The Virgin Islands Consortium

Plan to Refinance Territory's Debt Receives Skeptical Reception at Senate; Measure Sent to Finance Committee for Further Vetting, Amendments

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The skeptics were many during the Senate Committee of the Whole hearing on Tuesday, which was eventually dissolved into a special session to allow for potential action to be taken on Governor Albert Bryan's debt refinancing bill.

The only action taken, however, was senators' unanimous vote to send the bill to the Committee on Finance for further vetting, with lawmakers expressing a number of concerns with the complex measure.

The Bryan administration has contended that the legislation would provide $85 million in additional revenue to the territory every year for the next three years, some of which would be used to stave off collapse of the beleaguered Gov't Employees' Retirement System (G.E.R.S.).

The bill seeks to refinance the territory's most valuable asset: the Internal Revenue Matching Fund (IRMF), or rum cover-over funds. The USVI receives roughly $250 million from the U.S. Treasury annually in taxes paid on rum made in the USVI and sold in the U.S. The funds are used to pay a number of the territory's debts, most of which go directly to the bondholders while the remaining funds are then remitted to the local government. At times, the USVI receives roughly $30 million when all obligations are made whole.

Bryan administration testifiers contended on Tuesday that refinancing debt within the government, under the Public Finance Authority, would not be beneficial because the government's credit rating is low and would thereby not yield an interest rate that would allow for the kind of savings that would make a difference. To be successful, they contended, a special purpose vehicle, called in short SPV, would be needed to facilitate a credit rating that would pave the way for interest rates as low as an estimated 3.5 percent. Current interest rate levels for IRMF bonds are between 5.8 percent and 6.5 percent, according to Nathan Simmonds, director of finance and administration at the Public Finance Authority.

The SPV would take control of the IRMF from the government and would have sole dominion over its operations, with its scope of authority — including its commitment to pay the government's debt service — coded into law.

But lawmakers expressed skepticism throughout the session even as they listened to the merits of the bill.

For one, Senator Kurt Vialet contended that the numbers were off.

"They have not been able to give a clear explanation as to how they came up with the $85 million for the three years. Our present debt service is $108 million, and they are saying that in the first three years, the debt service is only going to be $17 million. This is literally impossible. Those numbers in no way would add up to debt service on a loan at 3 percent interest for $1 billion," Mr. Vialet told the Consortium Tuesday evening following the session. The $1 billion Mr. Vialet referred to is a rough estimate of the territory's debt under the IRMF.

A cost analysis was requested of Bryan administration testifiers that would make clear debt service payments showing all the particulars, including principal and interest payments broken down year by year, "which they have not turned over to us so that we could really make a determination so as to how they're structuring this loan," Mr. Vialet said.

He added, "From what we're seeing it is light on the front end in terms of repayment of debt service, but very heavy on the backend. So what we will be doing is mortgaging the people of the Virgin Islands 10-12 years from now when the debt service is going to balloon, and that's the way they have it structured." Mr. Vialet said the testifiers provided a chart showing that the loan balloons overtime.

A number of senators also voiced concern with the lack of an agreement from major stakeholders, including the U.S. Treasury, which remits the rum cover-over payments to the USVI, and the rum companies, namely Crucian Rum and Diageo, whose agreements as part of the original deal would be affected under the new agreement. According to the testifiers, Treasury hasn't given an indication on what it would do, arguing that Treasury's decision would in part hinge on local lawmakers' decision on the bill.

With "Treasury it's a chicken and hen problem," said Attorney Karol K. Denniston of Squire Patton Boggs, bond counsel representing the government. "They want to know that the legislation is in place and that the Virgin Islands is on board with this transaction." PFA's Mr. Simmonds along with PFA Attorney Kye Walker said talks were held with representatives of the rum companies. Mr. Simmonds said the companies had signaled support as their own interest rates would be lowered under the new agreement. Senators, however, were adamant on having documentation from both Treasury and the rum companies that would confirm those parties' stance on the bill.

"At the end of the day we're dealing with the people's money," said Senator Alicia Barnes. Stating that she was certain her mother and mother's church sisters were watching, she added, "They want to ensure that we do our due diligence as stewards of the people's resources."

The measure, if it is to be approved, would see a number of amendments, according to lawmakers. The bill takes the government's most valuable asset, the IRMF, removes it from the control of the government and places it under a special purpose vehicle. But the measure is lacking mechanisms to rein in the SPV.

While the special purpose vehicle's primary commitment is to pay the debt service as included in the bill, the measure lacks adequate limitations.

"It is what they could do after paying debt service," said Sen. Vialet. He said according to the bill in its current form, "the corporation could hire who they want. They could tell us that their operating budget is $15 million and there's no part that we could say that that's not allowable, because they don't come back to the Legislature for funding." Mr. Vialet added, "They're taking the money directly from the matching fund and there's no set amount or set structure; they're just saying that it's not going to need a lot of money. But the language clearly says that they could hire a whole slew of people."

Senators also want to include language in the bill that would keep the current structure of the escrow account — which holds $130 million — in its current form. As it stands now, the government cannot touch the $130 million. The funds in said account serve as a fail-safe backup if the government were to find itself in a position where revenues would be so diminished that it couldn't meet its financial covenants.

Mr. Vialet, chairman of the Committee of Finance, said a number of lawmakers were contemplating revisions to the bill that would provide much more funding — $1.7 billion — $700 million of which would go directly to the Government Employees' Retirement System. The way this would be accomplished, he said, is instead of the administration's original plan that would net the government $85 million every year for three years —

some of which would be used to undergird GERS — the idea is to use the government's current annual debt service payment of $108 million to float a much larger sum under the SPV while securing the same low interest rates.

"If we redirect that $108 million and they are able to refinance at a lower rate, then they could get more money," Mr. Vialet said. He said that at interest rates hovering around 3 percent to 3.5 percent, maybe less, the agreeing senators believe that the government could float $1.7 billion at the same amount of debt service currently being paid, which is $108 million annually.

"So we're saying let's float $1.7 billion and we'll give the $700 million to the retirement system so that they could invest and we could give the system 8-10 more years. But to just give G.E.R.S. $85 million one year, and the government can't prove how they're going to get that $85 million, it's a waste of time to us," Mr. Vialet said.

The measure will be heard in the Committee on Finance on Thursday at 11:00 a.m., which is expected to be followed by a session at 3:00 p.m.