

Holomua



Employees' Retirement System
of the State of Hawaii
Working to fulfill your retirement dreams...



2013 Proposed Legislation

The 2013 Hawaii State Legislature opened on January 16, 2013 and will run through May 2, 2013. There were four Employees' Retirement System (ERS) related bills introduced by the administration to be heard and discussed during this session. Below are summaries of the proposals. For more information on these and other legislation, you may visit the State Capitol website at www.capitol.hawaii.gov.

H.B. 805: Relating to Federal Tax Qualification of the Employees' Retirement System

The ERS is a tax-exempt, qualified retirement plan under section 401(a) of the Internal Revenue Code (Code). Compliance with the requirements of the Code allows for favorable tax treatment of member contributions and does not require members to pay federal income taxes on the present value of their accrued vested benefits. In order for the System to retain its tax-qualified status, this bill proposes two amendments: (1) to reinforce the benefit limitations imposed by the Internal Revenue Code, and (2) to clarify vesting rules for the accrued retirement benefits for ERS members. Both amendments are technical clarifications to the existing ERS statutes and do not change requirements or benefits provided by the ERS.

H.B. 807: Relating to Retirement Benefits for Judges

This proposal corrects errors in the current ERS statutes to restore parity, with respect to age and service requirements for retirement, between current members who become judges after June 30, 2012 and other Contributory plan members who became members prior to July 1, 2012.

H.B. 808: Relating to the Employees' Retirement System and Civil Unions

In order to maintain its tax-qualified status (see proposal above), the ERS must comply with certain federal tax law requirements that specify when civil union partners are not considered "spouses" under federal law. This proposal amends three areas: (1) the right to a 100% joint survivor benefit when a civil union partner beneficiary is more than a specified number of years younger than the retirant, (2) the right to defer death benefits, and (3) preferential rollover rights for lump sum payments. Civil union partners would still have the rights accorded to spouses under the portions of the ERS statutes that are not restricted by the IRS Code. This bill also adds a new section to ERS Chapter 88 to confirm marital and spousal terms are inclusive of civil unions and civil union partners, unless to do so would jeopardize the tax-qualified status of the ERS.

S.B. 1036: Relating to Employees' Retirement System Personnel

As successful investment of the ERS fund is one of the foundations to the longevity and stability of the system, this proposal allows the ERS Board of Trustees, through its administrator, to appoint investment officers for the ERS investment office. The ERS currently has over \$12 billion in assets and an unfunded liability of \$8.4 billion. The investment office and new investment officers would assist and advise the ERS Board with critical information needed to structure the ERS investment portfolio to meet its asset goals and reduce the System's unfunded liability. In addition, this proposal changes the title of the ERS "Administrator" to "Executive Director" to be consistent with other government agencies and public pension funds.

Results of these proposals shall be covered in our June 2013 *Holomua*. Until then, you may follow these bills online at the State Capitol website noted above, by following our Administrator, Wes Machida, on Twitter at <http://twitter.com/ERSHawaii> or by accessing the ERS website at <http://ers.ehawaii.gov>.

ERS Board of Trustees:

Emmit A. Kane
Chair

Vincent E. Barfield
Vice Chair

Colbert M. Matsumoto
Jackie Ferguson-Miyamoto
Pilialoa E. Lee Loy
Jerry E. Rauckhorst
Wayne J. Yamasaki
Kalbert K. Young

Administrator
Wesley K. Machida

Assistant Administrator
Kanoë Margol

Chief Investment Officer
Vijoy (Paul) Chattergy

Inside this issue:

Emmit A. Kane
elected new ERS
Board of Trustees
Chair

Your 2012
Internal Revenue
Service (IRS) Form
1099-R Update

Report from
Vijoy Chattergy,
Chief Investment
Officer

News from the
EUTF

Wes' Corner



By now, we should be close to or past the 1st quarter of 2013. I hope the year is going well for you. As for the ERS, we had about 600 retirements in December 2012, which is usually our busiest month of the year for retirements. Recently on average, we have had about 500 retirements during December and about 400 retirements for June in any one year. While there are more than 14,000 members who are eligible to retire, we have yet to see a significant spike in retirements in the last couple of years. Many of those 14,000 come from the Department of Education, University of Hawaii, and Department of Health.

The markets have been favorable, as our investments increased to a value of about \$11.9 billion at the end of the first 6 months of our 2013 fiscal year. This equals a 7% investment return for the 6 months. We are hoping for continued positive outcomes as we close out the 2nd half of the fiscal year.

All active members should now have access to the self-service information that reports their years of service and account balance (for Contributory and Hybrid Plan members only). We hope to update this information at least semi-annually, if not more often.

We will continue to stay busy tracking legislation affecting the ERS. Many of the bills introduced that impact the ERS have been held or deferred and are no longer active for the 2013 legislative session. However, the good news is that the ERS initiated bills are still active (although it could change by the time you receive this newsletter). Our goal for this session was to be able to make the necessary tax compliance changes, so that we can maintain our tax-exempt status and continue to enjoy the favorable tax treatments afforded with this status. Another goal is to build our investment office, so that we can enhance investment revenues and control investment costs.

One of our future plans will be to look into the feasibility of having an office in the Kapolei area. We will keep you posted on this and our other efforts as the year progresses. Until then, stay healthy and happy.

Aloha,
Wes Machida

Your 2012 Internal Revenue Service (IRS) Form 1099-R Update

The ERS mailed out the 2012 IRS Form 1099-R at the end of January 2013. Approximately 300 Form 1099-Rs were returned to our office due to incorrect addresses or stamped by the Post Office "Return to Sender" or "Moved, No address." To submit an address change, the form is on our website under Resources>>AllForms>>General>>**ERS-211 Address Change**.

We have also received questions about the IRS Form 1099-R. For more 1099-R information, go to the same navigation path to 1099-R Form for a **sample Form 1099-R and Frequently Asked Questions** that can help you or your tax preparer.

Below are two most common questions from our retirees and beneficiaries regarding the Form 1099-R:

(1) What is Box 5 (Employee contributions / Designated Roth contributions or insurance premiums)?

Box 5 represents the amount of your benefits received for the year that is not subject to taxes. This amount is based on the "after-tax" contributions you made prior to your retirement and is the difference between Box 1 and Box 2a.

For example, Mr. Retiree selected the Maximum Allowance and received a gross distribution (pension payment) of \$36,000 annually (or \$3,000 per month). When he retired, Mr. Retiree had contributions that were already taxed and now could enjoy a "tax-free" recovery of his after-tax contributions. In this case, Mr. Retiree's nontaxable amount for the year is \$600 and is reported in Box 5 of the 1099-R. This calculation is based on the retiree's age, total after-tax contributions and the estimated number of monthly pension payments.

As a result, his taxable income for 2012 is \$35,400 (\$36,000 - \$600) which is reported in Box 2a – Taxable Amount.

(2) Why did the Distribution Code in Box 7 change from last year?

If you were receiving benefits prior to age 59 1/2, your 1099-R may reflect a distribution code 2 (Early distribution, exception applies) in Box 7. Code 2 allows benefit recipients to receive distributions with exception to any penalties from the IRS for amounts paid prior to age 59 1/2. Upon reaching age 59 1/2, the benefits paid to you will be reflected on the 1099-R with distribution code 7 (Normal distribution).

In the tax year in which you reach age 59 1/2, you will receive two 1099-Rs. The IRS requires us to identify payments made to you while under age 59 1/2 and payments made to you upon reaching age 59 1/2.

We hope this explanation helps you better understand your IRS Form 1099-R. The ERS calculates all the amounts and codes for you to file your taxes. Although the ERS does not provide any tax advice, you may call our office at (808) 586-1735 should you need further assistance.

Report from Vijoy Chattergy, Chief Investment Officer

Aloha Kakou. In the previous Holomua, I identified the important challenges of asset allocation, manager selection, performance measurement, and risk management as critical tasks for ensuring the success of the investment portfolio and the health of the ERS pension plan. I do want to delve into each of these topics, but first it might be informative to step back and ask why the Investment Office exists. What do we produce that is of any value?

If we were a shoe factory, we'd produce shoes. If we were a barber shop, you'd expect haircuts. As the Investment Office, we produce "returns," and by investment returns, I mean some change in the dollar or percent valuation of the assets in the portfolio from an earlier time period. Basically, our product is a number, or more accurately, a change in a number.

What do we produce that is of any value?

If the critical tasks identified above are executed, will a return be produced? Yes, but unlike a shoe factory or barber shop, there is probably more variability in the quality of the investment return than that of the shoe or haircut. In other words, doing these tasks, even with great skill, does not guarantee that the investment product (i.e., the return) will be what was expected.

Why is that? What exactly goes into manufacturing an investment return? In a word, it is "information."

Information is not only bits and bytes on a computer, although that often comes to mind. It's really anything and everything. An investor building "return" can take any news on the radio, report on a desk, or walk down a supermarket aisle to develop an investment thesis. For example, noticing instant noodles selling out at the local grocery might initiate an investigation into consumer confidence and cause a change in stocks held.

Of course, investing (i.e., building return) is not as straight forward as in this example. It's messy, uncertain, and inaccurate. That is the reason for the inconsistency of returns. Information is difficult to interpret.

So where does this leave our Investment Office; fumbling with gobs of data and trying to decide where to invest, so as to possibly create a quality return measured over 30 years? Well, the only real characteristics that can help, other than plain "luck" (which is a topic for another Holomua), is "experience" and the "ability to learn." Combining the concepts, "earned experience" (i.e., knowledge or wisdom) through years or circumstance is probably an investor's only hope at deliberately constructing returns.

This brings me back to the question of why we have an Investment Office. The Investment Office exists to produce investment returns that support the health of the ERS pension plan. To accomplish that objective, the Investment Office must be staffed by experienced professionals who view the world as an investment opportunity and who can interpret information to manufacture investment returns. Their primary responsibility and dedication must be to the sustainability of the ERS with the goal of providing current and future members with their promised benefits.

As the only current full-time investment professional on staff, I expect to hire two Investment Specialists in 2013. I hope to add up to three Investment Officers to the team soon after that. With six investment professionals, the ERS will be well served and even on its way to becoming a high quality investment returns "factory."

The Investment Office exists to produce investment returns that support the health of the ERS pension plan.



Emmit Kane elected new ERS Board of Trustees chairperson

The ERS Board of Trustees has elected Mr. Emmit Kane as its new Chair. Mr. Kane is one of four elected trustees on the eight-member board and his term will run through January 1, 2018.

Mr. Kane is an Assistant Fire Chief with the Honolulu Fire Department and has more than a decade of supervisory, management, and long-range planning experience. He was an East-West Center Degree Fellow and holds a Master of Business Administration degree from the University of Hawaii. In addition, he has served on the Executive Board of the Hawaii Fire Fighters Association.

Mr. Kane has been a member of the ERS Board since 2010 when he was appointed to complete the term of a retiring trustee. During the past 3 years he has chaired the board's Audit committee and has been a member of the board's Administrative and Investment committees. He replaces Colbert Matsumoto, the previous board chair. Vincent Barfield, Senior Vice President at Bank of Hawaii and appointed trustee, was elected as the board's Vice Chair.

ERS by the Numbers

Every year, our actuaries of the ERS provide us with the valuation report (see "What's New" on the ERS website) to analyze the ERS' financial condition. As part of this analysis, they review statistical data on the ERS active, inactive and retired members. These numbers present an interesting, and sometimes surprising, portrait of our membership.

ERS Membership as of June 30, 2012:

Active members	65,599
Retirees and beneficiaries	40,774
Inactive, vested members	6,909
Total:	113,282

Active Members:

Of the distribution of active members by 5-year age ranges, these ranges were highest in number:

Age 50 – 55	10,008
Age 55 – 59	9,834
Age 45 – 49	9,316
Age 40 – 44	8,587

There were 554 active members under the age of 25 and 3,397 active members age 65 and older.

Of the distribution of active members' years of service, these ranges were the highest in number:

5 – 9 years of service	13,899
10 – 14 years of service	10,689
20 – 24 years of service	9,016

There were 3,357 active members with less than 1 year of service and 1,642 active members with 35 years or more of service.

Retirees and Beneficiaries:

Average life expectancy of ERS retirees:

Males:	Age 85
Females:	Age 89

Ratio of active members to retirees (includes service and disability retirees and beneficiaries):

1.6 to 1 (about one and 1/2 active members for every retiree)

Average monthly pension (please note that each benefit plan and benefit category has different retirement benefit formulas, and that retirees select their monthly benefit from several options):

Average monthly Contributory pension amount	\$2,315
Average monthly Noncontributory pension amount	\$1,538
Average monthly Hybrid pension amount	\$2,090

News from the EUTF

Some helpful reminders for retirees regarding Medicare Part D prescription drug coverage and Medicare Part B premium reimbursement:

- Effective April 1, 2013, EUTF added a supplemental drug benefit to enhance Medicare retirees' existing EUTF Medicare prescription drug plan. The Medicare prescription drug plan continues to be administered through SilverScript Insurance Company.

The supplemental drug benefit is an extra benefit that doesn't cost any additional premium and provides additional coverage above and beyond what Medicare covers. Most importantly, your co-payment amounts remain the same as they were for the 2012 plan year and in some cases may be lower.

By now, you should have received material from SilverScript introducing the new supplemental drug benefit. Please continue to use the SilverScript ID card you received in 2012 to fill prescriptions.

If you have not received any information about the supplemental drug benefit because you recently changed your address and phone number, or, if you have any questions about the EUTF Medicare prescription drug plan and supplemental drug benefit, please contact SilverScript Customer Care, 24 hours a day, 7 days a week, toll-free at 1-877-878-5715 (TTY users should call 1-866-236-1069). In addition, please notify the EUTF in writing if you have a change of address or telephone number.

- Every January the Medicare Part B Premium amount which is reimbursed to EUTF Medicare retirees resets to the Medicare standard amount which is \$104.90 for 2013. If you have a higher income-related premium contribution, please submit to the EUTF a copy of your letter from Social Security which indicates your 2013 Medicare Part B Premium amount.
- Some retirees are still receiving their Medicare Part B premium reimbursement by check. If you are in this group, you may find that direct deposit of the payment to your bank account delivers the money to you faster and is far more convenient. To switch to direct deposit, please call the EUTF at 586-7390 or toll-free at 1-800-295-0089 and we will mail you a Direct Deposit Agreement (DDA) form. You can also visit our website at www.eutf.hawaii.gov. Click on the Retiree Section and click on EUTF Retiree Forms, Direct Deposit Authorization Print and Fill Form. Please complete the DDA form as instructed, have your financial institution certify your account information and return your completed DDA form to the EUTF at the following address:
 - P O Box 2121, Honolulu, HI 96805-2121; or,
 - drop it off at our office located in the City Financial Tower at 201 Merchant Street, Suite 1520 in Honolulu.
- Once you enroll in Medicare Part B make sure you provide the EUTF with proof of your enrollment. Submit a copy of your Medicare Part B ID card along with a Direct Deposit Agreement Form (DDA). This will start your quarterly Medicare Part B premium reimbursement payments coming to you.

Important: The EUTF is a separate organization from the ERS. If you have any questions about information in this article, please **DO NOT** contact ERS. Please contact the EUTF directly at 586-7390 or toll-free at 1-800-295-0089, or email the EUTF at eutf@hawaii.gov. You can also visit our website for more information @ www.eutf.hawaii.gov.



Employees' Retirement System
of the State of Hawaii
Working to fulfill your retirement dreams...



PRESORTED
STANDARD
U.S. POSTAGE
PAID
HONOLULU, HI
PERMIT NO. 643

201 Merchant Street, Ste. 1400 • Hon, HI 96813-2980



Scan the QR code with your smartphone
to directly access the ERS website.

Holomua

Retirees

January/February/March 2013

Ask ERS

Answers to some frequently asked questions:

Q: How often should I be receiving the Statement of Retirement Allowances and Deductions?

A: You will receive the statement only when there is change to the pension amount, as your pension would remain the same until the next change. The ERS mailed statements in January 2013 due to the change in federal tax withholding. It is recommended that you keep the statement for your records.

Q: How do I change the federal tax withholding on my pension payments?

A: You must complete and send the Form W-4P (Withholding Certificate for Pension and Annuity Payments) to our office. The form is on our website under Retirees->Pension Forms. Please allow at least one month for the tax withholding change.

Q: Do retirees under service connected disability retirement need to report their pension?

A: If all or portion of your pension benefit may be excluded from gross income under Internal Revenue Code (IRC) Section 104(a)(1). You will receive a Form 1099-R for the portion of your benefit that is reportable to the IRS. For the amount of your benefit that is non-reportable, you will receive a letter from the ERS regarding this information.

How to Contact Us

Monday-Friday 7:45 a.m. - 4:30 p.m.
(except State holidays)

Oahu Office, Phone: (808) 586-1735

Kauai Office, Phone: (808) 274-3010

Hawaii Office, Phone: (808) 974-4077

Maui Office, Phone: (808) 984-8181

Molokai & Lanai, toll free to Oahu:
1-800-468-4644

Continental U.S. toll free to Oahu:
1-888-659-0708