DAVID Y. IGE
GOVERNOR

THOMAS WILLIAMS
EXECUTIVE DIRECTOR

KANOE MARGOL
DEPUTY EXECUTIVE DIRECTOR

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

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

TO THE HOUSE COMMITTEE ON FINANCE
ON

HOUSE BILL NO. 1182, H.D. 1

FEBRUARY 22, 2017, 3:00 P.M.

RELATING TO THE EMPLOYEES' RETIREMENT SYSTEM

Chair Luke, Vice Chair Cullen and Members of the Committee,

H.B. 1182, H.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, H.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, H.D. 1 with the following comments:

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 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. The 91st annual valuation was presented and adopted by the board on January 9, 2017, for the year

ending June 30, 2016. It was posted to the ERS website (at ers.ehawaii.gov) immediately following board acceptance ad was discussed with key House members during a briefing session on January 10, 2017. Table 9c of the valuation provides the 30-year projections of assets, liabilities and funded ratio proposed in H.B. 1182, H.D. 1 from 2016 through 2045. That table is attached for your reference as 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, 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.

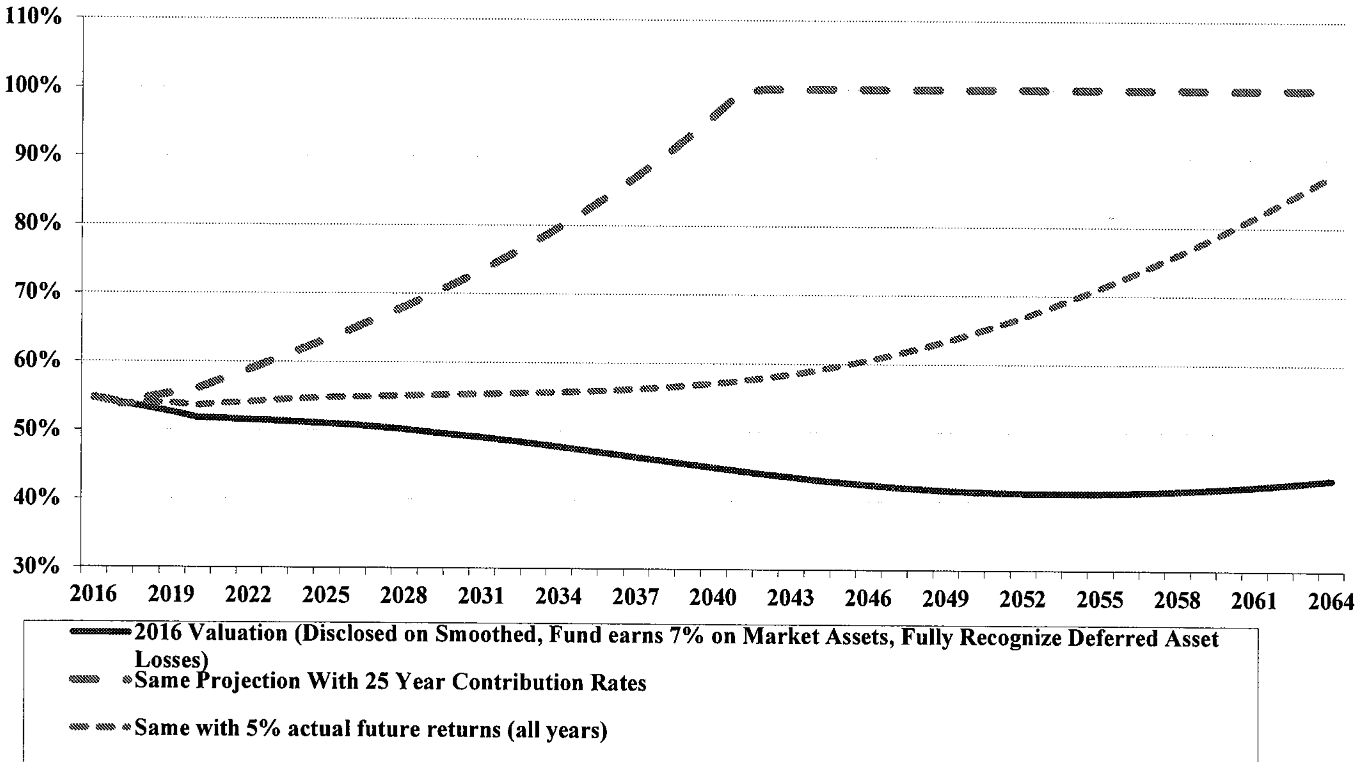
In summary, the ERS Board and staff believe that this information being requested is largely already made available for the Legislature's consideration and that any additional report needed may be incorporated into our annual actuarial report. On behalf of the Board of Trustees and staff of ERS we wish to thank you for the opportunity to testify.

Projection Results Based on June 30, 2016 Actuarial Valuation

Valuation as of June 30,	Employer Contribution Rate for Fiscal Year Following Valuation Date	Compensation (in Millions)	Employer Contributions (in Millions)	Actuarial Accrued Liability (AAL, in Millions)	Actuarial Value of Assets (AVA, in Millions)	Unfunded Actuarial Accrued Liability (UAAL, in Millions)	Funded Ratio
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(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 assumptoins 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

GRS

The House Committee on Finance
Wednesday, February 22, 2017
3:00 pm, Room 308

RE: HB 1182, HD1, Relating to Employees' Retirement System

Attention: Chair Sylvia Luke, Vice Chair Ty Cullen and
Members of the Committee

The University of Hawaii Professional Assembly (UHPA) **supports the intent of HB 1182, HD1,** requiring the Employeees' 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.

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,

Kristeen Hanselman
Executive Director

University of Hawaii
Professional Assembly

1017 Palm Drive ✦ Honolulu, Hawaii 96814-1928
Telephone: (808) 593-2157 ✦ Facsimile: (808) 593-2160
Website: www.uhpa.org

University of Hawaii
Professional Assembly

1017 Palm Drive ✦ Honolulu, Hawaii 96814-1928
Telephone: (808) 593-2157 ✦ Facsimile: (808) 593-2160
Website: www.uhpa.org

THE PEW CHARITABLE TRUSTS

2005 Market Street, Suite 2800
Philadelphia, PA 19103-7077
215.575.9050 Phone

901 E Street NW
Washington, DC 20004
202.552.2000 Phone

www.pewtrusts.org

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February 22, 2017

The Honorable Sylvia Luke, Chair
House of Representatives Committee on Finance
Hawaii State Capitol, Room 306
Honolulu, Hawaii 96813

Dear Chair Luke and Members of the Committee,

We are writing to express Pew's support for HB 1182, which would require the Employees' Retirement System (ERS) actuary to conduct annual stress tests of the system and direct the ERS board to submit annual reports of the tests to the legislature.

Regularly producing stress test analysis would inform policymakers on benefit costs and fiscal impacts using different economic conditions and investment return assumptions, help policymakers to plan for uncertainty, and underscore the importance of fully funding pension promises. The bill's specifications are informed by Pew's research on the fiscal health of public retirement systems, practices in place in other states, and related recommendations of the Society of Actuaries' Blue Ribbon Panel on Public Pension Funding.

Pew has conducted extensive research and analysis on pension system stress testing and we are available for discussion at any time. More information about Pew's research on public pensions may be found at the following website: www.pewtrusts.org/publicpensions. Please do not hesitate to contact me at kselenski@pewtrusts.org should you have any questions.

Thank you,

Katie Selenski
State Policy Director, States' Public Sector Retirement Systems
The Pew Charitable Trusts