LATE TESTIMONY

DEPARTMENT OF BUDGET & FISCAL SERVICES

CITY AND COUNTY OF HONOLULU

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PETER B. CARLISLE
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DIRECTOR

February 11, 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: Senate Bill Nos. 1262, 1264, 1265, 1216, and 1341
Relating to Employees' Retirement System

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 Senate Bills 1262, 1264, 1265, 1216, and 1341 as part of a package of bills proposing changes aimed at addressing the Retirement System's unfunded liability. The City does not support **these bills unless they are part of a package designed to address the unfunded liability issue in a comprehensive manner**— with reasonable changes to benefits and a moratorium on benefit enhancements, as well as increases in the Employer contribution rate.

The increases in the Employer contribution provided in Senate Bill 1264 will have a severe negative impact on our budget going forward. Senate Bill 1216 may also negatively affect our budget. However, this is balanced by the provisions included in SB 1262, SB 1265, and SB 1341 that place a moratorium on benefit enhancements and 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 these measures.

Yours truly,

Michael R. Hansen

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

Vera L. Ong

Noel T. Ono, Director
Department of Human Resources

HAWAII FIRE FIGHTERS ASSOCIATION
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LATE TESTIMONY

The Twenty-Sixth Legislature
The Senate
Committee on Judiciary and Labor
February 11, 2011

Testimony by
Hawaii Fire Fighters Association

S.B. No. 1265 RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM
S.B. No. 1341 RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

My name is Robert H. Lee and I am the President of the Hawaii Fire Fighters Association, Local 1463, IAFF, AFL-CIO. HFFA represents the 2,800 active and retired professional fire fighters throughout the State. As proposed, HFFA cannot support S.B. No. 1265 and S.B. No. 1341 as proposed although HFFA appreciates that this measure retains the current benefit calculation and structure for active employees.

While HFFA has many concerns about the bill, we strongly oppose the provision which adds the age requirement of 55 years old to the 25 years of service requirement to be eligible for unreduced benefits. In 1975, the Legislature removed the age requirement for fire fighters, police officers and corrections officers. House Standing Committee Report 702 (1975) recognized the "physical and mental stress caused by the hazards of the occupation(s)." Today, fire fighters face increased exposures to toxic biological materials, blood and air borne pathogens. A 2010 CareerCast.com study ranked fire fighting at the top of the list of most stressful professions citing "Firefighters frequently work irregular or unusual hours, or remain on call throughout the night. They risk heat exhaustion, smoke inhalation, and serious injury while on the job, and even the state of anticipation preceding a major threat can be highly stressful in itself. Firefighters are also sometimes required to spend long hours outdoors in bad weather." In addition, a 2007 Harvard study published in the New England Journal of Medicine found that coronary heart disease events such as heart attacks, is the leading cause of death of fire fighters on the job

In recognition of the working conditions, we would urge the committee to keep the current retirement eligibility the same for all fire fighters, active and prospective.

Thank you for the opportunity to comment on S.B. No. 1265 and S.B. No. 1341 and HFFA respectfully request full and forthright discussion to continue to allow for reasonable reform to the system. Thank you for the opportunity to provide comments on S.B. No. 1265 and S.B. No. 1341.

TESTIMONY BY WESLEY K. MACHIDA
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE SENATE COMMITTEE ON LABOR
ON
SENATE BILL NO. 1341

FEBRUARY 11, 2011

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Chair Hee and Members of the Committee:

S.B. 1341 provides for retirement benefit changes for State and County employees who become members of the Employees' Retirement System of the State of Hawaii (ERS) after June 30, 2012. The ERS Board of Trustees strongly supports this bill.

The ERS Board would accept a contribution only solution to the current ERS financing issues. However, because the increases in employer contributions necessary to amortize the ERS's unfunded actuarial accrued liability (UAAL) within a 30-year period may not be feasible at this time, the ERS Board of Trustees has been working with its Actuary to design a benefit structure for new employees that reduces the long-term costs of the ERS, and also provides a reasonable retirement package to State and county employees when combined with other retirement vehicles such as Social Security. This bill is the result of those efforts.

This measure seeks to reduce future liability by making changes for future State and County employees, which will provide for reasonable changes to employer contribution rates while State and county employers face challenging budgets. Changes are being proposed for all employee groups to reduce the benefit multiplier, post retirement increase, and Hybrid Plan account; increase the retirement age, vesting period, average final compensation (AFC) period, and employee contribution rate. The estimated dollar impact of these changes on the fiscal year 2013 contributions is as follows:

All Other Employees:

Area	Change	Estimated Dollar Impact to Contributions
Retirement Age	55 to 60; 62 to 65	$17 million
Benefit Multiplier	2% to 1.75%	$17.3 million
Post Retirement	2.5% to 1.5%	$12.8 million
Hybrid Plan Account Multiplier	150% to 120%	$4.4 million
Average Final Compensation Period	3 years to 5 years	$7.1 million
Vesting Period	5 years to 10 years	$4.8 million
Employee Contribution Rate	6% to 8%	$36.1 million

Police & Fire:

Area	Change	Estimated Dollar Impact to Contributions
Retirement Age	No age to 55; 55 to 60	$3.1 million
Benefit Multiplier	2.5% to 2.25%	$2.2 million
Post Retirement	2.5% to 1.5%	$2.3 million
Average Final Compensation Period	3 years to 5 years	$1.4 million
Vesting Period	5 years to 10 years	$.1 million
Employee Contribution Rate	12.2% to 14.2%	$3.6 million

All of these changes will result in cost savings, which will help to prevent further increases to the employer contribution requirements that would otherwise be necessary to amortize the ERS's UAAL within a 30-year period. The following cost savings (or reduced contribution savings) estimated by the ERS Actuary for the next 5 fiscal years are anticipated if all of the benefit changes for new hires are implemented:

FY 2012: $74.1 million
FY 2013: $112.7 million
FY 2014: $116.4 million
FY 2015: $120 million
FY 2016: $123.8 million

The passage of this bill, along with H.B. 1142 will result in employer contribution rates stabilizing over the next several years as follows:

All Other Employees (current rate at 15% of payroll; 6% for normal cost and 9% for unfunded liability):

FY 2012: 15%
FY 2013: 15.5%
FY 2014: 16%
FY 2015: 16.5%
FY 2016: 17%
FY 2017: 17%

Police and Fire (current rate at 19.7% of payroll; 6% for normal cost and 13.7% for unfunded liability):

FY 2012: 19.7%
FY 2013: 22%
FY 2014: 23%
FY 2015: 24%
FY 2016: 25%
FY 2017: 25%

If S.B. 1341 is not enacted, the employer contribution rates would require immediate increases in FY 2012 from 15% to 17% for all other employees and from 19.7% to 23% for Police & Fire to meet the 30-year amortization period for paying down the UAAL. These rates would be expected to increase to 19% for all other employees and 27% for Police and Fire over the next several fiscal years as the remaining investment losses from fiscal year 2009 are recognized.

As a result, the ERS Board of Trustees strongly supports the passage of S.B. 1341. Thank you for the opportunity to testify on this important measure.

LATE TESTIMONY

TESTIMONY OF COLBERT MATSUMOTO

Chairman of the Board of Trustees
Employees' Retirement System of the State of Hawaii

SENATE COMMITTEE ON JUDICIARY AND LABOR

Senator Clayton Hee, Chair
Senator Maile S.L. Shimabukuro, Vice Chair

February 11, 2011
9:15 a.m.
State Capitol, Conference Room 016

Senate Bill No. 1216
Senate Bill No. 1341

On behalf of the Board of Trustees of the Employees' Retirement System of the State of Hawaii ("ERS"), I offer this testimony in support of the above-referenced bills that are aimed at ameliorating the rapidly rising public employees pension contribution burden faced by the State and counties.

The unfunded liability of the ERS will continue to place a rapidly escalating financial burden on the State and the counties ("Public Employers") as the annual required contribution ("ARC") grows both as to the required rate of contribution as well as the dollar amounts. This would not be a concern if the Public Employers were readily able to satisfy the ARC. However, doing so will be increasingly daunting as the rising number of retirees and the pension benefits payable to them accelerates beyond the expected rate of growth of both Hawaii's economy and public revenue sources.

If the invested assets of the ERS stood at a much higher level rather than its presently low funded ratio, the burden on the Public Employers would not be as great since the ERS would be able to generate greater cash returns on its larger investment base. The fact that the assets of ERS have declined from 95% to a 61% funded ratio means that fewer dollars generated from investments are available to pay the current pension benefits owed to our rapidly increasing pool of public employee retirees.

To depict the problem simplistically, imagine if the ERS were fully funded with $18 billion, the targeted 8% rate of return would generate almost $1.5

billion in total return. That would likely be enough to meet the approximately $1 billion in cash benefits payable to current retirees. However, because the ERS only has $11 billion in assets, a targeted 8% rate of return would generate less than $900 million in total return. Since most of the total return is illiquid, not enough cash is generated to fund required pension payments. That is why the ARC from the Public Employers is critical to ensure that the ERS has sufficient cash to pay the pension benefit obligations without having to sell off more investments and further undermine its funded ratio.

Consequently, the Public Employers must today contribute 15% of payroll for general employees and 20% of payroll for police and fire employees rather than merely the 6% "normal cost" for currently accruing pension benefit liabilities. The dollar contributions have grown at an annual double-digit rate from $166 million in FY 2002 to $550 million in FY 2010.

Unless something in the current design of the public employees pension plan changes, the ERS will soon need to seek an increase in the rate of contributions from the Public Employers to 19.5% of payroll for general employees and 28.5% of payroll for police and fire employees to maintain the financial integrity of the plan design.

Recognizing that the annual payments required of the Public Employers are growing at a rate that could overwhelm their financial resources and consequently, the stability of the ERS, the Board of Trustees of the ERS have put forth proposals to modify the design features of the public employees pension plan as set forth in the above-referenced Senate Bills.

The proposed legislation will only affect new public employees by reducing the pension benefits they would accrue as compared to that of current public employees. No doubt these changes will not be popular. Moreover, the fiscal impact and the relief derived from these changes will be slight in the near term. However, without these modifications, the Public Employers can expect that the pension contribution burden they are struggling with today will worsen in years ahead.

On behalf of the Board of Trustees of the ERS, I urge you to support SB 1216 and SB 1341 with the recognition that the measures they contain are important steps in dealing with the grave financial challenges facing the State and the counties.