

2013

The Road to Pension Reform

Pension Reform Taskforce Report
on the Government Employees Retirement System

Final Pension Reform Taskforce & Advisory Committee Findings
Government of the U.S. Virgin Islands
4/29/2013



PENSION REFORM TASKFORCE

NO. 5047 KONGENS GADE
CHARLOTTE AMALIE, ST. THOMAS, 00802

April 29, 2013

Honorable John P. deJongh, Jr.
Governor
Government House
No. 21-22 Kongens Gade
Charlotte Amalie, US Virgin Islands 00802

Dear Governor de Jongh:

The Pension Reform Taskforce Report on the Government Employees Retirement System (GERS) of the U.S. Virgin Islands is hereby submitted for your consideration. I would like to express my sincere appreciation to you for allowing me to serve as Chairman of this Taskforce, as we worked together with the Pension Reform Advisory Committee to identify and recommend solutions in the best interest of the members of the GERS and the Territory.

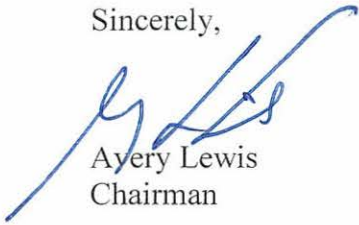
The Government Employees Retirement System is critically at risk due to a growing unfunded liability of approximately \$1.8 billion. Factors contributing to this situation are: insufficient contributions, a decreasing ratio of actives to retirees, and unfunded legislative mandates. Absent a change in the current approach, the system will become insolvent by September 30, 2023, resulting in the curtailment of many benefit payments. Therefore, throughout the summer and fall of 2012, the Pension Reform Taskforce and Advisory Committee have been analysing the System's actuarial data and policies, obtaining feedback from stakeholders and reviewing what actions were taken in other jurisdictions to address their pension issues.

As a result, we have developed recommendations, grounded in key data provided by the GERS Actuary and the Government of the Virgin Islands financial advisors, that will meet the goal of eliminating the insolvency of the System by holding employers and employees accountable, and reducing the Systems liability by imposing changes in various requirements. Additionally, we have considered the findings of an Attorney General's Opinion issued on April 16, 2012, which indicates that system changes can legislatively be effectuated.

The importance of securing the Government Employees Retirement System's benefit plan is a challenge which must be address to ensure that employees who have worked and contributed to the system will have annuities upon their retirement. Clearly, it is understood that some sacrifices

will have to be made to accomplish this task since economic and financial conditions will continue to cause concern for the Territory. However, the Pension Reform Taskforce and Advisory Committee agree that the time is now at hand for the Executive and Legislative Branches to acknowledge and address this issue.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Ayery Lewis', with a long, sweeping flourish extending upwards and to the right.

Ayery Lewis
Chairman

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SUMMARY

The Government Employees Retirement System (GERS) is critically at risk due to a growing unfunded liability of approximately \$1.8 billion. Factors contributing to this situation are: insufficient contributions, a decreasing ratio of actives to retired members, and unfunded legislative mandates. Absent a change in the current approach, the system will become insolvent by September 30, 2023, resulting in the curtailment of many benefit payments.

In 2008, Governor John P. de Jongh, Jr. realized the importance of addressing the unfunded liability of the GERS, and began the process of addressing this situation. He directed the payment of a \$20 million cash infusion and increased the employer contribution rate from 14.5% to 17.5%. This action increased annual employer funding from approximately \$60.5 million to \$76.0 million; this level of funding continues to grow.¹ Additionally, he began to explore increasing rum industry revenues, specifically the Internal Revenue Matching Fund, to address the growing GERS deficit; however this plan was derailed due to the Great Recession, the closing of HOVENSA, and the departure of several economic development beneficiaries.

In May 2012, Governor de Jongh signed Executive Order No. 458-2012 which required the formation of a Pension Reform Taskforce and Advisory Committee tasked with identifying recommendations to address this critical situation. The recommended reform policies, herein, are projected to remove insolvency and attain a funded percentage of 36%-42% by 2031, with the adoption of proposed scenarios and recommendations².

Recently, the GERS Board initiated further action by submitting legislation to the 29th Legislature of the Virgin Islands to amend Title 3, Chapter 27 and 28. However, these amendments were not acted upon and must be resubmitted to the 30th Legislature. On February 13, 2013, the Board met with members of the 30th Legislature to discuss the state of the pension system.

THE PROBLEM

A February 2010 Pew Center Report, indicated that a \$1 trillion gap exists between the \$3.35 trillion in pension, health care and other retirement benefits states have promised their current and retired workers as of fiscal year 2008 and the \$2.35 trillion they have on

¹ Fiscal Strategies Group, *Memorandum to the Governor on Pension Reform Issues and Options*, June 11, 2012, p. 1.

² The Segal Group, *GERS Financial Impact of the Final Pension Reform Taskforce Recommendations*, March 19, 2013.

hand to pay them. This shortfall will have to be paid within the next 30 years.³ This report clearly demonstrates that the solvency of public pension funds is a “hot button” issue across the nation and internationally.

Accordingly, the Government Employees Retirement System is not alone in its precarious situation, and the need for reform has been acknowledged for years resulting in some reforms. Earlier reform measures implemented include: the passage of Act No. 6794 which changed the way that pension payments are calculated, the creation of a Tier II classification for persons employed after Fiscal Year 2005 except for judges or legislators, increasing the employer contribution from 14.5% to 17.5%, and changing investment practices by allowing alternative investments.

However, concerns arose because the GERS continued to pay cost of living increases, while the legislature passed several unfunded mandates and early retirement incentive programs. Additionally, the Actuary reduced the rate of investment return from 8% to 7.50% with its most recent actuarial valuation of the System. The Actuary also indicated that if the System's cash flow issues are not solved, that it is highly unlikely that the long-term 7.50% assumption will be met. The government financial advisors, Fiscal Strategies Group, has raised a concern about the use of this percentage and references that,

A critical step in reform is choosing the assumption with respect to the discount rate (or the rate of investment return). They state that the GERS, like approximately 2/3 of plans nationally, uses a discount rate of 8%, and that this rate is achievable with a balanced portfolio of bonds and stocks during the boom years of the 1980s and 1990s, but this has not been an achievable rate over the course of the past decade. While many pensions systems are responding to this by reducing the actuarial yield by 25 or 50 basis points, arguably an appropriate rate going forward would be in the 5 to 6% range. A higher discount rate dangerously results in the understating of liabilities and the overstating of funded ratios.⁴

This is also emphasized in a statement by Moody's Investor Service, Inc. Moody's discussed its plan to implement adjustments to pension liability, asset and cost information reported by US state and local governments and their pension plans. Its Managing Director, Timothy Blake, stated that, “Pension liabilities are widely acknowledged to be understated, and that the proposed adjustments will improve the comparability and transparency of pension information across governments, enhancing our approach to rating state and local government debt.” In its public

³The Pew Center on the States, *The Trillion Dollar Gap: Underfunded State Retirement Systems and the Roads to Reform*, February 2010, p. 15.

⁴ Fiscal Strategies Group, *Memorandum to the Governor on Pension Reform Issues and Options*, June 11, 2012, p. 6-7.

statement, Moody's indicated that it would utilize a discount rate of 5.5% to judge and compare the financial soundness of state and city pension funds.⁵

This action is of significance, since the major impact with reducing the actuarial rate is that the unfunded liability and the annual required contribution would be increased putting further pressure on the local budget and credit ratings. Additionally, according to the GERS' Actuary most pension professionals and plan sponsors consider this inappropriate for proper long-term funding of retirement systems. The recent Governmental Accounting Standards Board Statements 67 and 68 confirm that proper funding for public sector retirement systems should reflect the long-term expected investment return for the system and not short-term market conditions to the extent that proper funding is in place.

PENSION REFORM TASKFORCE AND ADVISORY COMMITTEE

In September of 2011, the U.S. Department of Interior-Office of the Inspector General completed an audit of the Government Employees Retirement System to assess the long-term sustainability and performance of its administrative functions. Recommendations identified in this Audit were:

1. Establish a joint taskforce composed of Government of the Virgin Islands 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.
4. Require Retirement System managers to identify areas for improvement.⁶

On May 26, 2012, the Governor signed Executive Order No. 458-2012 to establish the Pension Reform Taskforce and the Advisory Committee to work jointly to address the solvency of the pension system. Appointed members for the Taskforce included representatives from the St. Thomas/St. John and St. Croix Chambers of Commerce, the Central Labor Council, the Finance Committee Chair or Post Auditor, the Director of the Office of Management and Budget, the GERS Administrator, GERS Board Chairman, and the Governor's Deputy Chief of Staff. The Advisory Committee representatives

⁵ Moody's Investors Service, Inc., *Moody's Proposes Adjustments to US Public Sector Pension Data*, July 2012.

⁶ Office of the Inspector General, US Department of the Interior, *Administrative Functions of the Virgin Islands Government Employees Retirement System*, Report No. VI-EV-OIA-0004-2011, September 2011.

were the St. Thomas/St. John and St. Croix Chambers of Commerce, the Central Labor Council, American Association of Retired Persons, the Advocates for the Preservation of GERS, Commissioner of Finance, the Director of the Division of Personnel, GERS Actuary (Segal) and Government's Financial Advisor (Fiscal Strategies).

Throughout the last few months, the Taskforce and Advisory Committee have been analysing the System's actuarial data and policies, obtaining feedback from stakeholders and reviewing what actions were taken in other jurisdictions to address their pension issues. They have developed recommendations that will meet the goal of eliminating the insolvency of the System by holding employers, employees and retirees accountable, and reducing the Systems liability by imposing changes in various requirements. These recommendations will be presented to the Governor and will be submitted to the Legislature.

KEY FINDINGS

The Taskforce and Advisory Committee participated in mini-presentations with GERS representatives and the Segal Group, the GERS' Actuary. They reviewed documents, made specific inquiries and were presented with scenarios which led to the key findings included here.

- After the implementation of the Virgin Islands Economic Stability Act of 2011 (VIESA) the active population was reduced to 9,376 employees.

Membership Summary-Preliminary Data As of September 30, 2011			
Year Ended September 30, 2011			
Category	2006	2011	2011 After Layoff
Active Participants In Valuation			
Number	10,736	10,376	9,376
Average age	45.1	45.7	45.3
Average years of service	14.0	13.9	13.3
Average salary	\$36,744	\$38,885	\$38,693
Retired Members and Beneficiaries			
Number in pay status	7,282	7,592	7,918
Average age	68.8	69.4	68.9
Average semi-monthly benefit	\$928	\$1,104	\$1,124

Source: GERS for Segal Presentation June 30, 2012 GERS Retreat

- Membership figures as of February 13, 2013, demonstrated a further decrease in the ratio of active members to retirees & beneficiaries to 1.1 to 1 or a total of 9,093 Active and 8,256 Retirees & Beneficiaries.

- In 2012, the GERS brought on a new Benefit System and has been actively reconciling membership records.

The Actual Financial Impact on GERS from VIESA			
	YTD Fiscal 2012	YTD Fiscal 2011	Variance
Employer Contributions	\$68,618,971	\$80,849,762	(\$12,230,791)
Employee Contributions	\$36,796,993	\$42,997,145	(\$6,200,152)
Annuity/Expense Payments	\$243,670,772	\$223,034,000	\$20,636,772

Source: GERS February 13, 2013

- The dismissal of government workers as well as early retirement incentives have worsened the financial position of the System; and will continue to do so if implemented to address General Fund deficits.
- Several unfunded legislative mandates have impacted the System.

Chronology of Unfunded Legislative Mandates		
Unfunded Mandates	Act No.	Year
Omnibus Authorization Act of 1984	4877	1983
Early Retirement for Department of Education Personnel	4896	1984
Early Retirement Incentive Training and Promotion Act of 1994	6007	1994
To Extend 6007	6088	1995
Early Retirement Benefits Options & to Reduce Expenditures	6361	2000
To Increase Retirement Benefits for Superior Court Judges	6391	2001
To Fund Salary Increases for Retirees & Eligible Employees	6415	2001
To Place Employees on Step	6427	2001
Expansion of Eligible Members of Early Retirement Program	6429	2001

Source: GERS November 2012

- Structural deficits in the General Fund made full funding of the annual required contribution impossible based upon the existing revenue structure of the Government; new revenues or the diversion of existing revenues is necessary to fund the growing System deficit.

- Actual amounts contributed by the government employers and government employees to the GERS have historically been far less than the actuarially required contribution amount.

Contributions vs. Benefit Payments & Expenses			
Fiscal Year	Total Contributions	Benefits Payments & Expenses	Surplus/Deficit
1994	61.7	46.7	15.0
1995	74.9	64.6	10.3
1996	71.7	73.3	(1.6)
1997	74.3	80.0	(5.7)
1998	71.9	91.6	(19.7)
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	120.3	193.9	(73.6)
2010	117.1	208.3	(91.2)
2011	123.8	223.0	(99.2)
2012 (unaudited)	105.4	243.7	(138.3)

Source: GERS February 13, 2013

- The historical and continuing shortfalls in the contributions made to the GERS have resulted in increasing negative cash flow, which was affected by decreases in the value of underlying assets during the market downturn.
- The employer contribution rate of 17.5% of payroll was deemed insufficient to prevent the insolvency of the System when utilized in several scenarios presented by the GERS Actuary.

UNFUNDED LIABILITY				
Year	(a) Actuarial Value of Assets	(b) Unfunded Actuarial Accrued Liability (UAAL)	Actuarial Accrued Liability (a)+(b)	Funded Ratio (a)/(c)
1998	1,078,291,775	307,300,371	1,385,592,146	77.82%
1999	1,255,210,822	518,608,964	1,773,291,625	70.78%
2000	1,330,089,822	525,608,964	1,855,698,786	71.68%
2001	1,342,894,336	731,727,064	2,074,621,400	64.73%
2002	1,337,676,064	815,884,419	2,153,560,483	62.11%
2003	1,346,906,862	921,669,858	2,268,576,720	59.37%
2004	1,360,288,336	977,502,024	2,337,790,360	58.19%
2005	1,366,982,183	1,088,574,553	2,455,556,736	55.67%
2006	1,421,093,035	1,236,571,529	2,657,664,564	53.47%
2007	1,509,244,380	1,241,138,878	2,750,383,258	54.87%
2008	1,530,604,789	1,310,218,726	2,840,843,515	53.88%
2009	1,534,899,736	1,397,261,661	2,932,161,397	52.35%
2010	1,505,970,212	1,513,059,673	3,019,029,885	49.88%
2011	1,448,926,591	1,719,110,906	3,168,037,497	45.74%

Source: GERS February 13, 2013

POLICY RECOMMENDATIONS

The Pension Reform Taskforce after discussion with the Advisory Committee made policy recommendations grounded in key data provided by the GERS Actuary and the Government of the Virgin Islands financial advisors. The policy recommendations address items in the U.S. Department of Interior-Office of the Inspector General's Evaluation Report-Administrative Functions of the Virgin Islands Government Employees' Retirement System, Report No. VI-EV VIS-0002-2010 and concerns raised by various stakeholders. They do the following:

- Memorialize measures to be taken to impact the contribution levels coupled with future proposed actions recommended for implementation to address same;
- Identify realistic measures which could be implemented by the Governor and the Legislature to enhance the sustainability of GERS;
- Communicate a viable, adequate and sustainable funding source going forward for the retirement system.

To arrive at its recommendations, the Taskforce reviewed the National Association of State Retirement Administrators, *"Selected Approved Changes to State Public Pensions to Restore or Preserve Plan Sustainability"*, The Pew Center Report, *"The Trillion Dollar Gap, Underfunded State Retirement Systems and the Roads to Reform, GERS Legislation, and various other articles.*

THE ATTORNEY GENERAL'S OPINION

Additionally, through correspondence of October 12, 2012, the Taskforce requested an Attorney General's Opinion to address two issues which emerged at its initial meeting:

1. Whether the current retirement benefits of employees in the Tier I and Tier II Retirement Benefits Program can be adjusted?
2. Whether the retirement benefits of retirees can be changed?

On April 16, 2013, the Attorney General issued his Opinion (**See Appendix A**). The short answer provided to both questions was "yes", however, a qualification was offered. The Attorney General's Opinion indicated that any actions taken would be subject to strong constitutional opposition, but that current law could be changed by legislative action. It was stated that, "...annuitants and prospective annuitants may raise significant challenges to any reduction of retirement benefits. The significant challenges will be based on two provisions of the United States Constitution which are made applicable by the Revised Organic Act of 1954. 48 USC, Section 1561—improper impairment of contract and violation of the Fourteenth Amendment's substantive and procedural due process protections."⁷

This Opinion also indicated that consideration would have to be given to political ramifications and more importantly "...that a strong argument can be made for the adjustment of retirement benefits as a result of public necessity due to the fiscal crisis of the Virgin Islands, however such legislative action must include a full analysis of the financial condition of GERS and that analysis must be preserved in the legislative record to support the action."⁸

With consideration of the Attorney General's Opinion and the GERS Actuarial Reports which projected insolvency by September 30, 2023, unless changes are made to the current plan of benefits and contribution rates, the Taskforce issued this report. The proposed reforms include contribution increases and plan modifications to reduce plan costs. The recommendations are applicable to both Tier I and Tier II employees. The following are the recommendations:

Retirement Age

- Regular Tier II Government Employees- Employees may not collect retirement income until they are age 62 with 10 years of service, eliminating the any age with 30 years of service provision.
- Class III Tier II Government Employees- Employees may not collect retirement income unless age 55 with 25 years of service or age 60 with

⁷ USVI Department of Justice, Office of the Attorney General, Attorney General Opinion, "Adjustments of Tier I & II Retirement Benefits; Change of Retiree Benefits". April 16, 2013. p 2.

⁸ Ibid, p 9.

10 years of service, eliminating the any age with 20 years of service provision.

Suspension of the Cost of Living Adjustment (COLA)

- The COLA should not be given for five years except for persons with disabilities as established by the Virgin Islands Code and approved by the Government Employees Retirement System. This provision should be revisited after five years.

Increase the Employer and Employee Contribution Rates & Adjust Benefits

- *Option A*- Submit legislation to increase employer contribution by 2% and employee contribution by 1% respectively for 7 years beginning 10/1/2013 and reduce Tier I benefits by 10%.
- *Option B*-Submit legislation to increase employer contribution by 2% for 7 years, and employee contributions by 1% for first 3 years and by 0.5% for the next 4 years beginning 10/1/2013 and reduce Tier I benefits by 10%.
- Legislators-Submit legislation to increase the contribution rate of Legislators to 15%.
- Judges-Submit legislation to increase Judges contributions as follows:
 - i. New Judges-17%
 - ii. Sitting Judges-15% at beginning of next term
 - iii. Sitting Judges-16% at beginning of second year of new term
 - iv. Sitting Judges-17% at beginning of third year of new term and thereafter

Eliminate Double Dipping

- v. Enforce 75 days of employment after retirement;
- vi. Remove all 75 day exemptions by amending legislation pertaining to teachers, police, fire etc...
- vii. If a retiree goes over 75 days their pension will be suspended.

Salary Cap

- Eliminate the salary cap of \$65,000; increase to social security cap of \$110,000; use the bifurcated calculation, proposed by the Actuary, to determine annuities for salaries over \$65,000.

Refund of Contributions

- Allow refund of employee contributions to non-vested members only and no interest should be paid on refunds.

Personal Loans

- Increase personal loans from \$50,000 to \$75,000.
- Increase commercial loans from \$250,000 to \$350,000.

Revenue Generation

- That the Government of the Virgin Islands commit rum excise tax receipts deposited into the Internal Revenue Fund to back a bond or to fund directly the 2% increase in employer contributions recommended here in. The GERS payment shall be deducted after the payment of debt services and any priority funding now committed. The purpose of this recommendation is to have an established revenue source dedicated directly to fund the GERS' unfunded liability.

According to the GERS Actuary (**See Appendix B**), the following are the effects of the recommendations:

- All benefit changes and contribution rate changes under Option A
 - Projections show that the funded percentage will decline from 46% in 2011 to a low of 37% in 2018, and then start to increase in 2024 and thereafter
 - The market value of assets is projected to decline to an estimated low of \$1,068 million in 2018 and then begin to increase thereafter
- All benefit changes and contribution rate changes under Option B
 - Projections show that the funded percentage will decline from 46% in 2011 to a low of 35% in 2024, and then start to increase in 2028 and thereafter
 - The market value of assets is projected to decline to an estimated low of \$1,060 million in 2019 and then begin to increase thereafter

CONCLUSION

The state of the Government Employees Retirement System's benefit plan is a challenge for the Government of the Virgin Islands. However, it is a challenge which must be address to ensure that employees who have worked and contributed to the system will have annuities upon their retirement. Clearly, it is understood that some sacrifices will have to be made by government employers, employees and retirees to accomplish this task since economic and financial conditions will continue to cause concern for the Territory. As such, it is imperative that this problem is acknowledged and addressed by the Executive and Legislative Branches going forward.

ACKNOWLEDGEMENTS

MEMBERS OF THE PENSION REFORM TASKFORCE

Avery Lewis, Chairman and President of Central Labor Council
Raymond James, Esquire, Vice-Chairman and Former Chairman of the Board of Trustees of GERS
Debra Gottlieb, Secretary and Director of the Office of Management and Budget
Austin Nibbs, Administrator of the Government Employees' Retirement System
Nathan Simmonds, Deputy Chief of Staff/Principal Advisor
Jose L. George, Post Auditor
Tom Brunt, St. Thomas/St. John Chamber of Commerce

MEMBERS OF THE ADVISORY COMMITTEE

Angel Dawson, Jr., Commissioner of Finance
Kenneth Hermon, Jr., Director of Personnel
Sebastiano Paiewonsky, St. Thomas/St. John Chamber of Commerce
Wayne Harty, St. Croix Chamber of Commerce
Helene Smollett, Advocates for the Preservation of GERS
Denyce Singleton, American Association of Retired Persons

OTHER

Anise I. Hodge, Policy Advisor to the Governor & Government House Liaison to GERS
Leon F. (Rocky) Joyner, Vice President and Actuary, the Segal Group
David Paul, Fiscal Strategies Group
Joe Aubain, St. Thomas/St. John Chamber of Commerce

APPENDIX A



THE UNITED STATES VIRGIN ISLANDS
DEPARTMENT OF JUSTICE
OFFICE OF THE ATTORNEY GENERAL

VINCENT F. FRAZER, ESQUIRE
ATTORNEY GENERAL

April 16, 2013

ATTORNEY GENERAL OPINION

Hon. John P. de Jongh
Governor, U.S. Virgin Islands
Office of the Governor
Nos. 21-22 Kongens Gade
St. Thomas, Virgin Islands 00802

Re: Opinions: Adjustment of Tier I & II Retirement Benefits; Change of Retiree Benefits

Dear Governor de Jongh:

In an October 12, 2012 letter, you requested an opinion on certain issues posed to you from the Government Employees Retirement System Pension Reform Task Force (hereinafter referred to as "Pension Reform Task Force"). The issues raised by the Pension Reform Task Force were stated as follows:

Issue 1. Whether the current retirement benefits of employees in the Tier I and Tier II Retirement Benefits Program can be adjusted?

Issue 2. Whether the retirement benefits of retirees can be changed?

It is my understanding that this request was made as a result of questions raised by the Pension Reform Task Force at the very first meeting. The members of the Pension Reform Task Force inquired as to whether it is a viable legal option under the statute to make adjustments to the benefit package granted to government employees.

SHORT ANSWERS

Turning to the specific questions you proffered, my responses are as follows:

Issue 1. Yes

Issue 2. Yes

SUMMARY

While the short answers to the questions are in the affirmative it must be made clear that there is a qualification, in that any action taken based upon the affirmative responses may be subject to strong opposition at a constitutional level; however that opposition is not insurmountable. The current law can be changed by legislative action, but we can expect that the annuitants and prospective annuitants may raise significant challenges to any reduction of retirement benefits. The significant challenges will be based on two provisions of the United States Constitution which are made applicable by the Revised Organic Act of 1954. *48 USC. § 1561*. First, the opponents will certainly raise a claim of improper impairment of contract. Second, the opponents may also raise a claim for the violation of the *Fourteenth Amendment's substantive and procedural due process* protections. There may be other minor claims of rights but we do not believe those arguments will have significant import.

ANALYSIS

The Virgin Islands Government created the retirement system

...to encourage qualified personnel to enter and remain in the service of the Government of the Virgin Islands by establishing an orderly means whereby those who become superannuated or otherwise incapacitated as the result of age or disability, may be retired from service without prejudice and without inflicting a hardship upon the employees retired, and to enable such employees to accumulate reserves for themselves, their dependents and their beneficiaries, to provide for old age, death, disability and termination of employment, thus promoting economy and efficiency in the administration of government. 3 V.I.C. 701 (b).

(emphasis added). There is no dispute that vital to the success of any retirement system is the monetary contributions of the member employees and the employer which serve as the basis for any benefits that are distributed to or received by a member employee. More attractive to the government employee contributor is the section of the applicable law that states:

Each member shall, by virtue of the payment of contributions to this system, receive a vested interest in such contributions, and in consideration of such vested interest shall be conclusively deemed to

undertake and agree to pay the same and to have them deducted from his compensation as herein provided. 3 V.I.C. §722. (emphasis added).

Virgin Islands law further provides:

The right of any member or other beneficiary to any annuity, benefit or refund shall accrue as of the date of establishment.

Except as herein specifically otherwise provided, any annuity provided herein shall be payable for life in equal semimonthly installments from the beginning date thereof as fixed by the Administrator, on the fifteenth and last day of each month, first payment to be due as of October 15, 1959; Provided, That for the purpose of effectuating administration, a small pro rata amount may be paid for part of the month when the annuity or benefit payment begins after the first day of the month, or ends before the last day of the month.

No annuity or benefit shall be increased, decreased, revoked or repealed, except for error, or where specifically otherwise provided by this chapter. 3 V.I.C. 723. (emphasis added).

By definition, retirement benefits for government employees under Virgin Islands law refers to the acceptance of a retirement annuity upon withdrawal from service with the Government of the Virgin Islands. 3 V.I.C. §702(q). At the onset, I must state that the distinction between Tier I and Tier II benefits is based on whether the employee entered the government service before or after October 1, 2005. Persons entering government service before October 1, 2005 are entitled to the benefits under Tier I (*Title 3 VIC Chapter 27*). Persons entering the government service after October 1, 2005 are entitled to benefits under Tier II (*Chapter 28A*). However, whether the member falls within Tier I or Tier II, is not of significant relevance in responding to the issues you have raised since “[a]ll provisions of chapter 27 are applicable” to the Tier II Retirement Benefits Program. 3 V.I.C. 750(e). Chapter 27, in relevant part, can be referred to as the Tier I Retirement Benefits Program established October 1, 1959. 3 V.I.C. §701 (d). Therefore, the single analysis set forth below responds to both benefits programs.

Vesting of Retirement Benefits

The law currently does not provide any specific exception that allows for decrease or repeal of an annuity or benefit. This begs the question whether there can be an adjustment to benefits that a retiree is currently receiving as the law suggests that at some point the retiree’s benefits would

have vested. We note however, that it is within the discretion of the Virgin Islands Legislature to make or change laws in the interest of the people of the Territory. *CJS §10; State of Indiana ex rel. Anderson v Brand, 303 U.S. 95, 100 (1938); Such v. State, 950 A.2d 1150 (R.I. 2008); In re Goldman, 868 A.2d 278 (N.H. 2005).*

Notwithstanding the above, there is another consideration. *Section 722*, cited above, speaks only to vesting of the employee's contributions and is silent as to the employer's contribution. Moreover, *T.3 V.I.C. §718(i)* makes it clear that the amounts contributed to the system by the employer on behalf of the employee "shall not" be considered as the employee's contribution. This may suggest that adjustments to benefits may be possible only at the level of the employer's contribution.

Most Government employees' interest in a retirement annuity will vest after the employee has earned thirty (30) years of credited service and has contributed into the system for each of those years. Employees who attain the age of fifty (50) years and have worked for the government for 10 years may have a vested interest in an annuity, with a penalty. (*T.3 V.I.C. §705(d)*). Peace officers and hazardous duty employees have a vested interest in an annuity after twenty (20) years of credited service. (*T.3 V.I.C. §705d*). However the right to the annuity does not attach until the employee applies for retirement. The vested interest in an annuity for the members of the Judiciary attaches after serving one term. (*T. 3V.I.C. §§ 733, 7701*). The vested interest in an annuity for the Members of the Legislature attaches after serving six years. (*T.3 V.I.C. §§714,763*). Therefore while it is clear that the interest in retirement benefits vests or attaches at different times for different types of government employees, the interest in retirement benefits for most government employees vests after serving thirty years.

Impairment of Contract Claim under the Contract Clause of the Federal Constitution

Any legislated adjustment to a retiree's benefits will very likely be met with a claim for "impairment of contract rights". Under the Contract Clause of the Federal Constitution, "No State shall ... pass any ... Law impairing the Obligation of Contracts...." *U.S. Const. Art. I, § 10, cl. 1*. The *Revised Organic Act* incorporates the federal Contract Clause, providing that: "No law impairing the obligation of contracts shall be enacted." *Rev. Org. Act of 1954 § 3, cl. 6.*, (codified at *48 U.S.C. § 1561*); *WICO, Ltd. v. Gov't of the V.I.*, 844 F.2d 1007, 1009 (3d Cir.1988).

Thus, the contract clause of the United States Constitution is incorporated into Virgin Islands law by § 3 of the *Revised Organic Act*. "In order to state a claim under the Contract Clause, the plaintiff must allege that: (1) a contractual right existed, (2) a change in state/territorial law impaired the contract, and (3) the impairment was substantial." *Swift v. McKeesport Hous. Auth.*, 726 F.Supp.2d 559, 570 (W.D.Pa.2010) (citing *Transp. Workers Union of Am., Local 290 v. SEPTA*, 145 F.3d 619, 621 (3d Cir.1998)); see also *Perano v. Twp. of Tilden*, 423 Fed.Appx. 234, 239 (3d Cir.2011) . Although the prohibition on the impairment of contractual rights under the Contract Clause applies only to exercises of legislative power, the application of the Contract Clause is not limited solely to formal enactments and statutes of the legislature. If administrative conduct bears the appearance of legislative authority when it changes the preexisting conditions by making new rules to be applied thereafter to all or some part of those subject to its power the government conduct can be viewed as legislative in nature. *Mabey Bridge & Shore, Inc. v. Schoch*, 666 F.3d 862, 874 (3d Cir.2012). An administrative adjustment to employee retirement benefits that is less favorable may be considered an impermissible new rule or law that violates the constitutional mandate disapproving impairment of contract rights. However, in this instance we assume that the inquiry regarding the adjustment of these benefits contemplates adjustments that are made by legislative action, since the benefits are clearly established by statute.

Courts have recognized two types of contract rights that are protected under the Fourteenth Amendment. See *Unger v. Nat'l Residents Matching Program*, 928 F.3d 1392, 1397-99 (3d Cir.1991). First, contract rights are afforded protection where the contract confers a protected status, such as those characterized by a quality of either extreme dependence in the case of welfare benefits, or permanence in the case of tenure, or sometimes both, as frequently occurs in the case of social security benefits. *Id.*, *Unger*, 928 F.3d at 1399 (quoting *S & D Maint. Co. v. Goldin*, 844 F.2d 962, 966 (2d Cir.1988)). Second, contract rights are also afforded protection where the contract itself includes a provision that the state/territory entity can terminate the contract only for cause. *Id.*, citing *Cleveland v. Bd. of Educ. v. Loudermill*, 470 U.S. 532, 538-39 (1985) (recognizing a property right created by a for-cause termination provision in an employment contract). For the purposes of our discussion, the second type of contract is not relevant here as there is no issue of terminating a contract for cause. *Id.*, *Unger*.

The threshold requirement for the recognition of public contracts has been referred to as the "unmistakability doctrine." See *United States v. Winstar*, 518 U.S. 839 (1996)). Because legislatures cannot bind future legislatures from employing their sovereign powers in the absence of the clearest of intent to create vested rights protected under the Contract Clause, courts developed canons of construction

disfavoring implied governmental contractual obligations unless such surrender has been expressed in terms too plain to be mistaken. The requirement that the government's obligation be "unmistakably clear" serves the dual purpose of limiting contractual incursions on a state's/territory's sovereign powers and of avoiding difficult constitutional questions about the extent of state/territory authority to limit the subsequent exercise of legislative power.

The U.S. Supreme Court, in a Contract Clause case, found that there was ample evidence to support that a promise was made by the state in a contractual setting, in return for a specific bargained-for benefit and that the statutory scheme clearly employed the language of contract. See *United States Trust Co. vs. New Jersey*, 431 U.S. 1, 18, 97 S.Ct. at 1515 (involving a legislative covenant between New York and New Jersey and future bondholders where the very "purpose of the covenant was to invoke the constitutional protection of the Contract Clause as security against repeal"). In giving weight to this U.S. Supreme Court pronouncement, we must be prepared to concede that 3 V.I.C. 701(b), cited above does express language that will allow a Court to most likely conclude that a contractual right inures to the benefit of long term employees.

It is quite foreseeable and reasonable to argue that the retirees of the Government of the Virgin Islands do have a protected status by law and are, in great part, dependent upon the expected benefits for which they have made monetary contributions and remained in government employ. So long as the retirees have fulfilled the preconditions and have begun to receive their annuity, they would have standing to protest any diminishment of their specifically bargained-for retirement benefits found in the statutory scheme which employs the language of a contract.

It is our opinion that if the legislature enacts legislation which adjusts the benefits of the members of the Government Employees Retirement System (hereinafter referred to as "GERS") and such adjustment is supported by a demonstrated need to financially stabilize the GERS system; a reviewing Court may find that there has not been an impermissible impairment of contract. The financial ills of the GERS will have to be included in the deliberative record of the legislature to show that there is a "rational legislative purpose" and an "important and legitimate public purpose" that precipitates the adjustment of the benefits. *Maryland States Teachers Association v. Harry Hughes, Governor*, 594 F. Supp. 1353 (D.C. Md. 1984). Certainly the adjustment will have to be carefully tailored to distinguish between active employees and current annuitants. Because the interest in benefits for current annuitants may have already vested, it is less

likely that a court will find that there has not been an impermissible impairment of contract for this group.

Moreover the Legislature can also take notice of the fiscal plight of the Government of the Virgin Islands as the "employer-contributor" who bears the cost of contributing its portion into the system at an increasing rate which will continue to increase if the benefits are not decreased. The government was previously forced to reduce the salaries of its employees in order to avoid a possible full blown fiscal melt down. As part of its deliberation, the legislature can give due consideration to the need and the reasonableness of the adjustment of the benefits in light of the government's financial condition.

Procedural and Substantive Due Process Claims under the 14th Amendment

Having addressed the "impairment of contract" argument, there is another basis for a challenge to an adjustment of the benefits based on the Fourteenth Amendment. In addition to the "impairment of contract" argument, a retiree will very likely raise the issue of the violation of his or her Fourteenth Amendment's substantive and procedural due process rights. Specifically, the retiree may allege a *taking* of vested property rights, i.e., retiree benefits, without due process in violation of the Fourteenth Amendment. As indicated, however this argument will be available only to an employee who has already retired.

The Fourteenth Amendment prohibits a state/territory from depriving any person of life, liberty, or property, without due process of law. *U.S. Const. amend. XIV, § 1*. The Due Process Clause of the Fourteenth Amendment contains both procedural and substantive due process protections. In order to state a claim under the Fourteenth Amendment Due Process Clause, the retiree would have to establish that a property interest existed and that his or her due process was violated in the deprivation of that property interest. *Schuster v. Thruen*, 18 V.I. 287, 296 (D.V.I.1981). It is beyond debate that, in order to have a property interest in a benefit, an individual must have a "legitimate claim of entitlement" to the benefit, *Board of Regents v. Roth*, 408 U.S. 564, 577 (1972). Local law will determine whether such a claim exists. See *Schuster*, 18 V.I. at 296.

Virgin Islands law provides that government employees shall receive benefits from the Retirement System upon the occurrence of any one of four events: (1) retirement, (2) work-related disability, (3) non-work related disability, or (4) death. See *Molloy, et al. vs. Todman, et al*, 30 V.I. 164, 1994 WL 326237 (DCVI 1994). The current retirees (annuitants) would be able to establish their right to benefits by virtue of their

retirement. At this juncture, any legislation adjusting the benefits for these individuals would arguably be considered retroactive legislation, which is not favored by courts. Such an adjustment would allegedly be burdensome to the retirees, but beneficial to the GERS.

To establish a substantive due process violation, a plaintiff must prove a deprivation of an interest protected by the substantive due process clause and that the government's deprivation of that protected interest shocks the conscience. *Chambers ex rel. Chambers v. Sch. Dist. of Phila. Bd. of Educ.*, 587 F.3d 176, 190 (3d Cir.2009) (citing *Chainey v. Street*, 523 F.3d 200, 219 (3d Cir.2008)); see also *Iredin v. Fitzgerald*, No. 10-228, 2010 WL 2994215, at *5 (E.D.Pa. July 27, 2010). Although courts have held that laws amending rights to pension funds do not shock the conscience, clearly persuasive arguments may be made by vested elder retirees within the context of Virgin Islands law. See *Molloy vs. Monsanto, et al.*, (DCVI 1994) 30 V.I. 164. The political drama thereafter will, of course, introduce another aspect with which to contend.

In order to state a procedural due process claim, a claimant would have to prove he/she was deprived of an individual interest that is encompassed within the Fourteenth Amendment's protection of life, liberty, and property and that the procedures available to him/her prior to the deprivation of these rights did not provide due process of law. *Hill v. Borough of Kutztown*, 455 F.3d 225, 233-34 (citing *Alvin v. Suzuki*, 227 F.3d 107, 116 (3d Cir.2000)). For a procedural due process claim to be proven, courts must determine whether the individual had a protected interest in making available the due process protections, and if so, whether the individual was afforded appropriate process. *Id.*, *Iredin*, 2010 WL 2994215, at *5 (citing *Shoats v. Horn*, 213 F.3d 140 (3d Cir.2000)). Although the procedural component of the Due Process Clause will not protect everything that might be described as a 'benefit', a court will consider the dimensions by considering existing rules or understandings that stem from an independent source such as state/territory law. *Town of Castle Rock v. Gonzales*, 545 U.S. 748, 756, 125 S.Ct. 2796, 162 L.Ed.2d 658 (2005) (quoting *Paul v. Davis*, 424 U.S. 693, 709, 96 S.Ct. 1155, 47 L.Ed.2d 405 (1976)). Courts have held that pension benefits are not fundamental constitutional rights or even vested rights (see *Kegolis v. Borough of Shenandoah*, No. 03-0602, 2006 WL 3814311, at *3 (M.D.Pa. Dec. 27, 2006) and *Walker v. City of Waterbury*, 601 F.Supp.2d 420, 425 (D.Conn.2009); however a court will most likely look at the statutes of the Virgin Islands cited herein above to determine what rules exist and what understandings a retiree may have regarding pension benefits. Virgin Islands laws with respect to retiree pensions can reasonably be interpreted to mean that the rights of the retirees are vested and cannot be reduced once the retirement threshold has been satisfied, unless there is "an important and legitimate

public purpose". Further, once vesting occurs, it can fairly be said that adjustments may not be had without a GERS Board hearing and a strong legislative record, to satisfy procedural due process rights.

With regards to the adjustment referred to in your letter, this proposed adjustment seems to contemplate amending the law to alter or diminish expected retirement benefits rather than simply proposing a different interpretation as to the actual benefits retirees are entitled to. The latter would place a greater burden on a retiree to prove both the impairment of contract rights which they relied upon and expected, and the taking of property without due process. Ordinarily, courts afford substantial deference to a legislature's "judgment as to the necessity and reasonableness of a particular measure." *U.S. Trust Co. vs. New Jersey*, 431 U.S. 1, 23 (1977). However, where the state/territory itself is a party to a contract, "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the [territory's] self-interest is at stake." *Id.* at 26. Thus if action is taken to adjust the benefits under the current facts, it is unlikely that a court will presume that the government acted out of reasonableness or necessity.

CONCLUSION

In conclusion, to withstand Contracts Clause inquiry and denial of due process claims, a legislative action by the government that adjusts retiree benefits would of necessity have to be sufficiently important and serve a legitimate public interest. See *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 444-48 (1934) (statute impairing mortgages found to be constitutional in light of depression-era exigencies); *Buffalo Teachers Fed'n v. Tobe*, 464 F.3d 362, 368 (2d Cir.2006) (wage freeze impairing municipal labor contracts found to be supported by an important public interest in light of the city's fiscal crisis). When the public purpose is not significant, state/territory action impairing a contract has been found to be constitutionally infirm. See *WICO, Ltd. v. Gov't of the V.I.*, 844 F.2d 1007, 1022 (3d Cir.1988). To withstand a due process claim the government's action cannot be seen as arbitrary or irrational. *Woodwind Estates, Ltd. v. Gretkowski*, 205 F.3d 118, 123 (3d Cir.2000)). Any generalized adjustment to pension benefits overall, and most certainly, any adjustment to current retiree benefits will be met with claims of contractual impairment and denial of due process of the retiree pension beneficiaries. Furthermore, any proposal to reduce the benefit package of government employees must take into consideration the extent of the political ramifications. In sum, it is my opinion that a strong argument can be made for the adjustment of retirement benefits as a result of public necessity due to the fiscal crisis of the Virgin Islands, however such legislative action must include a full analysis of the

Letter: Vincent F. Frazer to Gov. John P. de Jongh

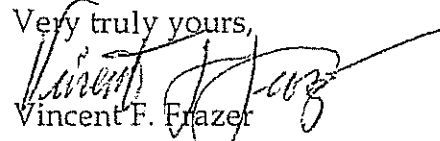
Re: Opinions: Adjustment of Tier I & II Retirement Benefits; Change of Retiree Benefits

April 16, 2013

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financial condition of GERS and that analysis must be preserved in the legislative record to support the action.

Very truly yours,

A handwritten signature in black ink, appearing to read "Vincent F. Frazer", with a long horizontal flourish extending to the right.

Vincent F. Frazer
Attorney General

APPENDIX B



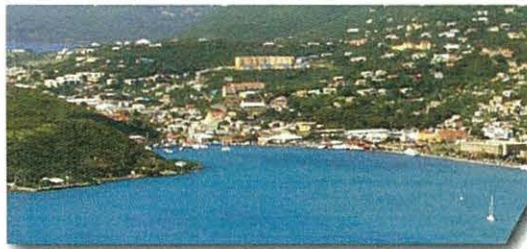
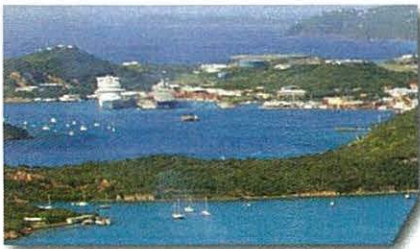
GOVERNMENT OF THE VIRGIN ISLANDS RETIREMENT SYSTEM

*Financial Impact of the FINAL Pension Reform Taskforce Committee
Recommendations*

March 19, 2013

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 **SEGAL**

Executive Summary

- As requested, we have analyzed the potential financial impact of the Final Pension Reform Taskforce Committee recommendation
- Significant input was provided by the Advisory Committee
- Our projections are based on the data, assumptions and results of the October 1, 2011 actuarial valuation. In addition, the following developments since the 2011 valuation have been reflected in the actuarial projections shown in this report:
 - 10% decline (about 1,000 actives) in the active population after September 30, 2011 due to the Economic Stability Act of 2011
 - Effective January 1, 2013, the Board approved suspending the plan's Cost of Living Adjustments (COLA) to non-disabled retirees
- The Pension Reform Taskforce Committee recommendations are summarized in the next slide and include both increasing contributions to the plan and modifying the plan provisions to reduce plan costs
 - The Committee's recommendations are applicable to both Tier 1 and Tier 2 employees
 - Changes to the benefit provisions of Tier 1 employees are based on the Committee's discussions with the Attorney General
- As previously reported, our projections show that the Plan will become insolvent during the Plan Year ending September 30, 2023 assuming no changes are made to current plan of benefits and contribution rates

Executive Summary *continued*

- Based on our projections, the recommendations have the following effects:
 - All benefit changes and contribution rate changes under Option A
 - Our projections show that the funded percentage will decline from 46% in 2011 to a low of 37% in 2018, and then start to increase in 2024 and thereafter
 - The market value of assets is projected to decline to an estimated low of \$1,068 million in 2018 and then begin to increase thereafter
 - All benefit changes and contribution rate changes under Option B
 - Our projections show that the funded percentage will decline from 46% in 2011 to a low of 35% in 2024, and then start to increase in 2028 and thereafter
 - The market value of assets is projected to decline to an estimated low of \$1,060 million in 2019 and then begin to increase thereafter

This report was prepared under the supervision of
Aldwin Frias, FSA, FCA, MAAA, EA and Rocky Joyner, ASA, FCA, MAAA, EA

Summary of Current Key Benefit Provisions

Service Pension	Eligibility	Tier 1—Amount	Tier 2—Amount
Regular Employees	Age 60 with 10 years of service or any age with 30 years of service	2.5% of Final Average Salary* per year of service up to 100%	1.75% of Final Average Salary* per year of service up to 100%
Public Safety Employees	Age 55 with 10 years of service or any age with 20 years of service	3% of Final Average Salary* per year of service up to 90%	2.1% of Final Average Salary* per year of service up to 90%
Legislature	Age 50 with 6 years of service or any age with 20 years of service	2.5% of highest compensation for years 1-6 3% of highest compensation for years 7-12 4% of highest compensation for years above 12 up to a maximum of 75%	3.5% of highest compensation for years 1-6 4% of highest compensation for years 7-12 4.5% of highest compensation for years 13-20 5% of highest compensation for years above 20 up to a maximum of 100%
Judges	Age 50 with 6 years of service	5% highest compensation per year of service up to 100%	
* Final Average Salary for Regular and Public Safety employees is based on the average of the highest annual salary up to a maximum of \$65,000 for any five years in the last 10 years.			

Early Pension	Eligibility	Amount
Regular Employees	Age 50 with 10 years of service	Service pension reduced 3.9% per year less than age 60
Public Safety Employees	Age 50 with 10 years of service	Service pension reduced 3.9% per year less than age 55

Deferred Retirement (Vesting)	Eligibility	Amount
	10 years of service and leave contributions in System	Service pension accrued at termination

Summary of Current Key Benefit Provisions *continued*

	Eligibility	Tier 1—Amount	Tier 2—Amount
Duty Connected Disability	Total and permanent disability as a result of performance of duty	75% of salary less workers compensation	52.5% of salary less workers compensation

	Eligibility	Tier 1—Amount	Tier 2—Amount
Non-Duty Connected Disability	9 years of service and total and permanent disability	2% of Final Average Salary* per year of service Minimum of 20% Maximum of 60%	1.4% of Final Average Salary* per year of service Minimum of 14% Maximum of 42%

* Final Average Salary for Regular and Public Safety employees is based on the average of the highest annual salary up to a maximum of \$65,000 for any five years in the last 10 years.

Post-Retirement COLAs	1.5% of the original retirement benefit each year after age 60. Effective January 1, 2013, this COLA is suspended
	1% of the original retirement benefit each year up to age 60 for Disability Pensioners
	No annual increases apply to survivor annuitants

Severance Benefit	Refund of contributions with 4% annual interest, if no other benefit is payable
-------------------	---

Contribution Rates	Tier 1	Tier 2
Regular Employees	8%	8.5%
Public Safety Employees	10%	10.625%
Legislature	9%	11%
Judges	11%	

Summary of Pension Reform Taskforce Committee Recommendations

Plan of Benefits

- For all employees, provide benefits for salaries above \$65,000
 - 1% of each year's salary above \$65,000
 - Benefits above \$65,000 are limited to the Social Security cap (currently at \$110,000)
- Tier 1 benefits are suspended by 10% for all active, non-active and in pay participants
- Tier 2 Retirement ages are modified:
 - Regular employees – age 62 with 10 years of service
 - Public Safety employees – age 55 with 25 years of service or age 60 with 10 years of service
- Severance benefit is only payable to non-vested participants and no interest granted
- Benefit changes to Tier 1 employees are based on the Committee's discussions with the Attorney General

Contribution Rates

- Employer
 - Effective October 1, 2013, increase 2% of pay per year for 7 years to an ultimate rate of 31.5% of pay at October 1, 2019
 - The increase in employer contributions will be supported by a bond
- Regular and Public Safety employees
 - Option A: Effective October 1, 2013, increase 1% of pay per year for 7 years
 - Option B: Effective October 1, 2013, increase 1% of pay per year for 3 years and 0.5% for the next 4 years
- Legislature
 - Increase to 15% of pay
- Judges
 - Effective at beginning of new term for current sitting judges, increase to 15%, 16% and 17% of pay for each of next 3 years of new term
 - Effective immediately for new judges, 17% of pay
- Contributions will be made for total salaries up to the Social Security cap

Actuarial Cost Analysis – Proposed Benefit Changes

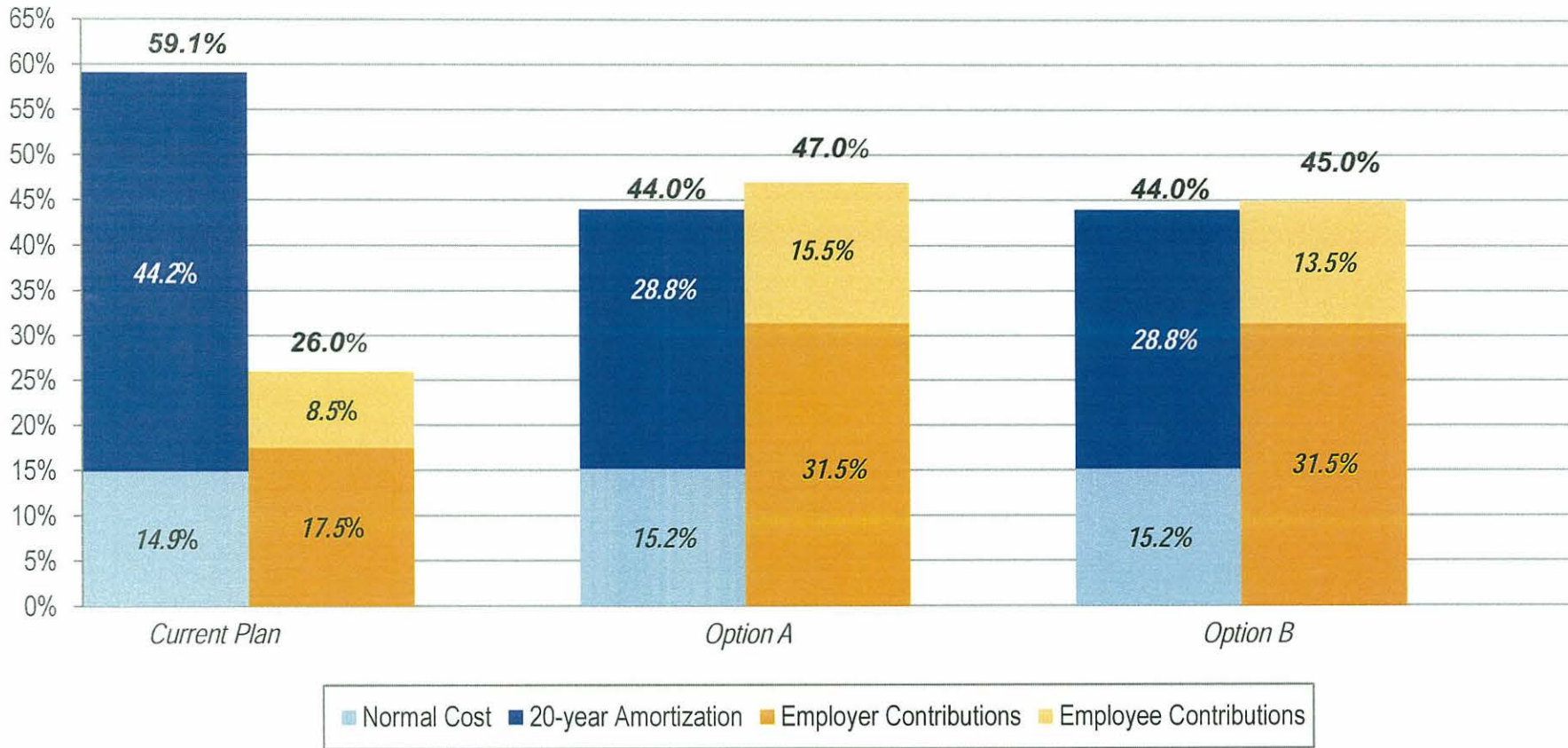
Proposed Changes to Benefit Provisions – Effect on Total Costs Amounts Based on October 1, 2011 Actuarial Valuation (\$Millions)

	Provisions as of October 1, 2011 after reflecting the Economic Stability Act of 2011	Proposed Benefit and Contribution Changes
1. Total Salary	\$362.8	\$374.0
2. Normal Cost*		
• Dollar	\$39.3	\$41.9
• Percent of Salary	10.8%	11.2%
3. Actuarial Accrued Liability	\$3,204.5	\$2,631.0
4. Unfunded Accrued Liability**	\$1,755.6	\$1,182.1
5. 20-year Amortization of the Unfunded Liability		
• Dollar	\$160.2	\$107.9
• Percent of Salary	44.2%	28.8%
6. Annual Cost: (2) + (5) including Provision for Expenses		
• Dollar	\$214.4	\$164.7
• Percent of Salary	59.1%	44.0%

* The increase in the Normal Cost is primarily due to the additional 1% accruals for salaries over \$65,000 and the increase in employee contribution rates. This increase in cost is more than offset by the additional contributions for salaries over \$65,000.

** Based on Actuarial Value of Assets of \$1,448.9 Million

Comparison of Alternative Annual Plan Costs (including all future contribution increases)



These results are based on the October 1, 2011 valuation and reflects the impact of the Economic Stability Act of 2011 that caused a 10% decline in the active population

Projection Parameters

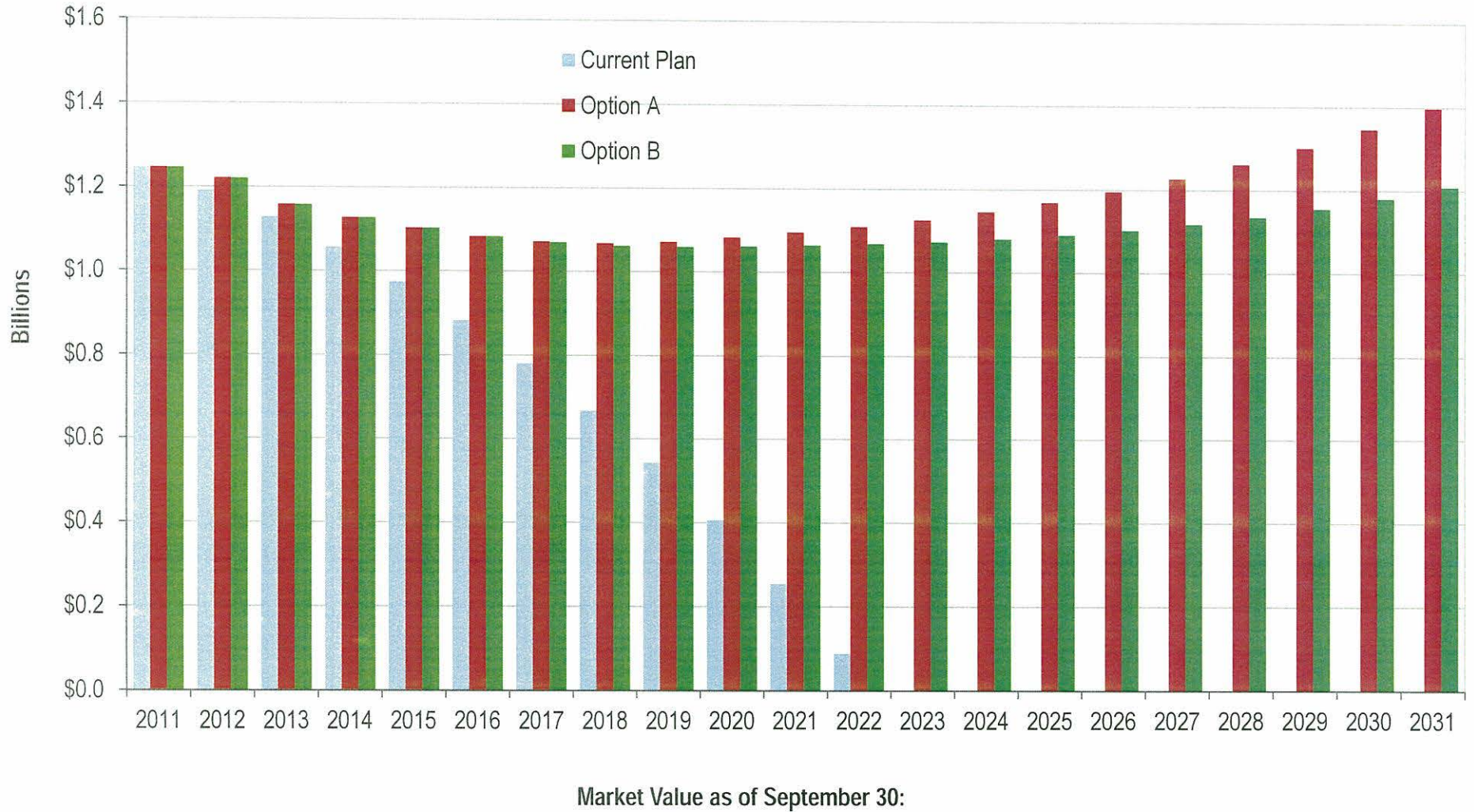
Projection Assumptions:

- After the decline in the active population due to the Economic Stability Act of 2011, the active population is assumed to remain level at 9,376 employees
- Total payroll of \$362.8 remains level during the period of contribution rate increases and is assumed to increase 2.5% per year thereafter in addition to any increases due to changes in salary limits
- Administrative expenses are assumed to increase 3% per year
- Benefit payments for the first 15 years are projected based on the 2011 valuation results. Benefit payments after 15 years are assumed to increase 2% per year to account for retirements from new entrants after 2011.
 - The benefit payment stream is updated based on suspending the COLA effective January 1, 2013, and other proposed plan changes
- Assets are assumed to earn a 7.5% return each year, unless otherwise stated

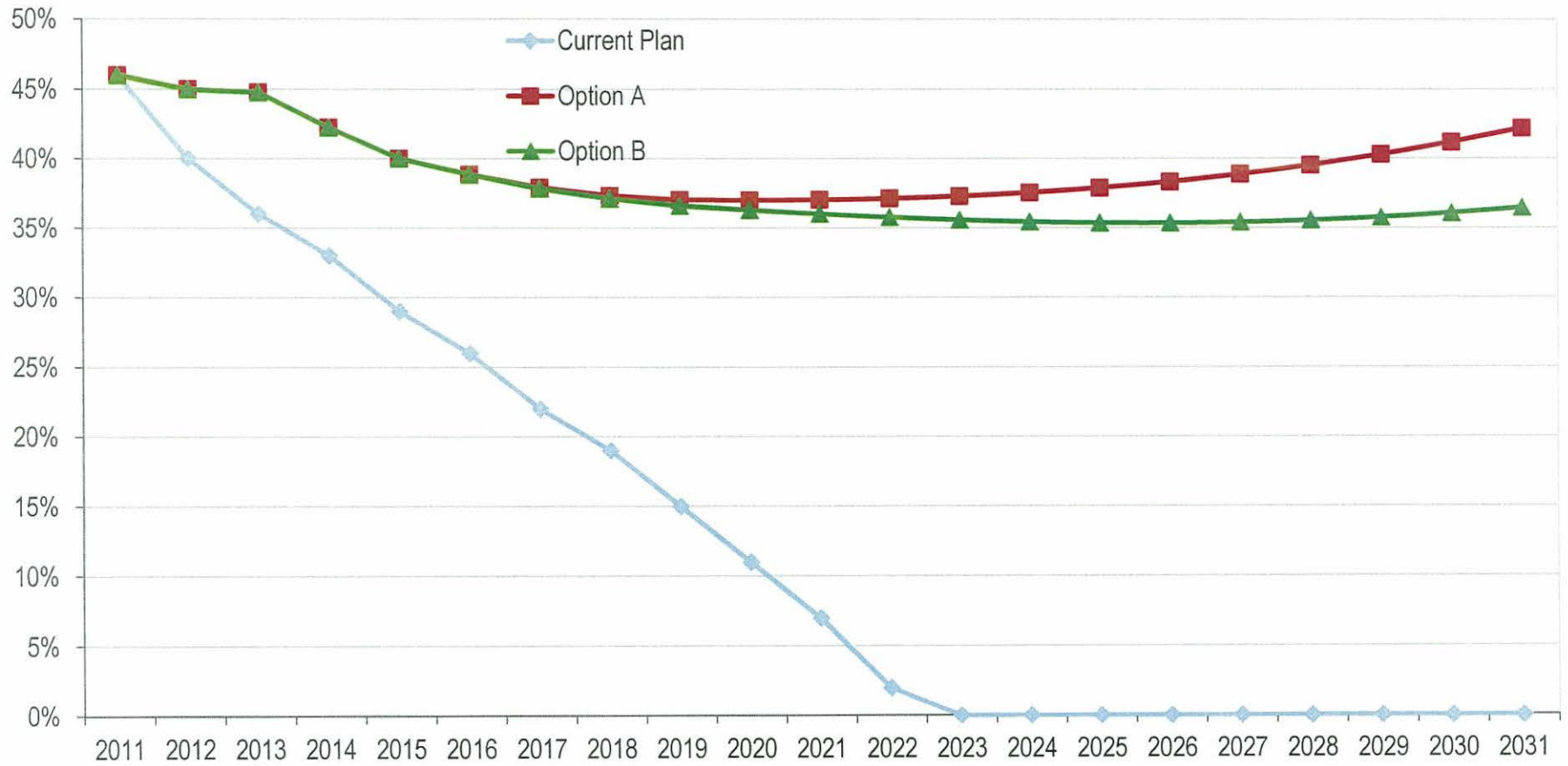
Caveats:

- The closer the plan gets to insolvency, asset illiquidity may become an issue and earning the assumed return may become more difficult.
- Projections, by their nature, are not a guarantee of future results. The projections are intended to serve as estimates of future outcomes, based on the information available to us and the assumptions described herein. Emerging results may differ significantly if the actual experience proves to be different from these assumptions.

Projection of Market Value of Assets



Projection of Funded Percentages



Funded Percentage as of September 30:

Projection of Market Value of Assets (In Millions)

Current Plan

Annual Net Investment Return: 7.5%
Employer Contribution Rate: 17.5% of payroll
Employee Contribution Rate: 8.5% of payroll

Year ending Sept. 30:	Contributions			Disbursements		Return on Assets	Market Value of Assets	Funded Percentage (AVA/AAL)
	Employee	Employer	Benefit Shortfall	Benefit Payments	Expenses			
2011							\$1,246.0	46%
2012	\$30.8	\$63.5	-	\$222.4	\$14.9	\$88.1	1,191.2	40%
2013	31.6	65.1	-	228.1	15.3	83.8	1,128.3	36%
2014	32.4	66.7	-	234.0	15.8	79.0	1,056.6	33%
2015	33.2	68.4	-	240.0	16.3	73.4	975.3	29%
2016	34.0	70.1	-	246.2	16.7	67.2	883.7	26%
2017	34.9	71.8	-	252.6	17.2	60.2	780.8	22%
2018	35.8	73.6	-	256.4	17.8	52.4	668.4	19%
2019	36.7	75.5	-	261.4	18.3	43.8	544.7	15%
2020	37.6	77.4	-	268.4	18.8	34.4	406.8	11%
2021	38.5	79.3	-	273.3	19.4	23.9	255.8	7%
2022	39.5	81.3	-	279.2	20.0	12.5	89.9	2%
2023	40.5	83.3	\$91.4	284.5	20.6	-	-	0%
2024	41.5	85.4	183.1	288.7	21.2	-	-	0%
2025	42.5	87.5	186.2	294.3	21.8	-	-	0%
2026	43.6	89.7	187.7	298.5	22.5	-	-	0%
2027	44.7	91.9	191.1	304.5	23.2	-	-	0%
2028	45.8	94.2	194.4	310.6	23.9	-	-	0%
2029	46.9	96.6	197.9	316.8	24.6	-	-	0%
2030	48.1	99.0	201.3	323.1	25.3	-	-	0%
2031	49.3	101.5	204.9	329.6	26.1	-	-	0%

Projection of Market Value of Assets (In Millions)

Option A

Annual Net Investment Return: 10% for plan year ending 9/30/2012, 7.5% thereafter
Employer Contribution Rate: 17.5% of payroll, increasing 2% per year from 10/1/2013 to 31.5% after 7 years
Employee Contribution Rate: 8.5% of payroll, increasing 1% per year from 10/1/2013 to 15.5% after 7 years
All recommended plan provisions

Year ending Sept. 30:	Contributions			Disbursements		Return on Assets	Market Value of Assets	Funded Percentage (AVA/AAL)
	Employee	Employer	Bond for 2% Increases in Employer Rate	Benefit Payments	Expenses			
2011							\$1,246.0	46%
2012	\$30.8	\$63.5	-	\$222.4	\$14.9	\$117.5	1,220.6	45%
2013	30.8	63.5	-	227.6	15.3	86.0	1,157.9	45%
2014	35.5	65.4	\$7.5	205.6	15.8	82.6	1,127.5	42%
2015	39.2	65.4	14.9	208.5	16.3	80.6	1,102.9	40%
2016	43.0	65.4	22.4	212.8	16.7	79.0	1,083.2	39%
2017	46.7	65.4	29.9	214.2	17.2	77.9	1,071.7	38%
2018	50.4	65.4	37.4	216.2	17.8	77.3	1,068.2	37%
2019	54.2	65.4	44.8	219.3	18.3	77.4	1,072.4	37%
2020	57.9	65.4	52.3	224.1	18.8	77.9	1,083.1	37%
2021	59.4	67.0	53.6	226.7	19.4	78.8	1,095.8	37%
2022	60.9	68.7	55.0	230.0	20.0	79.7	1,110.0	37%
2023	62.4	70.4	56.3	232.9	20.6	80.8	1,126.5	37%
2024	63.9	72.2	57.7	234.8	21.2	82.2	1,146.5	38%
2025	65.5	74.0	59.2	237.8	21.8	83.7	1,169.3	38%
2026	67.2	75.8	60.7	239.6	22.5	85.5	1,196.4	38%
2027	68.8	77.7	62.2	242.2	23.2	87.6	1,227.4	39%
2028	70.6	79.7	63.7	244.8	23.9	90.0	1,262.8	40%
2029	72.3	81.7	65.3	247.6	24.6	92.7	1,302.6	40%
2030	74.1	83.7	67.0	249.8	25.3	95.8	1,348.2	41%
2031	76.0	85.8	68.6	252.8	26.1	99.3	1,399.0	42%

Projection of Market Value of Assets (In Millions)

Option B

Annual Net Investment Return: 10% for plan year ending 9/30/2012, 7.5% thereafter
Employer Contribution Rate: 17.5% of payroll, increasing 2% per year from 10/1/2013 to 31.5% after 7 years
Employee Contribution Rate: 8.5% of payroll, increasing 1% per year for 3 years from 10/1/2013 and 0.5% for the next 4 years to 13.5% after 7 years
All recommended plan provisions

Year ending Sept. 30:	Contributions			Disbursements		Return on Assets	Market Value of Assets	Funded Percentage (AVA/AAL)
	Employee	Employer	Bond for 2% Increases in Employer Rate	Benefit Payments	Expenses			
2011							\$1,246.0	46%
2012	\$30.8	\$63.5	-	\$222.4	\$14.9	\$117.5	1,220.6	45%
2013	30.8	63.5	-	227.6	15.3	86.0	1,157.9	45%
2014	35.5	65.4	\$7.5	205.6	15.8	82.6	1,127.5	42%
2015	39.2	65.4	14.9	208.5	16.3	80.6	1,102.9	40%
2016	43.0	65.4	22.4	212.8	16.7	79.0	1,083.2	39%
2017	44.8	65.4	29.9	214.2	17.2	77.8	1,069.7	38%
2018	46.7	65.4	37.4	216.2	17.8	77.1	1,062.3	37%
2019	48.6	65.4	44.8	219.3	18.3	76.7	1,060.2	37%
2020	50.4	65.4	52.3	224.1	18.8	76.7	1,062.2	36%
2021	51.7	67.0	53.6	226.7	19.4	76.9	1,065.3	36%
2022	53.0	68.7	55.0	230.0	20.0	77.2	1,069.2	36%
2023	54.3	70.4	56.3	232.9	20.6	77.5	1,074.2	36%
2024	55.7	72.2	57.7	234.8	21.2	77.9	1,081.8	35%
2025	57.1	74.0	59.2	237.8	21.8	78.5	1,091.0	35%
2026	58.5	75.8	60.7	239.6	22.5	79.3	1,103.2	35%
2027	60.0	77.7	62.2	242.2	23.2	80.3	1,118.0	35%
2028	61.5	79.7	63.7	244.8	23.9	81.5	1,135.7	36%
2029	63.0	81.7	65.3	247.6	24.6	82.8	1,156.4	36%
2030	64.6	83.7	67.0	249.8	25.3	84.5	1,181.0	36%
2031	66.2	85.8	68.6	252.8	26.1	86.4	1,209.1	36%

Questions

