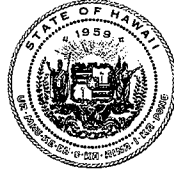


DAVID Y. IGE
GOVERNOR



THOMAS WILLIAMS
EXECUTIVE DIRECTOR

KANOE MARGOL
DEPUTY EXECUTIVE DIRECTOR

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

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

TO THE SENATE COMMITTEE ON WAYS AND MEANS
ON

HOUSE BILL NO. 1182, H.D. 1, S.D. 1

MARCH 28, 2017, 1:30 P.M.
Room 211

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Chair Tokuda, Vice Chair Dela Cruz and Members of the Committee,

H.B. 1182, S.D. 1 proposes that the actuary of the Employees' Retirement System (ERS) conduct an annual stress test of the System with regards to actuarial projections of the funded status for the ERS for each of the next thirty years based on "then-current" actuarial assumptions, including the assumed rate of return and projected lower rates of return. In addition, H.B. 1182, S.D. 1 would require that the actuary provide estimates of their actuarial projections with assumptions including extreme decreased investment returns and liabilities and costs based on the assumed discount rate and thirty-year treasury notes. The results of the stress test would be submitted as an annual report to the legislature twenty days prior to the convening of each regular session.

The ERS Board notes its concerns with H.B. 1182, S.D. 1 as the increased cost to the ERS to provide these additional reports will total approximately \$12,500 annually, while the information being requested is largely already made available for the Legislature's consideration and any additional information needed may be incorporated into our annual actuarial report. Please consider the following:

1. Most of the projections listed under §88-___(c)(1) regarding projections of assets, pension debt, net amortization and funded ratio over a thirty year time-frame are already



Employees' Retirement System
of the State of Hawaii

included in the annual Report to the Board of Trustees on the actuarial valuation of the ERS. This report is typically presented to the Board in January based on data review as of June 30 of the previous year and is made publically available immediately following adoption by the board to the legislature and all interested parties. Table 9c of the June 30, 2016 actuarial valuation provides the 30-year projections of assets, liabilities and funded ratio proposed in H.B. 1182, S.D. 1 from 2016 through 2045 (see Attachment 1). The proposed bill's second requirement is that we provide projections "assuming that investment returns are two percentage point lower than the assumed rate of return." Attachment 2, to this testimony, also extracted from the current valuation, is responsive to that request.

2. ERS management, staff and actuaries annually hold briefing sessions for the Senate and House at the beginning of the legislative session to review the valuation results, plan experience, projections and funding issues. During these sessions, the actuaries provide various "stress test" scenarios as noted in §88-___(c)(2) which illustrate varying investment returns and their effect on ERS funding policy recommendations. We can easily incorporate required additional illustrations into that briefing.
3. As to projections of a twenty-year period of investment returns 2% below the assumed rate under §88-___(3) or that we project liabilities and assets based on the "ten-year average of the yield of thirty-year treasury notes," the ERS actuaries would be able to model results on any of these scenarios and such other scenarios as are deemed relevant.
4. As a final note regarding the reporting of this information to legislature 20 days prior to each session, as the ERS actuaries do not typically publish valuation information prior to the Board's review and acceptance, any results produced in December or earlier would have to be based on data available from the previous fiscal year, which would differ from that reflected in the valuation presented in January.

Thank you for this opportunity to testify.

Employees' Retirement System of the State of Hawaii

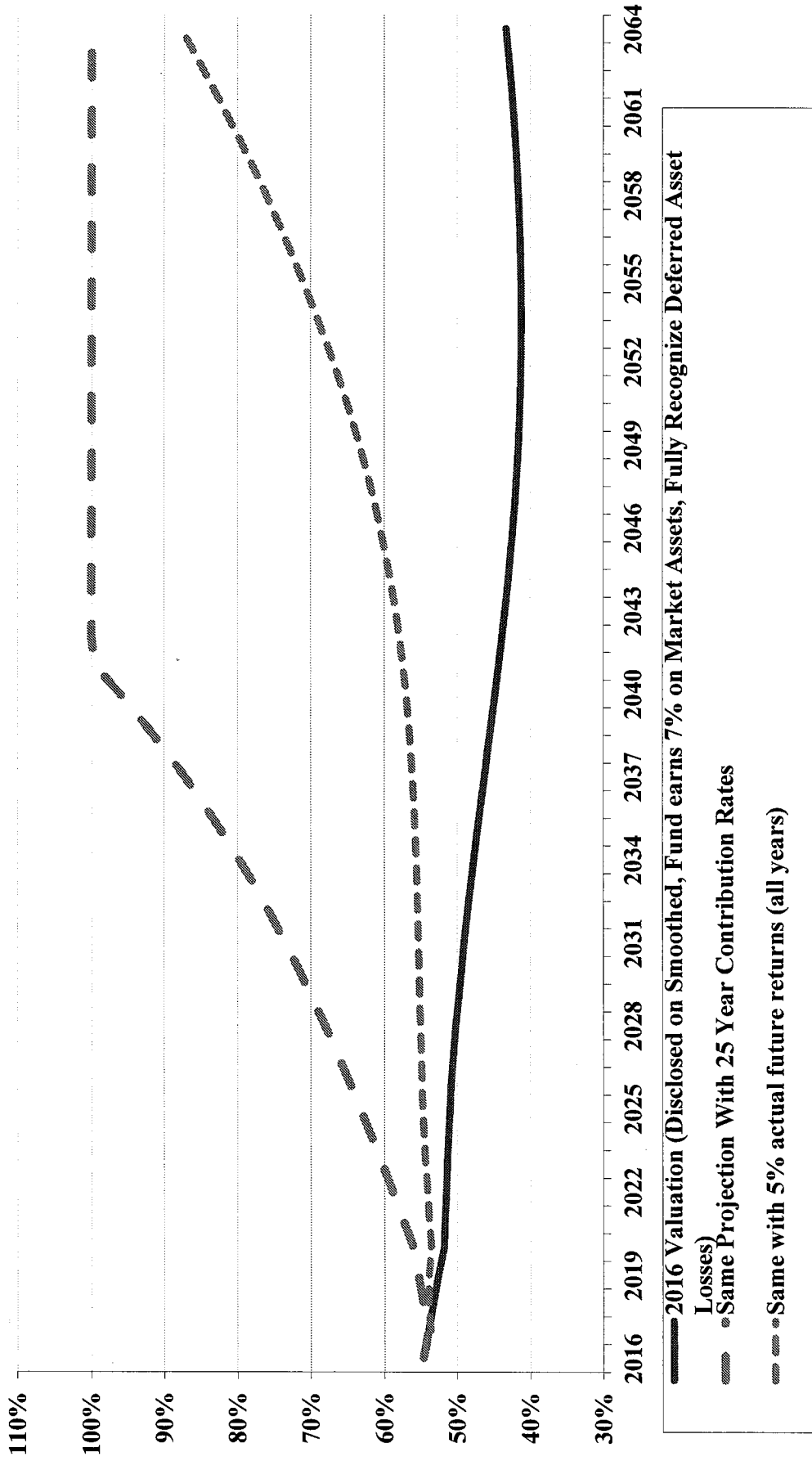
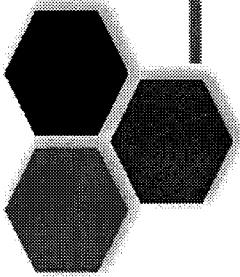
Table 9c

Projection Results Based on June 30, 2016 Actuarial Valuation

| Valuation as of June 30, (1) | Employer Contribution Rate for Fiscal Year Following Valuation Date (2) | Compensation (in Millions) (3) | Employer Contributions (in Millions) (4) | Actuarial Accrued Liability (AAL, in Millions) (5) | Actuarial Value of Assets (AVA, in Millions) (6) | Unfunded Actuarial Accrued Liability (UAAL, in Millions) (7) | Funded Ratio (8) |
|------------------------------|---|--------------------------------|--|--|--|--|------------------|
| 2016 | 17.91% | \$ 4,258.9 | 763 | \$ 27,439 | \$ 14,997 | \$ 12,443 | 54.7% |
| 2017 | 17.91% | 4,348.5 | 779 | 28,504 | 15,626 | 12,878 | 54.8% |
| 2018 | 17.91% | 4,449.4 | 797 | 29,643 | 16,318 | 13,325 | 55.0% |
| 2019 | 17.91% | 4,557.6 | 816 | 30,785 | 17,002 | 13,783 | 55.2% |
| 2020 | 17.90% | 4,672.8 | 837 | 31,929 | 17,676 | 14,252 | 55.4% |
| 2021 | 17.90% | 4,793.9 | 858 | 33,074 | 18,341 | 14,733 | 55.5% |
| 2022 | 17.90% | 4,920.0 | 881 | 34,220 | 18,995 | 15,224 | 55.5% |
| 2023 | 17.90% | 5,052.4 | 904 | 35,365 | 19,639 | 15,726 | 55.5% |
| 2024 | 17.89% | 5,190.1 | 929 | 36,510 | 20,271 | 16,239 | 55.5% |
| 2025 | 17.89% | 5,333.8 | 954 | 37,651 | 20,889 | 16,763 | 55.5% |
| 2026 | 17.88% | 5,484.6 | 981 | 38,788 | 21,492 | 17,296 | 55.4% |
| 2027 | 17.88% | 5,642.6 | 1,009 | 39,921 | 22,081 | 17,840 | 55.3% |
| 2028 | 17.87% | 5,807.9 | 1,038 | 41,051 | 22,658 | 18,393 | 55.2% |
| 2029 | 17.87% | 5,981.2 | 1,069 | 42,179 | 23,223 | 18,956 | 55.1% |
| 2030 | 17.87% | 6,162.1 | 1,101 | 43,307 | 23,779 | 19,528 | 54.9% |
| 2031 | 17.86% | 6,351.0 | 1,134 | 44,436 | 24,328 | 20,108 | 54.7% |
| 2032 | 17.86% | 6,547.3 | 1,169 | 45,565 | 24,869 | 20,696 | 54.6% |
| 2033 | 17.86% | 6,750.8 | 1,205 | 46,694 | 25,404 | 21,290 | 54.4% |
| 2034 | 17.85% | 6,963.1 | 1,243 | 47,827 | 25,935 | 21,891 | 54.2% |
| 2035 | 17.85% | 7,184.2 | 1,282 | 48,964 | 26,466 | 22,498 | 54.1% |
| 2036 | 17.85% | 7,414.0 | 1,323 | 50,108 | 26,999 | 23,109 | 53.9% |
| 2037 | 17.85% | 7,653.7 | 1,366 | 51,261 | 27,538 | 23,723 | 53.7% |
| 2038 | 17.85% | 7,904.3 | 1,411 | 52,429 | 28,088 | 24,340 | 53.6% |
| 2039 | 17.85% | 8,165.8 | 1,458 | 53,614 | 28,656 | 24,959 | 53.4% |
| 2040 | 17.85% | 8,438.4 | 1,506 | 54,823 | 29,246 | 25,577 | 53.3% |
| 2041 | 17.85% | 8,722.4 | 1,557 | 56,060 | 29,866 | 26,194 | 53.3% |
| 2042 | 17.86% | 9,017.3 | 1,610 | 57,331 | 30,523 | 26,808 | 53.2% |
| 2043 | 17.86% | 9,324.0 | 1,665 | 58,642 | 31,225 | 27,417 | 53.2% |
| 2044 | 17.86% | 9,643.1 | 1,722 | 59,998 | 31,977 | 28,021 | 53.3% |
| 2045 | 17.86% | 9,974.2 | 1,781 | 61,406 | 32,790 | 28,616 | 53.4% |

Projection assumes all assumptions exactly met, including a 7.00% annual return on the current actuarial value of assets.

Impact of Higher Contribution Rates and Perpetual Low Investment Returns



Assumes employer contribution rates of 42.5% for Police and Fire and 24.75% for All Other Employees beginning in FY2018 and for all years thereafter until 100% funded
 Assumes all assumptions met, including assumed rate of return each year on the current *market* value of assets



To The Committee on Ways and Means
Tuesday, March 28, 2017
1:30 pm, Room 211

RE: HB 1182, HD1, SD1, RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Attention: Chair Jill Tokuda, Vice Chair Donovan Dela Cruz and
Members of the Committee

The University of Hawaii Professional Assembly (UHPA) continues to request **support for the intent of HB 1182, HD1**, requiring the Employees' Retirement System (ERS) actuary to perform annual stress tests of the system and the ERS Board to submit annual reports of the tests to the legislature as we previously testified.

Due to market indicators nationally, the ERS Board had previously taken a responsible approach by slowly lowering the assumed rate of return 50 basis points over a five year period. However, the recent decision by the ERS Board to reduce the assumed rate of return 50 basis points all at once has caused a great deal of anxiety for beneficiaries and the public as a whole. That one action by the ERS Board immediately increased the unfunded liability by \$1.7 Billion, and has statutorily forced the legislature to review the required employer contributions. When actions by the ERS Board have statewide fiscal implications, additional oversight may be required to ensure the beneficiaries have confidence their interests are being addressed.

Requiring the ERS actuary to perform an annual stress test and report its findings to the legislature will provide a level of transparency that is currently not in place and ensure that the decisions of the ERS Board are not made in a vacuum since the decision to reduce the assumed rate has statewide implications.

UHPA supports the intent of HB 1182, HD1.

Respectfully submitted,

A handwritten signature in black ink that reads "Kristeen Hanselman".

Kristeen Hanselman
Executive Director

**University of Hawaii
Professional Assembly**