GOVERNMENT EMPLOYEES RETIREMENT SYSTEM
OF
THE VIRGIN ISLANDS

PRESENTATION
TO
THE COMMITTEE ON FINANCE
OF
THE THIRTY-FIRST LEGISLATURE
OF
THE VIRGIN ISLANDS OF THE UNITED STATES

Earle B. Ottley Legislative Hall
February 17, 2015
9:00 a.m.

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Good morning, Honorable Clifford F. Graham, Chairman, Committee on Finance of the 31[st] Legislature, other Committee members, and other distinguished Senators who are present in the chambers. Good morning to all. My name is Austin L. Nibbs, Administrator/CEO of the Employees' Retirement System of the Government of the Virgin Islands (GERS). Cathy M. Smith, General Counsel, Shoran D. Sasso, Director, Member Services, Curtis Garner, Director, Information Technology, and Jasmin M. Greaux, Special Assistant/Team GERS V3 Facilitator are appearing with me this morning.

Thank you Mr. Chairman for your invitation to appear before the Committee on Finance to give testimony relating to the GERS.

The invitation listed six issues that the Committee wanted us to focus on. 1). Loan Refunds. 2). Death Benefits. 3). Status of the Vitech Software. 4). Status of Annuity Payments. 5). Status of Government of the Virgin Islands Outstanding Contributions. 6). Overall Financial Health of GERS.

Loan Refunds /Refunds of Contributions in General

The GERS has been processing refunds of contributions in the new V3 System since March 2012. In 2013, the System encountered some issues after the software had to be configured to process the mass refunds of contributions for the retirees who had received retroactive wages. After the configuration, the system did not recognized personal loan balances, resulting in the inability of the system to process any refunds for members who had personal loan balances, and were entitled to refund of contributions. This issue has been resolved. A total of 152 of these cases have been completed and the refund checks have been processed.

In addition, there are 29 employees who were terminated or resigned from the Juan F. Luis Hospital and Medical Center. Because Juan Luis Hospital was delinquent with remitting the employee's contributions timely, in order to assist the employees, the GERS went ahead and processed partial refunds to these employees. After receiving the remaining contributions from Juan Luis Hospital for these employees, we attempted to process the refunds for the remaining balances and encountered difficulties. We determined that the system was not programmed to issue a refund twice. The system attempted to remove the total loan balances for a second time. This issue has been resolved. We have completed 20 of these refunds and the checks were processed. We are conducting research on the remaining 9 cases. It appears that these members have returned to work.

Death Benefits

<u>Active Deceased Members</u>

Since the V3 System went live in March 2012, the System has never encountered any problems completing the cases for members who passed away while they were active employees.

<u>Retired Deceased Members</u>

We have not processed any of these cases since the V3 System went live in March 2012. We recently tested several cases, and encountered discrepancies in the calculations. We are working with the software provider to have this issue resolved by March 31, 2015.

Status of the Vitech Software

The search for a software provider to replace the 3 different systems that were not talking to each other began in 2006. An RFP was advertised and 3 vendors responded. Ventera Corporation of McClean, Virginia - $19.8 million, Levi, Ray & Shoup, Inc. (LRS) of Springfield, Illinois - $12 million, and Vitech Systems Group, Inc. of New York City - $7.9 million. A committee (Team GERS) was established consisting of GERS staff and outside consultant (LRWL). The appropriate due diligences were conducted and Vitech Systems Group, Inc. was selected in 2007 as the most appropriate vendor. Negotiations for a best and final offer proceeded thereafter, and GERS entered into a contract with Vitech System Group, Inc. in December 2007, in the amount of $7.3 million, to implement a comprehensive retirement system software solution known as V3.

The project kicked off in February 2008. The objective of this software implementation, which was accomplished, was to merge the GERS' legacy benefits and loan administration systems into a state-of-the-art, web-based, business solution that provides the technology foundation to enable and sustain the business agility of the GERS, in addition, to being fully integrated with the central government, and the other government instrumentalities that interfaced with the GERS.

The project consisted of three rollouts (phases):

- Rollout 1: Digital Conversion of GERS' member files
- Rollout 2: V3 Imaging and Line of Business Implementation
- Rollout 3: V3 Self-Service Implementation

The project which was expected to be completed in 24 - 30 months was completed in 48 months due to delays mainly because of unforeseen legislative mandates.

All expected results of this upgrade were implemented except:

- Online loan applications and payments
- Improved ability of GERS to produce annual statements

The V3 System is functioning at 85% capacity. The under capacity of 15% is due mainly to functionality issues mainly in the loans module. The GERS is one of about four public pension systems in the U.S. that offers loan services, and the only one that offers mortgagees. The entire loan module had to be build based on past practices and rules which are in conflict with best practices and industry rules. We are working closely with the software provider to resolve these issues in a timely manner.

Status of Annuity Payments

As of February 13, 2015, there are 210 members with retirement dates from May 4, 2012 through December 31, 2014 waiting for an initial annuity payment. 93 members with retirement dates from May 4, 2012 through October 31, 2014 have been completed. The system is being updated to give credit for 10 missing pay periods after V3 went live in March 2012. This update will reflect the actual employer missing contributions that are due, and letters and invoices (billings) prepared to forward to the central government.

The majority of the additional 117 members with retirement dates through December 31, 2014 are pending receipt of retirement notice of personnel actions (NOPAs). The estimated amount that is due for the 210 members is $2.1 million.

We continue to receive many calls regarding salary adjustments in accordance with the Virgin Islands Economic Stability Act – VIESA (ACT 7261). There are 364 cases pending completion. Also, there are 30 cases pending completion under Act 7128 for 2010, where adjustments of annuities have to be made for those retirees where the Government of the Virgin Islands paid for their Sick and Excess Annual Leave. $3 million was appropriated and received by GERS under Act No. 7128.

Status of GVI Outstanding Contributions

In a report titled Potential Missing Employer Contributions Study by The Segal Group dated June 2013, the Actuary estimated that there are missing employer contributions owed to the GERS as of October 1, 2011 on behalf of active employees of approximately $47 million. The Actuary concluded that the percentage of missing employer contributions is generally consistent with the percentage of missing employee contributions at retirement. Historical data of employee contributions for those who retired from 1974 to 2011 were reviewed, and the Actuary determined that the period of data from 2007 to 2011 best represents the missing contribution as of October 1, 2011.

Since 2012, we have billed $5,433,718.06 and received $2,733,872.26 ($237,825.67 in 2012, $2,154,738.76 in 2013, and $341,307.83 in 2014) in missing employer contribution payments. Therefore, we have estimated that the Government of the Virgin Islands owes the GERS approximately $44.3 million in missing employer contributions.

We are in the process of drafting a memorandum of understanding with the Juan F. Luis Hospital and Medical Center to collect in excess of $5 million that is due to the System for employee contribution deductions and employer contributions that were not remitted to the GERS since February 2013.

Overall Financial Health of GERS

The overall health of the GERS continues to deteriorate.

Since 1996, the benefits payments have been outpacing the contribution income. For Fiscal Years 2013 and 2012, the benefits payments of $234.4 million and $225.8 million respectively were in excess of the contribution income of $98.5 and $104.4 million respectively, resulting in deficits of $135.9 million and $121.4 million respectively. For Fiscal Year ending September 30, 2014, the benefits payments (unaudited) of $238.7 million were in excess of the contribution income (unaudited) of $99.5 million, resulting in a deficit of $139.2 million.

We note that the contribution income decreased by $19.4 million between 2011 and 2012, and continues to decrease. This decrease was due primarily to Act 7261 (The Virgin Islands Economic Stability Act of 2011) which resulted in a combination of employees being laid off, terminated, entering into early retirement, and or being refunded their contributions. Similarly, the benefits paid to retired members increased by $22.9 million between 2011 and 2012, and continue to increase.

We thank the 30th Legislature for granting the Board of Trustees the authority to increase the contribution rates (employee and employer) for Tier II. These rates were effective February 5, 2015. We note that the Board of Trustees had the authority to increase the Tier I contribution rates (employee and employer), which they did, effective January 1, 2015. These rate increases are expected to increase contributions by approximately $14 million annually. Increasing the contribution rates is only one of the measures that were recommended by the Board, the Actuary, and the Pension Reform Taskforce, and included in the Pension Reform Bills that were submitted to the 29th and 30th Legislatures.

The market value of the portfolio at December 31, 2014 was $869 million, down from $982 million one year ago. The significant decrease in value was due mainly to withdrawals from the Fund to pay for benefit payments.

The Total Plan earned:

- 11.06% in calendar year 2012
- 15.18% in calendar year 2013

In calendar year 2014:

- Domestic Equity earned 13.2%
- International Equity -2.4%
- Fixed Income 4.4%

The Plan has earned 9.24% since inception compared to a Total Policy Index of 10.28%.

The investment fund portfolio is managed with the specific goal to grow the assets to meet the System's pension liability and ensure a reliable cash flow that provides for the funding requirements of near-term pension obligations. To achieve these goals, the Board allocates the Fund's assets to a variety of asset types and strategies in consultation with our in-house Investment Unit and Investment Advisor Meketa Investment Group. Generally, equity investments are included for their long-term return and growth characteristics, and fixed income assets are added for their ability to control investments risk and provide for a reliable cash flow that meets the System's funding requirements. The Fund's successful long-term performance confirms the importance of asset diversification and controlling investment risk within each asset class. An integral part of the overall investment policy is the strategic asset allocation policy. The targeted strategic asset allocation is designed to provide appropriate diversification and balance expected total rate of return with the volatility of expected returns. Specifically, the fund is broadly diversified across and within asset classes to limit the volatility of the total fund investment returns and to limit the impact of large losses on individual investments. Both traditional and nontraditional assets are incorporated into the asset allocation mix.

The System will continue its commitment to a disciplined investment strategy that focuses on long-term results. Our mission is to promote long-term financial security for our membership while maintaining the stability of the Fund. The System's investment fund is presently managed by 14 investment managers. Since August 2013, the Board has terminated 8 investment managers (6 equity managers and 2 bond managers) for underperformance. and added 4 new equity managers. Approximately, $416.4 million were transitioned from 7 managers that were terminated, and invested in index strategies. Indexing is a "passive" form of fund management that has been successful in outperforming most actively managed funds. The portfolio is constructed to match or track the components of a market index, such as the Standard & Poor's 500 Index. The primary advantage of investing in these strategies is to provide broad market exposure, low operating expenses and low portfolio turnover.

One of the new index strategies - Treasury Inflation Protected Securities (TIPS) is considered an extremely low risk investment since they are backed by the U.S. government. Their par value rises with inflation, as measured by the Consumer Price Index, while their interest rate remains fixed. TIPS are indexed to inflation in order to protect investors from the negative effects of inflation. The estimated savings in management fees due to the restructuring is expected to be $1.4 million.

Mr. Chairman, every time we have appeared before this body, we have stressed that the portfolio should not be counted on to save the System. The Actuary continues to advise that it will take a combination of a large infusion of cash in the form of a Pension Obligation Bond (POB), increase in the contribution rates, and restructuring of the benefits structure of the Plan. The Actuary has also advised that if nothing was done, the Plan will run out of cash in 2022, which is now 7 years away. There has been a start with the increase in the contribution rates. However, this body must address and pass the other measures that were included in the Bills that were before the 29^{th} and 30^{th} Legislatures.

Mr. Chairman, this concludes our presentation. We are available to respond to any questions the Committee may have.