



OFFICE OF  
**INSPECTOR GENERAL**  
U.S. DEPARTMENT OF THE INTERIOR

# **ADMINISTRATIVE FUNCTIONS OF THE VIRGIN ISLANDS GOVERNMENT EMPLOYEES RETIREMENT SYSTEM**

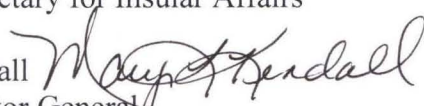


**OFFICE OF  
INSPECTOR GENERAL**  
U.S. DEPARTMENT OF THE INTERIOR

SEP 27 2011

Memorandum

To: Anthony M. Babauta  
Assistant Secretary for Insular Affairs

From: Mary L. Kendall   
Acting Inspector General

Subject: Evaluation Report – Administrative Functions of the Virgin Islands Government  
Employees Retirement System  
Report No. VI-EV-OIA-0004-2011

Our recent evaluation of the Virgin Islands Government's Employee Retirement System determined that system to be at critical risk due to a growing unfunded liability of more than \$1.4 billion. Factors that have contributed to this situation include insufficient contribution levels, an unhealthy ratio of active to retired members, and unfunded legislative mandates. Without immediate action, the system could default in 14 to 19 years or less. Although Governor deJongh responded to our concerns with equal awareness of the situation and an apparent plan to rectify it, the severity of the situation is such that we are seeking additional support from your office to monitor actions taken by the Virgin Islands Government in response to our recommendations.

Specifically, we offered four recommendations, concerning which we requested a response within 30 working days. Governor deJongh responded to the draft report on August 30, 2011 (Appendix 2). Based on his acknowledgement of our recommendations and his plan of action we compiled a table laying out the timeline for accomplishing the actions his Administration is pursuing (Appendix 3).

You may note that in response to recommendation 1, Governor deJongh proposes to work with staff to develop a task force to fulfill the intention of our recommendation by the first quarter of 2012 (noted in Appendix 3 as March 1, 2012).

Regarding recommendation 2, Governor deJongh agrees to direct this task force to work closely with the legislature of the Virgin Islands to develop realistic measures to ensure the sustainability of the retirement system. Given the complex relationship between retirement funds and revenues collected by the Virgin Islands Government, we particularly are interested in the outcome of recommendation 2, also earmarked for accomplishment by the first quarter of 2012.

In response to recommendation 3, Governor deJongh indicates that he plans to issue a policy statement indicating that future legislation related to retirement provisions must be linked to a funding source (due by the first quarter of 2012).

Finally, in response to recommendation 4, Governor deJongh acknowledged our request that retirement system managers identify areas of improvement through such steps as performing periodic data quality reviews, and identified ongoing efforts to improve the quality of data collection pertaining to member information for individuals in the retirement system.

Due to the long-standing, pervasive nature of the issues described in our report, and the resulting risk facing the Virgin Islands retirement system and those who rely on it, we are requesting your assistance in tracking improvements in this area. We recommend, therefore, that the Office of Insular Affairs (OIA):

1. Ensure that the Virgin Islands Government provides documentation that demonstrates implementation of much needed and agreed upon actions that revamp and strengthen the Virgin Islands' retirement system to avoid default.

Please provide us with your written response to this report within 30 days. The OIA response should provide information on actions to address the Virgin Islands Government's plan as outlined in Governor deJongh's response to our report outlined in Appendix 2 and Appendix 3, which provides his agreed timeline. Please address your response to:

Ms. Kimberly Elmore  
Assistant Inspector General for Audits, Inspections, and Evaluations  
U.S. Department of the Interior Office of Inspector General  
Mail Stop 4428  
1849 C Street, NW.  
Washington, DC 20240

If you have any questions regarding this memorandum or the subject report, please do not hesitate to contact me at 202-208-5745.

Attachment



OFFICE OF  
**INSPECTOR GENERAL**  
U.S. DEPARTMENT OF THE INTERIOR

# **ADMINISTRATIVE FUNCTIONS OF THE VIRGIN ISLANDS GOVERNMENT EMPLOYEES RETIREMENT SYSTEM**



OFFICE OF  
**INSPECTOR GENERAL**  
U.S. DEPARTMENT OF THE INTERIOR

SEP 27 2011

The Honorable John P. deJongh, Jr.  
Governor of the Virgin Islands  
No. 21 Kongens Gade  
St. Thomas, VI 00802

Subject: Evaluation Report — Administrative Functions of the Virgin Islands Government  
Employees Retirement System  
Report No. VI-EV-VIS-0002-2010

Dear Governor deJongh:

This report contains the results of our evaluation of the Virgin Islands Government Employees Retirement System (Retirement System). We determined that the Retirement System is at critical risk due to a growing unfunded liability of more than \$1.4 billion. Factors include insufficient contribution levels, an unhealthy ratio of active to retired members, and unfunded legislative mandates. Without immediate action, the Retirement System could default in 14 to 19 years or less.

We offered four recommendations, concerning which we requested a response within 30 working days. We appreciate your August 30, 2011 response to the draft report (Appendix 2) and are pleased that you concur with our recommendations.

We also applaud your willingness to work collaboratively with the Retirement System and the Virgin Islands Legislature to identify and implement realistic measures that could begin to address the serious issues surrounding the pension system. The urgency of the current situation cannot be understated. The conditions facing pensioners of the Virgin Islands may mirror similar concerns across the United States but, though the circumstances may be dire, they also provide a platform from which significant changes can be made. We recognize that it is imperative for your government to work expeditiously toward a solution and remain hopeful that the steps you outline will provide solutions to the issues we identified.

Based on your response, we consider the four recommendations resolved but not implemented (Appendix 3). If you have questions concerning this letter or the subject report, or wish clarification regarding the ways in which our recommendations could further interface with your stated actions, please contact Mr. Hannibal M. Ware, Assistant Regional Manager, at 703-487-8058.

Sincerely,

Mary L. Kendall  
Acting Inspector General

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## Results in Brief

We identified a number of factors that have contributed to a Government of the Virgin Islands (GVI) Retirement System (Retirement System) unfunded liability of over \$1.4 billion. This liability, which has been growing for years, represents a gap between the amount of retirees' future annuities and the projected value of Retirement System assets.

The contributing factors include employee/employer contribution levels, the ratio of active to retired members, and early retirement legislative mandates. As a result, the long-term sustainability of the Retirement System, which is comprised of just over 18,000 members, is critically at risk.

Without a combination of increased contributions and a large infusion of funds, the unfunded liability can only worsen. In fact, the most recent actuarial Retirement System evaluation, which was done in 2006, projects:

- default of the Retirement System in just 14 to 19 years and
- a corresponding cessation of benefits payments.

We also found that the Retirement System does not always maintain accurate member information, which could actually lead to employees retiring earlier or later than should be authorized under the System. The Retirement System could also find itself paying incorrect annuities.

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# Introduction

## Objective

In light of the many retirement funds currently facing challenges, we conducted this evaluation to assess the long-term sustainability of the Government of the Virgin Islands (GVI) Retirement System (Retirement System). (See appendix 1 for scope, methodology, and prior coverage).

## Background

### Overview of the Virgin Islands Retirement System

The Retirement System is an independent, subsidiary branch of the GVI that is governed by a seven-member Board of Trustees (Board). The Retirement System administers a defined-benefit pension plan for GVI employees. Such plans pay their members a specific retirement annuity for life.

All employees of the Executive Branch and of independent instrumentalities of the GVI must become members of the Retirement System as a condition of their employment. Employees of the Legislative and Judicial Branches automatically become members of the Retirement System unless they opt out within 90 days of their service entry dates.

The Retirement System is funded through employer and member contributions, interest income, and other income, as prescribed by the Board. The GVI and its independent instrumentalities are required by law to contribute 17.5 percent of their employees' salaries. Members are required to contribute at a rate based on job classifications and places of employment. The rate ranges from 8 to 11 percent.



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## Findings

We found that sustainability of the GVI Retirement System is critically at risk due to an unfunded liability of more than \$1.4 billion. Although the U.S. financial market downturn of 2008 played a role in increasing this unfunded liability, several other factors within GVI control had a major impact. These factors include insufficient contribution levels, a decreasing ratio of active to retired members, and unfunded early retirement legislative mandates.

Moreover, inaccurate information maintained in the Retirement System has resulted in premature or deferred retirements and payment of inaccurate retirement benefits. As a result, some Retirement System members have been forced to make catch-up payments to qualify for entitled benefits.

### **Retirement System Sustainability**

#### **Insufficient Contribution Levels**

GVI law requires that actuarial valuations be made every year to determine the level of payroll contributions necessary to fund the Retirement System. Such valuations are also required to determine the Retirement System's current condition and to analyze changes in actuarially-determined contribution rates. The last valuation was conducted in 2009 based on conditions as of September 30, 2006.

The actuarial consultant contracted by the GVI determined at that time that Retirement System sustainability required a payroll contribution of 43.2 percent. Such contributions are made up of both employee and GVI contributions. Today, the Retirement System is receiving payroll contributions at a rate of only 25.5 percent and pays out more benefits each year than payroll contributions can support.

For comparison purposes, we reviewed other State defined-benefit pension plans and found that actual payroll contributions commonly differ from the levels recommended to sustain viability. For instance, the average State defined-benefit retirement plan is funded at 96 percent of the amount that actuarial experts prescribe for solvency. Funded at only 60.7 percent of required levels (see figure 1), the GVI Retirement System is one of the most under-funded plans in the Nation. If insufficient contribution levels are not addressed, the GVI may be unable to meet future payments to members.

### 2008 Percentage of Actuarially-Required Payroll Contributions

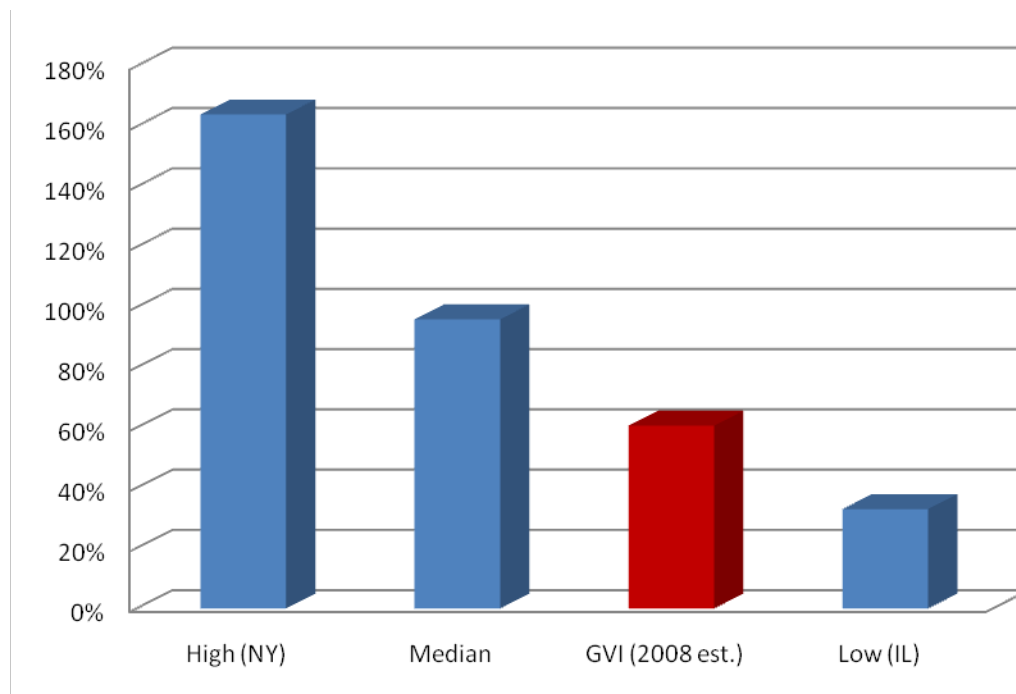


Figure 1. State versus GVI Funding of Defined-Benefit Pension Plans. Sources: Segal and The Pew Center on the States.

### Declining Ratio of Active to Retired Members

Compounding the issue of insufficient contribution levels is the continually declining ratio of active members to retired members. In past years, the Retirement System had over 12,000 active members and about 5,400 retirees, for a ratio of 2.2 active members to 1 retiree. In 2010, the Retirement System had about 10,800 active members and about 7,500 retirees, for a perilously low ratio of 1.4 active members to 1 retiree. Accordingly, although the Retirement System took in approximately \$117 million in payroll contributions on behalf of its members in 2010, benefits and expenses were about \$208 million for the same period.

Combined, the declining member ratio and contributions gap have forced Retirement System managers to meet financial obligations by withdrawing an average of \$5 to \$6 million each month from the Retirement System's investment portfolio. As a result, the Retirement System's annual deficit, which contributes to the overall unfunded liability, ballooned from \$23.7 to \$70.2 million from FY 1999 to FY 2009. (See figure 2.)

### **Retirement System's Ballooning Deficits**

Fiscal Year	Total Contributions (millions)	Benefits Payments & Expenses (millions)	Deficit (millions)
1999	\$71.7	\$95.4	\$23.7
2000	\$70.2	\$103.7	\$33.5
2001	\$69.1	\$121.2	\$52.1
2002	\$80.1	\$133.0	\$52.9
2003	\$82.1	\$138.0	\$55.9
2004	\$84.9	\$142.6	\$57.7
2005	\$81.9	\$153.0	\$71.1
2006	\$99.3	\$161.0	\$61.7
2007	\$96.6	\$170.5	\$73.9
2008	\$112.8	\$184.7	\$71.9
2009	\$116.8	\$187.0	\$70.2

Figure 2. Retirement System Deficits That Span a Decade.

#### **Unfunded Early Retirement Mandates**

Between 1984 and 2001, the Virgin Islands Legislature (Legislature) passed various laws designed to encourage workers to retire early. Although the GVI was successful in reducing its workforce, each of the laws passed either made lucrative provisions for early retirement or significantly increased benefit packages. The Legislature failed, however, to fund these retirement laws or funded them insufficiently, which has also increased the Retirement System's unfunded liability.

To quantify the effects of these laws on the Retirement System, we reviewed retiree data for the Early Retirement Incentive, Training and Promotion Act of 1994 and a later amendment (legislative provisions). Under these legislative provisions, active Retirement System members could become eligible for early retirement for a limited time through three options:

- Option A allows each active member whose age plus years of service totals at least 75 to retire without a reduction of annuity.
- Option B allows each 50- to 59-year-old active member with 10 to 29 years of service to add 3 years to his or her age.
- Option C allows a 4 percent increase to the average compensation amount for members with at least 30 years of service.

According to officials in the Retirement System's Benefits Division, roughly 850 members have retired under these options. We found, however, that historical data could be verified for only 648 retirees.

For the 648 retirees, we calculated the effect of the legislative provisions. We used the Retirement System's annuity formula and information from the retiree report listing. Next, we consulted with the Retirement System's Director of Member Services to verify the correct use of the formula relative to each option. Based on these calculations, the early retirement authorizations prevented the Retirement System from collecting \$121 million.

Recognizing that the Retirement System would incur losses based on the legislative provisions, the Legislature of the Virgin Islands paid a total of \$31 million to offset the losses. Proper funding of the early retirement incentive still fell short by at least \$90 million.

### **Partial Implementation of the Retirement System Reform Act**

Recognizing that the Retirement System is in danger, the GVI enacted the Retirement System Reform Act (RSRA) in 2005. To secure the sustainability of the pension fund, the RSRA was designed to reduce unfunded liabilities by increasing contributions and decreasing benefits. The RSRA created two tiers of GVI employees. Tier 1 employees are those hired before September 30, 2005. Tier 2 employees are those hired on and after October 1, 2005. Employees in each tier are to receive different retirement benefits (see figure 3).

#### **RSRA Changes to the Retirement System**

	Tier 1 Employees	Tier 2 Employees
Benefits Rates	2.5% per year of service	1.75% per year of service
Contribution Rates	8% of regular employee salary 10% of hazardous duty employee salary	8.5% of regular employee salary 10.625% of hazardous duty employee salary
Average Salary	5 highest salaries within the last 10 years of work	Last 5 salaries within the last 10 years of work

Figure 3. Major RSRA Retirement System Changes in 2005.

The RSRA also penalizes members who fail to pay service contributions to the Retirement System. It prohibits payment of credited service benefits for excess annual leave, sick leave, leave without pay, Federal service in the Virgin Islands, or for prior military service until the Retirement System receives contribution payments from the employee.

As of 2011, the RSRA has not been fully implemented. While Tier 1 changes were implemented in January 2010, implementation of Tier 2 changes was postponed at the request of the Governor of the Virgin Islands.

Because of the many challenges detailed above, an infusion of money is required to prevent the impending default of the Retirement System. The actuarial

consultant has reported that the Retirement System's unfunded liability could reach more than \$4 billion by 2027 — even with favorable market returns and an increase of 3 percent in contributions every 5 years (beginning in FY 2009).

### **Recommendations**

1. The Governor of the Virgin Islands should establish a joint taskforce composed of GVI financial experts and an actuarial expert to determine how to address the difference between current and recommended payroll contribution levels and to provide recommendations to the Legislature.
2. Taking the taskforce's recommendations into account, the Governor of the Virgin Islands should work with the Virgin Islands Legislature to develop and implement measures to improve the Retirement System's sustainability.
3. The Governor of the Virgin Islands should work with the Virgin Islands Legislature to ensure that any future early retirement legislative provisions are adequately funded.

## **Deficiencies in Maintaining Member Information**

We found that the Retirement System does not always ensure that member contributions are made on time or maintain accurate member data. Specifically, the Retirement System has recorded contributions unsupported by official personnel records, failed to reliably record member service entry dates, and documented service entry dates that conflict with official personnel records. In fact, the Retirement System is often unable to determine whether contributions have been made.

To test the integrity of member information maintained by the Retirement System, we selected a sample of 50 active members and reviewed their official personnel records. We compared that information to the Retirement System's computer-generated Contributions History Report. We found that discrepancies existed in 38 of the 50 active-member files reviewed.

### **Untimely Contributions**

According to Virgin Islands law, members with service entry dates prior to October 2001 were to begin contributions upon completion of 1 year of service. Members with service entry dates after October 2001 were to begin contribution upon completion of 1 month of service. In 31 of the cases reviewed, however, contributions were not paid into the Retirement System within required time frames. Such delays impact both the Retirement System and the employees involved. While the Retirement System is not receiving all contributions due, late-

contributing Retirement System members will be required to make catch-up payments before they can receive retirement benefits.

Knowing that the Retirement System does not always capture contribution data, the Retirement System Director wrote to the heads of the independent instrumentalities and to the Virgin Islands Executive, Legislative, and Judicial Branches in December 2009. The letter requested that active Retirement System members with unpaid prior service contributions initiate payment plans before January 29, 2010.

Retirement System members who responded had to complete Payroll Deduction Authorizations and a Prior Service Form by the deadline to avoid paying interest and losing investment opportunity. In these cases, Retirement System managers plan to complete an official search and to refund any unwarranted payment. The Retirement System now has 1,690 inquiries from members who are waiting to learn how much to contribute for prior service that may not have been captured or to receive refunds for excess contributions.

### **Inaccurate Data**

The Retirement System does not always maintain the information needed to confirm member service entry dates. For example, one active member, who is waiting to learn how much money she owes, informed us that Retirement System records show that her contributions began in 2005 despite the fact that she began GVI employment in 1991. According to the Retirement System, this member has to pay \$24,000 in catch-up contributions for 15 years of service prior to 2005. As of November 2010, a payment plan had not been initiated because the member was off-island when the December 2009 letter was issued. Therefore, the \$24,000 in catch-up payments would be subject to penalties such as interest and lost investment opportunity.

Another example of inaccurate service entry dates relates to the case of an active Retirement System member who began GVI employment in 1967. This member informed us that not only does the Retirement System reflect three different dates of entry — 1967, 1970, and 2005 — but that officials alleged in a March 2010 letter that the member owes \$1,500 for prior service contributions.

Since the Retirement System shows 2005 as the member's entry date, retirement ineligibility resulted. In April 2010, the member filed an appeal with the Board. In September 2010, Retirement System officials offered a \$79 settlement that the member declined. The matter is still pending before the Board.

We reviewed the Application for Service Retirement Annuity and the Final Annuity Calculator Worksheet for 50 retirees and found that inaccurate member information also resulted in delays in processing annuity payments to newly retired Retirement System members. These delays may have created undue financial hardship on these members. Specifically, the Retirement System required an average of almost 5 months to issue initial annuity payments. The longest delay was 16 months.

We recognize that the Retirement System has taken measures to resolve some of these inaccuracies and to improve annuity payment timeliness. Specifically, the Retirement System is currently converting to a new computer system that should connect both the System and the Division of Personnel, which maintains official personnel records. Retirement System managers expect this new system to resolve the deficiencies that we found in member information maintenance.

System implementation was to “go live” in February 2011. The contractor did not, however, meet that requirement and has requested a delay of 4 to 6 months. The new system is currently in the design phase.

#### **Recommendation**

4. The Governor of the Virgin Islands should require Retirement System managers to identify areas for improvement. At a minimum, managers should address:
  - a. collection of retirement contributions within established timeframes;
  - b. reconciliation of member data with official GVI payroll records to ensure accuracy and, therefore, minimize contribution delays; and
  - c. performance of periodic data quality reviews to ensure the integrity of member information.



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# Conclusion and Recommendations

## Conclusion

The Retirement System faces default in as few as 14 to 19 years or less and may be unable to meet its contractual obligation to deliver promised retirement benefits. Unless the GVI acts quickly to implement drastic reforms, GVI employees who have made mandatory retirement contributions for years may find themselves with no retirement income at all. In the meantime, Retirement System managers cannot guarantee the accuracy of calculations involving length of service, annuity disbursements, and catch-up payments for prior service because they have not always maintained accurate employment data.

## Recommendation Summary

We recommend that the Governor of the Virgin Islands:

1. Establish a joint taskforce composed of GVI financial experts and an actuarial expert to determine how to address the difference between current and recommended payroll contribution levels and to provide recommendations to the Legislature;

**VI Response:** The Governor will formally identify applicable members of his staff, financial team, and others to constitute the recommended task force. An implementation plan and due date are provided.

**OIG Reply:** We consider the recommendation resolved but not implemented.

2. Work with the Legislature — taking into account the taskforce’s recommendations — to develop and implement measures to improve the Retirement System’s sustainability.

**VI Response:** The Governor will direct the task force to work closely with the Legislature to develop and implement realistic measures to enhance the sustainability of the Retirement System. An implementation plan and due date are provided.

**OIG Reply:** We consider the recommendation resolved but not implemented.

3. Work with the Virgin Islands Legislature to ensure that any future early retirement legislative provisions are adequately funded.

**VI Response:** The Governor will issue a policy statement to the Legislature in writing, establishing that any future retirement legislative provisions must be linked to an identified, viable, adequate and sustainable funding source. An implementation plan and due date are provided.

**OIG Reply:** We consider the recommendation resolved but not implemented.

4. Require Retirement System managers to identify areas for improvement. At a minimum, managers should address:
  - a. collection of retirement contributions within established timeframes;
  - b. reconciliation of member data with official GVI payroll records to ensure accuracy and, therefore, minimize contribution delays; and
  - c. performance of periodic data quality reviews to ensure the integrity of member information.

**VI Response:** The Office of the Governor will initiate a meeting among appropriate entities to address matters related to timeliness of member contributions, the basis for recording these contributions, service entry dates, and other information. An implementation plan and due date are provided.

**OIG Reply:** We consider the recommendation resolved but not implemented.

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# **Appendix I: Scope, Methodology, and Prior Coverage**

## **Scope**

This evaluation's objective was to assess the long-term sustainability and performance of administrative functions of the Retirement System. Our scope was limited by Retirement System officials' inability to provide historical data for unfunded mandates and retirees' payroll processed prior to August 2001 by the Department of Finance. We could only determine, therefore, the amount that the Retirement System lost in contributions for 648 members who elected early retirement incentives that were passed by the Legislature in 1994.

## **Methodology**

We performed our work in accordance with the "Quality Standards for Inspections" issued by the Council of Inspectors General on Integrity and Efficiency. To accomplish our objective, we interviewed Retirement System officials, the contracted actuarial consultant, and both active and retired members. We reviewed records pertaining to the unfunded liability, contributions, retirement benefits, loans, contracts, and credit cards. We studied defined benefit pension plans similar to that of the Virgin Islands. We also reviewed employment records of the Division of Personnel and visited the new Retirement System office project site on St. Croix.

## **Prior Coverage**

March 1999, Government Employees Retirement System, Government of the Virgin Islands (No. V-IN-VIS-002-98). The report noted inadequate administering of loans to members and ineffective management and monitoring of employer and employee contributions.

September 1991, Follow-up of Recommendations Concerning the Employees Retirement System, Government of the Virgin Islands (No. V-IN-VIS-002-91). The report noted that improvements were needed with regard to loan administration.

September 1985, Employees Retirement System, Government of the Virgin Islands (No. V-TG-VIS-24-84). The report detailed that improvements were needed in the controls over reserve funding, loan policies and administration, interest income, the performance of professional investment managers, and computing duty-connected disability annuities.

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## **Appendix 2: Virgin Islands Government Response**

The Virgin Islands Government's response to the draft report follows on page 14.



**THE UNITED STATES VIRGIN ISLANDS**

OFFICE OF THE GOVERNOR  
GOVERNMENT HOUSE

Charlotte Amalie, V.I. 00802  
340-774-0001

August 30, 2011

Ms. Kimberly Elmore  
Assistant Inspector General for Audits, Inspections and Evaluations  
U.S. Department of the Interior  
Office of Inspector General  
1849 C Street, NW MS 4418  
Washington, DC 20240

**RE: Response by the Government of the Virgin Islands to the Draft Evaluation Report -  
Administrative Functions of the Virgin Islands Government Employees Retirement  
System (Report No. VI-EV-VIS-0002-2010, June 2011)**

Dear Ms. Elmore:

I am in receipt of your Draft Evaluation Report — Administrative Functions of the Virgin Islands Government Employees Retirement Systems, Report No. VI-EV-VIS-0002-2010, dated June 2011. I would say at the outset, before responding specifically to the four (4) recommendations that the Government of the U.S. Virgin Islands concurs with the overall conclusion stated in your letter of introduction. The Employees Retirement System of the Government of the Virgin Islands (GERS) is indeed at critical risk due to a growing unfunded liability.

This is not a new situation or a new challenge, nor is it unique to the United States Virgin Islands. Each of the bond rating agencies have issued warnings on this National issue over the past year, and there has been a broad recognition that the official estimate of state and local government pension underfunding of \$900.0 billion may well understate the actual shortfall, and that the actual underfunding may approximate the \$3.7 trillion estimate from JP Morgan in April of this year. Factors contributing to the higher number include five year smoothing that tends to mask the true market value of public pension fund assets, as well as other factors.

I applaud the effort of the U.S. Department of the Interior's Office of the Inspector General to draw attention to this crucial situation. In February 2007, in my first State of the Territory Address, I first warned that we must as a Territory develop a comprehensive solution to a pension funding gap that at that time had already exceeded \$1.0 billion. I also hosted a Summit in July 2009 with GERS' trustees and management and members of the Virgin Islands Legislature to address systemic concerns. Additionally, my Administration took proactive steps and increased the employer contribution from 14.5% to 17.5%.



The gravity of the pension funding challenge has lent urgency to our economic development efforts, and in particular our efforts to develop and expand the rum industry in the Territory and grow our matching fund revenues. As your report states, and as the GERS actuary has stated in each report they have issued, the central problem faced by GERS has been and continues to be underfunding of the annual required contribution from the Government. That underfunding, which has steadily grown over the years to reach approximately \$80.0 million annually, has been a central budget challenge, and one that we believe requires new revenues if it is to be successfully addressed. Accordingly, it has been our expectation that the new rum revenues would provide a revenue stream that could be dedicated to meeting this challenge.


Unfortunately, in the intervening years, the downturn in the global economy, and specifically the collapse in our Corporate Income Tax receipts, have placed additional stress on the budget of the Government, and has made carving out the \$80.0 million or more necessary to meet the GERS' annual obligation an ever greater challenge. Those new rum revenues, which were originally anticipated to be sufficient to address the GERS funding need, are now needed as well by the General Fund, which has suffered substantial revenue declines since 2007. We also note that the size of this annual deficit will also be adversely impacted by the recent implementation of the Economic Stability Act of 2011 and proposed amendments thereto.

Based on our monthly cashflow information, this projection may in fact understate the urgency of the current situation. Based upon recent data, the current negative cashflow of the GERS going forward is well in excess of \$80.0 million, and will result in the system running out of funds in 10-12 years. This has been and remains the central financial challenge facing the Government

You have in your draft report offered four (4) recommendations for our concurrence or non-concurrence. We have addressed each of these in the attached GVI Response to the report (Exhibit I).

We greatly appreciate the time and effort that went into the development of this report. This is an issue of critical concern for us and all of the stakeholders of the Territory, and it affects our capacity to address all other problems and challenges that we face. Accordingly, my administration is committed to working collaboratively with GERS and the Virgin Islands Legislature to identify and implement realistic measures to begin to address this major opportunity to strengthen and sustain GVI's pension system.

Sincerely,



John P. de Jongh, Jr.  
Governor

Attachment

**Government of the Virgin Islands Response to Draft Evaluation Report  
of the Office of the Inspector General (OIG) to the Administrative Functions  
of the Virgin Islands Government Employees Retirement System  
(Report No. VI-EV-VIS-0002-2010, June 2011)**

**FINDING #1: RETIREMENT SYSTEM SUSTAINABILITY**

The sustainability of the Government of the Virgin Islands (GVI) Retirement System is critically at risk due to an unfunded liability of more than \$1.4 billion. Although the U.S. financial market downturn of 2008 played a role in increasing this unfunded liability, several other factors within GVI control had a major impact. These factors include insufficient contribution levels, a decreasing ratio of active to retired members, and unfunded early retirement legislative mandates.

**Recommendations (Governor of the Virgin Islands):**

1. Establish a joint task force composed of GVI financial experts and an actuarial expert to determine how to address the difference between current and recommended payroll contribution levels and to provide recommendations to the Legislature.
2. Taking the task force's recommendations into account, work with the Virgin Islands Legislature to develop and implement measures to improve the Retirement System's sustainability.
3. Work with the Virgin Islands Legislature to ensure that any future early retirement legislative provisions are adequately funded.

**Government's Response**

**Payroll Contribution Levels**

The Governor of the Virgin Islands (Governor) concurs with Recommendation #1 in Finding #1, but notes that in essence this step may be redundant. We have worked with GERS' actuary, SEGAL, on a regular basis, and they have provided the suggested information. In fact, at the Governor's Summit in July 2009, SEGAL presented this specific information at our request. We are not opposed to the creation of a task force as recommended herein, but would suggest that the determination of the required contribution levels is not itself a challenge.



## **Action Plan**

The Governor will formally identify applicable members of his staff, financial team, and in general, his Administration who have already been working with GERS and its actuary to constitute the recommended task force. The team will continue to work with SEGAL and will memorialize measures taken to-date (e.g. change in employer contribution rate) that impact the contribution level coupled with future proposed actions recommended for implementation to address same.

**Implementation Date:** FY 2009

**Due Date:** 1<sup>st</sup> quarter of FY 2012

**Person Responsible:** Chief of Staff, Office of the Governor

## **Retirement System Sustainability**

The Governor fully concurs with Recommendation #2 in Finding #1. We note that the central challenge facing the Legislature and the Executive alike is that the \$80.0 million annual obligation to GERS constitutes approximately 10% of the net revenues to the General Fund, and accordingly, to fund this obligation within the current context of declining revenues will require a range of actions in combination that will likely include (i) substantial cuts in other areas and layoffs of personnel beyond the levels already contemplated (ii) expansion of the existing tax base through tax base expansion and economic development initiatives, (iii) implementation of revenue raising measures that may include increased taxes or fees, (iv) legislative actions to address growing retirement system costs. This obligation, as your report has correctly stated, is an absolute obligation, the failure of which to fund will lead to severe fiscal repercussions down the road.

## **Action Plan:**

The Governor will direct the task force to work closely with the V.I. Legislature to develop and implement realistic measures to enhance the sustainability of the Retirement System.

**Due Date:** 1<sup>st</sup> quarter of FY 2012

**Person Responsible:** Chief of Staff, Office of the Governor

### Funding Early Retirement

The Governor fully concurs with Recommendation #3 in Finding #1. Although it does not constitute an early retirement bill, but rather addresses employees with 30 or more years of service, with the most recent passage of the Economic Stability Act of 2011, identification of a funding source for the incentive payments, etc. was a prerequisite to affixing my signature to this legislation. Accordingly, my continued commitment to ensuring adequate funding also extends to future retirement legislative proposals.

#### **Action Plan:**

The Governor will issue a policy statement which will be articulated to the V.I. Legislature in writing that any future retirement legislative provisions, inclusive of early retirement measures (pursuant to the requirements of Title 3, Chapter 27, Sections 718 (j) and (k), VIC), must be linked to an identified, viable, adequate and sustainable funding source that is not already committed to general fund operations, or other key or critical purposes. Further, Title 3, Chapter 27, Section 718a. (f) Virgin Islands Code (VIC) which reads as follows will also be emphasized.

*The system shall not provide any new increases in benefits to members or beneficiaries unless the Government has deposited the funding for the prior fiscal year into the bank account of the system and concurrently makes a provision for the funding of all future benefit improvements on a sound actuarial basis in the budget.*

It is imperative to the viability of the GERS that key stakeholders understand that in accordance with Title 3, Chapter 27, Section 718 (l) VIC, GERS is precluded from paying benefits if the combined contribution (employee and employer contributions) does not “adequately finance benefits and related costs”.

**Due Date:** 1<sup>st</sup> quarter of FY 2012

**Person Responsible:** Chief of Staff, Office of the Governor

### **FINDING #2: DEFICIENCIES IN MAINTAINING MEMBER INFORMATION**

Inaccurate information maintained in the Retirement System has resulted in premature or deferred retirements and payment of inaccurate retirement benefits. As a result, some Retirement System members have been forced to make catch-up payments to qualify for entitled benefits.

**Recommendation (Governor of the Virgin Islands):**



1. Require Retirement System managers to identify areas for improvement. At a minimum, managers should address:
  - a. collection of retirement contributions within established timeframes;
  - b. reconciliation of member data with official GVI payroll records to ensure accuracy and, therefore, minimize contribution delays; and
  - c. performance of periodic data quality reviews to ensure the integrity of member information.

## **Government's Response**

### **Maintaining Member Information**

The Governor fully concurs with Recommendation #1 (a/k/a Recommendation #4, overall in the draft report) in Finding #2. The lack of sufficient information, including ongoing census information, has impeded the development of actuarial reports on an annual and timely basis.

However, for the past several months, GERS has been engaged in a massive project to introduce technology in the administration of benefits, and it is anticipated that these efforts will ameliorate this situation. Over 2 million pieces of member records have been converted to electronic files. There has been extensive review of members' records through data recovery from members and cleansing of members' data to insure that the correct member information is in their files. Further, GERS has entered into Memoranda of Agreements (MOAs) with various departments to obtain the member information on a timely basis.

The new Benefits Administration System is scheduled to "go live" on September 30, 2011. Employees received hands-on training on the system from July 15 – August 15. Between August 15 and the "go live" date of September 30<sup>th</sup>, the staff will run simulations to test the integrity of the system.

### **Action Plan:**

To preclude the possibility of deficiencies in member information due to the timing of the receipt of initial information and updated data, the Office of the Governor (OFG) and/or the Division of Personnel, as directed by OFG will initiate a meeting between GERS, the Division of Personnel, the Department of Finance, and the Human Resources/Personnel and Payroll Managers for the semi-autonomous and autonomous government entities to address matters germane to the following: timeliness of member contributions and basis for recording them, service entry dates, executed NOPAs (Notifications of Personnel Action), etc.

Further, the Office of the Governor will require the task force and/or the Department of Finance (and the Division of Personnel) to meet with GERS to address the three (3) areas indicated in the audit report: the collection of retirement contributions within established

timeframes, the reconciliation of member data with official GVI payroll records, and the performance of periodic data quality reviews of member information.

At present, some of the measures that are already in place that enhance the reliability and validity of member information are as follows:

- (A) Personnel Officers Meeting – GERS conducts an annual seminar to update Human Resource (HR) managers territory-wide.
- (B) HR/Personnel Officers Meeting – At least once a month, the Division of Personnel (DOP) meets with Human Resource and personnel/payroll employees government-wide.
- (C) Employee Orientation Workshop – Monthly or quarterly (as needed), DOP makes available a workshop for new and existing Government employees. This began as an orientation for new employees, but developed into a forum for other interested Government employees, as well.

To enhance the on-going efforts by GERS and DOP, the Government will also implement the following actions: (i) GERS will provide the Department of Finance (DOF) with a written notice (re: checking member information (e.g. retirement contributions on pay stub, service dates on NOPAs)) to be printed on a future pay stub for Government employees; and (ii) GERS will follow-up in writing on the status of legislation submitted to change the date of contribution payments to begin immediately upon hire.

**Implementation Date(s):** Annually & on-going - GERS Personnel Officers Meeting  
Monthly & on-going – DOP HR/Personnel Officers Meeting  
As needed & on-going – DOP Employee Orientation Workshop  
2010 – MOAs with departments  
2010 – draft legislation to the Senate

**Due Date(s):** September 30, 2011 – new Benefits Administration System  
1<sup>st</sup> quarter of FY 2012 – DOP/GERS, etc. meeting  
1<sup>st</sup> quarter of FY 2012 – Task Force/GERS, etc. meeting  
4<sup>th</sup> quarter of FY 2011 to 1<sup>st</sup> quarter of FY 2012 – pay stub notice  
4<sup>th</sup> quarter of FY 2011 – follow-up re: draft retirement legislation

**Person Responsible:** Administrator and Director of Member Services, GERS  
Chief of Staff, Office of the Governor

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## Appendix 3: Status of Recommendations

Recommendations	Status	Action Required
1	Resolved; not implemented.	Implementation by March 1, 2012.
2	Resolved; not implemented.	Implementation by March 1, 2012.
3	Resolved; not implemented.	Implementation by March 1, 2012.
4	Resolved; not implemented.	Implementation dates: September 30, 2011 – Benefits Administration System December 1, 2011 – Draft of Retirement Legislation March 1, 2012 – Task Force Meeting/Pay Stub Notice

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