessive fees paid to Trans World, Wallach, and Winick cannot be viewed in isolation. Rather, it must be judged in light of their overall handling of the Fund's assets and affairs.

As reported by the City Comptroller's Audit Report of November, 1980, the Trustees have allowed the Fund's assets to be wasted in a number of ways in addition to the improvident insurance arrangements described in this Report. The Audit Report, for example, asserts that the Fund unreasonably pays over \$200,000 a year for the salaries of employees of Local 237 and for Union related administrative expenses; that the Union, which leases space in the Fund's building, is under-

charged for rent; that the travel and entertainment expenses of the Trustees are excessive or improperly documented; and that the Fund pays large sums to consultants without the benefit of written contracts and without presenting documentation demonstrating what services the consultants perform.*

These findings by the Comptroller's office reinforce this Commission's view that the Trustees did not meet their fiduciary duties in dealing with the Fund's assets with respect to the Fund's insurance program, and that a substantial portion of the Fund's assets have dissipated as a result of the Trustees' neglectful practices.

C. The lack of controls by governmental regulatory authorities

Public-employee welfare funds are not subject to the requirements of ERISA. To the limited extent that such funds are insured and jointly administered, they are subject to the jurisdiction of the New York Insurance Department. However, most public-employee welfare funds are unilaterally administered and, there-

* The 1977 draft audit report also had disclosed that the Fund had placed up to \$750,000 in non-interest bearing accounts at the Amalgamated Bank; a practice which ended at the end of 1977 only in reaction to the auditors' disclosures.

fore, may not be under the jurisdiction of the Insurance Department. The Insurance Department clearly is to be complimented for the vigorous job it did in uncovering the abuses documented in this Report. But the Insurance Department is frequently powerless to prevent other such abuses.

In view of these gaps in regulatory power, a fund, such as that maintained by Local 237, is virtually without controls. Such funds are required to file reports with the City Comptroller's office and are subject to audit. But these audits are a low priority, and the Comptroller apparently has no authority to take independent enforcement action with respect to any abuses that may be discovered.

XI. RECOMMENDATIONS

1. The United States Attorney for the Southern District of New York, and the District Attorney for New York County, should institute criminal proceedings against those who criminally defrauded the Fund.

2. Barry Feinstein and the other Trustees of the Fund who were in office at the time these events occurred should resign or be removed as Trustees of the Fund.

3. The Fund should sue Trans World, Serv-Co, Wallach, Winick, and all others believed to be responsible -- including the Trustees if necessary--to recover the losses suffered by the Fund as the result of the fraudulent practices described herein.

4. Consistent with its other priorities, the Comptroller's office should consider instituting a stepped-up audit program for welfare funds.

5. The Insurance Department should continue to seek from the Legislature broader powers to provide better controls over the administration of public-employee welfare funds. Other agencies should consider whether to seek similar authority.

6. The City of New York should review the present system of managing public-employee welfare funds and should consider whether to insist that such funds be managed jointly by persons selected by the

Unions and representatives of the City, or that the benefits be provided through an entirely different system.