HB 1035
HD1

WRITTEN ONLY

TESTIMONY BY KALBERT K. YOUNG
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE SENATE COMMITTEE ON WAYS AND MEANS
ON
HOUSE BILL NO. 1035, H.D. 1

April 1, 2011

RELATING TO EMPLOYEES' RETIREMENT SYSTEM BENEFIT ENHANCEMENT MORATORIUM

House Bill No. 1035, H.D. 1, institutes a moratorium on the enhancement of Employees' Retirement System benefits until the system's fund ratio is one hundred percent.

The Department of Budget and Finance strongly supports this amended Administration bill which will allow the Employees' Retirement System to improve and protect its funded status. Placing a moratorium on the enhancement of Employees' Retirement System benefits until the system's fund ratio is one hundred percent will prevent the unfunded liability from growing through enactment of benefit enhancements during this period.

The Administration believes that stability in the level of benefits received by current and former employees is an important factor in facilitating the Employees' Retirement System's ability to eventually eliminate its unfunded liability and ensure the long-term viability of the system.

DEPARTMENT OF BUDGET & FISCAL SERVICES

CITY AND COUNTY OF HONOLULU

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PETER B. CARLISLE
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DIRECTOR

April 1, 2011

The Honorable David Ige, Chair
and Members of the Committee on Ways and Means
The Senate
State Capitol
Honolulu, Hawaii 96813

Dear Chair Ige and Members:

Re: H.B. 1035, H.D.1 – Relating to Employees' Retirement System Benefit Enhancement Moratorium

The City and County of Honolulu (City) is well aware of the serious challenges the Retirement System is facing and recognizes the need for significant course corrections. The City offers the following comments on House Bill 1035, House Draft 1. The City views H. B. 1035, H. D. 1 as part of a package of bills proposing changes aimed at addressing the Retirement System's unfunded liability. The City supports **these bills as a collective package designed to address the unfunded liability issue in a comprehensive manner**—with reasonable changes to benefits as well as increases in the Employer contribution rate.

The moratorium on benefit enhancements proposed in this bill makes sense as the unfunded liability issue is being addressed, and it complements the update to the benefits structure contained in H.B. 1038 which is also being heard today. These changes along with increases in the Employer contribution provided in H.B. 1038 will, we hope, ultimately result in a system that is more stable and Employer costs that are more predictable. This is the reason the City is willing to support the changes even though the increase in the Employer contribution will have a severe negative impact on our budget going forward.

We realize this Committee is facing very difficult decisions on many matters, including this one. We urge the Committee to take the comprehensive approach needed to set the Retirement System on a sustainable path.

Thank you for the opportunity to comment on this measure.

Yours truly,

Michael R. Hansen, Director
Department of Budget & Fiscal Services

Noel T. Ono, Director
Department of Human Resources

IMUALLIANCE

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TESTIMONY ON HOUSE BILL 1035, HOUSE DRAFT 1, RELATING TO EMPLOYEES' RETIREMENT SYSTEM BENEFIT ENHANCEMENT MORATORIUM

Senate Committee on Ways and Means
Hon. David Y. Ige, Chair
Hon. Michelle Kidani, Vice Chair

Friday, April 1, 2011, 9:00 AM
State Capitol, Conference Room 211

Honorable Chair Ige and committee members:

I am Kris Coffield, representing the IMUAlliance, a nonpartisan political advocacy organization that currently boasts over 60 local members. On behalf of our members, we offer this testimony in support of HB 1035, HD1.

As of today, the Employee Retirement System (ERS) is facing a $7.1 billion shortfall, with an addition $1.5 billion deficit being added to the underfunded liability over the next two years because of market losses resulting from the recent recession. Within four years, the state's legally required contribution to the pension system is expected to top $650 million, yet the funding ratio for ERS has declined, by most measures, to approximately 60 percent. Coevally, the pension fund portfolio's average rate of return has dipped to 2.8 percent over the past decade, far short of the 8 percent mandated by state law.

To offset the disparity between current contributions and contracted benefits, the state is selling an increasingly large share of its pension-related assets. As an investigation of the problem by *Hawaii Business Magazine* revealed, this month, the ERS is set to cannibalize approximately $200 million in assets, in 2011, and potentially $600 million a year—or more—by the end of the decade, if nothing is done to stem the bleeding. The actuarially required contribution, which calls for the system to be fully funded within 30 years despite expanding lifespans and payrolls, already consumes nearly 10 percent of the state's general fund budget, reaching $400 million for state employers, in 2010. Without implementing precautionary measures, the underfunded liability will only continue to grow.

Thus, it is imperative that ERS enhancements be truncated until the fund is more robust. Halting additional benefits is only one part of a solution that will likely include increasing the number of years it takes employees to become vested and changing how final salaries are calculated, but it's an important step toward fixing a broken system. Even with employee contributions elevated to 15 percent for general employees and 19.7 percent for police officers and firefighters, the fund's amortization period still exceeds 30 years. Wesley Machida, the ERS administrator, has said that those rates would need to be raised, by next year, to 17 percent and 25 percent, respectively, for the amortization period to once again comport with statutory prescriptions. Other actuaries who have reported on the problem have suggested rates as high as 18.8 percent and 27.3 percent, respectively, which seems politically and economically untenable, given the current budget crunch. What is left, then, is a cap on benefit enhancements, the least painful in a menagerie of unpopular alternatives.

Mahalo for the opportunity to testify <u>in support</u> of this bill.

Sincerely,
Kris Coffield
Legislative Director
IMUAlliance