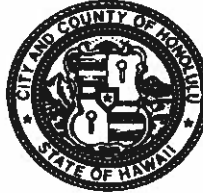


HB1035,HD1

Testimony

DEPARTMENT OF BUDGET & FISCAL SERVICES
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PETER B. CARLISLE
MAYOR



MICHAEL R. HANSEN
DIRECTOR

March 15, 2011

The Honorable Clayton Hee, Chair
and Members of the Committee on Judiciary and Labor
The Senate
State Capitol
Honolulu, Hawaii 96813

Dear Chair Hee and Members:

Subject: House Bill No. 1035, 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 views House Bill 1035, House Draft 1 as part of a package of bills proposing changes aimed at addressing the Retirement System's unfunded liability. The City only 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 increases in the Employer contribution provided in other bills will have a severe negative impact on our budget going forward. However, this is balanced by the provisions included in this bill, which will provide a moratorium on benefit enhancements, and others that update the benefits structure making it more realistic and sustainable. This comprehensive approach will, we hope, ultimately result in a system that is more stable and Employer costs that are more predictable.

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 testify on this measure.

Yours truly,

Handwritten signature of Michael R. Hansen in black ink.

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

Handwritten signature of Noel T. Ono in black ink.

Noel T. Ono, Director
Department of Human Resources

TESTIMONY BY WESLEY K. MACHIDA
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE SENATE COMMITTEE ON JUDICIARY AND LABOR
ON
HOUSE BILL NO. 1035, H.D. 1

MARCH 15, 2011

RELATING TO EMPLOYEES' RETIREMENT SYSTEM
BENEFIT ENHANCEMENT MORATORIUM

Chair Hee and Members of the Committee:

The Employees' Retirement System of the State of Hawaii's (ERS) Board of Trustees strongly supports H.B. 1035, H.D. 1 that places a moratorium on benefit enhancements until such time as the ERS has a funded ratio of 100% or more. As outlined below, the employers covered by the ERS already are facing significant increases in their contribution rates. Any benefit enhancements granted at this time would require even larger contribution rate increases.

The ERS unfunded accrued actuarial liability (UAAL) is at \$7.1 billion as of June 30, 2010. The UAAL is likely to increase beyond the \$7.1 billion because of deferred losses of \$1.5 billion that must be applied over the next 2 years, unless significant investment earnings are realized in FY 2011 to offset these losses.

State law requires the UAAL to be amortized (paid off) in 30 years. If the projected amortization period is greater than 30 years, employer contributions are subject to increase. Currently, the amortization period for the UAAL exceeds 40 years. Current employer contribution rates are 15% (9% for the UAAL) of payroll for general employees and 19.7% (13.7% for the UAAL) for Police Officers and Firefighters. If no other legislation is enacted, the employers contribution rates will have to be increased to 23% for Police and Fire employees and 17% for All Other employees in fiscal year 2012 to bring the amortization period back to 30 years.

Based on the \$7.1 billion, the ERS has a funded ratio of 61.4%, which means that the ERS is short by 38.6% of pre-funded monies currently available to take care of current and future pension

benefits. This places the ERS in the bottom 25% of public pension plans.

Furthermore, projections from the ERS Actuary report that the current \$1 billion in annual pension payments to 40,000 pensioners is estimated to increase to \$4 billion in the next 30 years. Moreover, the current \$550 million in annual employer contribution payments is estimated to increase to about \$2 billion in the next 30 years. Sales of ERS's investment assets will likely be needed to cover the shortfall between the benefit payouts and contributions received. Such sales erode the ERS's assets and further undermine its funded status. As a result, solutions are required to prevent the total depletion of ERS's investment assets in the future. One of the solutions that will help with the ERS funding is to prevent future benefit increases that will be detrimental to its funded status and jeopardize its financial viability in the future.

Based on the information provided, the ERS strongly supports the passage of H.B. 1035, H.D. 1. Thank you for the opportunity to testify on this important measure.