

TESTIMONY BY WESLEY K. MACHIDA
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON LABOR & PUBLIC EMPLOYMENT
ON
HOUSE BILL NO. 835

FEBRUARY 8, 2011

PROPOSING AN AMENDMENT TO ARTICLE VII, SECTION 6, OF THE HAWAII
CONSTITUTION, RELATING TO THE DISPOSITION OF EXCESS REVENUES

Chair Rhoads and Members of the Committee:

The Legislative Committee of the Employees' Retirement System of the State of Hawaii (ERS) supports H.B. 835 that proposes to deposit excess general fund revenues into a fund that will help to fund pension benefits.

As of June 30, 2010, the ERS had an unfunded actuarial accrued liability (UAAL) of \$7.1 billion. One of the main reasons for this large UAAL was attributed to a previous state law provision that allowed for excess ERS investment earnings to be credited against the annual employer contribution requirements. For example, if the State was required to contribute \$100 million to meet its annual required employer contribution payment, and the ERS realized excess investment earnings of \$50 million, then the State would contribute only \$50 million instead of \$100 million. When the ERS earned more than its assumed investment return assumption, the State reaped the benefits. The investment return assumption is a long-term assumption and when the investment markets cycled downward in the 2000's the excess investment earnings from the prior decades were not in the System to help cushion the blow.

Over a 36-year period from 1967 to 2003, the ERS credited over \$1.68 billion to the State and county employer contribution requirements (funds). Recently, the ERS Actuary determined that if those contributions had been made to the ERS, then combined with the investment earnings on those contributions, today the ERS's UAAL would be approximately \$500 million. This means that the ERS would have a funded ratio of more than 95% if that had occurred. If the System were in that position today, the recommended contribution rate to the System would likely be less than 10% of pay.

Therefore, it seems appropriate that excess general fund revenues be earmarked to help restore financial health to the ERS, since the ERS excess investment earnings helped the general fund in the past.

As a result, the ERS supports H.B. 835 that assists with the funding of the ERS.

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TESTIMONY BY KALBERT K. YOUNG
INTERIM DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON LABOR & PUBLIC EMPLOYMENT
ON
HOUSE BILL NO. 835

February 8, 2011

PROPOSING AN AMENDMENT TO ARTICLE VII, SECTION 6, OF THE HAWAII CONSTITUTION, RELATING TO THE DISPOSITION OF EXCESS REVENUES

House Bill No. 835 proposes a constitutional amendment to require the Legislature to deposit excess general fund revenues into one or more funds to reduce unfunded liabilities for pension benefits and other post-employment benefits for employees of the State in any fiscal year in which general fund revenues are projected to exceed the general fund revenues of the previous fiscal year by 7% or more.

The Department of Budget and Finance supports the intent of the bill to reduce the State's unfunded liabilities; however, we do not support a constitutional requirement to earmark "excess" general fund revenues for this purpose. It would be more appropriate to fund unfunded liabilities via the budget process, which would allow the Executive Branch and the Legislature to consider the required funding against the State's other priority budget requirements and available resources.

We have other concerns about this bill:

- It does not specify what "excess" general fund revenues are.
- It requires the Legislature to deposit "excess" revenues based on revenue projections, which can change during the course of a fiscal year, not the general fund balance at the close of the fiscal year.

- It does not take into consideration the general fund balance or revenue growth during prior fiscal years, or funding requirements for other priority programs.
- It earmarks all "excess" general funds for the State's unfunded liabilities while maintaining the requirement that the Legislature provide a tax refund or credit or make a deposit to the State's Rainy Day fund, when specified criteria are met, which will further erode the State's general fund balance.