

**TESTIMONY BY KALBERT K. YOUNG
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON LABOR AND PUBLIC EMPLOYMENT
ON
HOUSE BILL 806**

February 8, 2013

RELATING TO EMPLOYEES' RETIREMENT SYSTEM PERSONNEL

House Bill No. 806 authorizes the Board of Trustees of the Employees' Retirement System (ERS), through its administrator, to appoint investment officers for the system and to change the title of the "Administrator" of the system to "Executive Director".

The Department of Budget and Finance strongly supports this Administration bill which is necessary to strengthen the ability of the ERS to continue to grow its corpus which currently has in excess of \$12 billion dollars in domestic and international investments. Successful investments of these funds are critical to the current and future funding of the ERS, which has an unfunded actuarial accrued liability of \$8.4 billion as of June 30, 2012. The ERS' investment staff consists of a Chief Investments Officer and an Investment Specialist which is inadequate given the uncertainty and complexity of the modern financial markets and the need for the ERS Board to be provided with ongoing tactical and strategic insights into the risk-return trade-offs of multiple asset class investments. The ability of the ERS Board, through its administrator to appoint exempt, qualified and experienced investment officers is necessary to ensure that the ERS' investment portfolio is best positioned to meet its asset goals and reduce the ERS' unfunded liability. Further in-house knowledge and expertise can also serve to save up

to \$1 million in annual research, analytics, transition, monitoring, and other functions that ordinarily would be paid to consultants. Finally, the proposed title change of the “Administrator” of the ERS to “Executive Director” is necessary to be consistent with the title of the administrative head of other governmental agencies and other public pension funds.

TESTIMONY BY WESLEY K. MACHIDA
ADMINISTRATOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII
TO THE HOUSE COMMITTEE ON LABOR AND PUBLIC EMPLOYMENT
ON
HOUSE BILL NO. 806

FEBRUARY 8, 2013

RELATING TO EMPLOYEES' RETIREMENT SYSTEM PERSONNEL

Chair Nakashima and Members of the Committee:

H.B. 806 proposes a new section to chapter 88, Hawaii Revised Statutes, to allow the Employees' Retirement System (ERS) administrator to appoint one or more investment officers to the ERS investment office. In addition, this bill proposes to change the title of ERS' "Administrator" to "Executive Director."

Successful investment of the funds of the Employees' Retirement System is one of the foundations to the longevity and stability of the system. The system currently has over twelve billion dollars in domestic and international investments and decisions made by the Board of Trustees of the system concerning these investments are critical to the current and future funding of the system, which has an unfunded actuarial accrued liability of 8.4 billion dollars as of June 30, 2012.

The role of assisting and advising the board with structuring the system's investment portfolio falls primarily with the system's investment staff which currently consists of a Chief Investment Officer and an investment specialist. The current staffing is not adequate given the uncertainty and complexity of modern financial markets. Furthermore, the current staffing structure is out of line with best practices of other similarly sized public pension plans. The investment portfolio has increased its allocations to equity products, covered calls, real return assets, and private equity. Dedication to these investments requires experience and expertise of seasoned professionals. The investment staff provides the Board with ongoing tactical and strategic insights into the risk-return trade-offs of multiple asset class investments. The ERS currently uses 2 investment consultants to assist with the monitoring of the program, including doing research and analysis on future strategies and products. They also assist with transitioning investment managers.

The individuals hired for these exempt investment officer positions must have the knowledge and experience to ensure a favorable outcome for the ERS. In order to maximize revenue and to secure a professional pool of applicants, the ERS anticipates that salaries for these exempt employees would be within an acceptable range of compensation earned by investment professionals in comparable public pension funds. With this expertise, however, the ERS anticipates savings ranging from tens of thousands to millions of dollars in any given year in both explicit and implicit costs related to research, analysis, transition, monitoring, and other fees and opportunities that would ordinarily be accrued to the consultants and other service providers at the expense of the ERS.

In order to meet its asset goals and reduce the system's unfunded liability, the expanded and complex investment program requires an expanded professional staff to ensure that the investment portfolio is well-researched, monitored and evaluated. This proposal, therefore, allows the Board, through its Executive Director, to appoint exempt, qualified and experienced investment officers to the Employees' Retirement System investment office.

This bill also changes the title of the "Administrator" of the Employees' Retirement System to "Executive Director", to be consistent with the title of the administrative head of other government agencies and other public pension funds.

The ERS Board of Trustees strongly supports this bill.

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