Funding Assurance Plan

An innovative banking proposal for distressed multiemployer plans

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Summer 2017

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A Social Welfare Crisis

- 10 million Americans are participants in multiemployer pension plans (“MEPPs”), and nearly 1 million of those are in plans which may go insolvent within 10 years.
- Nearly 100 billion dollars in future benefits obligations exist for these participants, yet only 40 billion in assets are available to pay these promised – and previously guaranteed benefits.
- The Pension Benefit Guarantee Corporation (“PBGC”) or the insurance program which backstops insolvent pension plans, is also projected to go insolvent by 2025, despite recent and significant increases to premiums paid by multiemployer pension plans.
- Decades of hard work and vested retirement benefits are in jeopardy for millions of Americans and their families, unless adequate funding sources are designed and implemented to protect multiemployer plans and provide another layer of protection against their failure.

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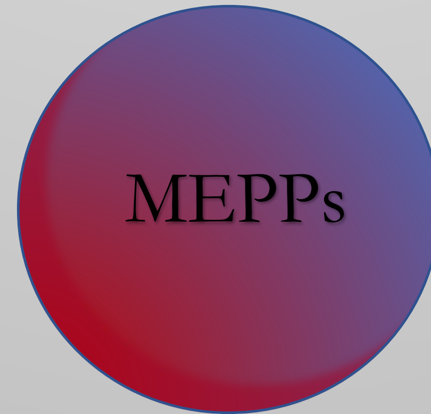
Two Decades of Funding Pressure

Late 1990s to present: Noticeable declining employer participation and contributions; increasing reliance on portfolio returns to pay benefits.



Late 1990s and early 2000s: Adverse economic cycles: The dotcom bubble crash and post-9/11 recession lead to poor investment portfolio returns.

2007-2008: Financial market meltdown and extended period of recession following. Many funds lost up to 40% of their asset base during these years, exponentially hindering recovery prospects.

2017 and forward : Employer participation will continue to decline as funds continue to fail. Market stability is questionable, while actuarial assessments continue an upward trend. Technology and automation will continue to impact job growth and overall worker contribution funding to plans.

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Inadequate Solutions

- **The Pension Protection Act of 2006 ("PPA")** required trustees of distressed, critical status plans to implement rehabilitation plans which were designed to improve a plan's funding status to 84% within a 10 year period. Despite extending the age of retirement for active workers and drastically cutting future benefit accrual rates, these measures have failed to achieve expected outcomes in over 100 multiemployer plans.

- **The Multiemployer Pension Reform Act ("MPRA")** or Kline-Miller legislation passed in 2014, has not been shown to provide adequate solutions to fix distressed multiemployer plans. Benefit suspensions under MPRA law appear only to allow plans to, at best, "tread water" and not close most existing plans' operating deficits.

As employers and employees are losing faith in the multiemployer system as a whole, companies are and will continue to leave multiemployer plans – or opt out of joining - at an increasing and alarming rate. These actions further compound the funding pressure on plans and their remaining participants.

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The Need *for* Funding Assurance

- ***Employers*** want, and need to have a reasonable expectation – that their investment in their worker's retirement benefits will be secure. Past and current multiemployer funding improvement legislation has not provided this security.

- ***Employees*** currently active, have had to postpone retirement, accept wage deferrals, forfeited vacation time, and future benefit accruals. They also have a reasonable expectation of retirement security and want to be assured that what they have given up has not been in vain.

- ***Retirees*** have also diverted wages and benefits to fund pension promises, and they also have a reasonable expectation that their decades of labor will be honored, and that retirement security will be restored and placed once again on solid ground – and within a reasonable period of time.

Enticing new employers to join multiemployer plans will be difficult unless rehabilitation period and recovery times are both more proactively avoided, and then, as necessary, minimized and addressed more rapidly through the design and effective implementation of and accessibility to new funding sources for multiemployer plans.

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A Funding Solution

- If multiemployer plans are going to survive, they must be allowed to adapt. One potential component of an adaptive strategy that is available to the multiemployer plan system is banking revenue.

- Recognizing the shortfall in MEPP's employer contributions over the last two decades, the need to create a new revenue stream for MEPPs has been clearly identified. Designing a special-purpose credit union, specifically for participants and families of the multiemployer group, can, demonstrably, help close the operating deficits of many plans now facing insolvency, while also potentially preventing future declines in currently stable funds.

- Developing a special-purpose credit card program issued by the MEPPs credit union, would allow members in distressed pension plans to forfeit card rewards, rebates, and bonus points. As members forfeit their "dividends," they will be helping fund their own retirement plans and thereby reduce the need for devastating benefit reductions.

- Currently, many popular credit card programs allow customers to forfeit "rewards", thereby funding a special-purpose cause. These include college 529 plans and other goal achievement programs. As family members make purchases with their credit cards, 1% to 5% of the transaction helps fund a particular cause.

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A Brief History *of* Credit Unions

BEHIND THE HEADLINES

Revealing your ancestors' everyday lives at the time of major world events

MMXVII

No. 124

1846

THE POTATO FAMINE

Villagers in County Kerry during the famine, 1846

Potato blight was spreading through northern and central Europe in 1845, so its appearance in Ireland was anticipated, if dreaded.

More than a third of the Irish potato crop was lost in the harvest of 1845. Potato shoots on the wet ground were covered with a film of thin white filaments. An unusually wet but warm summer had given the opportunity for the down-like fringe of blight to be spread, and the potato fields seemed to be ruined overnight. Beneath the ground, blight was attacking the potatoes themselves from spores washed down through the soil. Cell after cell of the potato was destroyed until the vegetable became pulp.

It is now known the blight was caused by *phytophthora infestans*, a tiny organism, but for your ancestors it was thought of as a deadly fungus.

The crop that was lifted in autumn 1845 was blighted and that caused hardship but it was not out of the ordinary. There had been 17 potato crop failures in Ireland in the 100 years before 1846. Now, week by week, conditions worsened. In 1846, three-quarters of the harvest was lost. This caused unending misery for the Irish peasantry who were already living at the lowest level.

Their conditions were commented on in an official report: "In many districts their only food is the potato, their only beverage water… their cabins are seldom a protection against the weather." Tenants had to work for their landlords in return for the patch of land they needed to grow their own potatoes. They were reliant not only on a single crop, but on a single variety, the 'Irish Lumper', so

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77

The origin of credit unions date back to the mid 19th century in Europe. During the devastating crop failure and famine of the 1840s, cooperatives were formed to lower the cost of bread and provide low cost credit to farmers. In 1850, the first financial cooperative was formed, called the "The People's Bank." Social welfare causes helped develop today's modern day credit unions.

The first American credit union was established in 1909. In 1917, during World War I, credit unions were given non-profit tax exempt status. In 1934 President Franklin Delano Roosevelt signed the Federal Credit Union Act into law, creating a national system to charter and to supervise federal credit unions.

- Credit unions are member owned, and have no shareholders.
- Democratic governance.
- Each member has one vote, regardless of the size of the member's deposits.
- Member-elected board of directors and are volunteer based.

Establishing a national, special-purpose credit union to address the multiemployer funding crisis, is now more necessary than ever and an idea whose time has come.

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America is Credit Union Strong

Number of U.S. Credit Unions: 5,857
Total membership: 109.3 million
Total assets: 1.355 trillion

Source: CUNA, March 2017

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Five Well-Capitalized U.S. Credit Unions

Navy Federal Credit Union

Members: 6.99 million
Assets Managed: $81.5 billion

State Employees Federal Credit Union

Members: 2.22 million
Assets Managed: $36.5 billion

Pentagon Federal Credit Union

Members: 1.51 million
Assets Managed: $22.4 billion

Boeing Employees Credit Union

Members: 1.02 million
Assets Managed: $17.2 billion

Congressional Federal Credit Union

Members: 47,272
Assets Managed: 927 million

The "NewCU"

A Special-Purpose Multiemployer Federal Credit Union

Determining Field of Membership and Purpose

- To meet the legal requirements for establishing a credit union charter, the field of membership must share a common bond. This can include occupational, associational, or a well-defined geographical community location. The 10 million participants of the multiemployer pension retirement system would meet the *common shared bond (CSB)* requirements of a credit union charter.
- Member deposits into the credit union, otherwise known as shares, allow the member to become an owner of the credit union with a right to vote.
- Shares provide primary funding for the lending and investment activities of the credit union.
- Credit unions are non-profits and distribute profits in the form of dividends, low-interest rates, or rewards programs.
- The **NewCU** would allow its members to forfeit or give back dividends to help fund their retirement plans. A dominant credit card program would allow members to use their cash back, rebates, and rewards points for this same funding cause.

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The "NewCU"

A Special-Purpose
Multiemployer
Federal Credit Union

Building The Institution

- To form the **NewCU**, a new charter could be created, or the **NewCU** could be established through mergers and acquisitions with existing charters.
- There were 200 credit union mergers in 2016. Most of these mergers allowed for credit unions to combine assets and expand products and services.
- Dozens of small U.S. credit unions are already established, serving union multiemployer participants and family members. These include the Teamsters union, Actors & Musicians unions, International Brotherhood of Electrical Workers (IBEW), UPS employees and many others.
- Potential membership with the **NewCU**: 10 million multiemployer participants plus their family members.
- Total field of membership that have a common shared bond with multiemployer pension affiliations could be as high as 40,000,000 Americans (including participants and family members).

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Revenue & Earnings Potential

Part I

The Most Profitable Product for a Credit Union

- ***Credit cards are the most profitable product a credit union can offer.***
- Section 8 of the *Fair Credit and Charge Card Disclosure Act of 1988* directs the Federal Reserve Board to transmit annually to the Congress a report about the profitability of credit card operations of depository institutions.
- In 2016, The disclosure report to Congress confirmed that credit card operations remain the most profitable sector of all banking activities.
- Member loans are considered a bank's assets, providing an ongoing revenue stream for the institution. For all commercial banks, the average return on average assets (ROAA), before taxes and extraordinary items was 1.30 percent in 2015 compared to 4.36 percent for the large credit card banks.
- Credit card programs make money through customer fees, interest on revolving debt, and merchant fees (a percentage of the purchase price from the merchant), ranging from 1%-3% per purchase.

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Revenue & Earnings Potential

Part II

Identifying the Revenue Stream

American Household Debt

Q1 2017

	Total money owed by average U.S. household carrying this type of debt.
Credit Cards	$16,425
Mortgages	$180,018
Auto Loans	$29,058
Student Loans	$50,868
Any Type of Debt	$135,924

NerdWallet report, based on data from the Federal Reserve Bank of New York and the Census Bureau.

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Revenue & Earnings Potential

Part III

Preliminary Start-Up Roadmap

Projected Membership and Financial Goals

	Year One	Year Two	Year Three	Year Five
Membership	500,000	750,000	1,000,000	3,000,000
Assets	10 Billion	15 Billion	20 Billion	35 Billion
Required Capital	900 Million	1.35 Billion	1.8 Billion	3.15 Billion

Field of Membership:

i. Multiemployer participants (appx. 10,000,000)
ii. Multiemployer participants and family members (appx. 40,000,000)
iii. Multiemployer plans (appx 1,400)

Capital Requirements:

In order to meet capital requirements (9% of assets), seeking secondary capital markets may be required, which would be pursuant to Congressional action.

High-Impact Membership Marketing Plan:

Unions, employers and plan sponsors will collaborate and follow a special marketing outreach plan targeting potential members. A strong membership drive will include the support of all stakeholders.

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Revenue & Earnings Potential

Part IV

Gaining Benefit from the Cooperative

The “NewCU”, Returning Value to Membership

- Credit Unions are non-profits, and the general tenet in these cooperatives is to return value to members equally as opposed to banks which maximize profits for shareholders.

- The NewCU would have to balance the accumulation of retained earnings to support capital for its growth, with the desire to return “value” in the form of surplus earnings, to offset multiemployer pension deficits.

- Following the models and balance sheets of the most high-performing credit union in America, will help achieve the Funding Assurance Plan’s objectives.

- A credit union model with a strong credit card program, and a significant portion of its assets in credit card lending, would allow the cooperative to potentially achieve 2.5% or greater return on assets. These earnings and member’s dividends will help close funding deficits of distressed multiemployer plans.

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“Multiemployer Pension Plan Security Act”

The fourteen plans that have applied for pension cuts under the Multi-Employer Pension Reform Act of 2016 (“MPRA”), together with the United Mine Workers plan (“15 Plans”), are facing (in aggregate) an annual operating deficit of $1.7 billion, which represents an associated capital shortfall of $23.2 billion (based on an estimated annual return of 7.5%).

We propose repealing and replacing MPRA with the Multi-Employer Pension Plan Security Act (“MPSA”), which will be designed to provide a “once and for all”, comprehensive framework that delivers (i) retirement security to millions of families across the United States and (ii) critical balance sheet stability to American companies seeking to provide retirement support for their employees while maintaining competitive business operations in a global economy. We have provided below a brief summary of some of the key financial highlights of MPSA. We are optimistic that we can work together with other stakeholders, including leadership in the U.S. Congress and President Trump, to build a public-private partnership to fix a problem that has been decades in the making and that could have been avoided. We owe it to the generations of Americans that came before us, and those that will follow to keep building a better America: one that works together as a team and keeps its promises.

“Multiemployer Pension Plan Security Act”

All keys stakeholders in the multi-employer pension system (employer sponsors, union sponsors, employee participants and the U.S. Government) will be asked to play a role in addressing the capital shortfall. Please see below for the key highlights describing how we will recover the missing $23.2 billion. Plans that file for assistance in the future will follow a similar framework for resolution.

1. Employer Sponsors, Employee Participants and a **newly established special purpose credit union (or credit union program)** will share responsibility for **injecting $6.9 billion** into the 15 Plans to cover estimated **existing orphan liabilities**. The Treasury Department will be asked to support this injection with a 5-year zero interest loan to Employee Participants and a minimum level guarantee for Employer Sponsors (to support private financing) reflecting the potential cost to PBGC in the event of plan failures.

2. The Treasury Department will provide a 1% interest loan of $25 billion. Interest on the loan will be paid annually, and the principal will be returned in 14 years. This loan will be partially guaranteed by a reserve pool of $2 billion dollars to be raised equally from Employer Sponsors and Employee Participants.

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3. Employee Participants, their family members and other key private stakeholders will work with an existing credit union, or establish their own **special purpose credit union**, which will be responsible **for injecting a further appx $6.8 billion** over 14 years to support the MPSA comprehensive solution: (i) $2.3 billion coverage of appx 1/3 of the estimated orphan liability, (ii) approximately $1 billion to reduce the capital shortfall, and (iii) the remaining nearly $3.5 billion will be used to pay the interest on the Treasury Department loans.

4. Employer Sponsors who fully comply with their funding obligations under MPSA will extinguish any remaining responsibility for future funding shortfalls **related to employees from other companies**. MPSA also will include a **premium increase** aimed at **raising the minimum guaranteed pension benefits** for employees in plans that fail.

5. MPSA also will incorporate a series of mostly non-financial measures to address identified shortcomings in the regulation of the multi-employer pension plan system and will be accompanied by minor legislative changes in other areas to support the overall framework being proposed.

“Multiemployer Pension Plan Security Act”

See below for a summary of how the various stakeholders will work together to address the capital shortfall:

Stakeholder	$, Billions
Employer Sponsor Orphan Liability Coverage	3.48
Employee Participant Orphan Liability Coverage	1.16
Funding Assurance Program Capital Injection	3.32
U.S. Treasury Loans Capital Replenishment	17.55
Total Capital Replenishment in 14 Years	25.51
Funding Assurance Program Interest Coverage	3.5
U.S. Treasury Loans Operating Deficit Coverage	15.7
Reserve Pool from Employee Sponsors and Employee Participants	2.0

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Funding Assurance Plan (FAP) proposal, by Mark Greene and Mike Dardzinski

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