Americans for Financial Reform Education Fund

Sun Capital: A Case Study in Private Equity Looting

Introduction

Private equity (PE) controls a large and growing portion of the economy, including businesses and other assets like housing, that workers and consumers rely upon for jobs, goods and services. But too often predatory and extractive private equity business practices enrich the Wall Street firms while imposing painful costs on workers and communities. PE has increased in size nine-fold over the past two decades from $700 billion in global assets in 2000 to $6.5 trillion in 2019. Today, private equity controls some 8,000 companies in the United States, more than twice as many companies as are publicly traded on U.S. stock markets. Private equity firms manage more than $4 trillion in U.S. assets and now own companies that collectively employ nearly 9 million American workers.

Like many PE firms, Sun Capital Partners often buys up existing businesses, loots their assets, squeezes workers, decimates jobs through layoffs and bankruptcy, and threatens workers' retirement benefits.

Sun Capital

Sun Capital Partners was founded in 1995 by Rodger Krouse and Mark J. Ledder. Over the last 25 years the firm has acquired hundreds of companies, and the two partners have amassed a combined net worth of over $1 billion. This wealth accumulation has often come at the expense of workers, as evidenced in the examples below.

Sun Capital's Track Record of Greed

Shopko

Shopko was a Green Bay, Wisconsin retail chain established in 1962. Sun Capital purchased Shopko in 2005 in a leveraged buyout that saddled the company with $1 billion in debt. Sun then sold Shopko's real estate, forcing the company to rent back stores it once owned and while simultaneously stripping it of assets.This tactic is known as a sale-leaseback agreement, and it is one often used by PE firms to enrich themselves even though it weakens companies they own. Sun also paid itself several dividends, including a $50 million payback in 2015, along with quarterly consulting fees of $1 million and 1% consulting fees on at least six Shopko transactions.[1]

In 2019 this situation created by Sun Capital pushed Shopko into bankruptcy, in part due to a debt-to-asset ratio of 10-1. The subsequent liquidation cost the 14,000 Shopko employees their jobs. When the bankruptcy was announced, workers were promised severance pay to stay with the company through the grueling liquidation process. But the company later reneged on that promise.. Longtime workers like Jim Jordan, who had over 30 with the company, were left with nothing. "Like so many others at Shopko, all I wanted was to be able to work hard, support my family and retire with dignity," he wrote in a 2020 op-ed. "Instead, our future fell victim to vulture capitalists who cared more about buying up companies and running them into the ground — rewarding wealth, instead of hard work.[2]

Emerald Performance Chemicals[3]

Sun Capital formed Emerald Performance in 2006 after acquiring the company from Lubrizol and incorporating it together with other chemical companies they bought over the next four years. The company manufactured chemicals for industrial and commercial uses -- dangerous work requiring skilled labor.

Under Sun Capital, Emerald cut jobs, slashed pay an average of 30%, decreased vacation and overtime pay, outsourced the quality control lab, and eliminated the health and safety inspector. Emerald workers resisted these changes, and as a consequence of their fight back, on March 27, 2011, 42 workers at a Henry, Illinois plant were locked out, leaving them with no jobs and no health insurance. The workers were replaced with less skilled replacements, prompting health and safety and environmental concerns from the local community.[4]

During the lockout, there were five accidental releases into the air of hydrogen sulfide and three of carbon disulfide reported to the National Response Center (NRC) by Emerald. On July 20, 2011, an outside caller reported the release into the air of an unidentified substance to the federal agency, leading the Environmental Protection Agency (EPA) to fine Emerald $158,000 for failing to inform authorities in a timely manner of this accident, which released carbon disulfide and hydrogen sulfide in excess of acceptable limits.

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[1] https://www.axios.com/shopko-bankruptcy-sun-capital-547b97ba-901c-4201-92cc-6d3168357fa3.html

[2] https://madison.com/ct/opinion/column/jim-jordan-the-shopko-swindle-rewarding-wealth-instead-of-hard/article_cc733346-3a2e-5ba7-bd02-3dbe4fc4dec2.html

[3] https://www.teamster.org/sites/teamster.org/files/91211SunCapitalEmeraldToxicReport.pdf

[4] https://www.prnewswire.com/news-releases/teamsters-community-leaders-and-labor-allies-send-delegation-to-emerald-performance---sun-capital-partners-123575839.html

The Emerald Performance workers eventually returned to work and won a contract after a hard fight. Sun Capital later sold the company to another PE firm, American Securities, in 2014.[5]

Mervyn's

Mervyn's was a California-based department store chain founded in 1949. Sun Capital and partners acquired Mervyn's department stores in 2004 for $1.2 billion through a leveraged buyout with $400 million in equity, saddling the company with $800 million in debt. Like Shopko, Mervyn's was stripped of its assets, including through a sale-leaseback agreement that doubled their rental costs, with the proceeds going to the PE firms. Over the next 4 years Sun cut 30,000 jobs at Mervyn's and in 2008 the 18,000 workers who survived the original cuts were laid off without notice or severance.

Marsh Supermarkets[6]

In 2006, Sun Capital Partners purchased Marsh supermarkets, a grocery store chain founded in 1936. The company had 104 supermarkets and 154 convenience stores. Sun Capital put up $88m in the deal and piled $276 million in debt on the supermarket chain. Sun Capital sold off Marsh's real estate holdings for $260 million and $40 million worth of Marsh's convenience stores, generating undisclosed commissions for private equity executives, while forcing the grocery stores to lease back their stores.

Marsh had three retirement plans. One for the top five executives and two for workers.Only the executives' plan was fully funded and Marsh's top five executives were awarded $14 million in retirement payments, with CEO Don Marsh receiving $7 million and corporate counsel P. Lawrence Butt receiving $2.2 million. The workers' pension plans were underfunded by tens of millions of dollars, causing pension payments to workers in the fund to be cut by up to 25%.

Scott Brass

Founded in 1956, Scott Brass was a family-owed brass and copper parts manufacturing company with plants in Rhode Island and Indiana. In 2007, Sun Capital purchased Scott Brass (one Sun Capital fund bought 70% of the company and another bought the remaining 30%). Although the funds claimed there was no partnership between them, the funds placed Sun

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5 https://www.prnewswire.com/news-releases/american-securities-agrees-to-acquire-emerald-performance-materials-261876941.html

6 https://www.washingtonpost.com/business/economy/as-a-grocery-chain-is-dismantled-investors-recover-their-money-worker-pensions-are-short-millions/2018/12/28/ea22e398-0a0e-11e9-85b6-41c0fe0c5b8f_story.html

Capital employees in two of the three Scott Brass board seats.[7] The manufacturer was acquired for $7.8 million, which included $4.8 million in debt loaded on to the portfolio company.

In announcing the acquisition an official press release highlighted the private equity firms' access to capital to help the company "realize substantial growth and profit enhancement."[8] But in 2008 the story quickly changed when the factory was abruptly shuttered, leaving around 80 workers without a job. "Friday night we got a phone call. They said the plant was closed and not to come in, cause we was [sic] scheduled to work that night," one worker was quoted as saying in a local news report at the time. "I'm very shocked and saddened because I iked working there, most people did, they were a pretty fair company."[9] Scott Brass went into bankruptcy the following month.

Sun Capital Partners vs the New England Teamsters Pension Fund

When Scott Brass filed for bankruptcy in 2008, workers there were members of the Teamsters Union Local 364. Based on the collective bargaining agreement, the company owed $4.5 million in pension fund liabilities to the New England Teamsters Pension Fund - money that would go to pay the retirement benefits workers had earned and negotiated for. The Pension Fund demanded payment from Scott Brass and from Sun Capital, but they refused to pay, and said they were not responsible, setting off a decade-long legal battle.

In the legal case, the pension fund argued that the two Sun Capital funds, which indirectly owned 70% and 30% each of Scott Brass, should be held liable for the withdrawal liability triggered when the portfolio company stopped contributing to the multiemployer plan. The lower district court agreed, but then late last year, the First Circuit Court overturned that ruling, finding that, although the two Sun Capital funds together owned 100% of Scott Brass, they did not form a "partnership in fact."[10]

The November 2019 ruling meant that Sun Capital did not have to pay $4.5 million in liabilities to the pension fund after taking portfolio company Scott Brass into bankruptcy in 2008. The already extraordinarily rich executives of Sun Capital got a little bit richer, and working people were robbed of the retirement security they earned. The case also had broader implications for the entire private equity industry; the decision protected private equity's ability to exploit

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7 https://www.sullcrom.com/files/upload/SC-Publication-First-Circuit-Overturns-Sun-Capital-Decision.pdf

8 https://www.businesswire.com/news/home/20070212006043/en/Affiliate-Sun-Capital-Partners-Acquires-Scott-Brass

9 https://www.wndu.com/home/headlines/30924254.html

10 https://www.ropesgray.com/en/newsroom/alerts/2019/11/Sun-Capital-Prevails-in-Long-Running-ERISA-Liability-Dispute-But-Pension-Risks

loopholes in law and regulation to shield themselves from the consequences of their management decisions, and to hide behind complex ownership structures to extract profits from portfolio companies at the expense of workers at those companies.

“This is outrageous,” wrote private equity industry expert Eileen Applebaum in an email responding to the decision. “To be liable [for the pension withdrawal], Sun would have had to own at least 80% of Scott Brass. One of its funds owned 70% and another of its funds owned 30%. The question before the justices was whether this added up to 80% (or more).” Applebaum, who had written about the case in her book (with Rosemary Batt) “When Wall Street Manages Main Street,” explained “Sun Capital manages all of its funds to its own advantage. The [general partner] of each fund consists of a group of principals of Sun Capital. To pretend that these partners and employees of Sun Capital do not talk to each other or that Sun is not calling the shots is a travesty.”

The New England Teamsters Pension Fund petitioned the court to rehear the case, but iIn October of 2020, the high court declined without explanation, jeopardizing the solvency of the fund and giving the private equity industry the green light to shirk pension obligations to the workers of companies they own.[11]

Fighting Back to Stop Wall Street Looting

The greedy and harmful practices of Sun Capital are all too common in the private equity industry, and workers and policymakers are fighting back. Shopko workers organized a successful campaign to pressure Sun Capital to provide severance to those who lost their jobs. And in 2019, Senators Elizabeth Warren, Bernie Sanders, Tammy Baldwin, and Kirsten Gillibrand introduced the Stop Wall St Looting Act (S.2155 / HR 3848), along with Representatives Pocan, Jayapal, García, Grijalva, Khanna, Lee, Pressley, Schakowsky, and Tlaib in the House.

The Stop Wall Street Looting Act , if enacted, would prevent abuses like the ones Sun Capital’ engaged in. Specifically, the proposed legislation would define company ownership in a way that would have made Sun Capital liable for the pension obligation for workers at Scott Brass. Instead of allowing private equity executives to hide behind complex structures built to shield them from liability, the Stop Wall Street Looting Act would define ownership by who actually controls a company. The Act would stop rewarding private equity executives for loading portfolio companies with debt, stripping away assets, and paying themselves extractive fees and dividends. It would hold them responsible if they break the law or drive firms into bankruptcy. And it would protect workers if firms do go under, making sure they get severance and pension contributions they were promised, and elevating the priority of worker wages and benefits, while preventing bonuses and special payouts to executives.

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[11] https://www.plansponsor.com/supreme-court-denies-review-pe-firm-withdrawal-liability-case/