

TESTIMONY BY DAVID SHIMABUKURO
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE SENATE COMMITTEE ON JUDICIARY AND LABOR
ON
SENATE BILL NO. 3005

FEBRUARY 8, 2008

RELATING TO FEDERAL TAX QUALIFICATION
OF THE EMPLOYEES' RETIREMENT SYSTEM

Chair Taniguchi and Members of the Committee:

Congressional legislation requires the Internal Revenue Service (IRS) to determine whether governmental public pension plans are complying with federal income tax laws. In this regard, ERS and other pension plans are now required to submit determination letters to the IRS and make remedial plan amendments based on a 5-year cycle system. The deadline for the initial 5-year cycle will be January 31, 2009.

It is critical that ERS comply with the Internal Revenue Code so our members can continue to benefit from tax advantages that a qualified governmental plan can provide, some of which are:

- Deferral of federal income taxes to the member on employer contributions and plan investment earnings until distribution is made.
- Deferral of federal income taxes on employee contributions to the ERS and service credit purchases.

The following provisions are required to comply with the federal income tax laws and maintain the ERS' tax-qualified status:

- Adds a new section which allows certain newly elected officials to make a one-time irrevocable election to join the ERS. At the present time, elected officials can elect to become ERS members or withdraw from ERS membership at any time during their term of office.
- Current elected officials will be given the opportunity to remain, join or terminate membership in the ERS before October 1, 2008. If no election is made, the elected official will retain the same ERS membership status.

- Current elected officials who are retirees will be given the opportunity to continue or terminate their pension before October 1, 2008. If no election is made, their pension will continue and they cannot return to active membership while serving as an elected official.
- Sets forth the circumstances under which retirants may return to service as elected officials without suspension of their retirement benefits.
- Repeals the provision that allows elected officials and judges who have reached the 75% statutory cap on retirement benefits to withdraw from ERS membership by retiring even though they remain in office.

The Board of Trustees supports this Administration Bill and recommends its passage.

Thank you for the opportunity to testify on this Bill.

TESTIMONY BY GEORGINA K. KAWAMURA
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE SENATE COMMITTEE ON JUDICAIRY AND LABOR

ON
SENATE BILL NO. 3005

February 8, 2008

RELATING TO THE FEDERAL TAX QUALIFICATION OF THE EMPLOYEES'
RETIREMENT SYSTEM

Senate Bill No. 3005 amends statutes governing the Employees' Retirement System (ERS) to protect its tax qualified status.

The Department of Budget and Finance supports this administration measure.

The amendments eliminate optional membership in the ERS and include 1) implementation of a one-time irrevocable election (at the time of initial election to office) to join the ERS by elective officers and 2) prohibition of the current practice by elective officers and judges to retire upon reaching the statutory cap on retirement benefits but delaying receipt of the benefits until a future separation date. Entrance into membership is currently at the option of elective officers and this optional membership jeopardizes the ERS' tax qualified status. The practice of retiring but delaying receipt of benefits until a future separation date while the judge or elective officer continues in office raises tax qualification issues on optional membership and in-service distribution of pre-tax contributions. The bill also sets forth conditions under which a retiree may return to service as an elective officer and continue to receive their pension.

Senate Bill 3005 protects the ERS' tax qualified status and ensures the continued favorable tax treatment of employee contributions made on pre-tax basis.



Testimony to the Senate Committee on Judiciary and Labor

Senator Brian T. Taniguchi, Chair
Senator Clayton Hee, Vice Chair
Friday, February 8, 2008, 9:00 a.m.
State Capitol, Conference Room 016

By

Sharen Tokura
Human Resources Director

WRITTEN TESTIMONY ONLY

Bill No. and Title: Senate Bill No. 3005, Relating to Federal Tax Qualification of the Employees' Retirement System.

Purpose: To repeal the provisions of chapter 88, Hawai'i Revised Statutes, that provide for optional membership in the Employees' Retirement System (ERS).

Judiciary's Position:

The Judiciary supports the intent of Senate Bill No. 3005 in retaining the tax-qualified status of ERS. However, we are concerned about the impact of repealing Section 88-61(c) without consequent changes to Sections 88-74(2) and (3).

The repeal of Section 88-61(c) removes the provision which allows an elective officer or judge to nominally retire upon reaching the statutory cap on retirement benefits while still remaining in service and not making further contributions to the ERS. The repeal will require elective officers and judges who have reached the maximum retirement allowance to continue to be active members and contribute to the ERS without any added retirement benefits.

Sections 88-74(2) and (3) set the maximum retirement allowance for elective officers and judges at seventy-five per cent of the member's average final compensation and provide for the return to the member of the excess accumulated member contributions held by ERS upon retirement. The withholding of member funds for no retirement purpose does not appear appropriate.



Senate Bill No.3005, Relating to Federal Tax Qualification of the Employees'
Retirement System
Senate Committee on Judiciary and Labor
Friday, February 8, 2008
Page 2

It would appear that members who continue to make contributions are active members and should be provided with retirement benefits based on the total contributions made to ERS while on active status. To do so, however, may jeopardize the plan for reasons unknown at this time to the Judiciary. Therefore, we are using this vehicle to raise this concern.

The Judiciary understands the impact to the larger membership should ERS lose its tax exempt status and fully supports the retention of the tax-exempt status through legislative amendments to the retirement program. However, we ask that consideration be given to either lifting the 75% ceiling or permit the elective officers and judges to continue to accrue retirement benefits based on their contributions to ERS while on active status.

Thank you for the opportunity to provide testimony on Senate Bill No. 3005.