

WRITTEN ONLY

TESTIMONY BY KALBERT K. YOUNG
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON JUDICIARY
ON
HOUSE BILL NO. 835, H.D. 1

February 14, 2012

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

House Bill No. 835, H.D. 1, proposes a constitutional amendment to Article VII, Section 6, to authorize 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 State employees. The deposit of excess revenues would occur whenever general fund revenues in one fiscal year are projected to exceed general fund revenues in the previous fiscal year by 7% or more.

The department supports the intent of this bill to address the unfunded liabilities issue. It is a growing concern shared throughout the State that will undoubtedly require action. However, there is uncertainty about the impact of implementing the provisions of this bill.

For example, in FY 03, general fund revenues (tax and non-tax revenues) were 10.1% or \$347.9 million greater than FY 02 general fund revenues. Thus, the criteria for diverting excess revenues would have been met; however, if the excess revenues had been diverted to reduce unfunded liabilities, the fund balance at the end of FY 03 would have been reduced from \$117.2 million to -\$230.7 million.

This bill is planful in its approach to develop a means and measure that starts to address unfunded liabilities. We need to work together to understand the impact and implications on the financial plan - especially, in light of current and anticipated

financial conditions of the State. While the solution is not likely to be positive all-around, we recognize that the bill is strategic in implementing a financial structure to deal with these long standing problems.

We look forward to working with the Legislature on these important matters and would welcome the opportunity to further explore the potential for solutions.

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SUBJECT: CONSTITUTIONAL AMENDMENT, Deposit excess revenues to reduce unfunded liabilities for post-employment benefits of state employees

BILL NUMBER: HB 835, HD-1

INTRODUCED BY: House Committee on Labor and Public Employment

BRIEF SUMMARY: Amends Article VII, section 6, of the state constitution to provide that if general fund revenues in any one fiscal year are projected to exceed general fund revenues in the previous fiscal year by 7% or more, the legislature shall deposit such amount into one or more funds to reduce the unfunded liabilities for pension benefits and other post-employment benefits for state employees.

EFFECTIVE DATE: Voter approval

STAFF COMMENTS: The proposed measure provides that when general fund revenues are projected to exceed general fund revenues of the previous fiscal year by 7% or more, the excess revenues shall be used to reduce the unfunded liabilities for benefits and other post-employment benefits for state employees.

Originally, the "disposition of excess revenues" provision was enacted in tandem with the general fund spending limit. Although initially not a part of the spending limit discussion, the refund provision was proposed to insure that consideration be given to returning excess funds to taxpayers rather than to remain a target for excessive public expenditure. While this measure proposes that excess revenues be deposited into one or more funds to reduce the unfunded liabilities for pension benefits and other post-employment benefits for state employees, its enactment could have the same effect as "repealing" the "excess revenues" provision.

While the "repeal" of the mandatory refund provision may have political appeal because lawmakers have tacitly complied with a minimum \$1 refund per taxpayer, the refund provision serves a purpose. That purpose is making sure the general public is aware of their state finances. This provision insures people are reminded of just how much money the state is keeping for itself while maintaining the high burden of taxes. If the true spirit of the excess revenues provision is to be maintained, then another alternative should be considered and that would be to require that the legislature make a permanent downward adjustment in income or general excise tax rates as these are the two largest tax resources which benefit the general fund.

No doubt the unfunded liabilities of the state retirement and health systems should be of major concern; however, relegating the funding of these liabilities to excess general fund revenues is an abdication of the responsibility to fully fund these benefits. The message here is that lawmakers will continue to spend on state programs and services and ignore the fact that there is insufficient funding of these benefits and they will only put money in if there is something left over. Lawmakers knew there was a problem as early as the 1980's when the retirement system went from a contributory to non-contributory

basis and the benefit ratio was reduced. Recommendations to also reform the health benefits were made at the same time but ignored. Lawmakers refused to scale back the benefits perhaps in fear of offending the public employee. Despite the fact that in the private sector retirement plans went from defined benefit plans to defined contribution plans, lawmakers resisted making changes.

Adding to the problem was that in those years when the earnings of the benefit plans allowed the earning to be taken from the plans, the legislature took millions out of the system and used those funds to expand government programs and services. As a result, when the earnings waned, the corpus shrank along with its sustainable earning power.

Fully funding these liabilities should be a permanent fixture of the state's general fund budget and be paid before any money is spent on current services just as much as repayment of the state's debt obligations is first call on the state's resources. Absolving the legislature of making the tough choices between funding these liabilities and spending on new or expanded state services or even reforming these benefits is irresponsible and totally unacceptable to taxpayers.

Digested 2/13/12