

TESTIMONY BY THOMAS WILLIAMS
EXECUTIVE DIRECTOR, EMPLOYEES' RETIREMENT SYSTEM
STATE OF HAWAII

TO THE SENATE COMMITTEE ON JUDICIARY AND LABOR
ON

SENATE BILL NO. 2346

FEBRUARY 5, 2016, 9:00 A.M.

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Chair Keith-Agaran, Vice Chair Shimabukuro and Members of the Committee,

S.B. 2346 would allow the Board of Trustees of the Employees' Retirement System of the State of Hawaii (ERS), through its executive director, to appoint one or more investment professionals, investment specialists and investment support staff, who may be exempt from chapters 76 and 89, Hawaii Revised Statutes. In addition, S.B. 2346 would authorize the ERS to make direct payments to the spouse or former spouse of an ERS member or retirant when the spouse or former spouse has been awarded all or a portion of the member's or retirant's retirement benefits pursuant to a qualified domestic relations order (QDRO).

The ERS Board of Trustees has not had the opportunity to review S.B. 2346 and therefore has not yet taken a formal position on this proposal; however, the ERS staff has the following comments and concerns:

- S.B. 2346 is comprised of two unrelated sections of Chapter 88, Hawaii Revised Statutes (HRS). Part I would amend section 88-29.5 regarding investment personnel and Part II would add a new section to Part IIC of Chapter 88 to authorize the ERS to make direct payments to alternate payees under a QDRO. The ERS would prefer two separate vehicles for this legislation already introduced as:
 - (1) S.B. 2288 Relating to Investment Personnel of the Employees' Retirement System, and
 - (2) S.B. 2847 Relating to Qualified Domestic Relations Orders
- Part I of S.B. 2346 would be beneficial to the ERS and its members.

Successful investment of the funds of the Employees' Retirement System is one of the primary pathways to the stability and sustainability of the system. A member's retirement benefit is funded through a combination of employer and employee contributions and investment earnings. Seventy to eighty percent of benefits provided are attributable to investment earnings. The system currently has over fourteen 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 eight billion seven hundred million dollars and a funded ratio of 62.2% as of June 30, 2014.

Although the members of the Board of Trustees, as fiduciaries, are responsible for the general management of the system's assets and implementation of the system's investment policy, they rely heavily on internal and external investment experts for advice. The role of assisting and advising the board in managing the system's assets falls primarily with the system's investment staff consisting of a Chief Investment Officer , two strategy specific officers (liquid and illiquid investments), a risk officer and two Investment Specialists who are civil service employees.

The current staffing structure is not expected to meet our long term needs. Staffing will need to be augmented given the complexity of portfolios our size and the dynamics of modern financial markets. The investment portfolio has increased its allocations to equity products, covered calls, real return assets, and private equity. In addition, the ERS is transitioning its portfolio to a risk-based asset allocation program, the implementation of which will require additional attention, monitoring, review and rebalancing. This rebalancing will be outsourced initially at considerable expense, and we would like eventually to bring the function in-house.

Dedication to these investments requires experience and expertise of seasoned professionals. Investment office staff provides the Board with ongoing tactical and strategic insights into the risk-return trade-offs of multiple asset class investments. Establishing our Investment Specialists as true members of the team will help with retention and provide a career path for these talented staff members. Any associated costs will be derived solely from ERS monies.

- In order to implement Part II of S.B. 2346, the ERS must have the adequate time, funding and resources for rule-making, member and public education, computer upgrades and testing, and the review of potential domestic relations orders. The ERS computer vendor estimated upwards of \$1 million for the modifications, changes, processing, reporting and coding required by this draft legislation. Public pension systems similar to the ERS have indicated that legal and actuarial review and a dedicated professional benefits staff person would be necessary for the accurate and efficient processing of QDROs.

Without the funding and resource provisions appropriated by sections 6 and 7 of S.B. 2346, the ERS will not be able to implement the requirements and additional payments stipulated by this proposal. The ERS board's support is subject to the provision of these additional resources.

Thank you for the opportunity to testify on these important measures.



HAWAII GOVERNMENT EMPLOYEES ASSOCIATION
AFSCME Local 152, AFL-CIO

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The Twenty-Eighth Legislature, State of Hawaii
The Senate
Committee on Judiciary and Labor

Testimony by
Hawaii Government Employees Association

February 5, 2016

**S.B. 2346 – RELATING TO THE
EMPLOYEES' RETIREMENT SYSTEM**

The Hawaii Government Employees Association, AFSCME Local 152, AFL-CIO strongly opposes Section 1 of S.B. 2346, which excludes positions from collective bargaining and expands the exemption from civil service within the Employees' Retirement System (ERS); however, we support the purpose and intent of Section 2 of S.B. 2346, which authorizes and requires the ERS to make direct payments to a spouse or a former spouse pursuant to a Qualified domestic relations order.

As drafted, Section 1 of this legislation allows the ERS to exempt from civil service and exclude from collective bargaining investment professionals and support staff, which creates a government workplace of "at will" employment with minimal employee rights. Further, Section 1 grants the ERS Board of Trustees the authority and sole discretion to exempt and exclude – a power that we respectfully argue should remain vested with the Legislature. Collectively, the expansion of excluding and exempting positions in state government is in direct conflict with the Article XVI, Section 1 of the Hawaii State Constitution and Chapters 76 and 89, HRS, which establish a merit-based civil service system free from coercive political influences and collective bargaining.

Separately, we support the provisions of Section 2 of S.B. 2346. A QDRO is a court ordered decree that recognizes an alternative payee's right to receive all or a portion of a benefits payable. Our members have raised concerns with the current process whereby an individual who is authorized by a QDRO to receive payments must rely on his or her former spouse to send the payment. In some cases, the former spouse does not send the full amount due, does not send payment in a timely manner, or does not send it at all, which causes unnecessary hardship to the individual. Passage of this legislation ensures that court orders are followed and that individuals receive regular, direct payment from the ERS instead of relying on a former spouse to send payment.

Thank you for the opportunity to testify in opposition of Section 1 and in support of Section 2 of S.B. 2346.

Respectfully submitted,

Randy Perreira
Executive Director

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March 23, 2015

To: Senate Committee on Judiciary And Labor
Senator Gilbert S.C. Keith-Agaran, Chair
Senator Maile S.L. Shimabukuro, Vice-Chair

From: Dyan K. Mitsuyama, Chair
Lynnae Lee, Vice Chair/Chair of the Legislative Committee
Family Law Section, Hawaii State Bar Association

Re: Testimony in Support of SB 2346
Hearing: Friday, February 5, 2016 at 9:00 a.m.

Good morning, Chair Keith-Agaran, Vice Chair Shimabukuro and the members of the Committee on Judiciary and Labor. The Family Law Section of the Hawaii State Bar Association supports this measure.

Last session, FLS supported the multiple measures authorizing the Employees Retirement System to essentially operate as any other private retirement plan insofar as providing direct payments to a spouse of a system member or retirant pursuant to a qualified domestic relations order.

The Family Law Section supports the intent of this measure as it is much needed to ensure that the division of an Employees' Retirement System member's retirement benefits are correctly divided and promptly paid with the appropriate tax consequences for both the member and the non-member former spouse by way of Court order.

Currently, only private employers are required to abide by the Employee Retirement Income Security Act (ERISA) which provides for non-member former spouses to receive retirement benefits awarded as a result of divorce property division directly from the retirement plan's administrator pursuant to a Qualified Domestic Relations Order (QDRO). The federal government as well though allows for direct payment to former spouses of retirement benefits as a result of divorce by and through a court order. The Hawaii state system, however, does not provide for direct payment.

This leads to much uncertainty and increased litigation for both the retired member and the non-member former spouse. Personally, through my practice, I have represented both members

and non-members in the enforcement of the division of the retirement system's benefits because there is no automatic method as in the case of those employed by the federal government or private sector. Currently, there is no system of record-keeping.

Falling in line with the practice for the division of retirement benefits earned in the private sector or federal government will not only be "fair" but it will also decrease litigation in this context. It will assure that the non-member is required to claim the funds received as income on her tax returns and assure that the member will not be held liable for the portion received by the non-member.

This is much needed.

NOTE: The comments and recommendations submitted reflect the position/viewpoint of the Family Law Section of the HSBA. The position/viewpoint has not been reviewed or approved by the HSBA Board of Directors, and is not being endorsed by the Hawaii State Bar Association.

TESTIMONY OF THOMAS D. FARRELL

Regarding Senate Bill 2346 Relating to the Employees' Retirement System

Senate Committee on Judiciary and Labor
Senator Gilbert S. C. Keith-Agaran, Chair

Friday, February 5, 2016 9:00 a.m.
Conference Room 016, State Capitol

Good morning Senator Keith-Agaran and Members of the Committee:

I support SB 2346.

All retirement plans, including ERS, are marital property and are divisible by the Family Court in a divorce action. This legislation does not change that. In most cases, when a non-member is awarded a share of a member's retirement plan, direct payment can be had from the plan administrator. In the private sector, this occurs by way of a "Qualified Domestic Relations Order" and there are similar devices in the case of military and federal Civil Service retirement pay. However, because of the inalienability provisions of Chapter 88, when ERS retirement plans are divided in a divorce, the plan member must make the payment to the former spouse and the plan administrator is not allowed to do so. This bill would reverse that and bring ERS into line with all other retirement plans.

This change would benefit the former spouse as well as the ERS member. In the case of the former spouse, the bill would ensure that he or she gets what the court ordered. In the case of the member, the bill would relieve him or her from a lifetime of writing monthly checks, and would also ensure that the ERS retiree is taxed only on that portion that he or she actually receives.

This bill is similar to SB 1324 which passed last session, but was vetoed by Governor Ige due to concerns over cost, and that the funding mechanism might jeopardize the tax exempt status of the system. This new version is the product of a year of study by ERS and incorporates pages and pages of technical language as well as detailed language for the pass-through of legal and actuarial costs, together with an appropriation. If this makes ERS happy, so be it. I do note, however, the drafter persists in wanting to call this animal a "Qualified Domestic Relations Order," notwithstanding that this is a term of art found in ERISA and nowhere else. I guess the term isn't copyrighted or trademarked, so you can name your cat "QDRO" if you want, but I would have chosen a different moniker. I note that HB2468 uses the term "Hawaii Domestic Relations Order."

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I understand that even after all of this, ERS will continue to oppose this needed legislation due to the cost of implementation. I have previously testified and continue to believe that ERS's estimates of the cost of implementation are far-fetched and have no basis in reality. In testimony last year before the Senate Ways and Means Committee, ERS claimed that it will take a million dollars to implement this, and in testimony a week later in front of the House Finance Committee, ERS upped its estimate to \$2 million---a figure they maintained last March during testimony before your committee. I suggest to you that these numbers are utter nonsense, and are not supported by any serious analysis.

There are about 5,000 divorces per year that are granted in Hawaii. About 1.4M people live in the State of Hawaii. This includes all the military folks that are assigned here. There are about 70,000 state and county employees. If the proportion of divorces involving state or county employees is the same as their proportion to the general population, then 5% of divorces will involve at least one ERS member spouse. That's a potential universe is 250 decrees per year to handle. However, most divorce decrees don't divide pension benefits; this tends to occur only in long marriages where there aren't sufficient assets to award the non-member to offset his/her interest in the member's pension. Perhaps 20% of these divorces would involve division of the ERS pension. That gets it down to about 50 cases per year. While there are potentially hundreds of divorce decrees out there that already divide ERS pensions, none of them will comply with the requirements that SB 2346 will impose without a trip back to Family Court for amendment. Most people aren't going to do that if the retirant is making direct payment in accordance with the existing decree or hasn't retired yet. The bottom line is that it shouldn't take \$2M to process 50 or so divorce decrees a year.

ERS has previously defended their inflated estimate by claiming that this number was given to them by the contractor who has designed their proprietary computer system. They say it takes \$2 million to rewrite the program to allow payment to a third-party non-member. That's nonsense because ERS is making deductions from members' retired pay and sending it to third-parties already. They withhold federal taxes, for example, and send them to the IRS. And they withhold child support when presented with a child support income withholding order, which can come from any one of literally hundreds of child support enforcement agencies throughout the country.

So don't let ERS scare you with big numbers that have no basis in fact. The real reason is that they just don't want to be bothered to do this. Everyone else does, however, and it's time for ERS to join the rest of the world.

From: mailinglist@capitol.hawaii.gov
Sent: Thursday, February 04, 2016 9:37 AM
To: JDCTestimony
Cc:
Subject: *Submitted testimony for SB2346 on Feb 5, 2016 09:00AM*

SB2346

Submitted on: 2/4/2016

Testimony for JDL on Feb 5, 2016 09:00AM in Conference Room 016

Submitted By	Organization	Testifier Position	Present at Hearing
J. Ashman	Individual	Support	No

Comments:

Please note that testimony submitted less than 24 hours prior to the hearing, improperly identified, or directed to the incorrect office, may not be posted online or distributed to the committee prior to the convening of the public hearing.

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