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Chapter 27 Redlined Amendments
Chapter 28A Redlined Amendments
Presentation to Legislature Amendments: Chap. 27 & 28A

Government Employees' Retirement System of the Virgin Islands

Office of the Administrator

To: Members of the GERS and Virgin Islands Community

The purpose of this letter is to communicate to the members of the Government Employees' Retirement System (The System) and the Virgin Islands community the Board actions and the recommended amendments to Bill No. 29-0099 (An Act relating to the retirement of Government personnel) that were submitted to the 29th Legislature.

For the past 24 months, the System has painstakingly gone through each section of the Code as it pertains to the retirement of personnel. Substantive changes were recommended because of ambiguities in the language in the Code. In addition, we also incorporated the recommended Board actions, proposed amendments and new legislation which came out of the Board retreat held in June 2012. These bold recommendations and proposed legislative changes to include changes to the plan benefits structure and the contribution rates represent shared sacrifices across the board that will guarantee the sustainability of the System. Before we present the recommended changes that were submitted to the Legislature, here are the facts:

- On June 24, 1959 Act 479 was signed into law by Governor John D. Merwin which created the Employees' Retirement System of the Government of the Virgin Islands as a **defined benefit pension plan.** The System began operations on October 1, 1959 when contributions by employees and the Virgin Islands Government started. Title 3, Chapter 27, Section 718(a) of the Virgin Islands Code mandates that the System be funded on an **"actuarial reserve basis",** which means that retirement benefits are funded during an employee's active employment so that by the time the employee retires, the benefits have been funded in advance to pay the employee's annuity for life. The Fund has not been funded on an actuarial reserve basis for the past 20 years; most notably because there were no increases in the contribution rates until 2010.
- For a defined benefit pension plan to survive, at the most basic level in the long run, it must balance the monies coming in **(inflows) through investment earnings and contributions** against the monies going out **(outflows) through benefit payments and expenses.** During any year in the life of the plan, one side of the equation will be greater than the other with the goal that both sides will balance in the long run.
- Beginning with fiscal year 1996, this was the first time in the history of the System that benefit payments and expenses were more than total contributions by $1.6 million – **a negative cash flow (deficit).** This trend has continued each year since 1996. However, there was a cushion up until 2002 where the investment gains (income) made up for the shortfall between the total contributions and benefit payments and expenses. **For the 11 months of fiscal year 2012 the negative cash flow is approximately $124.2 million.** This significant increase in the deficit is due mainly to 9 unfunded legislative mandates from 1983 – 2001 in the form of early retirement for various members, the decrease in active members and layoffs and the increase in retirees and beneficiaries caused by the enactment of the Virgin Islands Economic Stability Act of 2011 (VIESA).
- **As of June 30, 2012, the active membership was 9,935 and retirees and beneficiaries were 8,141 for a ratio of active to retirees of 1.22 to 1.** This has created a significant burden on the System's assets because in order to fund the shortfall between the total contributions and benefit payments and expenses, the System must make significant withdrawals from its investment portfolio.
- **In 2005, the Actuary estimated that the Fund would become insolvent in 14 years and recommended increases in the contribution rates and a large infusion of cash in the form of a Pension Obligation Bond (POB).** On October 19, 2005, the 26th Legislature passed the Reform Act of 2005 (Bill No. 26-0071/ Act No. 6794) and on December 28, 2005, Bill No. 26-0351/ Act No. 6905 which added a Tier II increasing contribution rates and a $600 million POB provision to "slow down the bleeding" of the Fund. The $600 million POB was never floated and the increases in the contribution rates were not implemented until January 2010.
- In 2006, the Actuary estimated that the **actuarial accrued liability (total obligations to members)** was $2.7 billion and the **unfunded actuarial accrued liability (shortfall between the total obligations to members and total assets of the System)** was $1.2 billion. As of June 30, 2012 the actuarial accrued liability is estimated to be $3.1 billion and the unfunded actuarial accrued liability is estimated at $1.7 billion.
- Based on the recent actuarial valuation projections, **if there are no changes to the Plan (status quo)** using the following assumptions of active employees remaining at a level of 9,376, payroll of $362.8 million increasing 2.5% annually, administrative expenses increasing 3% annually, benefit payments increasing 2% annually to account for retirement of new retirees, a net annual investment return of 7.5% and employer and employee contribution rates remaining at 17.5% and 8.5% of payroll respectively, **the System would use up its portfolio (run out of cash) by year 2022.** This means that the System will become insolvent in 10 years and will not have the ability to pay annuities to its retirees unless the plan sponsors (central government, semi and autonomous agencies and instrumentalities) contribute an additional $91.4 million in contributions in 2023 and up to $204.9 million in 2031.

In order to save and sustain the System, the Board has made and also submitted a comprehensive legislation package which is now in the Committee on Rules and Judiciary for a vote on October 22, 2012. All recommendations will be effective October 1, 2013 except where noted.

Board Actions:

Contribution Rates

- **TIER I - REGULAR EMPLOYEE**

  Increase the contribution rate from 8% to 9% for FY 2014, 10% for FY 2015 and 11% for FY 2016. The Board will determine the rate thereafter.
- **TIER I - CLASS 3 EMPLOYEE**

  Increase the contribution rate from 10% to 11% in FY 2014, 12% in FY 2015 and 13% for FY 2016. The Board will determine the rate thereafter.

Cost of Living Allowance (COLA)

Effective Beginning with year 2013

Suspend the COLA indefinitely for all retirees.

Legislation Submitted to the 29th Legislature:

Contribution Rates

- **TIER II – REGULAR EMPLOYEE**

  Increase the contribution rate from 8.5% to 9.5% for FY 2014, 10.5% for FY 2015 and 11.5% for FY 2016. The Board will determine the rate thereafter.
- **TIER II – CLASS 3 EMPLOYEE**

  Increase the contribution rate from 10.625% to 11.625% for FY 2014, 12.625% for FY 2015 and 13.625% for FY 2016. The Board will determine the rate thereafter.
- **LEGISLATORS**

  Increase the contribution rate to 15%.
- **JUDGES**

  Increase the contribution rate for new judges to 17%. Increase the contribution rate for sitting judges to 15% at beginning of next term.

  Increase the contribution rate for sitting judges to 16% at beginning of second year of new term.

  Increase the contribution rate for sitting judges to 17% at beginning of third year of new term and thereafter.
- **EMPLOYER**

  Increase contribution rate from 17.5% to 20.5% for FY 2014, 23.5% for FY 2015, 26.5% for FY 2016, 29.5% for FY 2017, 32.5% for FY 2018, 35.5% for FY 2019 and 38.5% for FY 2020. The Board will determine the rate thereafter.

Changing Retirement Age

- **TIER II – REGULAR EMPLOYEE**

  Age 60 to 65 with 10 years of service, eliminating the any age with 30 years of service.
- **TIER II – CLASS 3 EMPLOYEE**

  Age 50 with 25 years of service or age 55 with 10 years of service, eliminating the any age with 20 years of service.

Average Career Earnings

- **TIER II**

  Average Compensation shall mean the average rates of annual compensation for the years of credited service subject to the maximum salary limitations in effect during the service.

Personal Loans

Active Members

Increase from $50,000 to $75,000.

Refund of Contributions

- **TIER I & TIER II**

  Allow refunds to non-vested members only.

Contractual/Per Diem Employees

Allow employees compensated on a contractual, fee or per diem basis and who work exclusively for the Government at least 40 hours per week to be included as a member and receive service credit for such periods by paying contributions.

Additional Service Credit

Allow any member to purchase up to 5 years of additional service credit, which shall be added to his years of service credit already accrued for service worked and contributions paid. The member must have at least 10 years of service credit before he is eligible to purchase additional service credit. The purchase of service credit by members will be cost neutral to the System.

Retirement Notice

Require any member retiring to notify the System, in writing, of their intent to retire at least one (1) year prior to the date of retirement. The member shall notify his Department Head of his intent to retire at least three (3) months prior to the date of his retirement, but in no event shall a member give less than sixty (60) days notice of his intent to retire.

Experience and Education of Trustees

With the exception of the two members from the Central Labor Council, members of the Board of Trustees shall have at least five years experience and at least a bachelor's degree in any of the following: business management; business administration; investment banking; economics; finance; insurance; accounting; actuarial science; taxation; a medical degree, law degree or a licensed real estate appraiser. Individuals with a masters of business administration; accounting; business management; finance; insurance; actuarial science; and taxation shall also be eligible to serve on the Board of Trustees.

Mortgage Loans

Increase from $250,000 to $350,000.

Auto Loans

Increase from $18,000 to $40,000.

The purpose of the Reform Act of 2005 was to "slow down the bleeding" of the System. In order for the System to remain solvent and serve the members for the next 53 years, we now must go further and make changes to the plan benefits structure and contribution rates. The bold recommendations and legislative changes mentioned above represent shared sacrifices from all stakeholders. The System affirms its place in the territory's economy by providing a stable source of stimulus through the annuity payments to the retirees and beneficiaries (approximately $202.5 million for 11 months through August 31, 2012) and various loans to its members (approximately $31.5 million for 11 months through August 31, 2012). If there is no action taken by the Legislature on the recommended legislation which is intended to reform and sustain the Plan, and the central government and other plan sponsors cannot fund the additional contributions that will be required to sustain the System, the System will become insolvent. If the Plan becomes insolvent, this would eliminate approximately $234 million of retirement earnings and loans to members, eroding the spending power of the members, causing devastating economic consequences to the business community, especially small businesses, and impacting the tax base of the Government. Insolvency is not an option.

We urge all of our members, concerned citizens and the Virgin Islands community as a whole to contact the members of the Committee on Rules and Judiciary (Senators Usie Richards, Chairman, Sammuel Sanes, Ronald Russell, Alicia Hansen, Carlton Dowe, Patrick Simeon Sprauve and Celestino White) and other members of the 29th Legislature (Senators Nereida Rivera-O'Reilly, Terrence Nelson, Neville James, Shawn Michael Malone, Janette Millin-Young and Craig Barshinger) to support the reforms that are recommended and pass these sweeping reforms before the 29th Legislative Session ends.

The Government Employees' Retirement System remains committed to ensure that our members have a secure retirement.

SAY "YES" IN ORDER TO SAVE THE SYSTEM!

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Friday, October 19, 2012