



EXECUTIVE CHAMBERS

HONOLULU

LINDA LINGLE
GOVERNOR

January 5, 2004

The Honorable Calvin K. Y. Say, Speaker
and Members of the House of Representatives
Twenty-Second State Legislature
State Capitol, Room 431
Honolulu, Hawaii 96813

Dear Mr. Speaker and Members of the House:

For your information and consideration, I am transmitting herewith (2) copies of the Employees' Retirement System (ERS) study in accordance with House Concurrent Resolution No. 97, H.D. 1, which was adopted by the Twenty-Second Legislature of the State of Hawai'i, Regular Session of 2003. Pursuant to Act 231, Session Laws of Hawai'i 2001, I am also informing you that the report may be viewed electronically at www.state.hi.us/budget.

Sincerely,

/s/

LINDA LINGLE

Enclosures



EXECUTIVE CHAMBERS

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GOVERNOR

HONOLULU

January 5, 2004

The Honorable Robert Bunda, President
and Members of the Senate
Twenty-First State Legislature
State Capitol, Room 003
Honolulu, Hawaii 96813

Dear Mr. President and Members of the Senate:

For your information and consideration, I am transmitting herewith (2) copies of the Employees' Retirement System (ERS) study in accordance with House Concurrent Resolution No. 97, H.D. 1, which was adopted by the Twenty-Second Legislature of the State of Hawai'i, Regular Session of 2003. Pursuant to Act 231, Session Laws of Hawai'i 2001, I am also informing you that the report may be viewed electronically at www.state.hi.us/budget.

Sincerely,

/s/

LINDA LINGLE

Enclosures



GABRIEL, ROEDER, SMITH & COMPANY

Consultants & Actuaries

5605 N. MacArthur Blvd. • Suite 870 • Irving, Texas 75038-2631 • 469-524-0000 • fax 469-524-0003

December 31, 2003

Mr. David Shimabukuro
Administrator
State of Hawaii Employees' Retirement System
City Financial Tower
201 Merchant Street
Honolulu, HI 96813-2980

Dear David:

Subject: Report on Hybrid Contributory Plan as Requested by House Concurrent Resolution No. 97, H.D. 1

House Concurrent Resolution requested the Employees' Retirement System (ERS) to undertake a study to determine the feasibility of establishing a Hybrid Contributory Plan. In addition to providing the Hybrid Contributory Plan for new employees, the Resolution further requested that the study look at the feasibility of allowing class C Noncontributory members and class A Contributory members to convert to the Hybrid Contributory Plan. A copy of HCR No. 97, H.D. 1 is attached to this letter for your reference.

Requested Study

The Board of Trustees for the ERS requested that Gabriel, Roeder, Smith & Company (GRS) perform a study to determine the feasibility of allowing class C Noncontributory members as well as class A Contributory members to transfer to the Hybrid Contributory Plan. All new employees would become members of the Hybrid Contributory Plan with the following exceptions: Firefighters, Police Officers, Elected/Legislative Officers and Judges would remain in their current Contributory plans. The Hybrid Contributory Plan would be considered feasible if the total employer contributions requirements to ERS are not increased by implementing the Hybrid plan.

At its December Board meeting the Board decided on the final plan design for the new Hybrid Contributory Plan. In particular the Board decided to use a hypothetical account balance equal to 150% of the employee's contributions with interest rather than 200% as discussed in previous versions of the plan. Those changes have been reflected in this study. The ERS has prepared a summary comparing the proposed Hybrid Plan with the current Noncontributory and Contributory plans.

Summary

The following table shows the impact on selected cost items of ERS if only Noncontributory members are allowed to transfer and if both Noncontributory and Contributory members are allowed to transfer.

Valuation Cost Items	Current Plans	Noncontributory Members Transfer	Noncontributory and Contributory Members Transfer
Unfunded Actuarial Accrued Liability (\$millions)	\$2,872.7	\$3,268.9	\$3,244.2
Employer Contribution (\$millions)	\$444.4	\$436.3	\$433.7
Funded Ratio	75.9%	73.5%	73.7%

As can be seen in the table above, allowing just the Noncontributory members or allowing both the Noncontributory and Contributory members to transfer to the Hybrid Contributory Plan would not result in an increase in the employers' contribution requirement to the ERS and therefore both are feasible alternatives. It should be noted that while the unfunded liability of ERS would increase and the funded ratio of ERS would decrease by allowing the transfers of current members to the new program, the overall contribution requirement decreases because you have additional employee contributions to help pay for the additional liabilities.

The table above shows the impact on the current membership of ERS. It is also important to know what the impact of the new Hybrid Contributory Plan will be on the long term costs of ERS. Therefore, we have studied the impact of the new plan design on the average new employee. The net employer normal cost percentage for an average new employee under the current plans is 5.73%. Under the Hybrid Contributory Plan the net employer normal cost for an average new employee would be 5.26%. Therefore, the impact of adopting the Hybrid Contributory Plan produces a program that over the long term would require smaller contributions than the current program.

Other Comments

In determining the cost impact on ERS of allowing current members to transfer, we assumed that 100% of those Noncontributory members who are eligible for retirement or within five years of retirement and 60% of all other Noncontributory members would transfer. For the Contributory members we assumed that those employees currently eligible to retire under the Contributory plan but who would not be eligible to retire under the Hybrid Plan would elect not to transfer. We assumed 50% of those members under the age of 55 who have at least 25 years of service would transfer to the Hybrid Plan. For the remaining Contributory members we assumed 100% would transfer. It should not make a material difference to the actuarial

Mr. David Shimabukuro
December 31, 2003
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results if the number of transferring members is significantly different. In any event the overall costs of the new program would be less than the cost of the current program.

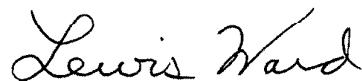
The cost numbers shown above assume that the transferring Noncontributory members would only receive the 2% multiplier for service earned after they transfer to the Hybrid Plan. If members are allowed to upgrade their prior Noncontributory service to the 2% multiplier, then we are assuming the members would be required to pay the full actuarial cost for upgrading that prior service.

After reviewing this report, please contact us if you have any additional questions or comments.

Sincerely,
Gabriel, Roeder, Smith & Company



W. Michael Carter, FSA
Senior Consultant



Lewis Ward
Consultant

kb

c: Rick Roeder, Gabriel, Roeder, Smith & Company

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HOUSE CONCURRENT RESOLUTION

REQUESTING THE EMPLOYEES' RETIREMENT SYSTEM TO CONDUCT A STUDY ON
THE FEASIBILITY OF A HYBRID RETIREMENT PLAN.

1 WHEREAS, during the 2001 Regular Session, the legislature
2 adopted Senate Concurrent Resolution (SCR) 159, directing the
3 Employees' Retirement System (ERS) to conduct a study of current
4 public sector pension benefits and make recommendations for
5 enhancement or change, and to study the feasibility of adding an
6 alternative defined contribution plan; and

7 WHEREAS, pursuant to SCR 159, the ERS conducted a
8 comprehensive study, the results of which were presented to the
9 2002 legislature; and

11 WHEREAS, the ERS study included a proposed "hybrid"
12 contributory plan; and

15 WHEREAS, the hybrid contributory plan could potentially apply
16 to new employees, class "C" non-contributory members and class "A"
17 contributory members; and

19 WHEREAS, the hybrid contributory plan could enhance public
20 sector pension benefits that could improve recruitment for and
21 retention of public sector employees; and

23 WHEREAS, there are various aspects of the hybrid plan that
24 must still be analyzed; now, therefore,

I do hereby certify that the within document
is a full, true and correct copy of the original
on file in this office.

John W. Glusker
Chief Clerk
House of Representatives
State of Hawaii

1 BE IT RESOLVED by the House of Representatives of the Twenty-
2 second Legislature of the State of Hawaii, Regular Session of
3 2003, the Senate concurring, that the ERS conduct a study on the
4 feasibility of establishing a hybrid contributory plan; and
5

6 BE IT FURTHER RESOLVED that the ERS determine, among other
7 pertinent issues, the feasibility of:

8

9 (1) Allowing class C non-contributory members to convert to
10 the hybrid contributory plan;

11

12 (2) Allowing class A contributory members to convert to the
13 hybrid contributory plan; and

14

15 (3) Allowing new employees to become members of the hybrid
16 contributory plan;

17 and

18

19 BE IT FURTHER RESOLVED that the ERS submit a report of its
20 findings and recommendations, including proposed legislation, to
21 the Legislature at least twenty days prior to the convening of the
22 Regular Session of 2004; and

23

24 BE IT FURTHER RESOLVED that certified copies of this
25 Concurrent Resolution be transmitted to the Administrator of the
26 Employees' Retirement System.

27