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
SENATE BILL NO. 2750, S.D. 1

February 28, 2012

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Senate Bill No. 2750, S.D. 1, proposes to revise the allowability of certain employee compensation for the calculation of retirement pension if the overall compensation in the final years of service are determined to have been enhanced through means of "spiking." The bill provides definitions for determining that spiking has occurred and establishes the threshold limitations for calculating the effect on an employee's final compensation. In preventing spiking of pension benefits, this bill will also address some of the impact on the unfunded actuarial accrued liability of the Employees' Retirement System (ERS) by limiting the amount of compensation included in "average final compensation" and requires employers to pay the additional costs resulting from spiking.

The Department of Budget and Finance strongly supports this Administration bill which will allow the ERS to minimize the effect of spiking. The ERS has an unfunded actuarial accrued liability of $8.164 billion (as of June 30, 2011). The strategy of spiking is not the only contributing factor for the unfunded liability, but there is no doubt that individuals whose retirement pension is bolstered as a result of spiking, have contributed to the overall systems' unfunded liability. Spiking can, and does, occur within all governmental employers in the State and is an inequitable financial advantage to certain ERS beneficiaries that is to the detriment of all other beneficiaries of the ERS.

Senate Bill No. 2750, S.D. 1, limits the amount an employee's salary can contribute to determining their annual pension amount, but it also places certain responsibility and accountability on employers whose employees' compensation is spiked in the immediate years prior to retirement. Such spiking action is the most detrimental to the funding liability of the ERS. Employers and employees contribute to the ERS amounts equal to a percentage of compensation. However, when employees' compensations are spiked just prior to retirement, that employees' pension benefit is enhanced beyond a rate of what either the employer or employee have contributed to the ERS. This contributes to the unfunded liability and is inequitable to the detriment of other beneficiaries because it compromises the overall viability of the ERS. The Administration believes that stability in the level of benefits received is an important factor in facilitating the ERS' ability to eventually eliminate its unfunded liability and ensure the long-term viability of the system.

The Department of Budget and Finance encourages the Senate Committee on Ways and Means to support Senate Bill No. 2750, S.D. 1.

HAWAII STATE TEACHERS ASSOCIATION
Teaching Today for Hawaii's Tomorrow

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SENATE COMMITTEE ON
WAYS AND MEANS

RE: SB 2750, SD 1 -- RELATING TO THE EMPLOYEES RETIREMENT SYSTEM.

February 28, 2012

WIL OKABE, PRESIDENT
HAWAII STATE TEACHERS ASSOCIATION

Chair Ige and Members of the Committee:

The Hawaii State Teachers Association offers comments on SB 2750, SD 1, which proposes to amend what is allowable compensation for calculating retirement pensions. This bill is particularly addressing the issue of "spiking" in the final years of service which enhances the overall compensation for the calculation of retirement pension. In preventing spiking of pension benefits, this bill will also address some of the impact on the unfunded actuarial accrued liability of the Employees' Retirement System (ERS) by limiting the amount of compensation included in "average final compensation" and requires employers to pay the additional costs resulting from spiking.

We understand the need to address the unfunded liability being carried by the Employees Retirement System and acknowledge the GASB's recent report on future liabilities and the impact on the State as a whole.

We are not in agreement that the actual unfunded liability is directly related to the issue of "spiking". There have been many decisions made by this body that have created a "pay as you go" system.

We do believe if an Employer authorizes overtime work, it is the Employer who should be liable for those costs. It is the Employers' right to decide how they assign work to their employees and we don't support measures by the Legislature to statutorily intervene. Language is contained in negotiated contracts and those agreements should be honored.

Now that there is a new awareness of this liability we should allow those most affected by the liabilities to address cost containment planning for the future and have confidence they will do this without having to pass new laws.

Thank you for the opportunity to give comments.

NEIL ABERCROMBIE
GOVERNOR

DWIGHT TAKAMINE
DIRECTOR

AUDREY HIDANO
DEPUTY DIRECTOR

STATE OF HAWAII
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February 24, 2012

The Honorable David Ige, Chair
Committee on Ways and Means
The State Senate
State Capitol, Room 215
Honolulu, Hawaii 96813

Dear Chair Ige:

Subject: S.B. 2750, S.D. 1 Relating to the Employees' Retirement System

I am Kenneth G. Silva, Fire Chief of the Honolulu Fire Department (HFD). The City and County of Honolulu (City) received additional information from the Employees' Retirement System and is in the process of evaluating the impact of this bill on the county and its employees.

We offer the following comments regarding control of the HFD's overtime:

The HFD's overtime is operationally driven due to emergency services provided on a 24 hours per day, 7 days per week basis. The HFD budgets holiday and nonholiday overtime costs, which involves work on state holidays. Employees on a 56-hour workweek schedule are allotted three hours of overtime per week and together with holiday overtime, this amounts to an approximate ten percent increase of the employee's base salary. These costs are determined through collective bargaining agreements. Nonholiday overtime is controlled and approved by the Department's executive staff to prevent abuse.

Other overtime is determined according to the nature of the work performed, i.e., Fire Investigators and Public Information Officers rotate being on standby, and such overtime is earned when callouts occur. The HFD consistently operates within its budget on holiday and nonholiday overtime costs.

While we respect the legislature's attempt to minimize the impact of spiking by government employees, the HFD believes that what may be an acceptable limit of overtime in one assignment may not be applicable to another duty assignment. Under these circumstances, employees with normally high overtime should not be classified or penalized for what may appear as spiking.

The HFD urges your committee's consideration of our comments and suggests a cautious approach to the passage of any version of S.B. 2750, S.D. 1.

Should you have any questions, please contact Battalion Chief Socrates Bratakos of our Fire Prevention Bureau at 723-7151 or sbratakos@honolulu.gov.

Sincerely,

KENNETH G. SILVA
Fire Chief

KGS/LR:cn

POLICE DEPARTMENT
CITY AND COUNTY OF HONOLULU
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PETER B. CARLISLE
MAYOR

LOUIS M. KEALOHA
CHIEF

DAVE M. KAJIHIRO
MARIE A. McCAULEY
DEPUTY CHIEFS

OUR REFERENCE JC-VYH

February 28, 2012

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

Dear Chair Ige and Members:

Subject: Senate Bill No. 2750, SD1, Relating to the Employees' Retirement System

I am Mark M. Nakagawa, Assistant Chief of the Administrative Bureau of the Honolulu Police Department (HPD), City and County of Honolulu.

The HPD opposes Senate Bill No. 2750, SD1. We believe this bill will have a disproportionate impact on police officers due to the requirements of their job and their assignments, some of which routinely require the expenditure of overtime to complete any given tasks on hand or assigned.

A meeting was held with the Employees' Retirement System (ERS) to better understand the proposals of, and the calculations used as the basis in this bill. Based on the information provided, our concerns about police officers being targeted by this bill have been confirmed.

We recognize the problem created by "spiking." However, "spiking" is not unique to the use of overtime; it can also occur through base pay, for instance, an employee may be placed in a job which involves a drastic increase in base pay during the employee's last three years of employment. This type of increase will have the same impact as "spiking," but is not addressed in the bill.

Using fairness as a determining factor, the HPD recommends that the ERS formula be applied to all creditable compensation earned by any state and/or city employee whose retirement compensation is determined by comparing their highest three or five years of income. In this way, the burden of the unfunded liability is shared equally by all so that one group is not responsible for carrying more than their share of the liability.

The HPD diligently works to manage the use of overtime and requires its officers to seek approval before accruing overtime. The nature of police work often requires the expenditure of overtime to meet departmental objectives. Officers are mandated by operational needs or safety concerns to work and placed into situations herein defined as "spiking." For these reasons, the HPD opposes this bill.

As a result, we are requesting the Ways and Means Committee to hold this bill.

Thank you for the opportunity to testify.

APPROVED:

LOUIS M. KEALOHA
Chief of Police

Sincerely,

MARK M. NAKAGAWA, Assistant Chief
Administrative Bureau

DEPARTMENT OF BUDGET & FISCAL SERVICES

CITY AND COUNTY OF HONOLULU

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PETER B. CARLISLE
MAYOR

MICHAEL R. HANSEN
DIRECTOR

February 28, 2012

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

Dear Chair and Members:

Subject: Senate Bill 2750, Senate Draft 1
Relating to the Employee's Retirement System

The City and County of Honolulu supports the intent of Senate Bill 2750, Senate Draft 1 to address the effects of spiking on the unfunded liability of the Employees' Retirement System; however, we continue to have questions on the method being used to determine "spiking" and the resultant impact to the employee and the employer. Accordingly, we suggest a cautious approach to the bill.

We recognize that some extreme situations involving City employees have come to light recently that may have played a part in creating an urgency to address spiking. We want to assure you that to the extent we are able, within the bounds of the collective bargaining agreements we are subject to and without affecting public safety, we are taking steps to address the situation. That being said, this is a complex issue.

- The proposed solution is also complex and we have only recently had a chance to meet with ERS representatives, but not their actuary, to discuss our questions. We were able to gain some insight on this measure as a result of the meeting and are in the process of evaluating the impacts. We believe that a thorough review and understanding is essential to ensuring the fair and equitable resolution (from both the employer and employees' perspective) that we understand the Board is seeking.

The City is committed to efforts to address the ERS unfunded liability. Last year we fully supported the measure that will increase substantially our employer contributions to the ERS. We have also supported measures to add a county representative to the ERS Board so that we may have input on, and a comprehensive understanding of, measures such as these. At this point, we do not have the understanding necessary to support all the provisions in this measure.

Thank you for the opportunity to comment on Senate Bill 2750.

Yours truly,

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

Noel T. Ono, Director
Department of Human Resources

WRITTEN ONLY

TESTIMONY BY WESLEY K. MACHIDA
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE SENATE COMMITTEE ON WAYS AND MEANS
ON
SENATE BILL NO. 2750, S.D. 1

FEBRUARY 28, 2012

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Chair Ige and Members of the Committee,

The provisions of S.B. 2750, S.D. 1 address "pension spiking" and represent one way in which public pension funds across the nation have been dealing with their growing pension and unfunded liabilities.

The ERS Board of Trustees strongly supports this bill as it will help to strengthen the integrity and sustainability of the ERS through proper funding, assist in addressing the growing pension liabilities, and eliminate benefit inequities.

The 2011 Legislature took an important step in addressing the growing pension liabilities when it passed the benefit changes for new hires starting after June 30, 2012. Although the changes enacted are significant, they affect the long-term future liabilities of the ERS. The solutions proposed in this bill will address pension liabilities (reported at $21 billion as of June 30, 2011), its effect on the total ERS Unfunded Liability (reported at $8.164 billion as of June 30, 2011) and help to ensure ERS' future sustainability.

The ERS Actuary has determined that the estimated present value of potential savings for the current group of employees who meet the bill's definition of pension spiking is $38.6 million for Police and Fire employees, and $77.6 million for the "25 years and out" and all other employees. In addition, the ERS Actuary has estimated that the impact on future reductions to the pension liabilities for new hires is about 5% for Police and Fire employees, 15% for the "25 years and out" employees, and 2% for general employees. In other words, if pension liabilities were to grow by $5 billion over the next 10 years for these new

employees, then approximately $150 to $200 million would be reduced from the growing pension liabilities.
The continued volatility and uncertainty of the investment markets, increasing longevity of ERS members, payroll declines (employer contributions are based on total payroll), and others have a significant impact on the increasing unfunded liability. In FY2011, employee and employer contributions were $715 million and almost $1 billion in benefit payouts were made. This means that approximately $300 million was liquidated from the investment portfolio to pay benefits. So far in FY2012, contributions of $425 million were received and $600 million in benefit payouts were made with $175 million being liquidated to cover the payouts. If these trends continue without significant increases to the investment portfolio, more solutions will be needed to prevent the investment corpus from being depleted.

As a solution, some states have converted from a defined benefit structure to a defined contribution structure. To do so would be detrimental to the ERS members and costly to employers and taxpayers over the next 15 years given the ERS' large unfunded liability. Rather than changing the structure, the restrictions to pension spiking being proposed in this bill is another appropriate step toward ERS' sustainability.

This bill addresses the unexpected increases in benefits of members of the Employees' Retirement System (ERS) and in the unfunded liability of the System by limiting the amount of compensation included in the "average final compensation" of new and current members (delayed by 3 years) and by requiring employers of current members to pay the costs attributable to additional benefits resulting from "pension spiking."

"Pension spiking" is the process whereby public sector employees significantly increase their compensation (through overtime, etc.) in the years immediately preceding retirement in order to receive a larger pension that they otherwise would be entitled to receive.

Public employers and ERS members provide contributions that fund a member's retirement benefits over the member's anticipated employment period, so that there will be sufficient money to pay the member's retirement benefit. For the career government employee, this could entail a span of between 25 or 30 years of service. If an employee's pay suddenly increases substantially in the final years of employment, the employee's retirement benefits (which are based on the employee's three or five highest paid years) can be increased dramatically without the years of contributions required to fund the increase. This, in turn, increases the unfunded actuarial accrued liability of the ERS.

The impact of pension spiking is illustrated by the following example. Assume that a member's average final compensation for the first 25-27 years of employment totaled $50,000. Without spiking and with "normal" salary increases, the last three years of pay would compute to an average final compensation of $56,243 and an annual maximum allowance of $33,746. However, if this member's average salary during the last three years increased to $200,000 due to overtime or other non-base pay, the member's pension would be spiked to an annual maximum allowance of $120,000. The additional contributions on the spiked pay received by the ERS would cover less than 2 years of the additional $86,254 in benefits that would need to be paid.

As indicated below, the ERS' unfunded liability based on this one example is increased by $1,134,720.

Description	Service Years	Average Final Compensation (Highest 3 years)	Annual Pension (Maximum Allowance)	**Actuarial Accrued Liability (unfunded liability) at Retirement**
Without Spiking	25 -27; 28 -30	$50,000; $56,243	$33,746	**$443,946**
With Spiking	25 - 27; 28 - 30	$50,000; $200,000	$120,000	**$1,578,666**
Difference		**$143,757**	**$86,254**	**$(1,134,720)**

If this sample case was multiplied several times as noted, for instance, in the December 2011 report by the City Auditor regarding excessive overtime pay of 10 EMS employees, the estimated impact/increase of the ERS' Unfunded Liability would be approximately $4 million (determined by the ERS Actuary - with certain assumptions).

As the ERS is a cost sharing, multi-employer plan, if the employers of ERS members with "spiked" benefits do not pay the additional cost resulting from spiking, the costs would be borne by all employers as part of the increase in the unfunded accrued liability of the Employees' Retirement System.

The ERS Board of Trustees reviewed several recommended options to remedy pension spiking and looked at the impact of overtime and other non-base pay on the unfunded liability. Furthermore, the Board discovered that there were at least 10 systems that excluded or restricted overtime in their pension calculations and there were 15 states that have anti-spiking provisions in their laws (as reported by the National Association of State Retirement Administrators). After reviewing the recommendations from the ERS Actuary and the pension spiking laws enacted by other states, the ERS Board took a moderate and balanced approach in its recommendation of the pension spiking criteria included in this bill. This criteria is summarized as follows:

- **For employees who become ERS members after June 30, 2012:** Limit the amount of compensation that can be included in the calculation of the member’s retirement benefits if the member’s non-base pay (such as overtime or bonuses) during the member’s “high-five” years exceeds limits based on the average of the member’s non-base pay during the last 10 years of the member’s service.

- **For existing members**: Limit the amount of compensation that can be included in the calculation of the member’s retirement benefits if the member’s non-base pay during the member’s “high-three” or “high-five” years exceeds limits as noted above; however, this calculation would only be applied to periods after June 30, 2015.

- **For existing members**: Require the member’s last employer to pay the additional costs resulting from sudden increases in the member’s non-base pay during the member’s final years of employment.

The ERS Board of Trustees believes that this proposed legislation is needed to help with the ERS’ pension and unfunded liabilities and to mitigate inequities. The overall goal is to ensure the sustainability of the ERS and the sufficiency of monies to pay promised benefits. Therefore, the ERS Board strongly supports the passage of this bill.

Thank you for the opportunity to testify on this important measure.

From:	mailinglist@capitol.hawaii.gov
To:	WAM Testimony
Cc:	jnmmori@hawaiiantel.net
Subject:	Testimony for SB2750 on 2/28/2012 9:00:00 AM
Date:	Friday, February 24, 2012 6:48:10 PM

Testimony for WAM 2/28/2012 9:00:00 AM SB2750

Conference room: 211
Testifier position: Comments Only
Testifier will be present: No
Submitted by: Martin Mori
Organization: Individual
E-mail: jnmmori@hawaiiantel.net
Submitted on: 2/24/2012

Comments:
Dear Chair Ige, Vice-Chair Kidani and members of the Committee:
Although I am an employee of the Employees' Retirement System (ERS), I am providing comments today as a concerned private citizen.
I have been with the ERS since 2004 and in that short time I have seen firsthand our actuarial funded ratio decrease from nearly 72% to 59% today. I have also witnessed the introduction of the Hybrid plan in 2006 (with its apparent unattainable set of assumptions) and the subsequent ability for those who elected to transfer to the plan to upgrade their previous Noncontributory service (which no doubt further eroded our actuarial funded ratio). Additionally, I have seen the dramatic increases in the percentage of the employer contribution share in an attempt to stem the growth of our unfunded liability.
The ERS Board of Trustees (BOT) finally took action to stop the bleeding with the passage of Act 163 last year. Unfortunately, we now have a two tier retirement system that basically places the continued success of the system on the backs of future employees and has further eroded Government's ability to attract the best and brightest. Act 163 will also not have any major impact on the unfunded liability for years to come.
It is time for real change, change that the ERS BOT has been unable or unwilling to take steps to achieve.
Although SB2750 will have a somewhat positive impact on the unfunded liability it does not go nearly far enough. What we need immediately is for an ERS member's compensation to be based solely on base pay. The system already provides a more than generous retirement benefit on base pay alone. This would be a win-win scenario since the ERS member would receive more in the form of take home pay (as there would be no employee contributions required on non-base pay), which they can invest through the deferred compensation program or by funding their own IRA. The employer contribution share will drop dramatically (contributions on base pay only). And it will have a major impact on reducing the ERS unfunded liability.
I ask that you give serious thought as to how we can make a real change to ensure the future financial stability of the ERS and not turn it into a huge burden to the taxpayers of the State of Hawaii. I respectfully request that the Committee look at amending this bill to limit compensation to base pay only or look at reviving SB1269 from last year's legislative session.
Thank you for your time and consideration.
Sincerely,
Martin Mori

From:	mailinglist@capitol.hawaii.gov
To:	WAM Testimony
Cc:	puunui@msn.com
Subject:	Testimony for SB2750 on 2/28/2012 9:00:00 AM
Date:	Sunday, February 26, 2012 10:38:16 AM
Attachments:	My name is Edward Fujioka and I am opposed to SB.docx

Testimony for WAM 2/28/2012 9:00:00 AM SB2750

Conference room: 211
Testifier position: Oppose
Testifier will be present: No
Submitted by: Edward Fujioka
Organization: Individual
E-mail: puunui@msn.com
Submitted on: 2/26/2012

Comments:
Under page seven, of SB 2750 (d) 1 and 2 why are members of the legislature allowed a multiplier of 4 and or 6 times their salary?

My name is Edward Fujioka and I am opposed to SB-2750. I am a City employee of 31yrs full time one year of part time and three years of summer work. I have been employed more than 34 years. I have read the bill and I now have more questions than answers. What is the definition of “spiking”? I know of co- workers that has sacrificed more than 15yrs of spiking. That is to say they have “worked” and earned his overtime wages. They have worked Holidays, weekends, days off, double shifts, shifts after training sessions, midnight, days and evening shifts when no one else was able or willing to work. Some of these shifts are “stuck shifts”. The stuck shifts are shifts were the employees have “no relief”, more commonly known as mandatory overtime.

We are professionals working is a job that is mentally and physically tasking. Our years of public service are limited. We are in a profession that required special training and biannual recertification. We would be physically challenged to perform of job at age 55 and beyond. This profession is one that we need to be 21yrs old to be hired. It then takes more than two years to reach Full time employable position. At age 23 or 24 we then placed in evaluation position before reaching “permanent full time status. Many of our new employees are college graduates. At age 23 or 24 then begin the training phase and become permanent full time workers at age 25-27. Since many retire at age 55 or sooner that leaves only 28-30yrs of employment. You can do the math.

Personally, I love my job. I hope to continue to service this great City and its visitors for another six years. If this bill passes I will have to seriously consider retirement in three years. There is so much work to do. In the present state of our profession we are just keeping our heads above water. If I am my fellow co-workers leave (all with decades of service) it would leave mid and upper management postion vacant. These are public safety positions. Police officers, Paramedics, Fire Fighters, Ocean Safety, Correction Officers, State Sheriff’s, DLNR, State and County Civil Defense, Sewer, Road Workers are several of these positions. Can you imagine what would happen if we had another 911? What if it happen here. In Wakiki or Down Town Honolulu or here at the State Capital building?

This raised another question, if we are faced with another 911 or a tsunami in Japan in 2011? Our public safety and service workers will be “forced” to work long days, nights, and shifts. Is limiting their retirement fair for the hazards we will face as first responders?

Government has placed us this situation my not funding positions and department budgets and now government is penalizing those that are forced or faced with working extended hours because there are vacant positions. I invite all of you to work a week with us in jobs like Police Officers, Paramedics who sometime miss meals due to high call volumes, work a week at Halawa correctional in both maximum and medium facilities! Then ask yourself can I do this job at age 50 and beyond?

Many of us do contribute to the retirement system every pay check. Another question. If we are capped at 20% over basepay, shouldn’t we cap our overtime payments be capped at 20%? How will this effect the retirement system? Presently all overtime is deducted and paid into the system. Doesn’t the overtime of the present workers help fund the system? If we our payments are not copped shouldn’t we get a tax deduction, since we are not compensated in the retirement formula now proposed? Thank you for your time.

Respectful submitted, Edward Fujioka