EMPLOYEES' RETIREMENT SYSTEM
OF THE
STATE OF HAWAII

COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF HAWAII

COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Prepared by the Staff of the:
Employees' Retirement System of the State of Hawaii
201 Merchant Street, Suite 1400
Honolulu, Hawaii 96813
(808) 586-1735 • (808) 586-1650
Facsimile (808) 586-1677 • http://www4.hawaii.gov/ers/

DAVID Y. SHIMABUKURO, Administrator
WESLEY K. MACHIDA, Assistant Administrator
RODNEY L. JUNE, Chief Investment Officer

Table of Contents

Employees' Retirement System

of the State of Hawaii

INTRODUCTORY SECTION

Certificate of Acheivement

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Employees Retirement System of the State of Hawaii

For its Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2007

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

President

Executive Director

Letter from the Chair

LINDA LINGLE
GOVERNOR

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

February 8, 2010

Honorable Linda Lingle
Governor, State of Hawaii
Honolulu, HI 96813

Dear Governor Lingle:

In these uncertain economic times, we sincerely appreciate the continued support to ensure that sufficient funds are available to pay the benefits promised to current and future retirees of the Employees' Retirement System. As you know, most investors and public pension funds were negatively affected by the volatility and marked downturn of the financial markets. The ERS was no exception and suffered its first investment loss (-3.5%) since FY 2001. Our average annual investment return was 10.1% over the five fiscal years ending on June 30, 2008, and we outperformed more than three quarters of the large public pension funds during this period.

The dramatic stock market slide since June 30, 2008 will increase our $5.168 billion unfunded liability. However, the new long-term retirement funding methodology that was implemented in July 2005, the increase in the employers' contribution rates beginning July 2008, and recent moratorium on retirement benefit enhancement proposals until January 2011 will help reduce our unfunded liability over time.

During the past fiscal year, we transitioned our investment portfolio to a new custodian bank which will result in significant cost savings and increased securities lending income over five years. New investment policies and procedures were also developed to implement the Hawaii Targeted Investment Program and to comply with the new law which prohibits the ERS from investing in certain companies that do business in the Sudan.

An important measure passed by the 2008 Legislature will allow members to rollover and transfer funds to ERS from their deferred compensation plans, tax sheltered annuities, individual retirement accounts, and private pension plans to purchase membership service credits or to upgrade their Noncontributory Plan membership service to Hybrid Plan. An ERS project team is developing program plans to enable over 24,000 Hybrid Plan members to upgrade their Noncontributory service and increase their future pension benefits.

Although we foresee significant challenges in the coming years, we know that our staff, investment managers and consultants are working extremely hard to better the retirement program for our members.

Respectfully submitted,

Jackie Ferguson-Miyamoto

Jackie Ferguson-Miyamoto, Chair
Board of Trustees

Employees' Retirement System
of the State of Hawaii

City Financial Tower • 201 Merchant Street, Suite 1400 • Honolulu, Hawaii 96813-2980
Telephone (808) 586-1735 • Fax (808) 586-1677 • http://www4.hawaii.gov/ers

Letter of Transmittal (continued)

LINDA LINGLE
GOVERNOR

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

February 8, 2010

Board of Trustees
Employees' Retirement System
of the State of Hawaii

Dear Board Members:

We are pleased to submit the Comprehensive Annual Financial Report (CAFR) of the Employees' Retirement System of the State of Hawaii (ERS) for the fiscal year ended June 30, 2008. Responsibility for both the accuracy of the data, as well as the completeness and fairness of the presentation, rests with the management of the ERS. We trust that you and the members of the ERS will find this report helpful in understanding your retirement system.

BACKGROUND

The ERS was established by the Legislature in 1925 to administer a retirement, disability and survivor benefits program for State and county employees including teachers, professors, police officers, firefighters, judiciary employees, judges, and elected officials. The ERS is a qualified defined benefit public pension plan covered under Section 401(a) of the Internal Revenue Code. Hawaii Revised Statutes Chapter 88 contains the actual language governing the pension trust. The plan covers all full-time State and county employees in the State of Hawaii. The ERS is funded on an actuarial reserve basis. Benefit funding comes from employer and member contributions, and investment earnings.

On March 31, 2008, the ERS' total membership of 108,696 was comprised of 66,589 active members, 36,260 retirees and beneficiaries, and 5,847 inactive vested members. This represents a 2.4% growth in the total membership over the past year. Participating employers include the State of Hawaii, City and County of Honolulu, and the counties of Hawaii, Maui and Kauai.

The ERS is also responsible for the custody of the Social Security Contribution Fund for the State of Hawaii. The Social Security contributions withheld from employees are remitted directly to the Internal Revenue Service by the State. As an agency type fund that is custodial in nature, the ERS has limited discretion in the management of this fund.

Employees' Retirement System
of the State of Hawaii

City Financial Tower • 201 Merchant Street, Suite 1400 • Honolulu, Hawaii 96813-2980
Telephone (808) 586-1735 • Fax (808) 586-1677 • http://www4.hawaii.gov/ers

MAJOR ACCOMPLISHMENTS AND INITIATIVES IN FY 2008

We made significant progress on several multi-year projects during the past fiscal year that will help improve member services and operational efficiencies. A discussion on the projects and legislative actions follows.

Hybrid Plan – A new hybrid contributory plan was implemented in July 2006 to provide members with enhanced benefits as compared to the existing Noncontributory Plan on a cost-neutral basis to the State and county governments. We worked with several national public pension plan organizations and the Hawaii Congressional delegation to secure federal legislation to allow for the upgrade of members' past Noncontributory Plan service credits from the 1.25% benefit multiplier to the 2% benefit multiplier under the Hybrid Plan. Our efforts were successful as a special amendment was included in the federal Pension Protection Act of 2006 which enables Hybrid Plan members to use their deferred compensation and tax-sheltered annuity monies to pay for the upgrade.

A project team was established to develop the overall plan and a budget request to retain a consulting firm to assist in this major project was approved by the 2008 Legislature. The team subsequently solicited proposals for consultant services to coordinate the communications campaign which included conducting statewide group meetings, developing a website, operating a call center, handling the elections, and collecting payments from Hybrid Plan members electing to upgrade their membership service. Proposals were evaluated and a contract was recently awarded to Buck Consultants. The upgrade program is anticipated to begin in late 2009.

Pension Management Information System – The second priority is the replacement of ERS' legacy computer systems that have been in use since the late 1980's. Vitech Systems Group, Inc. was hired in April 2005 to design and install a new computer and office automation system which will include the pension administration of the Contributory, Noncontributory, and new Hybrid retirement plans; imaging; workflow; accounting; etc. The new computer system will improve operational efficiencies and membership service. A new accounting system and portions of the Hybrid Plan pension administration system were completed in 2006.

During the past fiscal year, 19 million member transactions from 1957 were migrated into the new system and we began to scan and index 7.7 million historical paper and microfilmed membership documents. We also continued to design and test the Contributory and Noncontributory Plan pension administration systems and secured legislation to require employers to transmit payroll and personnel transactions electronically to the ERS by July 2010.

Member Statement Project – Our third major project was to research and correct membership data in our legacy computer systems. A project team worked with a computer consultant from General Enterprises on this initiative for several years. The goals are to research, secure, and adjust historical membership records so that we can load good data into the new pension management information systems. The accuracy of members' membership service credits will be especially important for those who plan to convert their Noncontributory service to the Hybrid Plan.

Other – The new ERS logo won an Award of Excellence in the 2008 Pele Awards competition. The Pele Awards is an annual creative competition that recognizes the best advertising and design work created in Hawaii. The ERS logo was selected from a total of 55 entries in the logo category.

The fact that the new ERS logo won this award is a professional affirmation of what we also believe – that our new logo tells the ERS story very well. The tree symbolizes growth; the center of the tree represents our members; the leaves are the fruits of their labor; and the branches are their arms raised in the air, as they enjoy retirement.

ACHIEVEMENT AWARDS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Employees' Retirement System of the State of Hawaii for its comprehensive annual financial report for the year ended June 30, 2007. This was the 17th year the ERS has received this prestigious award. In order to be awarded the Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report that satisfies both generally accepted accounting principles and applicable legal requirements.

ACCOUNTING SYSTEM AND REPORTS

The accrual basis of accounting is used to record financial transactions. Expenses are recorded when the liability is incurred, and revenues are recorded in the accounting period in which they are earned and become measurable. Interest earned is accrued on a monthly basis. Accounts receivable at year end, in addition to accrued interest receivable, reflect accrued employer charges and investment proceeds due on sales that have not yet settled. Investments are recorded at fair value. Fixed assets are recorded at cost less accumulated depreciation.

The *Notes to the Financial Statements (Notes)* contain additional detailed information on the statutory provisions under which the ERS operates. In addition, the *Notes* include a summary of significant accounting policies, and provide explanatory information to help readers better understand the data contained in the financial statements.

The management of the ERS is responsible for and has implemented systems of internal accounting controls designed to provide reasonable assurances for the safeguarding of assets and the reliability of financial records. We believe that the internal accounting controls currently in place are adequate to meet the purpose for which they were intended. To the best of our knowledge and belief, the enclosed data, including the financial statements, supporting schedules and statistical tables is accurate in all material respects and is reported in a manner that fairly presents the financial position and results of the ERS' operations.

INVESTMENTS

The Board of Trustees diversified the ERS' investment portfolio to secure consistent, positive long-term investment returns while preserving capital. The diversification of investments through a long-term asset allocation strategy is generally regarded as the most important decision made in the investment process. A summary of the ERS' long-term asset allocation strategy can be found in the Investment Section of this report.

Professional investment managers have been retained to execute the Board's investment strategies and have full discretion within statutory provisions, Board policies and their respective guidelines. The investment managers retained by the Board as of June 30, 2008 are listed in the Investment Section.

Net investment income, including dividends, interest, other investment earnings, and gains/losses on the sale of investments resulted in a negative $461 million return in FY 2008. This resulted in a 3.5% investment loss for the year, using rate of return methodologies that are generally accepted by the Global Investment Performance Standards (GIPS).

FUNDING AND ACTUARIAL OVERVIEW

The overall objective of the ERS is to accumulate sufficient funds to meet current and future retirement, disability and death benefit obligations to retirees and beneficiaries. The accumulated balance is referred to as the "net assets held in trust for pension benefits" in the audited financial statements in the Financial Section of this report. The actuarial accrued liability is disclosed in the required supplementary schedules following the notes to the financial statements. These schedules show the actuarial value of assets, which is based on a four-year smoothed valuation that recognizes the excess or shortfall of investment income over or under the 8% actuarial investment assumption. This is the value of assets used by the actuary each year to determine the employer contribution requirements to the ERS. Member contribution rates are established by statute and discussed in Note E to the financial statements.

The actuarial accrued liability of the ERS is determined by the actuary. It is a measure of the present value of actuarial accrued liabilities estimated to be payable in the future to current retirees, beneficiaries, and employees for service earned to date. The unfunded actuarial accrued liability increased slightly to $5.168 billion as of June 30, 2008.

The percentage computed by dividing the actuarial value of net assets available for benefits by the actuarial accrued liability is generally referred to as the "funded ratio". This ratio provides an indication of the funded status of the ERS on a going-concern basis and generally the greater the percentage, the stronger the pension trust. A higher level of funding gives the participants a greater degree of assurance that their pension benefits are secure. The benchmark funding period for the UAAL that is used in accordance with GASB Statement No. 25 is 30 years.

The ERS' funded ratio improved to 68.8% as of June 30, 2008. In addition, based on increased employer contribution rates beginning July 2008, the related funding period is within GASB standards at 22.6 years (compared to 25.5 years as of June 30, 2007). However, there are $534 million deferred investment losses which will decrease the funded ratio and increase the funding period over the next three years without an offsetting actuarial gain. The funded status and progress for the ERS are presented in the Required Supplementary Information Schedules of Funding Progress.

Letter of Transmittal (continued)

PROFESSIONAL SERVICES

Professional consultants are appointed by the Board to perform professional services that are essential to the effective and efficient operation of the ERS. Opinions from the certified public accounting firm, KPMG LLP, and the actuary, Gabriel, Roeder, Smith & Company, are included in this report. Pension Consulting Alliance, Inc. is our investment consultant and their report on the ERS' investment program and performance results is also included in this report.

ACKNOWLEDGEMENTS

This report represents the dedicated collaborative efforts of the ERS staff and consultants to provide extensive and reliable information as a basis for making management decisions, determining compliance with legal provisions, and for determining responsible stewardship of the assets contributed by the ERS' members and their employers. This report will be provided to the Governor, legislators, State and county departments, and other interested parties.

We would like to take this opportunity to express our gratitude to the Board of Trustees, the Staff, the advisors, and to the many people who worked so diligently to help our members.

Respectfully yours,

David Shimabukuro
Administrator

Board of Trustees

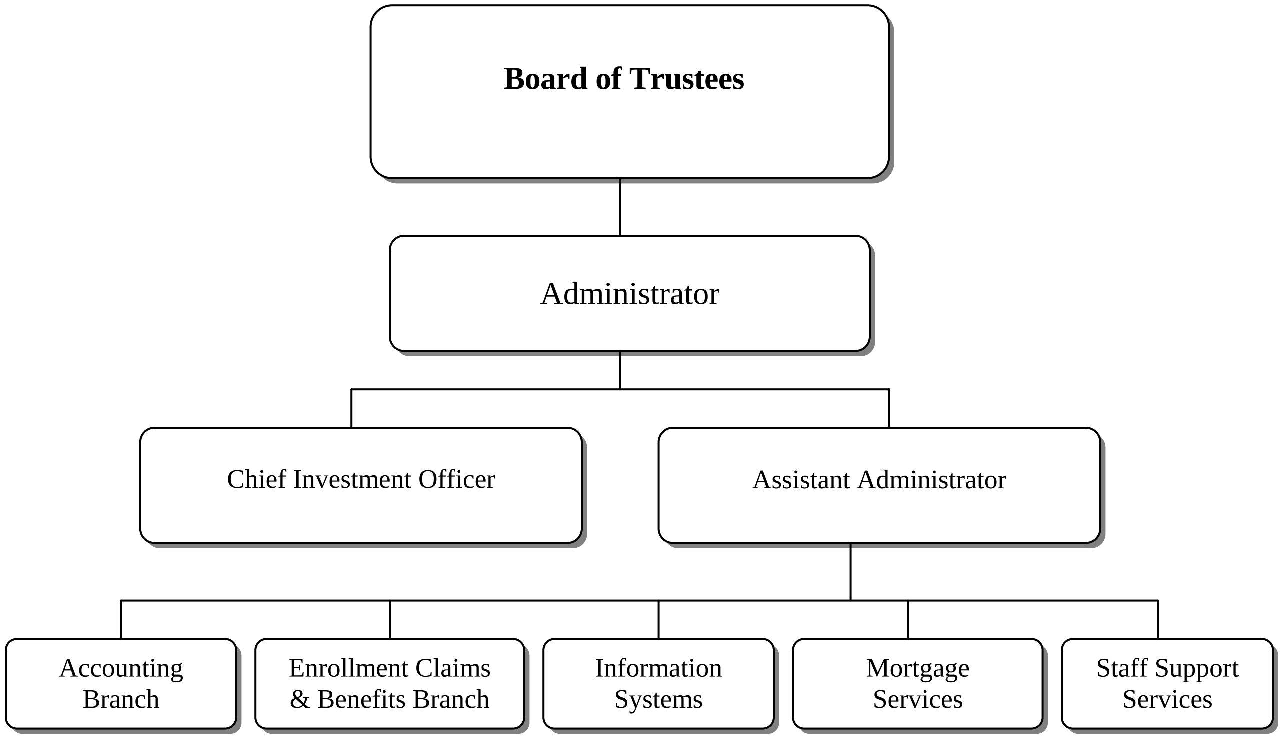
The Board of Trustees is the governing body of the Employees' Retirement System of the State of Hawaii, with certain areas of administrative control vested in the State Department of Budget and Finance.

Four of the eight members on the Board are elected by the membership: two general employees, a teacher and a retiree. Three members are citizens of the State, one of whom is an officer of a bank authorized to do business in the State or a person of similar experience, who are not employees and are appointed by the Governor. The State Director of Finance is an ex-officio member by statute.

Back Row (L-R): Wayne J. Yamasaki; Georgina K. Kawamura; Jackie Ferguson-Miyamoto, Chair; Pilialoha Lee Loy; Henry F. Beerman
Front Row (L-R): Alton T. Kuioka; Darwin J. Hamamoto; Colbert M. Matsumoto

	Date Current Term Began	Date Term Ends
Elected:		
Ms. Pilialoha E. Lee Loy	January 2, 2004	January 1, 2010
Mr. Darwin J. Hamamoto	January 2, 2006	January 1, 2012
Ms. Jackie Ferguson-Miyamoto, Chair	January 2, 2008	January 1, 2014
Mr. Wayne J. Yamasaki	January 2, 2008	January 1, 2014
Appointed:		
Mr. Henry F. Beerman	July 1, 2003	January 1, 2009
Mr. Alton T. Kuioka	March 31, 2005	January 1, 2011
Mr. Colbert M. Matsumoto	January 2, 2007	January 1, 2013
Ex-Officio:		
Ms. Georgina K. Kawamura	December 2, 2002	

Organizational Structure



Administrator	David Y. Shimabukuro
Assistant Administrator	Wesley K. Machida
Chief Investment Officer	Rodney L. June

Actuary
Gabriel, Roeder, Smith and Company

Auditors
KPMG LLP

Legal Advisor
Attorney General of the State of Hawaii

Medical Board
Dr. Patricia L. Chinn, Chair
Dr. Howman Lam, Member
Dr. Gerald J. McKenna, Member

** A list of investment professionals is located in the *Investment Section* of this CAFR.

Plan Summary

The Employees' Retirement System (ERS) of the State of Hawaii was established by the Legislature in 1925 to provide retirement, disability and survivor benefits for State employees, teachers, professors, county employees, police officers, firefighters, judges and elected officials.

The ERS is a qualified defined benefit pension plan under Section 401(a) of the Internal Revenue Code. As such, the ERS is exempt from federal income taxation on its investment earnings. Since January 1, 1988, member contributions have been tax deferred under Section 414(h) of the Internal Revenue Code.

Members are covered by the provisions of the Contributory, Hybrid or Noncontributory retirement plan. Except for employees in certain positions who are required to be members of the Contributory Plan, most new employees from July 1, 2006 are enrolled in the Hybrid Plan.

Those in the Contributory Plan are required to make contributions to the ERS and may also be covered by Social Security. Employees in the following occupational groups are required to be members of the Contributory Plan: police officers, firefighters, judges, elected officials, legislative officers, attorney general investigators, narcotics enforcement investigators, and public safety investigations staff investigators. As of March 31, 2008, 7,745 active employees were enrolled in the Contributory Plan, or slightly less than 12% of our active members.

On July 1, 2006, the Hybrid Plan became effective pursuant to Act 179/2004. Members in the Hybrid Plan must also contribute to the ERS and are generally covered by Social Security. The Hybrid Plan covers most employees hired from July 1, 2006, as well as certain employees hired before July 1, 2006 who elected to join the Hybrid Plan. The Hybrid Plan membership will continue to increase going forward as most new employees hired from July 1, 2006 will be required to become a member of the Hybrid Plan. As of March 31, 2008, the Hybrid Plan had 34,555 members or about 52% of the ERS' active membership.

Members of the Noncontributory Plan do not make contributions to the ERS and are covered by Social Security. The Noncontributory Plan covers employees hired from July 1, 1984 to June 30, 2006, as well as employees hired before July 1, 1984 who elected to join the Noncontributory Plan. As of March 31, 2008, there were 24,289 active employees in the Noncontributory Plan, which represents over 36% of all active members on this date.

A summary of the general retirement benefits, including retirement options, for Contributory, Noncontributory and Hybrid members are on the following pages. For more detailed and current information on the Hybrid Plan please visit the ERS website at http://www4.hawaii.gov/ers/.

Summary of Retirement Benefit Plan Provisions

	Noncontributory Plan	Contributory Plan	Hybrid Plan
Employee Contributions	No employee contributions	7.8% of salary	6.0% of salary
Normal Retirement			
Eligibility	Age 62 and 10 years credited service; ***or*** Age 55 and 30 years credited service	Age 55 and 5 years credited service	Age 62 and 5 years credited service; ***or*** Age 55 and 30 years credited service
Benefit	1-1/4% of average final compensation* times years of credited service	2% of average final compensation* times years of credited service	2% of average final compensation* times years of credited service, with a split formula for Noncontributory service at 1-1/4%

* Average final compensation (AFC) is an average of the highest salaries during any three years of credited service, excluding any salary paid in lieu of vacation or if ERS membership occurred prior to 1/1/71, AFC may be an average of the highest salaries during any five years of credited service including any salary paid in lieu of vacation.

	Noncontributory Plan	Contributory Plan	Hybrid Plan
Early Retirement			
Eligibility	Age 55 and 20 years credited service	Any age and 25 years credited service	Age 55 with 20 years credited service
Benefit	Maximum allowance reduced 6% per year under age 62	Maximum allowance reduced 5% per year under age 55 plus 4% per year under age 50	Maximum allowance reduced 5% per year under age 62
Deferred Vesting			
Eligibility	10 years credited service	5 years credited service and contributions left in the ERS	5 years credited service and contributions left in the ERS
Benefit	Accrued maximum allowance payable as early as age 55 or at age 65 with 10 but less than 20 years of credited service	Accrued maximum allowance payable at age 55	Accrued maximum allowance payable as early as age 55 or at age 62 with 5 but less than 20 years of credited service

Summary of Retirement Benefit Plan Provisions (continued)

	Noncontributory Plan	Contributory Plan	Hybrid Plan
Annuity Savings Account			
Interest	Not applicable	4.5% per annum on employee contributions and accrued interest	4.5% per annum on employee contributions and accrued interest
Refund Eligibility	Not applicable	Contributions may be withdrawn upon retirement or termination of employment; upon refund, all service and any future retirement benefit will be forfeited	Contributions may be withdrawn upon retirement or termination of employment; upon refund, all service and any future retirement benefit will be forfeited
Refund Benefit			
- Terminates with less than 5 years credited service	Not applicable	Return of member's contributions and accrued interest	Return of member's contributions and accrued interest
- Terminates with 5 or more years of credited service	Not applicable	Return of member's contributions and accrued interest	Return of member's Hybrid Plan contributions and accrued interest, times 150%; plus any non-Hybrid contributions and accrued interest
Ordinary Disability			
Eligibility	10 years credited service	10 years credited service	10 years credited service
Benefit	1-1/4% of AFC times years of credited service, unreduced for age (Minimum is 12.5% of AFC)	1-3/4% of AFC times years of credited service, unreduced for age (Minimum is 30% of AFC)	2% of AFC times years of credited service, unreduced for age; split formula for Noncontributory service at 1-1/4% (Minimum is 25% of AFC)

Summary of Retirement Benefit Plan Provisions (continued)

	Noncontributory Plan	Contributory Plan	Hybrid Plan
Service-Connected Disability			
Eligibility	Any age or credited service	Any age or credited service	Any age or credited service
Benefit	Lifetime pension of 35% of AFC	Lifetime pension of 50% of AFC plus refund of member's contributions and accrued interest	Lifetime pension of 35% of AFC plus refund of member's contributions and accrued interest
	** For accidents occurring before July 1, 2004, accrued maximum allowance, but not less than 15% of AFC	** For accidents occurring before July 7, 1998, a different benefit is used	
Ordinary Death			
Eligibility	Active employee at time of death with at least 10 years of credited service	Active employee at time of death with at least 1 year of service	Active employee at time of death with at least 5 years of service
Benefit	Surviving spouse/reciprocal beneficiary (until remarriage or reentry into a new reciprocal beneficiary relationship) and dependent children (up to age 18) receive a benefit equal to a percentage of member's accrued maximum allowance unreduced for age; ***or*** Option B (100% Joint and Survivor) lifetime pension for surviving spouse/reciprocal beneficiary if member was eligible for retirement at time of death	Lump sum payment of member's contributions and accrued interest plus a percentage of the salary earned in the 12 months preceding death; ***or*** Option 3 (50% Joint and Survivor) lifetime pension if member was not eligible for retirement at the time of death, credited with at least 10 years of service, and one beneficiary designated; ***or*** Option 2 (100% Joint and Survivor) lifetime pension if member was eligible for retirement at the time of death and one beneficiary designated, ***or*** If less than 1 year of service, return of member's contributions and accrued interest	Lump sum payment of member's Hybrid Plan contributions and accrued interest (times 150%) plus return of non-Hybrid contributions and accrued interest; ***or*** Option 3 (50% Joint Survivor) lifetime pension if member was not eligible for retirement at the time of death, credited with at least 10 years of service and one beneficiary designated; ***or*** Option 2 (100% Joint Survivor) lifetime pension if member was eligible for retirement at the time of death, and one beneficiary designated, ***or*** If less than 5 years of service, return of member's contributions and accrued interest

Summary of Retirement Benefit Plan Provisions (continued)

	Noncontributory Plan	Contributory Plan	Hybrid Plan
Service-Connected Death			
Eligibility	Any age or service	Any age or service	Any age or service
Benefit	Surviving spouse/reciprocal beneficiary receives monthly benefit equal to 30% of AFC (until remarriage or re-entry into a new reciprocal beneficiary relationship); additional benefits payable to surviving dependent children (up to age 18) If there is no spouse/reciprocal beneficiary or dependent children, no benefit is payable.	Lump sum payment of member's contributions and accrued interest to designated beneficiary, plus monthly benefit of 50% of AFC to surviving spouse/reciprocal beneficiary (until remarriage or re-entry into a new reciprocal beneficiary relationship); If there is no surviving spouse or reciprocal beneficiary, surviving dependent children (up to age 18) or dependent parents shall be eligible for a monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit shall be payable to the designated beneficiary.	Lump sum payment of member's contributions and accrued interest to designated beneficiary, plus monthly benefit of 50% of AFC to surviving spouse/reciprocal beneficiary (until remarriage or re-entry into a new reciprocal beneficiary relationship); If there is no surviving spouse or reciprocal beneficiary, surviving dependent children (up to age 18) or dependent parents shall be eligible for a monthly benefit. If there is no spouse/reciprocal beneficiary or dependent children/parents, the ordinary death benefit shall be payable to the designated beneficiary.

Summary of Retirement Benefit Plan Provisions (continued)

The plan provisions summarized in the preceding pages apply to teachers and most State and County employees. Special provisions applicable to other groups of employees are outlined below:

A) Police officers, firefighters, investigators of the Department of the Attorney General, narcotic enforcement investigators, and public safety investigations staff investigators contribute 12.2% of their monthly salary to the ERS instead of 7.8%. These members may retire at age 55 with 10 years of credited service or at any age with 25 years of credited service and receive a retirement benefit of 2-1/2% of average final compensation (AFC) for each year of such service up to a maximum of 80% AFC, provided the last 5 years is credited service in any of these occupations.

B) Judges, elected officials, and legislative officers may retire at age 55 with at least 5 years of credited service, or at any age with at least 10 years of credited service and receive a pension of 3-1/2% of AFC for each year of such service plus an annuity from their contributions allocable to the period of such service. This benefit cannot exceed 75% of the AFC. Judges hired after June 30, 1999 need 25 years of credited service in order to retire before age 55.

C) Sewer workers in specified classifications and water safety officers may retire at any age if they are credited with 25 years of such service with the last 5 or more years in these occupations. Those in the Hybrid Plan must contribute 9.75% of their salary to the ERS.

D) Emergency medical technicians (EMT) may retire at any age if they are credited with 30 years of such service with the last 5 or more years in these occupations effective June 30, 2003. The years of service to qualify for early retirement is gradually being reduced through June 30, 2008 when 25 years of EMT service will qualify these members for early retirement. Hybrid Plan members are required to contribute 9.75% of their salary to the ERS.

Post Retirement Benefit

Each retiree's original retirement allowance is increased by 2.5% on each July 1 beginning the calendar year after retirement. This cumulative benefit is not compounded and increases each year by another 2.5% of the original retirement allowance without a ceiling (i.e., 2.5% of the original retirement allowance the first year, 5% the second year, 7.5% the third year, etc.).

Taxation of Benefits

All retirement benefits are subject to Federal income tax but are exempt from Hawaii State income tax. Certain occupational (work related) disability benefits are exempt from Federal income tax. Arrangements to initiate voluntary withholding of Federal income tax can be made at any time. The ERS provides retirees with a 1099-R tax form on or before January 31 of each year.

Additional Benefits

Retirees, their spouses and dependent children under age 19 are eligible to receive life insurance, medical, dental, vision, and prescription drug coverage from the Employer-Union Health Benefits Trust Fund (EUTF) if they were hired before July 1, 1996, and retire with at least 10 years of continuous credited service. If they were first hired after June 30, 1996, health benefits are available on a cost-sharing basis as long as the member retires with at least 10 years of continuous service. A dependent of a retiree who is a full-time student at an accredited college, university or technical school and who is 19 through 23 years old is also eligible for coverage. A retiree with a hire date after July 1, 2001 will only receive coverage for him or herself on a cost sharing basis.

Unused sick leave is excluded from credited service in determining health benefit coverage.

Retirees are responsible for premiums in excess of the amount of employer contributions. Retirees and their spouses are eligible to receive a reimbursement of the Medicare Part B medical insurance premium. More information is available on the EUTF's website at www.eutf.hawaii.gov.

Applying for Retirement

A service retirement application can be filed with the ERS 150 days but no less than 30 days prior to the effective date of retirement. Once the application has been filed, cancellation prior to the effective date of retirement is permitted; however, the law requires mandatory retirement upon the third application. Members may obtain retirement information and application forms at the following locations:

Oahu Office
City Financial Tower
201 Merchant Street, Suite 1400
Honolulu, HI 96813
Phone: (808) 586-1735
Fax: (808) 587-5766

Kauai Office
3060 Eiwa Street, Room 302
Lihue, Hawaii 96766
Phone: (808) 274-3010
Fax: (808) 241-3193

Hawaii Office
101 Aupuni Street, Suite 208
Hilo, Hawaii 96720
Phone: (808) 974-4076
Fax: (808) 974-4078

Maui Office
54 S. High Street, Room 218
Wailuku, Hawaii 96793
Phone: (808) 984-8181
Fax: (808) 984-8183

Molokai and Lanai
Toll-free to Oahu:
1-800-468-4644, ext 61735

Continental U.S. only
Toll free to Oahu
1-888-659-0708

Counseling Service

It is the policy of the ERS to render every possible service to its members; however, as thousands of inquiries are received and answered annually, in addition to the actual processing of claims and benefits, present staff and appropriations restrict this service to those members whose immediate welfare is dependent upon the prompt settlement of benefits. Members who are definite about retirement should contact the ERS to request formal retirement estimates. For members who are not planning immediate retirement and interested in their benefit status a retirement benefit calculator and other retirement information are available on the ERS' website at www4.hawaii.gov/ers.

Retirement Options

CONTRIBUTORY AND HYBRID PLANS

Maximum Allowance: The member receives a lifetime maximum allowance; at death, the difference between the value of the member's contributions at the time of retirement and the retirement allowance paid prior to death is paid to the designated beneficiary(ies) or estate.

Option One: The member receives a reduced lifetime allowance based on age; at death, the difference between the initial insurance reserve and the retirement allowance paid prior to death is paid to the designated beneficiary(ies) or estate. In lieu of the lump-sum balance, the beneficiary may elect to receive an allowance for life based on the value of the balance; provided that the allowance is not less than $100 per month.

Option Two (100% Joint and Survivor): The member receives a reduced lifetime allowance based on ages of both the member and the sole beneficiary and at death; the same allowance is paid to the designated beneficiary for life. Should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease at the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree’s reduced pension “pops up” or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Option Three (50% Joint and Survivor): This plan is similar to Option Two. The member receives a reduced lifetime allowance which is higher than Option Two and is based on ages of both the member and the sole beneficiary; however, at death one-half of the allowance is paid to the designated beneficiary for life. Like Option Two, should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease at the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree’s reduced pension “pops up” or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Option Four: This option allows the member to devise a plan that will provide a benefit according to the member's specifications. It requires certification by the Actuary and approval of the Board of Trustees. The following Option Four plans have been approved:

Combination of Options Five and Maximum Allowance: The member receives a reduced lifetime allowance and is allowed to withdraw the pre-1987 nontaxable contributions, 50% of accumulated contributions, or 75% of accumulated contributions (Hybrid Plan members are not allowed the 75% option); at death, the difference between the value of the member's contributions at the time of retirement and the retirement allowance paid prior to death is paid to the designated beneficiary(ies) or estate.

Combination of Options Five and One: The member receives a reduced lifetime allowance and is allowed to withdraw the pre-1987 nontaxable contributions, 50% of accumulated contributions, or 75% of accumulated contributions (Hybrid Plan members are not allowed the 75% option); at death, the difference between the initial insurance reserve and the retirement allowance paid prior to death is paid to the designated beneficiary(ies) or estate.

Combination of Options Five and Two: The member receives a reduced lifetime allowance based on ages of both the member and the sole beneficiary, and is allowed to withdraw the pre-1987 nontaxable contributions, 50% of accumulated contributions, or 75% of accumulated contributions (Hybrid Plan members are not allowed the 75% option); at death, the same allowance is paid to the designated beneficiary for life. As in the case of Option Two, should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease at the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree’s reduced pension “pops up” or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Retirement Options (continued)

CONTRIBUTORY AND HYBRID PLANS (continued)

Combination of Options Five and Three: The member receives a reduced lifetime allowance based on ages of both the member and the sole beneficiary, and is allowed to withdraw the pre-1987 nontaxable contributions, 50% of accumulated contributions, or 75% of accumulated contributions (Hybrid Plan members are not allowed the 75% option); at death, one-half of the allowance is paid to the designated beneficiary for life. As in the case of Option Three, should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease at the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree's reduced pension "pops up" or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Option Five: The member receives a reduced lifetime allowance and is allowed to withdraw all accumulated contributions; at death, the prorated amount from the last pension payment through the date of death is payable to the beneficiary(ies) or estate.

Option Four and Option Five are restricted to those members with at least ten years of credited service excluding unused sick leave credit.

Regardless of the option selected, should death of the Contributory or Hybrid member occur during the first year of retirement, the designated beneficiary may elect to receive benefits as if death had occurred immediately prior to retirement in lieu of the death benefits described above.

NONCONTRIBUTORY PLAN

Maximum Allowance: The member receives a lifetime pension and at death, the prorated amount from the last pension payment through the date of death is payable to the beneficiary(ies) or estate.

Option A (50% Joint and Survivor): The member receives a reduced lifetime pension and at death, one-half of the pension is paid to the sole designated beneficiary for life. Should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease upon the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree's reduced pension "pops up" or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Option B (100% Joint and Survivor): The member receives a reduced lifetime pension and at death, the same pension is paid to the sole designated beneficiary for life. Like Option A, should the designated beneficiary predecease the retiree, another beneficiary cannot be named and all payments will cease upon the retiree's death. For retirements on or after December 1, 2004, should the beneficiary predecease the retiree, the retiree's reduced pension "pops up" or increases to the corresponding Maximum Allowance instead of remaining at the reduced amount.

Option C (Ten-Year Guarantee): The member receives a reduced lifetime pension. Should death occur within ten years of retirement, the same pension will be paid to the designated beneficiary for the balance of the ten-year period. Should the designated beneficiary predecease the retiree, another beneficiary can be named.

Regardless of the option selected, should death occur during the first year of retirement, the designated beneficiary may elect to receive benefits under Option B in lieu of the death benefits described above.

Legislative Highlights 2008

The following Acts were passed by the 2008 Legislature and approved by the Governor:

Act 41 – Retirement Plan Changes

- Allows members to rollover and transfer funds to ERS from their deferred compensation plans, tax sheltered annuities, IRAs, and private pension plans to purchase membership service credits or to upgrade their Noncontributory Plan service to Hybrid Plan service.
- Allows payments for the Hybrid Plan conversion with "after tax" employee payroll deductions. The Internal Revenue Service will no longer allow members to defer federal income taxes on their payroll deductions to upgrade membership service credits.
- Requires employers to make employee contributions for Contributory and Hybrid Plan members who are called to active military duty based on the compensation the member would have received had the member not been on military leave.
- Requires direct deposit for lump sum refunds of accumulated contributions greater than $250 if the member does not elect to rollover the payment into an eligible retirement plan.
- Provides for automatic increases in the annual ceiling on pension benefits to parallel the increases in the federal ceiling under Section 415 of the Internal Revenue Code.
- Prohibits returning vested Contributory Plan members from switching to the Hybrid Plan after June 30, 2008.
- Requires employers to transmit payroll and personnel transactions electronically to the ERS by July 1, 2010.
- Includes other housekeeping amendments to clarify and conform existing statutes to current practice.
- Effective July 1, 2008.

Act 47 – Relating to Federal Tax Qualification of the ERS

These amendments are required to comply with federal income tax laws and maintain the ERS' tax-qualified status.

- Allows all current elected officials to make an election to change their ERS membership status.
- Allows certain elected officials, serving from October 1, 2008 to make a one-time irrevocable election to be excluded from ERS membership.
- Repeals current provisions that allow elective officers and judges who have reached the 75% statutory cap on retirement benefits to retire while they remain in office.
- Effective October 1, 2008.

Act 156 – Return to Work of Retirees

- Allows State and County governments to hire retired State or County government employees while allowing them to continue to receive their retirement and health benefits without penalty.
- Requires a one-year waiting period before rehiring.
- Prohibits re-employment agreements prior to retirement.
- Requires employers to make retirement contributions based on the retiree's salary to amortize ERS' unfunded liability.
- Requires employers to file an annual report.
- Makes conforming amendments to Act 286, SLH 2006 relating to the rehiring of retired teachers and administrators; including the reduction of the employer's contribution rate on the retiree's salary from 13.75% to the amortized ERS' unfunded liability rate of 9.25%. Amends the sunset date from June 30, 2011 to June 30, 2013.
- Effective July 1, 2008; Sunsets on June 30, 2013.

Employees' Retirement System

of the State of Hawaii

FINANCIAL SECTION

Independent Auditors' Report

KPMG LLP
PO Box 4150
Honolulu, HI 96812-4150

The Board of Trustees
Employees' Retirement System of the State of Hawaii:

We have audited the accompanying combining statements of plan net assets – all trust and agency funds of the Employees' Retirement System of the State of Hawaii (the ERS) as of June 30, 2008 and 2007, and the related statements of changes in plan net assets – all trust funds for the years then ended. These financial statements are the responsibility of the ERS' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the ERS' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the ERS as of June 30, 2008 and 2007, and its changes in plan net assets for the years then ended, in conformity with U.S. generally accepted accounting principles.

Board of Trustees
Employees' Retirement System of the State of Hawaii

In accordance with *Government Auditing Standards,* we have also issued our report dated February 8, 2010, on our consideration of the ERS' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 26 through 33 and the schedules of employer contributions on pages 58 and 59 are not a required part of the basic financial statements, but are supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements of the ERS taken as a whole. The supplementary information included in schedules 1 through 4 for the years ended June 30, 2008 and 2007, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial, and statistical sections have not been subjected to the auditing procedures applied in the audits of the basic financial statements, and accordingly, we express no opinion on them.

KPMG LLP

Honolulu, Hawaii
February 8, 2010

Management's Discussion and Analysis (MD&A) of the Employees' Retirement System of the State of Hawaii (the ERS) provides highlights and comparisons of the financial position and performance of the ERS as of and for the years ended June 30, 2008 and 2007. The MD&A is presented as a narrative overview and analysis in conjunction with the Letter of Transmittal, which is included in the Introductory Section of the ERS Comprehensive Annual Financial Report (CAFR). For more detailed information pertaining to the ERS' financial activities, the reader should also review the actual financial statements, including the notes and supplementary schedules.

Overview of the Financial Statements

The ERS is responsible for administering a defined benefit pension plan for state government, local government, and public education employees in the State of Hawaii (the State). The ERS also oversees the short-term investments of the federal Social Security employer contributions for the State in the Social Security Contribution Fund (Contribution Fund).

The ERS' financial statements include fiduciary type funds that are used to account for resources held for the benefit of parties outside of the ERS. The primary fund is defined as a pension trust fund as these assets are held for the benefit of its members and their beneficiaries for the payment of pension benefits, while the Contribution Fund is an agency type fund that is custodial in nature. Throughout this discussion and analysis, units of measure (i.e., billions, millions, and thousands) are approximate, being rounded up or down to the nearest tenth of the respective unit value.

This discussion and analysis is intended to serve as an introduction to the ERS' financial reporting, which is comprised of the following components:

- The combining statements of plan net assets provide a snapshot of the financial position of the ERS at June 30, 2008 and 2007. These financial statements reflect the resources available to pay benefits to members, including retirees and beneficiaries, at the end of the fiscal years reported.
- The statements of changes in plan net assets summarize the ERS' financial activities that occurred during the fiscal year from July 1, 2007 to June 30, 2008 (FY 2008) and the fiscal year from July 1, 2006 to June 30, 2007 (FY 2007). The financial statements measure the changes in the resources available to pay pension benefits to members, retirees, and beneficiaries for fiscal years 2008 and 2007.
- The notes to financial statements provide additional information that is essential to a full understanding of the financial statements. The notes are an integral part of the financial statements and include detailed information that is essential to a full understanding of the data provided in the basic financial statements.
- The required supplementary information immediately following the notes to financial statements provides two schedules showing historical actuarial information concerning the funded status of the ERS and the employer contributions, along with related notes.

Financial Highlights

- The remaining supplementary information provides additional detailed information concerning the changes in operating funds established by legislation, and the operating and investment related expenses of the ERS.
- The pension plan net assets of the ERS decreased by $0.7 billion, or 5.4%, during fiscal year ended June 30, 2008, from $11.5 billion as of June 30, 2007. During fiscal year ended June 30, 2007, plan net assets increased by $1.5 billion, or 15.4%, from $9.9 billion as of June 30, 2006. The decrease in assets during the fiscal year reflects the overall market turmoil caused by increasing oil prices and the credit securities concerns. Net assets increased $736.5 million, or 8.0%, in the fiscal year ended June 30, 2006 (FY 2006). The asset growth was due to positive investment earnings and an increase in employer and employee contributions.
- The ERS experienced a 3.5% loss on investments during FY 2008 after successive years with positive returns on pension plan assets of 17.7% return in FY 2007 and 11.1% in FY 2006. The equity and real estate investments experienced negative returns after several years of strong performance.
- No significant legislation was enacted during the 2008 or 2007 legislative sessions that impacted the benefit provisions of the Pension Trust. On July 1, 2006, ERS implemented a new contributory "Hybrid Plan" that legislation passed in 2004 which provides future retirees enhance benefits on a cost-neutral basis to the employers since members pay for the improved benefits. This resulted in an increase in member contributions due to the number of Noncontributory Plan members that elected to transfer to the Hybrid Plan and new hires.

  However, legislation passed in 2007, and effective July 1, 2008, will increase employer required contributions to improve the funding status of the pension trust.. See the "Legislative Highlights 2008" in the Introductory Section of the CAFR for a summary of the 2008 legislative changes affecting the ERS and its membership. A historical summary of legislation impacting the ERS actuarial valuations are located in the "Summary of Plan Changes" in the Actuarial Section.
- Although ERS experienced an investment loss in FY 2008, the actuarial funded ratio increased to 68.8% on June 30, 2008 as a result of providing for market smoothing to realize actuarial investment gains and losses. This compared to 67.5% and 65.0% on June 30, 2007 and 2006, respectively. The corresponding unfunded actuarial accrued liability (UAAL) of the ERS remained relatively stable at $5.2 billion, $5.1 billion, and $5.1 billion on June 30, 2008, 2007, and 2006, respectively. Please refer to the ERS' 2007 and 2006 CAFR for results of the actuarial valuation for those years.
- Total employee and employer contributions increased by $53.0 million, or 8.8%, during FY 2008, $119.4 million, or 24.9%, during FY 2007, and $93.9 million, or 24.3%, during the FY 2006. Increases for FY 2008 and FY 2007 were primarily due to implementation of the new contributory Hybrid Plan that resulted in over 34,000 additional members making contributions to the ERS, while prior year increases was due to an increase in required employer contributions rates.

- Total pension plan benefit payouts increased $31.3 million or 4.1% during FY 2008 to $792.3 million compared to $40.5 million, or 5.6%, during FY 2007 to $761.0 million. Pension benefits continues to increase due to additional retirees and beneficiaries (36,260 in 2008, 35,324 in 2007, and 34,304 in 2006), an increase in the average pension benefit for new retirees, and the annual 2.5% post retirement increase.

- Administrative expenses increased by $1.1 million to $10.7 million in FY 2008, $1.1 million to $9.6 million in FY 2007 and $1.2 million, to $8.5 million in FY 2006. Administrative expenses for all years were within the ERS' budgeted amounts. Most of the increase during the three years was related to increased staffing and three significant multi-year projects undertaken by the ERS in late-FY 2005 to improve the services and benefits to our members – develop a communications and election campaign for the new Hybrid Plan that became effective on July 1, 2006; costs related to a new pension management information computer system; and the member statement project.

  In FY 2008, expenses with larger increases were filling additional positions established and increased workload related to the multi-year projects. There was a decrease in total computer automation projects costs due to following required capitalization accounting standards. During FY 2007, the expense categories experiencing larger increases were related to the computer and office automation systems being implemented, including maintenance and depreciation. There was also an increase during the two years for personnel related costs due to negotiated pay raises for employees, new and established positions, changes in the accrued vacation liability, and an increase in the fringe benefit rate.

Analysis of Plan Net Assets for Pension Trust

Summary of Plan Net Assets
June 30, 2008, 2007, and 2006
(Dollars in millions)

	2008	2007	FY 2008 % change	2006	FY 2007 % change
Assets:					
Cash and short-term investments	$ 692.4	$ 762.0	(9.1) %	$ 576.1	32.3 %
Receivables	375.8	253.1	48.5	107.0	136.5
Investments	10,767.3	11,122.3	(3.2)	9,738.9	14.2
Invested securities lending collateral	1,235.0	1,457.1	(15.2)	1,131.8	28.7
Capital assets	11.4	9.7	17.5	7.8	24.4
Total assets	13,081.9	13,604.2	(3.8)	11,561.6	17.7
Liabilities:					
Securities lending liability	1,235.0	1,457.1	(15.2)	1,131.8	28.7
Investment accounts and other payables	1,000.1	684.7	46.1	497.4	37.7
Total liabilities	2,235.1	2,141.8	4.4	1,629.2	31.5
Plan net assets	$ 10,846.8	$ 11,462.4	(5.4)	$ 9,932.4	15.4

Summary of Changes in Plan Net Assets
June 30, 2008, 2007, and 2006
(Dollars in millions)

	2008	2007	FY 2008 % change	2006	FY 2007 % change
Additions:					
Contributions	$ 652.1	$ 599.1	8.8 %	$ 479.7	24.9 %
Net investments income (loss)	(461.0)	1,705.0	(127.0)	988.3	72.5
Total additions	191.1	2,304.1	(91.7)	1,468.0	57.0
Deductions:					
Retirement benefit payments	792.3	761.0	4.1	720.5	5.6
Refund of contributions	3.7	3.5	5.7	2.5	40.0
Administrative expenses	10.7	9.6	11.5	8.5	12.9
Total deductions	806.7	774.1	4.2	731.5	5.8
Increase (decrease) in plan net assets	$ (615.6)	$ 1,530.0	(140.2)	$ 736.5	107.7

Investments, Investment Income, and Investment Expense

The ERS is a long-term investor and manages its pension assets with long-term objectives in mind. A primary element of the ERS' investment philosophy is diversification among various asset classes. The ERS makes estimates of long-term market returns and establishes an asset allocation strategy taking into account the risks associated with each asset class.

In FY 2008, the ERS experienced a 3.5% loss on investment assets due to turmoil in the world economy after several years of positive returns. The ERS' pension trust assets earned 17.7% on the investment portfolio in FY 2007, following a return of 11.1% in FY 2006. Asset classes with earnings in excess of the 8% portfolio benchmark for FY 2008 include international fixed income, alternative investments, and real estate, with returns of 14.6%, 11.3%, and 8.9%, respectively. These were offset by negative returns in domestic and international equities classes of -11.4% and -7.9%, respectively. The downturn in equity markets contributed to an overall net investment income loss of $461.0 million in FY 2008 after earning net investment income of $1,705.0 million in FY 2007 and $988.3 million in FY 2006 .

The asset distribution of the ERS' investment securities for the pension trust, excluding pending trade settlements and securities lending collateral, at June 30, 2008, 2007, and 2006 is presented below at fair market value. The actual investment mixtures will change over time based on market sectors' performance and our rebalancing efforts to maintain asset allocation targets. Please refer to the Investment Section of the CAFR for a discussion on asset allocation plan targets and investments by investment strategy.

Investments in short-term securities and cash are held by external investment managers for liquidity to settle pending trades and investments, and should not exceed ten percent of the investments. Fluctuations will occur based on the trading activity and timing of the settlements. The allocation to equity securities, including index funds and alternative investments, declined during FY 2008, due to investment losses, portfolio rebalancing, and changes in manager line-up. Changes for FY 2007 were due to the outstanding performance returns of the asset class and changes in the real estate manager line-up. Prior year declines were in accordance with the asset allocation strategy as investment earnings were used to pay pension benefits and fund real estate and fixed income managers. Net investments in equities decreased $970.0 million in FY 2008 compared to increased assets of $1,066.3 million and $377.3 million during FY 2007 and FY 2006, respectively.

Asset Class
June 30, 2008, 2007, and 2006
(Dollars in millions)

	2008	%	2007	%	2006	%
Short term investments and cash	$ 692.4	6.1 %	$ 762.0	6.4 %	$ 576.1	5.6 %
Equity securities	6,156.2	53.7	7,126.2	60.0	6,059.9	58.7
Fixed income	3,258.3	28.4	2,729.2	23.0	2,351.9	22.8
Real estate	895.2	7.8	874.1	7.3	957.1	9.3
Alternative investments	457.6	4.0	392.8	3.3	370.0	3.6
Total	$ 11,459.7	100.0	$ 11,884.3	100.0	$ 10,315.0	100.0

The net allocation to fixed income increased in accordance with the rebalancing the portfolio per ERS' asset allocation strategy and positive earnings. In FY 2007, additional manager funding was offset by weak investment returns in the bond markets. Fixed income holdings increased by $529.1 million in FY 2008, $377.3 million as of June 30, 2007, and $264.4 million as of June 30, 2006.

The real estate asset allocation increase in FY 2008 reflects positive investment earnings and funding additional managers. Although investment returns were positive for FY 2007, real estate related investments decreased due to the elimination on an investment manager during the year, and the pending funding of other investments. The real estate allocation increased in FY 2006 with the strong performance of the asset class and funding of an additional investment manager.

Investment expenses consist primarily of investment management fees paid to external investment advisor firms that oversee the ERS' investment portfolio. Investment expenses decreased in FY 2008 due to lower asset values that are used to calculate investment manager fees. The decrease in FY 2007 investment manager fees compared to FY 2006 was due to a smaller increase in asset values during the year for assets subject to incentive fees. Incentive fees are only paid to real estate managers upon the final disposition of the asset, although the net increase/decrease in the estimated fee is accrued for financial statement presentation annually. Net changes in the incentive fees are included in the liability for accounts and other payables on the combined statements of plan net assets.

The ERS requires external managers to provide the ERS with a "most favored nations" contract clause that guarantees the ERS with the lowest management fees the managers offer their clients for investment accounts with similar investment mandates and similar account size. Certain investment managers may receive an incentive fee for superior investment returns while maintaining an acceptable level of investment risk.

In FY 2008, ERS completed the procurement for our custodian banking and securities lending services that resulted in lower total custody fees and securities lending management fees effective April 1, 2008.

Contributions

Contributions from employers and employees totaled $652.1 million, $599.1 million, and $479.7 million during FY 2008, FY 2007, and FY 2006, respectively. This represents an increase of $53.0 million, $119.4 million, and $93.9 million for the three years, respectively. The FY 2008 increase includes higher total payrolls and continued increase in the number of Hybrid members making contributions. The FY 2007 increase reflects approximately 30,000 more members making contributions to the ERS with the start of the Hybrid Plan. The FY 2006 amount reflects a change in the funding methodology that established statutory rates for employers as a fixed percentage of covered payroll. The funding method was changed to help provide the employers with a consistent year-to-year rate for budgetary purposes and provide consistent cash flows to the ERS. Effective July 1, 2005, employers contribute 15.75% of covered payroll for police officers and firefighters and 13.75% for all other employees. These rates increased to 19.70% of covered payroll for police officers and firefighters and 15.00% for all other employees beginning July 1, 2008 per legislation passed in 2007. Please refer to the Actuarial Section in the ERS 2008 and 2007 CAFR for more information.

Pension Plan Benefits and Expenses

Pension benefit payments are the primary expense of the ERS with payments totaling $792.3 million during FY 2008, $761.0 million during FY 2007, and $720.5 million in FY 2006. Pension benefits continued to increase during the three fiscal years due to the additional number of new retirees, higher pension benefits for recent retirees; and the annual post retirement increase for ERS' retirees.

Refunds to terminating members increased slightly in FY 2008 and FY 2007 due to an increase in members making contributions under the Hybrid Plan and taking a refund compared previously to most members not making contributions to the ERS as a member of the Noncontributory Plan.

In FY 2008, administrative expenses increased $1.1 million to $10.7 million due to filling recently established positions and related to costs due to increased workload by undertaking three major projects since 2005. These projects that began in 2005 increased the ERS' workload in the near term, reflect the ERS' long-term investment to improve members' services and benefits over the longer term. In FY 2007, administrative expenses increased $1.1 million to $9.6 million. This compares to administrative expenses of $8.5 million during FY 2006. The FY 2008 and 2007 expense increases relates to the phased-in approach of computer and office automation projects, including increases in maintenance and depreciation. Certain functionality of the new pension management information system and financial accounting packages were implemented during the fiscal year. Expenses for FY 2006 include the one-time cost required to implement the first phase of the new Hybrid Plan effective July 1, 2006 – to conduct a communications campaign for over 58,000 existing members eligible to transfer to the new plan, conduct the membership election process, and to educate employers on the new retirement plan. For FY 2008, the largest increase reflects professional fees to support staff assigned to the multi-year projects. There was a decrease in computer and automation expenses with the capitalization of project costs in accordance with generally accepted accounting principles. Repairs and maintenance costs have increased over the past several years with the implementation of new server based technology required to operate the pension administration system that replaced legacy computer systems developed in the late-1980s. Personnel related costs included overtime due to increased workload for the three multi-year projects and salary and fringe benefit rate increases.

Pension Plan Changes

Pension plan changes, including legislative and Board of Trustees' actions, are summarized in the Introductory Section and Actuarial Section of the CAFR. The new "contributory" Hybrid Plan effective July 1, 2006 provides benefit enhancements to the members compared to the Noncontributory Plan, was implemented on a cost-neutral basis to the employers. There is a three-year moratorium on benefit enhancements from January 2, 2008 to January 2, 2011, if there is a UAAL in the pension trust.

Actuarial Valuations and Funded Status

The ERS uses an actuarial reserve type of funding that is financed by member contributions, employer contributions, and earnings from invested assets. An independent actuarial valuation of the ERS' actuarial assets and liabilities is performed annually. As part of this valuation, the progress towards funding pension obligations of the retirement system is measured by comparing the actuarial value of assets to actuarial accrued liability. This measurement is referred to as the funded ratio or funded status.

The actuarial funded status increased to 68.8% as of June 30, 2008, from 67.5% as of June 30, 2007, and 65.0% as of June 30, 2006. The ERS' UAAL stabilized at about $5.1 billion during the past three years.

The improvement in the funded status and stabilizing of the UAAL is a combination of deferring part of our market loss, four years of positive investment earnings, and an increase in future required employer contribution rates. These positive factors for FY 2007 were offset by a liability experience loss during the year due to actual salary increases exceeding the salary scale assumption.

The large increase in the UAAL, and corresponding decline in the funded ratio, during FY 2006 was due to changes in the non-statutory actuarial assumptions to reflect that ERS retirees are living longer than previously estimated, and to a lesser extent that active members are retiring earlier than previously estimated. The ERS' Board of Trustees adopted the revised non-statutory actuarial assumptions proposed by the ERS' actuary as part of the five-year Experience Study process, which was completed in accordance with Section 88-105 of the Hawaii Revised Statutes.

There was also an increase attributable to the reflection of the implementation of the Hybrid Plan, which caused a one-time adjustment to be recognized, and there was an increase due to liability experience losses resulting from gross salary increases, including negotiated pay raises, being larger than the statutory 4% assumption. While the implementation of the Hybrid Plan on July 1, 2006 resulted in a one-time liability adjustment or increase to be recognized for purposes of calculating the UAAL and funded ratio, it is important to note these calculations do not reflect the value or impact of the future employee contributions in the computation. Overall, the value of the future employee hybrid contributions offsets the one-time adjustment so that the Hybrid Plan is being implemented on a cost-neutral basis to employers.

The UAAL and funded ratio changes in prior years also include the impact of the employers' past practice of using the ERS' excess investment earnings to reduce their contributions. The diversion prevented the ERS from establishing reserves to weather periods of weak investment returns and capturing the earnings potential of the contributions when markets rise.

With the implementation of the percentage of payroll methodology for employer contribution funding in FY 2006, one of the primary purposes of the valuation report is to determine whether the adequacy of the current employer contribution rates is sufficient to amortize the UAAL within a specific number of years. Under the standards established by the Governmental Accounting Standards Board Statement No. 25 (GASB No. 25) that the ERS implemented in 1997, the standard for funding periods of the UAAL should not exceed 30 years.

The aggregate funding period, including the value of future employer and employee contributions, for the ERS as of June 30, 2008 was 22.6 years. This compares to 25.5 years and 35.2 years as of June 30, 2007 and 2006, respectively.

Requests for Information

This financial report is designed to provide a general overview of the Employees' Retirement System of the State of Hawaii's finances. For questions concerning any information in this report or for additional information, contact the Employees' Retirement System of the State of Hawaii, 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813.

Financial Statements (continued)

Combining Statements of Plan Net Assets – All Trust and Agency Funds

June 30, 2008 and 2007

	2008		
	Pension Trust	Agency	
	Employees' Retirement System	Social Security Contribution	Total
Assets			
Cash and short-term investments (notes C(2) and F)			
Cash	$ 41,772,898	$ 4,291	$ 41,777,189
Short-term investments	650,617,640	9,471,937	660,089,577
	692,390,538	9,476,228	701,866,766
Receivables			
Accounts receivable and others	391,174	-	391,174
Investment sales proceeds	318,541,558	-	318,541,558
Accrued investment income	41,405,112	-	41,405,112
Employer appropriations	11,765,521	-	11,765,521
Member contributions	3,742,183	-	3,742,183
	375,845,548	-	375,845,548
Investments, at fair value (notes C(2) and F)			
Equity securities	6,156,177,101	-	6,156,177,101
Fixed income securities	3,258,260,064	-	3,258,260,064
Real estate investments	895,199,859	-	895,199,859
Alternative investments	457,642,073	-	457,642,073
	10,767,279,097	-	10,767,279,097
Other			
Invested securities lending collateral (note F)	1,235,028,470	-	1,235,028,470
Equipment, at cost, net of depreciation	11,358,647	-	11,358,647
	1,246,387,117	-	1,246,387,117
Total assets	13,081,902,300	9,476,228	13,091,378,528
Liabilities			
Disbursements in excess of cash balances (note F)	1,592,615	-	1,592,615
Accounts and other payables	44,341,678	-	44,341,678
Investment commitments payable	954,150,572	-	954,150,572
Due to employers	-	9,476,228	9,476,228
Securities lending collateral (note F)	1,235,028,470	-	1,235,028,470
Total liabilities	2,235,113,335	9,476,228	2,244,589,563
Commitments and contingencies (notes F, G, and H)			
Net assets held in trust for pension benefits (note D) (a schedule of funding progress is presented on page 58)	$ 10,846,788,965	$ -	$ 10,846,788,965

See accompanying notes to financial statements

Financial Statements

2007		
Pension Trust	Agency	
Employees' Retirement System	Social Security Contribution	Total
$ 39,750,805	$ 4,638	$ 39,755,443
722,280,074	18,883,875	741,163,949
762,030,879	18,888,513	780,919,392
1,567,415	-	1,567,415
193,821,486	-	193,821,486
44,093,150	-	44,093,150
10,319,012	-	10,319,012
3,292,043	-	3,292,043
253,093,106	-	253,093,106
7,126,168,687	-	7,126,168,687
2,729,201,034	-	2,729,201,034
874,099,574	-	874,099,574
392,836,211	-	392,836,211
11,122,305,506	-	11,122,305,506
1,457,143,243	-	1,457,143,243
9,610,766	-	9,610,766
1,466,754,009	-	1,466,754,009
13,604,183,500	18,888,513	13,623,072,013
2,853,487	-	2,853,487
57,374,084	-	57,374,084
624,395,820	-	624,395,820
-	18,888,513	18,888,513
1,457,143,243	-	1,457,143,243
2,141,766,634	18,888,513	2,160,655,147
$ 11,462,416,866	$ -	$ 11,462,416,866

Statements of Changes in Plan Net Assets – All Trust Funds

Years ended June 30, 2008 and 2007

	2008	2007
Additions		
Appropriations and contributions (notes A(4) and E)		
Employers	$ 488,770,028	$ 454,494,286
Members	163,375,639	144,658,185
Total contributions	652,145,667	599,152,471
Investment income (note F)		
From investing activities		
Net appreciation (depreciation) in fair value of investments	(779,408,469)	1,375,356,923
Interest on fixed income securities	124,116,798	111,998,129
Income on real estate investments	43,893,125	47,481,937
Dividends on equity securities	112,013,702	95,957,447
Interest on short-term investments	23,169,090	31,023,920
Alternative investment income	32,598,189	70,896,573
Miscellaneous	4,404,811	6,115,828
	(439,212,754)	1,738,830,757
Less investment expenses	31,727,430	37,349,389
Net investment income (loss) from investing activities	(470,940,184)	1,701,481,368
From securities lending activities		
Securities lending income	61,308,269	67,718,394
Securities lending expenses		
Borrower rebates	49,457,874	63,373,456
Management fees	1,973,291	869,038
Less securities lending activities expense	51,431,165	64,242,494
Net investment income from securities lending activities	9,877,104	3,475,900
Total net investment income (loss)	(461,063,080)	1,704,957,268
Total additions	191,082,587	2,304,109,739
Deductions		
Benefit payments (note A(3))	792,312,830	761,004,748
Refunds of member contributions	3,668,857	3,497,590
Administrative expenses	10,728,801	9,601,756
Total deductions	806,710,488	774,104,094
Net increase (decrease) in net assets	(615,627,901)	1,530,005,645
Net assets held in trust for pension benefits (note D)		
Beginning of year	11,462,416,866	9,932,411,221
End of year	$ 10,846,788,965	$ 11,462,416,866

See accompanying notes to financial statements.

June 30, 2008 and 2007

Note A – Description of the ERS

1. General

The Employees' Retirement System of the State of Hawaii (the ERS) began operations on January 1, 1926, having been established by the Territorial Legislature in the preceding year. The ERS is a cost-sharing, multiple-employer public employee retirement system established to administer a pension benefits program for all State and county employees, including teachers, police officers, firefighters, correction officers, judges, and elected officials. The ERS provides retirement, survivor and disability benefits with multiple benefit structures known as the contributory, hybrid and noncontributory plans.

Employer, pensioner, and employee membership data as of March 31, 2008 and 2007 are as follows:

	2008	2007
Employers:		
State	1	1
County	4	4
Total employers	5	5
Pensioners and beneficiaries currently receiving benefits:		
Pensioners currently receiving benefits:		
Police and firefighters	2,925	2,875
All other employees	30,968	30,242
Total pensioners	33,893	33,117
Beneficiaries currently receiving benefits:		
Police and firefighters	175	165
All other employees	2,192	2,042
Total beneficiaries	2,367	2,207
Total pensioners and beneficiaries	36,260	35,324
Terminated vested members entitled to benefits but not yet receiving benefits:		
Police and firefighters	198	185
All other employees	5,649	5,369
Total terminated vested members	5,847	5,554
Current employees:		
Vested:		
Police and firefighters	3,904	3,857
All other employees	37,824	37,500
Nonvested:		
Police and firefighters	1,011	997
All other employees	23,850	22,897
Total current employees	66,589	65,251
Total membership	108,696	106,129

Note A – Description of the ERS (continued)

2. The Financial Reporting Entity

As required by U.S. generally accepted accounting principles, these financial statements present the ERS (the primary government) as a separate reporting entity from the State of Hawaii (the State). The ERS is not part of the State's financial reporting entity because it is a separate legal entity that is fiscally independent of the State. The ERS was established by Chapter 88 of the Hawaii Revised Statutes and is governed by a Board of Trustees (the Board) as discussed below. The ERS is comprised of the Employees' Retirement System and Social Security Contribution Funds.

The Board administers the ERS on behalf of public employees of both the State and county governments. Except for limited administrative functions, the State does not have the power to supervise or control the Board in the exercise of its functions, duties, and powers. The Board consists of eight members. The State Director of Finance is a statutory member of the Board. Four members of the Board are elected by members of the ERS and the other three members of the Board are appointed by the Governor. Decisions are made with the concurring vote of five members of the Board. The Board appoints the Administrator and Chief Investment Officer and engages actuarial and other services required to transact the business of the ERS.

3. Plan Descriptions and Funding Policy

Members of the ERS belong to the contributory, hybrid, or noncontributory plan. All assets of the ERS (in the Pension Trust) may be used to pay benefits to any member of the ERS. Contribution rates are determined by state law. Effective July 1, 2008, the employer contribution rate for employees in the Police and Fire category increased from 15.75% to 19.70%, and the rate for employees in the All Other category increased from 13.75% to 15.00%. These employer contribution rates are applied to the total covered payroll in each respective category to determine the required employer contributions. Administration of the Pension Trust is financed through contributions from the employers and employees (if applicable) and investment earnings.

Employees covered by Social Security on June 30, 1984 were given the option of joining the noncontributory plan or remaining in the contributory plan. All new employees hired after June 30, 1984 and before July 1, 2006, who are covered by Social Security, were generally required to join the noncontributory plan. Qualified employees in the contributory and noncontributory plan were given the option of joining the Hybrid Plan effective July 1, 2006, or remaining in their existing plan. Starting July 1, 2006, all new employees covered by Social Security are required to join the Hybrid Plan.

The three plans provide a monthly retirement allowance equal to the benefit multiplier % (1.25% or 2%) multiplied by the average final compensation (AFC) multiplied by years of credited service. The AFC is the average salary earned during the five highest paid years of service, including the payment of salary in lieu of vacation, or three highest paid years of service, excluding the payment of salary in lieu of vacation, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after this date is based on the three highest paid years of service excluding the payment of salary in lieu of vacation.

Note A – Description of the ERS (continued)

3. Plan Descriptions and Funding Policy (continued)

For post retirement increases, every retiree's original retirement allowance is increased by 2-1/2% on each July 1 following the calendar year of retirement. This cumulative benefit is not compounded and increases each year by 2-1/2% of the original retirement allowance without a ceiling (2-1/2% of the original retirement allowance the first year, 5% the second year, 7-1/2% the third year, etc.).

The following summarizes the three plan provisions relevant to the largest employee groups of the respective plan. Retirement benefits for certain groups, such as police officers, firefighters, some investigators, sewer workers, judges, and elected officials, vary from general employees. All contributions, benefits, and eligibility requirements are governed by Chapter 88 of the Hawaii Revised Statutes. For a more detailed summary of benefits for general employees and a description of special provisions to other groups of employees, refer to the Summary of Retirement Benefit Plan Provisions contained in the *Introductory Section* of this report.

Contributory Plan

General employees in the contributory plan are required to contribute 7.8% of their salary and are fully vested for benefits upon receiving 5 years of credited service. Under the contributory plan, employees may retire with full benefits at age 55 and 5 years credited service, or may retire early at any age with at least 25 years of credited service and reduced benefits. The benefit multiplier is 2% for employees covered by Social Security.

Police officers, fire-fighters, and certain other members that are not covered by Social Security contribute 12.2% of their salary and receive a retirement benefit using the benefit multiplier of 2-1/2% for qualified service, up to a maximum of 80% of AFC. These members may retire at age 55 with 10 years of credited service or at any age with 25 years of credited service, provided the last 5 years of credited service is any of the qualified occupations.

Hybrid Plan

General employees in the Hybrid Plan are required to contribute 6% of their salary and are fully vested for benefits upon receiving 5 years of credited service. Employees may retire with full benefits at age 62 and 5 years of credited service or at age 55 and 30 years of credited service, or may retire at age 55 and 20 years service with reduced benefits. The benefit multiplier used to calculate retirement benefits is 2%.

Noncontributory Plan

General employees in the noncontributory plan are fully vested upon receiving 10 years of credited service. The employer is required to make all contributions for these members. Employees may retire with full benefits at age 62 years and 10 years of credited service or age 55 and 30 years of credited services or age 55 years and 20 years of credited service with reduced benefits. The benefit multiplier used to calculate retirement benefits is 1-1/4%.

Note A – Description of the ERS (continued)

3. Plan Descriptions and Funding Policy (continued)

Ordinary disability retirement benefits require a minimum of ten years of service, whereas service-connected disability resulting from a job-related accident does not have any service requirement. Under all three plans, there is no age requirement.

Ordinary death benefits under the contributory, hybrid, and noncontributory plans require at least one year, five years, and ten years of service, respectively. Under all three plans, there is no service requirement for service-connected death benefits.

Schedule of Funded and Funding Progress

Actuarial valuation date	June 30, 2008
Actuarial value of assets (a)	$11,380,961,003
Actuarial Accrued Liability (AAL)	
Entry Age (b)	$16,549,069,054
Unfunded AAL (UAAL) (b-a)	$5,168,108,051
Percent Funded (a/b)	68.8%
Annual covered payroll (c)	$3,782,102,743
UAAL Percentage of Covered Payroll ((b-a)/c)	137%

Multi-year trend information regarding whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits can be found in the required supplementary information following the *Notes to the Financial Statements.*

Additional information as of the June 30, 2008 actuarial valuation follows:

Valuation date	June 30, 2008
Actuarial cost method	Entry Age Normal
Amortization method	Level percent, open
Remaining amortization period as of June 30, 2008	22.6 years
Asset valuation method	4-year smoothed market
Actuarial assumptions	
Investment rate of return (set by statute) *	8.00%
Projected salary increases *	4.00% to 17.75%
* Includes inflation at	3.00%
Cost of living adjustments (COLAs) **	2.5%

** COLAs are not compounded; they are based on original pension amounts.

4. The ERS as Employer

As an employer, the ERS participates in its pension benefits program, through the State. The ERS provides benefits for all of its full-time employees through the contributory or noncontributory plan. Contributions are calculated as part of the State's total contribution requirements and are reimbursed to the State's General Fund as part of the fringe benefit rate on the ERS' employees' actual salaries.

Note A – Description of the ERS (continued)

4. The ERS as Employer (continued)

The required pension contributions by all participating employers (in thousands) for the years ended June 30, 2008, 2007, and 2006, were $510,727, $476,754, and $423,446, respectively, which represented 13.5%, 13.6%, and 13.1%, of covered payroll. Actual contributions (in thousands) by all employers for the years ended June 30, 2008, 2007, and 2006, were $488,770, $454,494, and $423,446, respectively, which represented 95.7%, 95.3%, and 100.0%, of the required contributions for each year.

5. Other Post Employment Benefits (OPEB)

In addition to the retirement benefits provided by the ERS Pension Trust, the participating employers, pursuant to Hawaii Revised Statutes (HRS) Chapter 87, provides certain health care and life insurance benefits to all qualified employees and retirees.

For employees hired before July 1, 1996, the employer pays the entire monthly healthcare premium for employees retiring with ten or more years of credited service, and 50% of monthly premiums for employees retiring with fewer than ten years of credited services.

For employees hired after June 30, 1996, and who retire with fewer than 10 years of service, the employer makes no contributions. For those retiring with more than 10 years but fewer than 15 years, the employer pays 50% of the retired employees' monthly Medicare or non-Medicare premium. For employees hired after June 30, 1996 and who retire with at least 15 years but fewer than 25 years of credited service, the employer pays 75% of the retired employees' monthly Medicare or non-Medicare premium; for those retiring with over 25 years of credited service, the employer pays the entire healthcare premium.

Retirees are eligible for $2,372 of employer-sponsored, basic life insurance coverage with premiums paid entirely by the employer.

Note B – Social Security Contribution Fund

The Social Security Contribution Fund (Contribution Fund) was established under Section 88-224 of the HRS for the following purposes:

1. To receive all federal Social Security employers' contributions from the State and interest and penalties on unpaid amounts;

2. To receive any appropriations to the Contribution Fund;

3. To pay amounts required to be paid to the Internal Revenue Service (IRS); and

4. To invest and collect income on resources held by the Contribution Fund.

Note B – Social Security Contribution Fund (continued)

All other non-State governmental agencies remit Social Security contributions directly to the IRS. Social Security contributions withheld from employees are remitted directly to the IRS by the employers. The Contribution Fund is considered an agency fund for financial reporting purpose

Note C – Summary of Accounting Policies

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

1. Basis of Accounting

Fiduciary funds are used to account for assets held by the ERS in a trustee capacity or as an agent for individuals, private organizations, other governments, and/or other funds. The fiduciary fund types used by the ERS are a pension trust fund and an agency fund. Each of the fiduciary funds is considered a separate fiscal and accounting entity with a self-balancing set of accounts that comprise its assets, liabilities, equity, revenues and expenditures, or expenses, as appropriate. The accounting and reporting treatment applied to a fund is determined by its measurement focus. The Pension Trust Fund is accounted for on a flow of economic resources measurement focus. As an agency fund, the Contribution Fund is custodial in nature and does not measure results of operations.

The financial statements are prepared using the accrual basis of accounting under which expenses are recorded when the liability is incurred, and revenues are recorded in the accounting period in which they are earned and become measurable. Employer and member contributions are recognized in the period in which the contributions are due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Investment purchases and sales are recorded as of their trade date. Administrative expenses are financed exclusively with investment income.

2. Investments

Pursuant to Sections 88-119 and 88-119.5 of the HRS, the Pension Trust Fund may invest in real estate loans and mortgages; preferred and common stocks; government obligations; corporate obligations; certain other debt obligations (such as obligations secured by collateral of certain other authorized securities listed here, obligations issued or guaranteed by certain development banks, insurance company obligations); real property; alternative investments; and other securities and futures contracts. The investment decision is further dictated by internal investment policies and asset allocation established by the Board. Assets in the Pension Trust Fund may be invested in any of these assets, while investments in the Contribution Fund are limited to investment grade, short-term marketable securities.

Investments are reported at fair value. Where appropriate, the fair value includes disposition costs. Short-term investments are reported at cost, which approximates fair value. Securities (categorized as fixed-income, equity, index funds, and alternative investments) traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments. Fair values of limited partnership investments are based on valuations of the underlying companies of the

Note C – Summary of Accounting Policies (continued)

2. Investments (continued)

limited partnerships as reported by the general partner. Fair values of commingled funds are determined based on the underlying asset values. The fair value of real estate investments is based on independent appraisals and estimated values. Investments that do not have an established market are reported at estimated fair value.

3. Interest and Earnings Allocation

Pursuant to Sections 88-21 and 88-107 of the HRS, the Board shall annually allocate interest and other earnings of the Pension Trust Fund to the funds of the Pension Trust Fund, as follows:

a. Annuity Savings Fund – Fixed at 4-1/2% regular interest rate

b. Expense Fund – To be credited with all money to pay the administrative expenses of the ERS

c. Pension Accumulation Fund – To be credited with any remaining investment earnings.

4. Risk Management

The ERS reports liabilities, as discussed in note G, related to certain types of losses (including torts, theft of, damage to, or destruction of assets, errors or omissions, natural disasters, and injuries to employees) when it is probable that the losses have occurred and the amount of those losses can be reasonably estimated.

5. New Accounting Pronouncements

During 2008, ERS adopted the provisions of the following Government Accounting Standards Board Statements (GASB):

GASB Statement No. 50, *Pension Disclosures*: This Statement amends GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27, *Accounting for Pensions by State and Local Governmental Employers,* by requiring: how state and local governments should account for and report their costs and obligations related to OPEB, including post-employment benefits healthcare and other non-pension benefits. Including disclosure in the notes to the financial statements of pension plans and certain employer governments of the current funded status of the plan—in other words, the degree to which the actuarial accrued liabilities for benefits are covered by assets that have been set aside to pay the benefits—as of the most recent actuarial valuation date. Governments participating in multi-employer cost-sharing pension plans are required to discuss how the contractually required contribution rate is determined.

Note C – Summary of Accounting Policies (continued)

6. **Use of Estimates**

In preparing financial statements in conformity with U.S. generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investments in venture capital and other alternative assets tend to be illiquid and the underlying assets are generally not publicly traded companies. Because of the inherent uncertainty in valuing privately held securities, the fair value may differ from the values that would have been used had a ready market for such securities existed, and the difference can be material. Accordingly, the realized value received upon the sale of the asset may differ from the recorded fair value.

Note D – Description of Funds

Section 88-109 of the HRS requires the establishment and maintenance of specific funds within the ERS. The funds in the Pension Trust Fund and their purposes are described hereunder:

1. **Pension Accumulation Fund**

To accumulate contributions made by the State and counties, transfers of retired members' contributions plus related interest income from the Annuity Savings Fund and income from investments. All pension benefits, including the pensioners' bonus, are paid through this fund.

2. **Annuity Savings Fund**

To accumulate members' contributions and related interest income. Upon a member's retirement, the accumulated contributions and related interest income are transferred to the Pension Accumulation Fund or refunded to the member upon termination.

3. **Expense Fund**

To pay all the expenses necessary in connection with the administration and operation of the ERS. The Board estimates the amount of money necessary to be paid into the expense fund for the ensuing biennium to provide for the expense of operation of the ERS, and pays that amount into the expense account from the investment earnings of the ERS, subject to review by the legislature and approval by the Governor.

Note D – Description of Fund (continued)

Net assets held in trust for pension benefits as of June 30, 2008 and 2007 are as follows:

	2008	2007
Pension Accumulation Fund	$ 9,726,795,072	$ 10,437,314,519
Annuity Savings Fund	1,105,627,636	1,010,643,989
Expense Fund	14,366,257	14,458,358
Total net assets held in trust for pension benefits	$ 10,846,788,965	$ 11,462,416,866

Note E – Contributions

The ERS' funding policy provides for periodic employer contributions at actuarially determined rates, expressed as a percentage of annual covered payroll, such that the employer contributions, along with employee contributions and an actuarially determined rate of investment return, are adequate to accumulate sufficient assets to pay benefits when due. The funding method used to calculate the total employer contribution required is the entry age normal actuarial cost method. Employer contributions are governed by Chapter 88 of the HRS.

Effective July 1, 2005, employer contribution rates are a fixed percentage of compensation, including the normal cost plus amounts required to pay for the unfunded actuarial accrued liability. Employers contribute 15.75% for their police officers and firefighters, and 13.75% for all other employees. These rates increased, as of July 1, 2008, to 19.70% for their police officers and firefighters, and 15.00% for all other employees. Employer rates are set by statute based on the recommendation of the ERS actuary resulting from an experience study conducted every five years.

Prior to July 1, 2005, the actuary calculated an annual contribution amount for the employer contribution consisting of the "normal cost" plus the level annual payments required to amortize the unfunded actuarial accrued liability over the closed period ending June 30, 2029. The employer normal cost is the level percentage of payroll contribution required to pay all benefits. Actuarial gains and losses resulting from differences between actual and assumed experience are reflected in the employer unfunded accrued liability. The FY 2006 annual required employer contributions shown as part of the comparative reporting requirements was determined as part of actuarial valuations dated June 30, 2003.

Member contributions rates are statutorily established in accordance with Chapter 88 of the HRS, and are discussed in note A.3. Plan Descriptions and Funding Policy above.

Note F – Deposits and Investment Risk Disclosures

1. Deposits

Custodial Credit Risk for Deposits is the risk that in the event of a bank failure, the ERS' deposits may not be returned to them. The ERS has not adopted a formal policy specific to custodial credit risk. The ERS' policy is to deposit cash in excess of operating requirements in income producing investments to maximize investment income.

The deposits are held in several financial institutions, including the custodian bank for processing investment transactions. Per State statute, deposits, held by banks located in the State, in excess of Federal Deposit Insurance Corporation (FDIC) coverage are guaranteed by securities pledged as collateral by the bank with the State Director of Finance. Uninsured and uncollateralized amounts are primarily cash held by the investment custodian for settlement of investment transactions. The float caused by outstanding checks in the operating funds is invested, thus causing a possible negative book balance. Deposits are presented in the basic financial statements at cost, which represents market or fair value. The float for outstanding checks is included in the liabilities section of the Combining Statement of Plan Net Assets.

At June 30, 2008 and 2007, the carrying amount of deposits totaled approximately $40,184,574 and $36,901,956, respectively, and the corresponding bank balance was $44,110,631 and $41,485,673, respectively, of which $43,561,227 and $40,464,695, respectively, were exposed to custodial credit risk. The following shows the aggregate book and bank balances of all cash accounts.

	June 30, 2008	June 30, 2007
Carrying Amounts of Deposit - Book		
Cash	$ 41,777,189	$ 39,755,443
Disbursements in excess of cash balances	(1,592,615)	(2,853,487)
Total book balances	$ 40,184,574	$ 36,901,956
Depository Account - Bank Investment Custodian		
Insured	$ 549,404	$ 1,020,978
Subject to custodial credit risk		
Uninsured and collateral held by pledging bank's trust department not in the ERS' name (in name of Director of Finance, State of Hawaii)	3,288,164	13,782,327
Uninsured and uncollateralized	40,273,063	26,682,368
Total subject to custodial credit risk	43,561,227	40,464,695
Total bank balances	$ 44,110,631	$ 41,485,673

Note F – Deposits and Investment Risk Disclosures (continued)

2. Investments

As a long-term investor, the ERS has established through its investment policy that preservation of capital is the primary goal of the ERS. Preservation of capital is to be attained with a consistent, positive return for the fund by diversifying the investment portfolio. The ERS recognizes risk associated for individual securities or asset classes may be reduced through diversification. Investments will be prudent and consistent with the best investment practices, in accordance with the Board's asset allocation strategy, assigned investment mandate, and in compliance with Chapter 88, HRS, as amended. The following table shows the investments of the ERS by investment type as of June 30, 2008 and 2007. Please refer to note C(2) above for a discussion of fair value on investments.

Investments	**June 30, 2008**	**June 30, 2007**
Short-term securities pool, Social Security Contribution Fund	$ 9,471,937	$ 18,883,875
Short-term securities, domestic	32,000,524	159,098,586
Short-term securities, international	13,224,380	-
Short-term securities pools	605,293,129	561,179,706
Fixed income securities, domestic	1,959,136,223	1,611,024,030
Fixed income securities, international	845,612,034	632,546,774
Equity securities, domestic	2,470,161,206	2,858,873,667
Equity securities, international	1,652,032,945	1,733,026,613
Real estate investments	895,199,859	874,099,574
Alternative investments	457,642,073	392,836,211
Equity securities, domestic (pooled including index funds)	974,163,732	1,185,994,744
Equity securities, international (pooled including index funds)	288,658,161	376,602,907
Fixed income securities, domestic (pooled)	-	13,390,731
Investments held by broker-dealers under securities lending program (excluding securities sold, pending trade settlement):		
Short-term investments, domestic	99,607	2,001,782
Fixed income securities, domestic	431,995,246	356,394,279
Fixed income securities, international	21,516,561	115,845,220
Equity securities, domestic	548,282,911	655,901,260
Equity securities, international	222,878,146	315,769,496
Total investments	$ 11,427,368,674	$ 11,863,469,455
Securities lending collateral pool	$ 1,235,028,470	$ 1,457,143,243

3. Credit Risk Debt Securities

The ERS' fixed-income managers are assigned a domestic - "core bond" or "core bond plus" – or an international mandate by the Board. The ERS expects its debt securities investment managers to maintain diversified portfolios by using the following guidelines:

- Securities with a quality rating of below BBB are considered below investment grade.
- Invest in commercial paper (rated A1/P1); certificates of deposits and bankers acceptance; U.S. government and agency securities; 144A private placements; convertible bonds; collateralized mortgage obligations and asset backed securities; and corporate debt issues rated BBB or better.

Note F – Deposits and Investment Risk Disclosures (continued)

3. Credit Risk Debt Securities (continued)

- Domestic managers assigned a "core bond plus" mandate may:
  - Invest in preferred stock up to 10% of portfolio market value.
  - Allocate up to 15% in below investment grade or nonrated instruments, but the average credit rating for this "high yield" portion may not be below B rating.
    - Emerging market debt of up to 7.5% of portfolio (counted against the 15% below investment grade limit) must be owned by U.S. dollar denominated issues only; must be B rating or higher; and limited to countries in the JP Morgan Emerging Bond Index.
  - Allocate up to 15% of portfolio to non-U.S. dollar bonds (exclusive of any emerging market debt, which is applied to high yield allocation as outlined above).
- International managers may:
  - Not invest in U.S. dollar denominated securities, with the exception of cash equivalents.
  - Invest in foreign government securities and foreign corporate debt issues as described above for domestic securities.
  - Foreign debt securities are restricted to BBB or better quality rating.
  - Invest up to 10% of portfolio in emerging market debt and emerging market currency.

A table of the ERS' fixed income securities as of June 30, 2008 and 2007 is below. The weighted quality rating average of the domestic debt securities, excluding pooled investments, at June 30, 2008 is AA and the fair value of below grade investments is $135,893,053 or 5.7% of domestic securities in the portfolio. The weighted average of the international debt securities investments at June 30, 2008 is AA and the fair value of below grade investments is $32,998,931 or 3.8% of the international allocation. On June 30, 2007, the weighted quality rating average of the domestic debt securities, excluding pooled investments, is AA and the fair value of below grade investments is $77,734,963 or 3.9% of the domestic securities. The weighted average of the international debt securities investments is AA and the fair value of below grade investments is $11,341,361 or 1.5% of the international section. All short-term investments, not held in a pooled investment, are rated A1/P1 or better.

4. Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, the ERS will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. All securities, except certain pooled funds, are registered in the name of the ERS and are held in the possession of the ERS' custodial bank, State Street Bank and Trust. Pooled funds not held by the custodial bank, such as certain equity investments, are registered in the name of the ERS.

5. Concentrations of Credit Risk

The ERS' debt securities managers are expected to maintain diversified portfolios by sector, quality, and maturity as discussed above in Credit Risk Debt Securities.

Equity securities shall be diversified by industry and in number. An investment manager may not hold more than 5% of an individual company's stock; if that company's securities represent

Note F – Deposits and Investment Risk Disclosures (continued)

5. Concentrations of Credit Risk (continued)

less than 3% of the investment manager's respective benchmark. (If those securities constitute more than 3% of the respective benchmark, then the manager shall not hold more than the benchmark weight plus 2 percentage points.)

At June 30, 2008 and 2007, there was no single issuer exposure within the ERS' portfolio that comprises over 5% of the overall portfolio, or an investment that exceeded the above manager guidelines, and therefore, there is no concentration of credit risk.

Quality Rating	June 30, 2008			June 30, 2007		
	Domestic	International	Total	Domestic	International	Total
AAA	$ 541,283,140	$ 414,288,738	$ 955,571,878	$ 1,332,811,754	$ 428,110,027	$ 1,760,921,781
AA	129,171,228	202,741,005	331,912,233	78,297,331	162,590,549	240,887,880
A	190,575,081	160,126,391	350,701,472	130,451,269	114,288,974	244,740,243
BBB	131,934,681	56,973,530	188,908,211	115,832,996	32,061,083	147,894,079
BB	57,217,546	22,866,780	80,084,326	36,867,425	8,416,818	45,284,243
B	55,153,681	10,194,498	65,348,179	33,973,492	2,924,543	36,898,035
CCC	5,204,316	-	5,204,316	1,666,188	-	1,666,188
C	112,950	-	112,950	2,182,576	-	2,182,576
D	-	-	-	104,000	-	104,000
Not rated	18,204,559	(62,347)	18,142,212	2,941,282	-	2,941,282
Total credit risk debt securities	1,128,857,182	867,128,595	1,995,985,777	1,735,128,313	748,391,994	2,483,520,307
U.S. government and agencies	1,262,274,287	-	1,262,274,287	245,680,727	-	245,680,727
Total debt securities investment	$ 2,391,131,469	$ 867,128,595	$ 3,258,260,064	$ 1,980,809,040	$ 748,391,994	$ 2,729,201,034

6. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The ERS has not adopted a formal policy that limits investment maturities as a means of managing its exposure to fair value changes arising from changing interest rates. External investment managers are given full discretion within their operational guidelines and are expected to maintain a diversified portfolio between and within sectors, quality, and maturity.

Duration is a measure of a debt investment's exposure to fair value changes arising from changes in interest rates. It uses the present value of cash flows, weighted for those cash flows as a percentage of the investment's full price. At June 30, 2008 and 2007, the table below shows fixed income investment securities by investment type, amount, and the effective

Note F – Deposits and Investment Risk Disclosures (continued)

6. Interest Rate Risk (continued)

weighted duration for the ERS' total portfolio. Interest rate risk associated with swaps and other derivative instruments are discussed in the derivatives disclosure below:

Effective Duration of Fixed Income Assets by Security Type

	June 30, 2008		June 30, 2007	
	Fair value	Effective Weighted Duration (Years)	Fair Value	Effective Weighted Duration (Years)
Domestic Fixed Income Securities				
Asset backed securities	$ 70,097,972	0.4	$ 74,108,376	1.9
Commercial mortgage backed securities	31,202,698	4.7	81,552,583	5.2
Corporate bonds	585,863,914	4.4	402,026,205	4.4
Fixed income options, futures, and swaps	(6,773,761)	n/a	673,236	n/a
Government agencies	56,433,923	3	27,728,196	6.8
Government bonds	-	n/a	45,415,996	2.6
Government mortgage backed securities	1,102,982,600	4.6	974,667,804	8.0
Municipal/provincial bonds	7,145,676	11.6	-	n/a
Non-government backed CMOs	155,106,878	1.6	114,270,527	1.9
Other fixed income	9,932,411	0.3	16,482,313	n/a
U.S. Treasuries	379,139,158	7	243,883,804	5.6
Total fixed income securities, domestic	$ 2,391,131,469	4.6	$ 1,980,809,040	6.3
International Fixed Income Securities				
Asset backed securities	$ 12,587,964	0.1	$ 278,021	1.5
Corporate bonds	234,033,156	4.1	274,159,272	5.4
Fixed income options, futures, and swaps	(1,951,628)	n/a	3,172,029	n/a
Government agencies	175,222,843	6.2	402,128	3.7
Government bonds	397,603,283	6.2	458,712,424	6.3
Municipal/provincial bonds	30,693,676	3.9	-	n/a
Non-government backed CMOs	11,617,277	0.1	-	n/a
Other fixed income	7,322,024	0	11,668,120	0.4
Total fixed income securities, international	$ 867,128,595	5.4	$ 748,391,994	5.9
Fixed Income Securities - All	$ 3,258,260,064	4.6	$ 2,729,201,034	6.2

7. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. The foreign currency risk exposure to the ERS arises from the international fixed income and international equity investment holdings.

Board policy limits the use of foreign currency as a defensive measure to protect the portfolio value of non-U.S. equity and non-U.S. fixed income investments. External investment managers authorized to invest in these securities are given full discretion regarding their respective portfolio's foreign currency exposures, including using currency forward contracts, as established by their investment mandate. Cross-hedging is only allowed in non-U.S. fixed income portfolios. Counterparties for foreign currency derivatives must be rated A or equivalent. Derivatives investments are discussed in more detail below.

Note F – Deposits and Investment Risk Disclosures (continued)

7. Foreign Currency Risk (continued)

The following table summarizes the ERS' exposure to foreign currency risk in U.S. dollars as of June 30, 2008 and 2007. (Amounts are in millions, and securities denominated in U.S. dollars are not presented.)

Currency (dollars in millions)	June 30, 2008				June 30, 2007			
	Cash and STIF	Fixed Income	Equity	Total	Cash and STIF	Fixed Income	Equity	Total
Australian Dollar	$ 5	38	47	$ 90	$ -	$ 17	$ 54	$ 71
Brazilian Real	-	1	20	21	-	1	11	12
New Bulgarian Lev	-	-	2	2	-	-	1	1
Canadian Dollar	15	9	15	39	-	3	7	10
Czech Koruna	-	-	3	3	-	-	3	3
Danish Krone	-	9	9	18	-	5	9	14
Egyptian Pound	-	-	2	2	-	-	-	-
Euro	-	349	555	904	5	261	649	915
British Pound Sterling	8	65	244	317	4	45	304	353
Hong Kong Dollar	5	-	61	66	-	-	74	74
Hungarian Forint	-	-	5	5	-	13	7	20
Indonesian Rupiah	-	-	6	6	-	-	1	1
Israeli Shekel	-	-	3	3	-	-	3	3
Japanese Yen	4	146	281	431	7	187	282	476
Korean Won	-	-	27	27	-	-	47	47
Mexican Peso	-	-	17	17	-	-	15	15
Malaysian Ringgit	-	-	-	-	-	-	2	2
Norwegian Krone	-	-	29	29	-	12	16	28
New Zealand Dollar	-	28	-	28	-	20	-	20
Polish Zloty	-	46	9	55		34	13	47
Romanian Leu	-	-	1	1	-	-	4	4
Swedish Krona	1	9	8	18	-	-	35	35
Singapore Dollar	2	-	14	16	-	13	19	32
Swiss Franc	-	-	97	97	-	-	115	115
Thai Baht	-	-	8	8	-	-	11	11
New Turkish Lira	-	-	10	10	-	-	14	14
New Taiwan Dollar	1	-	25	26	-	-	26	26
South African Rand	-	-	4	4	-	21	6	27
Pooled investments (multi-currency)	-	-	289	289	-	-	377	377
Total	$ 41	$ 700	$ 1,791	$ 2,532	$ 16	$ 632	$ 2,105	$ 2,753

8. Securities Lending

The ERS participated in a securities lending program administered by its bank custodians. Under this program, which is permissible under Chapter 88 of the HRS, certain equity and fixed-income securities of the ERS were lent to participating broker-dealers and banks (borrowers). In return, the ERS received cash, securities issued or guaranteed by the U.S. government, and/or letters of credit as collateral. The ERS did not have the ability to pledge or sell collateral securities absent of borrower default. Borrowers were required to deliver

Note F – Deposits and Investment Risk Disclosures (continued)

8. Securities Lending (continued)

collateral for each loan equal to: (a) in the case of loaned fixed-income securities and loaned equity securities denominated in U.S. dollars or whose primary trading market was located in the U.S., 102% of the market value of the loaned securities; and (b) in the case of loaned equity securities not denominated in U.S. dollars or whose primary trading market was not located in the U.S., 105% of the market value of the loaned securities. The collateral was marked to market daily. If the market value of the collateral fell below the minimum collateral requirements, additional collateral was provided. Securities on loan for cash collateral with the broker dealers are identified in the schedule of investments above; securities on loan for securities collateral are classified according to the underlying security. At June 30, 2008 and 2007, the ERS had no credit risk exposure to borrowers because the market value of collateral held by the ERS exceeded the market value of securities loaned. As of June 30, 2008 and 2007, the market value of securities loaned amounted to approximately $1,224,772,471 and $1,445,912,037, respectively, and the associated collateral amounted to approximately $1,264,158,946 and $1,484,810,018 (of which $1,235,028,470 and $1,457,143,243 was in the form of cash), respectively. In addition, the bank custodians indemnified the ERS by agreeing to purchase replacement securities or return cash collateral in the event the borrower failed to return the loaned security or failed to pay the ERS for income distributions by the securities' issuers while the securities are on loan.

The ERS did not impose any restrictions on the amount of loans the bank custodian made on behalf of the ERS. Also, the ERS and the borrowers maintained the right to terminate securities lending transactions on demand. Cash collateral is invested in the lending agent's short-term investment pool. As such, the maturities of the investments made with cash collateral generally did not match the maturities of the securities loans. The extent of such mismatch as of June 30, 2008 and 2007 was 73 and 64 days, respectively.

9. Derivative Financial Instruments

Derivatives are instruments (securities or contracts) whose value is dependent on such things as stock or bond prices, interest rate levels, or currency exchange rates. These are financial arrangements between two parties whose payments are based on or "derived" from the performance of some agreed-upon benchmark. As with any investment, derivative contracts are subject to various types of credit and market risks. Notably, these would include the possible inability of a counterparty to meet the terms of the contract, changes in the market value of the underlying collateral, or changes in the interest rate environment. The ERS enters into various derivative investment contracts to hedge, for the minimization of transaction costs and as a means of implementing value added strategies to enhance returns as authorized by Board policy.

Generally, derivatives are subject both to market risk and counterparty risk. The derivatives utilized by the ERS typically have no greater risk than their physical counterparts, and in many cases are offset by exposures elsewhere in the portfolio. Counterparty risk, the risk that the "other party" to a contract will default, is managed by utilization of exchange traded futures and options where practicable (in which case the futures exchange is the counterparty and

Note F – Deposits and Investment Risk Disclosures (continued)

9. Derivative Financial Instruments (continued)

guarantees performance) and by careful screening of counterparties where use of exchange traded products is impractical or uneconomical. The ERS anticipates that counterparties will be able to satisfy their obligations under the contracts.

Derivative securities are priced and accounted for at their fair value. For exchange traded securities such as futures and options, closing prices from the securities exchanges are used. For fixed income derivatives such as collateralized mortgage obligations (CMOs), commercial pricing services (where available) or bid-side prices from a broker/dealer are used. Foreign exchange contracts are valued at the price at which the transaction could be settled by offset in the forwards markets.

The tables on the following pages summarize certain of the ERS' investments in derivative securities and contracts, held at June 30, 2008 and 2007, and their associated credit and market risks are described as follows: including currency forwards, futures, options and swaps. The notional values associated with these derivative instruments are generally not recorded in the financial statements; however, the amounts for the exposure (unrealized gains/losses) on these instruments are recorded. Interest risks associated with these investments are included in the tables. Investments in limited partnerships and commingled funds may include derivatives that are not shown in the derivative totals.

Forward Currency Exchange Contracts

The ERS enters into various forward currency exchange contracts to manage exposure to changes in foreign currency exchange rates and to facilitate the settlement of foreign security transactions. A forward contract is an agreement to buy or sell a specific amount of currency at a specific delivery or maturity date for an agreed-upon price. Risks associated with such contracts include movements in the value of the foreign currency relative to the U.S. dollar and the ability of the counterparty to perform in accordance with the terms of the contract. Changes in the market value of open and closed forward contracts are recorded as net appreciation (depreciation) in fair value of investments in the Statement of Changes in Plan Net Assets – All Trust Funds. The fair value of forward currency exchange contracts outstanding at June 30, 2008 and 2007 is as follows:

	June 30, 2008	June 30, 2007
Forward currency purchases	$ 853,882,344	$ 527,342,712
Forward currency sales	(856,669,031)	(527,168,018)
Unrealized gains (losses)	$ (2,786,687)	$ 174,694

Note F – Deposits and Investment Risk Disclosures (continued)

9. Derivative Financial Instruments (continued)

Futures

Futures represent commitments to purchase (asset) or sell (liability) securities at a future date and at a specified price. Futures contracts are traded on organized exchanges (exchange traded) thereby minimizing the ERS' credit risk. The net change in the futures contracts value is settled daily in cash with the exchanges. Net gains or losses arising from the daily settlements are included in the net appreciation in fair value of securities in the Statement of Changes in Plan Net Assets – All Trust Funds. At June 30, 2008 and 2007, the ERS' investments had the following balances:

Futures Contracts ***(Value covered by Contract)***	**June 30, 2008**	**June 30, 2007**
Long - cash and cash equivalents - futures	$ (3,217,203)	$ 58,014,730
Short - cash and cash equivalents - futures	804,856,871	(1,831,291)
Long - debt securities - futures	(72,539,416)	1,732,719,077
Short - debt securities - futures	183,780,816	-
Unrealized gains	$ 912,881,068	$ 1,788,902,516

Options

Options represent or give the buyers the right, but not the obligation, to buy or sell an asset at a preset price over a specified period. The option's price is usually a small percentage of the underlying asset's value. As a writer of financial options, the ERS receives a premium at the outset of the agreement and bears the risk of an unfavorable change in the price of the financial instrument underlying the option. As a purchaser of financial options, the ERS pays a premium at the outset of the agreement and the counterparty bears the risk of an unfavorable instrument underlying the option.

At June 30, 2008 and 2007, the ERS' investments had the following option balances:

Options	**June 30, 2008**	**June 30, 2007**
Cash and cash equivalents purchased call options	$ -	$ 1,462,517
Cash and cash equivalents written call options	-	(7,613)
Cash and cash equivalents purchased put options	-	501,558
Cash and cash equivalents written put options	-	(4,000)
Fixed income purchased call options	2,180,705	935,297
Fixed income written call options	(4,261,589)	(1,281,011)
Fixed income purchased put options	236,454	52,009
Fixed income written put options	(572,350)	(18,399)
Unrealized gains (losses)	$ (2,416,780)	$ 1,640,358

Note F – Deposits and Investment Risk Disclosures (continued)

9. Derivative Financial Instruments (continued)

Mortgage-Backed Securities

The ERS invests in mortgage-backed securities issued or backed by the U.S. government or its agencies, or corporate issues rated AAA by at least one of the major rating agencies. A mortgage-backed security depends on the underlying pool of mortgage loans to provide the cash flow to make principal and interest payments on the security. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. For example, if interest rates decline and homeowners refinance mortgages, thereby prepaying the mortgages underlying these securities, the cash flows from interest payments are reduced and the value of these securities declines. Conversely, if homeowners pay on mortgages longer than anticipated, the cash flows are greater and the return on the investment would be higher than anticipated. A collateralized mortgage obligation (CMO) is a mortgage-backed security that is comprised of classes of bonds created by prioritizing the cash flows of the underlying mortgage pool. Mortgage-backed securities held by the ERS as of June 30, 2008 and 2007 are presented in the tables within this note.

Swaps

Swaps represent an agreement between two or more parties to exchange sequences of cash flows over a period in the future. At June 30, 2008 and 2007, the ERS had interest rate, credit default swaps, and total return swaps as allowed by Board policy. In the most common type of interest rate swap arrangement, one party agrees to pay fixed-interest payments on designated dates to a counterparty who, in turn, agrees to make return interest payments that float with some reference rate. Credit default swaps are the most common global credit market derivative that allows flexibility as an active portfolio management tool based on its ability to customize the exposure to corporate credit such as credit spreads and default risks. Total return swaps combine both market risk and credit risk in a single product as the holder also receives capital gains or losses. Credit default spreads and total return swaps are also used to gain access to global markets that do not have the transparency or efficiency of the U.S. credit markets. Gains and losses from swaps are determined on market values and are included in the net appreciation in fair value of securities in the Statement of Changes in Plan Net Assets – All Trust Funds.

Derivatives, such as interest rate swaps, total return swaps, and credit default swaps, are a tool or instrument used to manage interest rate, credit quality, and yield curve exposures of the investments. In certain situations, derivatives may result in a lower overall cost to the portfolio than owning individual securities underlying the derivatives. When evaluating securities, risk and return are measured at the security and portfolio levels.

Note F – Deposits and Investment Risk Disclosures (continued)

9. Derivative Financial Instruments (continued)

Swaps (continued)

On June 30, 2008 and 2007, the ERS' investments had the following market value balances as shown in the tables below:

Swaps - by Currency	June 30, 2008	June 30, 2007
Interest rate swaps		
in Australian Dollars	$ (410,182)	$ 50,334
in British Pound Sterling	(973,464)	(1,093,177)
in Canadian Dollars	(5,316)	(19,588)
in Euro	1,140,845	3,720,873
in Japanese Yen	(435,233)	89,721
in Mexican Pesos	-	99,932
in United States Dollars	664,126	(639,572)
total	(19,224)	2,208,523
Credit default swaps		
in United States Dollars	(6,232,684)	(7,863)
total	(6,232,684)	(7,863)
Total return swaps		
in United States Dollars	(56,702)	4,247
total	(56,702)	4,247
Unrealized gains (losses)	$ (6,308,610)	$ 2,204,907

Note G – Risk Management

The ERS is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; natural disasters; and injuries to employees. As required by state law, the ERS participates in coverage with the State. The State retains various risks and insures certain excess layers with commercial insurance policies. The excess layers are consistent with the prior fiscal year. Settled claims for the State have not exceeded the coverage provided by commercial insurance policies during the fiscal years ended June 30, 2008 and 2007. Losses not covered by insurance are generally paid from legislative appropriations.

1. Torts

The ERS is involved in various litigation and claims, including claims regarding retirement benefits, the outcome of which cannot be presently determined. In the opinion of management, the outcome of these actions will not have a material adverse effect on the ERS' financial position.

Note G – Risk Management (continued)

2. **Property and Liability Insurance**

   The ERS also purchased property and liability insurance for all real estate owned from outside carriers. During the past three fiscal years, no loss settlements exceeded insurance coverages.

3. **Workers' Compensation Policy**

   The State has a self-insured workers' compensation policy. Workers' compensation claims are paid from legislative appropriations.

Note H – Commitments

In the normal course of business, the ERS enters into commitments with associated risks. The ERS adheres to the same credit policies, financial and administrative controls, and risk limiting and monitoring procedures for these commitments as for all investments.

For the ERS asset allocation plan for investments, the ERS has future financial commitments of up to an additional $292,494,000 as of June 30, 2008, consisting of $85,053,000 in real estate and $207,441,000 in alternative investments. Investment-related financial commitments were $376,066,000 as of June 30, 2007, consisting of $163,798,000 in real estate and $212,268,000 in alternative investments.

Note I – Deferred Compensation Plan

The ERS does not sponsor a deferred compensation program. The ERS' employees are eligible to participate in the deferred compensation plan sponsored by the State. The State-sponsored plan was created in accordance with Internal Revenue Code Section 457. The plan, available to all ERS employees, permits them to defer a portion of their salaries until future years. The deferred compensation is not available to the employees until termination, retirement, death, or an unforeseeable emergency. All compensation deferred under the plan is held in trust by a custodian for the exclusive benefit of participants and beneficiaries.

June 30, 2008

Schedule of Funding Progress
(In thousands)

Actuarial Valuation Date		Actuarial Value of Assets (1)	Actuarial Accrued Liability (AAL) (2)*	Unfunded Actuarial Accrued Liability (3)*= (2)-(1)	Funded Ratio (4)=(1)/(2)	Annual Covered Payroll (5)	UAAL as a Percentage of Annual Covered Payroll (6)=(3)/(5)
June 30:							
2008		$ 11,380,961	$ 16,549,069	$ 5,168,108	68.8%	$ 3,782,103	136.6%
2007	**	10,589,773	15,696,546	5,106,773	67.5%	3,507,040	145.6%
2006	*	9,529,371	14,661,399	5,132,028	65.0%	3,238,267	158.5%
2005		8,914,839	12,985,989	4,071,150	68.6%	3,041,083	133.9%
2004		8,797,133	12,271,331	3,474,198	71.7%	2,865,106	121.3%
2003		9,073,960	11,952,057	2,878,097	75.9%	2,826,682	101.8%

Note: * Assumption changes and new Hybrid Plan effective June 30, 2006.

** New salary scale assumption effective June 30, 2007.

Schedule of Employer Contributions
(In thousands)

	Annual Required Contribution	Actual Contribution	Percentage Contributed
Fiscal year ended June 30,:			
2008	$ 510,727	$ 488,770	95.7%
2007	476,754	454,494	95.3%
2006 *	423,446	423,446	100.0%
2005	328,717	328,717	100.0%
2004	235,686	235,686	100.0%
2003	190,586	190,586	100.0%

* Effective July 1, 2005, the required contributions are based on contribution rates and not specific dollar amounts.

Notes to Required Supplementary Information

June 30, 2008

The information presented in the required supplementary schedules was determined as part of the actuarial valuation at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	June 30, 2008
Actuarial cost method	Entry Age Normal
Amortization method	Level percent, open
Remaining amortization period as of June 30, 2008	22.6 years
Asset valuation method	4-year smoothed market
Actuarial assumptions:	
Investment rate of return (set by statute)*	8.0%
Projected salary increases (set by statute)*	4.0% to 17.75%
*Includes inflation at 3.0%	
Cost-of-living adjustments (COLAs) **	2.5% (not compounded)

** COLAs are not compounded; they are based on original pension amount.

Combining Schedules of Changes in Plan Net Assets – All Trust Funds

Years ended June 30, 2008 and 2007

	2008			
	Pension Accumulation Fund	**Annuity Savings Fund**	**Expense Fund**	**Total**
Additions				
Appropriations and contributions:				
Employers	$ 488,770,028	$ -	$ -	$ 488,770,028
Members		163,375,639	-	163,375,639
Net investment income (loss)	(461,063,080)	-	-	(461,063,080)
Total additions	27,706,948	163,375,639	-	191,082,587
Deductions				
Benefit payments	792,312,830	-	-	792,312,830
Refunds of member contributions	-	3,668,857	-	3,668,857
Administrative expenses	-	-	10,728,801	10,728,801
Total deductions	792,312,830	3,668,857	10,728,801	806,710,488
Other changes in net assets held in trust for pension benefits:				
Transfer due to retirement of members	110,292,076	(110,292,076)	-	-
Transfer of interest allocation	(45,568,941)	45,568,941	-	-
Transfer to pay administrative expenses	(11,025,246)	-	11,025,246	-
Return of unrequired funds due to savings in administrative expenses	388,546	-	(388,546)	-
	54,086,435	(64,723,135)	10,636,700	-
Net increase (decrease)	(710,519,447)	94,983,647	(92,101)	(615,627,901)
Net assets held in trust for pension benefits:				
Beginning of year	10,437,314,519	1,010,643,989	14,458,358	11,462,416,866
End of year	$ 9,726,795,072	$ 1,105,627,636	$ 14,366,257	$ 10,846,788,965

See accompanying independent auditors' report.

Supplementary Information (continued)

Schedule 1

2007			
Pension Accumulation Fund	**Annuity Savings Fund**	**Expense Fund**	**Total**
$ 454,494,286	$ -	$ -	$ 454,494,286
-	144,658,185	-	144,658,185
1,704,957,268	-	-	1,704,957,268
2,159,451,554	144,658,185	-	2,304,109,739
761,004,748	-	-	761,004,748
-	3,497,590	-	3,497,590
-	-	9,601,756	9,601,756
761,004,748	3,497,590	9,601,756	774,104,094
77,225,888	(77,225,888)	-	-
(40,365,159)	40,365,159	-	-
(8,622,888)	-	8,622,888	-
648,724	-	(648,724)	-
28,886,565	(36,860,729)	7,974,164	-
1,427,333,371	104,299,866	(1,627,592)	1,530,005,645
9,009,981,148	906,344,123	16,085,950	9,932,411,221
$ 10,437,314,519	$ 1,010,643,989	$ 14,458,358	$ 11,462,416,866

See accompanying independent auditors' report.

Schedule 2

Social Security Contribution Fund

Statements of Changes in Assets and Liabilities

Years ended June 30, 2008 and 2007

	2008			
	Beginning Balance	**Additions**	**Deductions**	**Ending Balance**
Assets				
Cash	$ 4,638	$ -	$ 347	$ 4,291
Short-term investments	18,883,875	10,650,113	20,062,051	9,471,937
Total assets	$ 18,888,513	$ 10,650,113	$ 20,062,398	$ 9,476,228
Liabilities				
Due to employers	$ 18,888,513	$ 196,186,415	$ 205,598,700	$ 9,476,228
Total liabilities	$ 18,888,513	$ 196,186,415	$ 205,598,700	$ 9,476,228

	2007			
	Beginning Balance	**Additions**	**Deductions**	**Ending Balance**
Assets				
Cash	$ 7,100,059	$ -	$ 7,095,421	$ 4,638
Short-term investments	11,527,246	8,053,819	697,190	18,883,875
Total assets	$ 18,627,305	$ 8,053,819	$ 7,792,611	$ 18,888,513
Liabilities				
Payable to Internal Revenue Service	$ 697,190	$ -	$ 697,190	$ -
Due to employers	17,930,115	184,428,270	183,469,872	18,888,513
Total liabilities	$ 18,627,305	$ 184,428,270	$ 184,167,062	$ 18,888,513

See accompanying independent auditors’ report.

Supplementary Information (continued)

Schedules of Administrative Expenses

Years ended June 30, 2008 and 2007

	2008	2007
Personnel services		
Salaries and wages	$ 4,448,790	$ 4,041,586
Fringe benefits	1,544,787	1,365,619
Net change in unused vacation credits	168,055	(193,167)
Total personnel services	6,161,632	5,214,038
Professional services		
Actuarial	93,000	117,950
Auditing and tax consulting	138,000	118,697
Disability hearing expenses	97,585	68,621
Legal services	310,875	322,494
Medical	416,869	343,154
Other services	488,629	167,543
Total professional services	1,544,958	1,138,459
Communication		
Postage	97,307	83,441
Printing and binding	49,208	6,633
Telephone	60,456	13,456
Travel	34,204	24,536
Total communication	241,175	128,066
Rentals		
Rental of equipment	50,037	54,892
Rental of premises	17,230	15,065
Total rentals	67,267	69,957
Other		
Armored car service	8,671	8,167
Computer and office automation systems	227,187	795,965
Equipment	6,350	1,835
Repairs and maintenance	890,853	624,517
Stationery and office supplies	50,192	46,598
Miscellaneous	78,829	83,159
Total other	1,262,082	1,560,241
Depreciation	1,451,687	1,490,995
	$ 10,728,801	$ 9,601,756

See accompanying independent auditors' report.

Schedule 4

Schedules of Investment Expenses

Years ended June 30, 2008 and 2007

	2008	2007
Investment expenses		
Investment manager/advisor fees	$ 30,710,444	$ 36,893,038
Bank custodian fees	346,500	361,000
Other investment expenses	670,486	95,351
Total investment expenses	31,727,430	37,349,389
Securities lending expenses		
Borrower rebates	49,457,874	63,373,456
Management fees	1,973,291	869,038
Total securities lending expenses	51,431,165	64,242,494
	$ 83,158,595	$ 101,591,883

See accompanying independent auditors' report.

Employees' Retirement System

of the State of Hawaii

INVESTMENT SECTION

Letter from Chief Investment Officer

LINDA LINGLE
GOVERNOR

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

February 8, 2010

Board of Trustees
201 Merchant Street, Suite 1400
Honolulu, HI 96813

Dear Members of the Board:

I am pleased to present investment highlights and performance for the Investment Section of the Comprehensive Annual Financial Report (CAFR) for the fiscal year ending June 30, 2008.

- ERS Plan assets were valued at $10.847 billion as of June 30, 2008. The ERS continues to be ranked as one of the 125 largest defined benefit plans in the United States.

- The ERS investment portfolio outperformed its public fund peer group by 0.9% over the fiscal year, outperformed its Policy Benchmark by 0.3% over the past three years, and by 0.1% over the past five years ending June 30, 2008.

CHALLENGES

During the fiscal year ending June 30, 2008, the stock markets reached their highest peak in history, with the Dow Jones Industrial Average reaching 14,165 on October 9, 2007. While some investors believed that there was no foreseeable end to the creation of wealth that helped to benefit a large number of Americans and other people around the world, some economic observers were unable to believe that economic and market conditions could continue to support such high security valuations without eventually experiencing a significant market correction – and they were right!

Since the peak of the market, a series grim market phenomena and gloomy economic indicators have surfaced, including an increase in defaults on sub-prime residential loans, excessive use of financial leverage, rises in unemployment and inflation, greater volatility in energy prices, wider swings in currency rates, and notable cases of business misdeeds. These kinds of events are merely reflections of an economy and market that may be in need of reckoning.

Employees' Retirement System
of the State of Hawaii

City Financial Tower • 201 Merchant Street, Suite 1400 • Honolulu, Hawaii 96813-2980
Telephone (808) 586-1735 • Fax (808) 586-1677 • http://www4.hawaii.gov/ers

Letter from Chief Investment Officer (continued)

STABILITY

Despite the growing difficulties in the global capital markets, the ERS Investment Office continues to manage Plan assets in conformance with the goals, objectives, and procedures of the ERS Investment Policy ("Policy"). Policy defines the structure by which the investment portfolio is developed, managed, and monitored; it includes the asset allocation strategic targets that further define the optimal mix of stocks, bonds, real estate, and alternative investments. If thoughtfully modeled, the asset allocation strategic targets should yield an optimal balance between attractive rates of return and prudent levels of investment risk. Thus, as the global economy continues to present formidable challenges to institutional investors, it becomes increasingly important that the Plan avoid "chasing returns" and, instead, be committed to its long-term Policy.

PROGRESS

The Policy functions as an anchor for an Investment Program that naturally exists within a dynamic, complex, and evolving global economy. Yet over time, the Policy should periodically be evaluated against shifting market conditions and, if necessary, undergo the appropriate adjustments. As such, staff and the general investment consultant have commenced on a structured approach to expand Policy, such as allowing a greater degree of non-US exposure in response to rising economic growth in many regions of the world.

To be sure, the US and non-US fixed income asset classes are in the process of becoming one global fixed income asset class that should create an enhanced optimal risk-return profile; the public equity, alternative investment, and real estate asset classes will be considered next. Finally, an asset/liability study will be initiated in the near future to determine the appropriate changes to the asset allocation policy and to consider new investment strategies.

Your Investment Office staff is keenly aware that their most important responsibility is to help protect and grow the plan assets leading to the timely payment of retirement benefits for its members and beneficiaries. To that end, we are dedicated to fulfilling that responsibility by practicing the highest degrees of investment management excellence with prudence, care, and integrity.

Respectfully yours,

Rod June

Rod June
Chief Investment Officer

Letter from Investment Consultant

Pension Consulting Alliance, Inc.
Los Angeles • Portland • New York

March 19, 2009

Board of Trustees
Employees' Retirement System of the State of Hawaii
City Financial Tower
201 Merchant Street, Suite 1400
Honolulu, HI 96813-2980

Dear Trustees:

Enclosed is our report on investment activity for the Hawaii Employees' Retirement System for periods ended June 30, 2008, as requested by the Government Financial Officers' Association (GFOA).

Hawaii ERS-Total Fund Performance

The total assets of the Retirement System were $10.8 billion as of June 30, 2008, a decrease of roughly $0.7 billion for the fiscal year. The portfolio generated negative absolute performance with mixed relative results across all of the major asset classes. The decrease in assets was primarily due to poor relative performance within the Domestic Equity and International Equity asset classes. The investment return for the total fund expressed as a time-weighted total rate of return was minus (3.5%) for the 2008 fiscal year, compared to the benchmark's return of minus (3.1%). For the three-year period ending June 30, 2008 the total fund returned +8.3% per annum versus the benchmark's +8.0%, and for the trailing five-year period the total fund posted a return of +10.1% per annum versus the benchmark's +10.0%.

Asset Class Performance

Domestic equity returned minus (11.4%) for the fiscal year, versus the Blended Equity Index's minus (12.8%) and the Northern Trust Domestic Equity Database median of minus (12.3%). Domestic fixed-income was up +6.3% for the fiscal year versus the Lehman Brothers Aggregate Index return of +7.1% and the Northern Trust Fixed-Income Database median return of +6.4%. International equity returned minus (7.9%) for the 2008 fiscal year versus the Blended International Index return of minus (8.3%) whereas international fixed-income returned +14.6% versus the Citigroup Non-US Government Bond Index return of +18.7%. Real Estate gained +7.6% for the year ending June 30, 2008 versus the NCREIF Total Index gain of +13.6%. Alternative investments were a positive contributor to performance, returning +11.4% for the fiscal year.

Market Conditions

Inflation, recession and credit market turmoil set the stage for a challenging market environment for the fiscal year 2008. All equity classes produced negative returns, both in and outside the

United States, with the only exception being emerging markets equity. Fixed income classes produced mixed results. Concerns about solvency of bond insurers and the potential of more big losses at investment banks along with high oil prices caused U.S. Treasuries to outperform other bond market sectors.

During the fiscal year 2008, equities within the U.S. declined by minus (12.7%) while non-U.S. equities declined by minus (10.2%). Developed international equity markets dropped along with U.S. markets driven by the credit turmoil and a weakening global economy. After a tumultuous start the dollar showed some stability towards the end of the fiscal year out-gaining both the Euro and the Japanese Yen during the last quarter of fiscal year 2008.

Trends that began in fiscal year 2007 continued in fiscal year 2008. Growth stocks, as a group, outperform value stocks while stocks of larger companies outpaced stocks of smaller companies. Emerging markets equities remained the one bright spot in global equities, posting a return of +4.9% for the fiscal year. This result was due largely to the favorable growth prospects for the emerging economies relative to developed economies. This dichotomy between developed and developing markets has led some economists to proclaim that the two markets had decoupled.

During the fiscal year, bond markets produced returns mainly in line with expectations. Investment-grade bonds, as measured by the Lehman Brothers Aggregate Bond Index, returned +7.1%. Government bonds outpaced other forms of debt as investor experienced a flight to safety. Mortgage-backed bonds increased by +6.3%, investment-grade corporate bonds rose by +3.8%, and high-yield corporate bonds returned minus (2.3%). Non-U.S. Government bonds experienced strong returns for fiscal year 2008 producing a return of +18.7%. Both U.S. and Non-U.S. Government bonds benefited from a sharp rise in risk aversion towards the end of fiscal year 2008. Interest rate cuts in the U.S. and anticipated rate cuts abroad also added to performance.

Fiscal 2008 proved to be a tale of two halves. It started with what appeared to be a mild to moderate housing market correction in isolated overinflated markets and a re-pricing of risk in lower quality mortgage backed securities. By the fourth quarter it became evident that problems that emerged in a relatively small number of housing markets and in subprime MBS would not be contained and that contagion to other housing and credit markets was inevitable. Throughout the tumultuous market conditions of the past few years, with its constant review and oversight, the Board continues to position the Retirement System for competitive performance consistent with its objectives.

Sincerely,

Pension Consulting Alliance, Inc.

Report on Investment Activity by Investment Consultant

Pension Consulting Alliance, Inc.
Los Angeles • Portland • New York

Report on Investment Activity for the
Employees' Retirement System of the State of Hawaii
Prepared by Pension Consulting Alliance, Inc.
March 2009

Outline of Investment Policies

The primary goal of the Plan is the preservation of capital. The Board of Trustees seeks preservation of capital with a consistent, positive return for the Fund. Although pure speculation is to be avoided, the Board appreciates the fact that an above average return is associated with a certain degree of risk. Risk to be assumed must be considered appropriate for the return anticipated and consistent with the total diversification of the Fund.

Expected Annualized Return and Risk

Based on 2008 capital market projections for 10 years, the target allocation is expected to achieve an average annualized return of 8.4% (5.4% real return with expected inflation of 3.0%). The annual nominal return over this 10-year period is expected to fall within a range of -3.4% and 20.1% two-thirds of the time.

Long-range Asset Allocation Target

The ERS will strategically invest in the following asset classes:

	Strategic Allocation
Domestic Equity	**41%**
International Equity	**17%**
Domestic Fixed-Income	**21%**
International Fixed-Income	**7%**
Equity Real Estate	**9% ***
Alternative Investments	**5% ****

* The real estate target will be the percentage actually invested up to 9% of the total fund. Changes in the real estate target will be offset by an equal percentage change in the domestic equity target.

** The alternatives target will be the percentage actually invested up to 5% of the total fund. Changes in the alternatives target will be offset by an equal percentage change in the domestic equity target.

Report on Investment Activity by Investment Consultant (continued)

Pension Consulting Alliance, Inc.
Los Angeles • Portland • New York

The target is evaluated on the basis of assets designated to each asset class by the Board, rather than on a current invested position. The target will be pursued primarily by cash flow on a long-term basis and will be revised if significant changes occur within the economic and/or capital market environment according to the rebalancing guidelines. The target is to be reviewed annually for reasonableness relative to significant economic and market changes. A formal asset allocation/liability study is conducted at least every three years to verify or amend the targets. The last formal asset allocation/liability study was completed in 2005. At that time, the Board chose to maintain the current strategic asset allocation implemented July 1, 2000. The target was reviewed in 2006. A full asset/liability study will next take place during fiscal year 2009.

Manager Evaluation

Individual domestic and international equity and bond managers are measured against relevant indexes and their respective peer groups of managers. Market indices and peer group benchmarks are assigned to each manager and are intended as a guide for the investment manager to understand the risk/reward posture of their portfolio. Real Estate managers are measured against the median performance of the State Street Real Estate database and the NCREIF Total Index. Managers have full discretion to manage the risk posture of their portfolios relative to their designated market index and may, with conviction and appropriate expertise, execute security strategies not reflected by their market index as long as they conform to the investment guidelines and the laws of the State of Hawaii.

Investment Practices

The full Investment Policy Statement (IPS) describes in detail acceptable investment practices, manager reporting requirements, manager performance guidelines, the distribution of brokerage commissions, and securities lending guidelines. Revisions to the IPS took place during fiscal year 2007, covering manager monitoring criteria and Sudan-related divestment guidelines.

All rates of return are calculated using methodologies that are generally accepted by the Global Investment Performance Standards (GIPS). All domestic equity manager returns are daily, time-weighted rates of return based on custodial data. International equity, domestic fixed-income, and international fixed-income returns are monthly, time-weighted returns. Real estate returns are calculated using statements received directly from the manager. This ensures that the performance is based on accurate cash flows and appraisal values.

Report on Investment Activity by Investment Consultant (continued)

Pension Consulting Alliance, Inc.

Los Angeles • Portland • New York

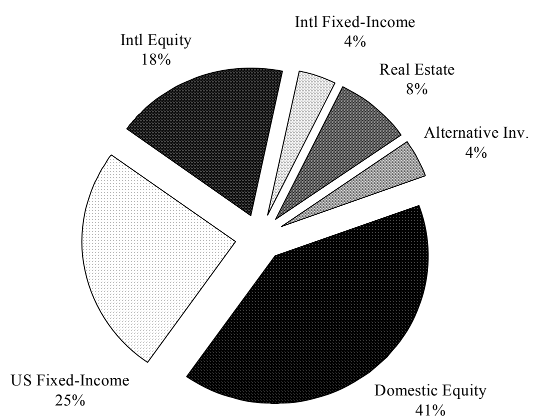
Investment Results as of June 30, 2008:

	Year Ended June 30, 2008	2007	2006	2005	2004	Three Years Ended 6/2008	Five Years Ended 6/2008
Domestic Equity	**(11.39%)**	**20.03%**	**9.39%**	**8.87%**	**21.80%**	**5.17%**	**9.06%**
Standard & Poor's 500	(13.12%)	20.59%	8.64%	6.30%	19.10%	4.41%	7.58%
NT Total Domestic Equity*	(12.32%)	19.75%	10.53%	8.53%	22.22%	5.09%	8.89%
Domestic Fixed-Income	**6.31%**	**6.40%**	**(0.13%)**	**7.21%**	**(1.45%)**	**4.15%**	**3.60%**
Lehman Bros. Aggregate	7.12%	6.12%	(0.81%)	6.80%	0.32%	4.09%	3.86%
NT Domestic Fixed*	6.41%	6.28%	(0.01%)	7.67%	1.30%	4.12%	4.36%
International Equity	**(7.93%)**	**29.81%**	**26.52%**	**17.12%**	**28.02%**	**14.78%**	**17.78%**
MCI EAFE Index	(10.61%)	27.53%	27.07%	14.13%	32.85%	12.84%	16.67%
NT Non-U.S. Equity*	(8.29%)	26.28%	27.17%	14.70%	31.05%	14.94%	18.00%
International Fixed-Income	**14.58%**	**2.00%**	**0.96%**	**7.17%**	**7.87%**	**5.67%**	**6.41%**
Citigroup Non-U.S. World Government Bond Index	18.72%	2.20%	(0.02%)	7.75%	7.60%	6.65%	7.06%
NT Non-U.S. Fixed*	2.65%	5.01%	0.36%	7.52%	7.45%	4.91%	5.49%
Real Estate	**7.64%**	**17.69%**	**27.08%**	**13.70%**	**7.94%**	**17.66%**	**14.86%**
NCREIF Total Property Index	13.58%	17.24%	18.67%	18.02%	10.83%	16.75%	15.07%
NT Real Estate Funds*	5.79%	15.48%	17.88%	19.67%	10.99%	13.61%	15.67%
Alternative Investments	**11.43%**	**22.46%**	**24.56%**	**17.92%**	**18.51%**	**19.30%**	**18.86%**
Total Fund	**(3.51%)**	**17.81%**	**11.50%**	**10.53%**	**15.48%**	**8.26%**	**10.12%**
Composite Benchmark	(3.14%)	16.99%	11.01%	9.78%	16.61%	7.95%	10.00%
NT Public Funds > $1 Billion*	(4.41%)	17.50%	10.18%	10.55%	16.69%	7.35%	10.28%

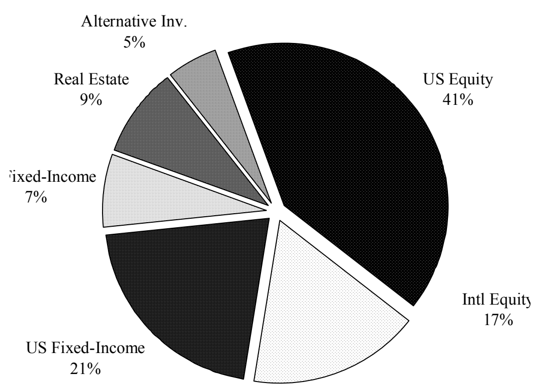
**Universe data provided by Northern Trust: Public Funds (DB) > $1 Billion, Median Results*

Asset Allocation as of June 30, 2008:

Actual Asset Allocation



Target Asset Allocation



Investment Professionals

INVESTMENT MANAGERS

U.S. EQUITIES

Ark Asset Management Co.
Bank of Hawaii
Barrow, Hanley, Mewhinney & Strauss
CM Bidwell & Associates
CS McKee Investment Managers
Denver Investment Advisors
Goldman Sachs Asset Management
Independence Investment Associates
Jennison Associates
Mellon Capital Management Corporation
Oppenheimer Capital Corporation
Systematic Investment Management
T. Rowe Price

REAL ESTATE

Angelo Gordon
Heitman Capital Management
Invesco Realty Advisors
LaSalle Investment Management
CB Richard Ellis

INTERNATIONAL EQUITIES

Acadian Asset Management
JP Morgan Chase
Julius Baer Investment Management
Mercator Asset Management
New Star Institutional Managers
Philadelphia International Advisors
Rexiter Capital Management
State Street Global Advisors

FIXED-INCOME

Bishop Street Capital Management
Bradford and Marzec
Oechsle International Advisors
Pacific Income Advisers
Pacific Investment Management Company
Western Asset Management Company

ALTERNATIVE INVESTMENTS

Abbott Capital Management, LLC
Hancock Timber Resource Group

OTHER SERVICE PROVIDERS

COMMISSION RECAPTURE BROKERS

Knight Equity Markets, LP
LJR Recapture Services
Rochdale Securities Corporation

CUSTODIAL BANK

Northern Trust Company

INVESTMENT ADVISOR

Pension Consulting Alliance, Inc.

Investment Schedules

List of Assets Directly Held (by fair value)*

as of June 30, 2008 (excludes investments in pooled vehicles)

** A complete list of holdings is available for review upon request.*

	Par / Shares	Security	Coupon	Maturity	Standard & Poors	Fair Value
Domestic Fixed Income						
1	146,153,000	Federal Nat Mortg (TBA July 30 Single Family)	5.000%	12/1/2099	AAA	$ 140,078,589
2	109,170,000	United States Treasury Note	3.875%	5/15/2018	AAA	108,257,448
3	100,000,000	Federal Nat Mortg (TBA July 30 Pass Throughs)	5.500%	12/1/2099	AAA	98,562,500
4	47,947,000	Federal Nat Mortg (TBA August 31 Single Family)	5.000%	12/1/2099	AAA	45,849,319
5	35,860,000	United States Treasury Note	3.500%	5/31/2013	AAA	36,126,153
6	35,603,613	Federal National Mortg (Pool 735224)	5.500%	2/1/2035	AAA	35,302,513
7	26,072,000	United States Treasury Note	3.250%	12/31/2009	AAA	26,383,639
8	26,000,000	Federal Nat Mortg (TBA July 30 Single Family)	6.000%	12/1/2099	AAA	26,227,500
9	25,725,000	United States Treasury Bond	4.375%	2/15/2038	AAA	25,073,849
10	22,784,476	Federal National Mortg (Pool 831811)	6.000%	9/1/2036	AAA	23,018,928
International Fixed Income						
1	22,000,000	Government of France	3.000%	1/12/2011	AAA	33,280,312
2	12,097,000	Government of United Kingdom	4.000%	9/7/2016	AAA	22,300,528
3	47,705,000	Republic of Poland	5.750%	3/24/2010	A	22,019,903
4	2,293,300,000	Euro Investment Bank	1.400%	6/20/2017	AAA	21,266,109
5	2,170,000,000	Japan Finance Corp for Municipal Enterprise	2.000%	5/9/2016	AA	21,233,267
6	2,192,000,000	Japan Finance Corp	1.550%	2/21/2012	AA	20,984,308
7	13,800,000	Kingdom of Belgium	4.000%	3/28/2014	AA	20,819,225
8	23,209,000	Landwirt Rentenbk	6.000%	5/30/2013	AAA	20,800,303
9	47,445,000	Republic of Poland	4.750%	4/25/2012	A	20,772,384
10	13,963,000	Freistaat Bayern	3.750%	1/21/2013	AAA	20,615,103
Domestic Equities						
1	767,164	Wal Mart Stores Inc				43,114,617
2	940,165	Qualcomm Inc				41,715,121
3	833,130	Phillip Morris Intl				41,148,291
4	1,489,514	Microsoft Corp				40,976,530
5	421,600	ConocoPhillips				39,794,824
6	409,780	Occidental Pete Corp				36,822,831
7	354,564	Chevron Corp				35,147,929
8	974,332	AT&T Inc				32,825,245
9	276,645	International Business Machines Corp				32,790,732
10	1,400,131	Cisco Systems				32,567,047
International Equities						
1	407,463	Total SA				34,795,225
2	260,721	Research in Motion Ltd				30,478,285
3	247,665	Schlumberger Ltd				26,606,651
4	682,642	ENI				25,490,217
5	8,526,542	Vodafone Group				25,309,408
6	481,260	Weatherford International Ltd				23,865,683
7	1,074,725	Glaxosmithkline				23,805,555
8	381,332	Suncor Entergy Inc				22,163,016
9	739,537	Telefonica SA				19,668,196
10	630,843	AXA				18,745,419

Investment Schedules (continued)

Investments Summary

(Dollar values expressed in thousands)

	Fair Value as of June 30, 2008	Percentage	Fair Value as of June 30, 2007	Percentage
Equity securities				
Common stock	$ 4,865,927	45.19%	$ 5,494,015	49.40%
Index funds	1,103,014	10.24%	1,377,893	12.39%
Pooled and others	187,236	1.74%	254,261	2.29%
	6,156,177	57.17%	7,126,169	64.08%
Fixed income securities				
Mortgage-backed securities	1,289,292	11.97%	1,170,491	10.52%
U.S. Government bonds	379,139	3.52%	289,300	2.60%
Foreign bonds	867,129	8.05%	748,392	6.73%
U.S. corporate bonds	585,864	5.44%	402,026	3.61%
Asset backed securities	70,098	0.65%	74,108	0.67%
Pooled and others	66,738	0.63%	44,884	0.40%
	3,258,260	30.26%	2,729,201	24.53%
Others				
Real estate equities	895,200	8.31%	874,100	7.86%
Alternative investments	457,642	4.26%	392,836	3.53%
	1,352,842	12.57%	1,266,936	11.4%
Total, investments at fair value	$ 10,767,279	100.00%	$ 11,122,306	100.00%

Schedule of Investment Fees

by Asset Class Allocation

(Dollar values expressed in thousands)

	Fair value as of June 30, 2008	Total FY 2008 Investment Fees	Basis Points
Equities			
U.S. equities	$ 4,374,129	$ 13,006	30 bp
International equities	1,954,463	8,967	46
	6,328,592	21,973	35
Fixed Income			
U.S. bonds	2,745,762	3,288	12
International bonds	434,067	1,726	40
	3,179,829	5,014	16
Other Asset Allocations			
Real estate	872,363	1,139	13
Alternative investments	456,697	2,175	48
	1,329,060	3,314	25
Other Investment Services			
Custodian fees	n/a	347	n/a
Investment consultant fees	n/a	409	n/a
Total	$ 10,837,481	$ 31,057	29

Schedule of Broker Commissions

The Employees' Retirement System participates in a Commission Recapture Program with three brokerage firms for equity trades, which are listed in the Investment Professionals section. Domestic and international investment managers are required to direct at least 35% of all brokerage transactions to participating brokers. Commissions charged per share are based on the investment manager's normal rate schedule. All commissions recaptured are used exclusively by the ERS for the benefit of its members and beneficiaries. ERS does not guarantee participating brokers any minimums, required volumes or fees. During the fiscal year ended June 30, 2008 the ERS recaptured $1,513,095 in commissions.

The following is a list of brokers who received $40,000 or more in commissions during Fiscal Year 2008. A complete list of all commissions is available for review upon request.

Brokerage Firms	Shares Traded	Dollar Volume of Trades	Commission Dollar Amount	Commission Per Share
Bank of New York Mellon/BNY Brokerag	21,112,181	$ 588,464,275	$ 636,119	$ 0.030
Credit Suisse First Boston	46,570,970	643,551,811	545,918	0.012
Merrill Lynch Pierce Fenner & Smith	21,825,269	459,241,937	483,014	0.022
J P Morgan Chase Bank	15,580,998	392,086,582	410,166	0.026
Broadcort Capital	13,340,621	378,502,455	409,339	0.031
Citigroup Global Markets	33,755,777	362,669,876	407,471	0.012
Bear Stearns & Co	17,040,752	408,126,853	389,746	0.023
Lehman Brothers	13,435,517	427,380,099	359,658	0.027
INSTINET	14,020,373	334,389,299	328,823	0.023
Pershing DLJ	17,847,470	276,990,842	319,308	0.018
UBS Warburg	22,899,993	324,972,708	312,732	0.014
Investment Technology Group	17,060,726	489,542,906	291,042	0.017
Deutsche Bank	18,529,309	239,137,596	259,239	0.014
Liquidnet	14,309,473	407,044,672	251,522	0.018
Exectution Services Inc	5,702,640	184,715,463	218,452	0.038
Goldman Sachs	19,452,867	193,644,294	215,617	0.011
Morgan Stanley	14,861,091	175,739,193	193,055	0.013
Sanford C Bernsten Co	6,832,829	178,075,931	174,071	0.025
Donaldson & Co	4,522,004	142,530,418	171,490	0.038
Bank of America Securities	5,514,477	190,574,334	143,446	0.026
Rochdale Securities	4,332,149	108,419,367	99,526	0.023
Macquarie Securities	7,439,074	50,655,140	84,197	0.011
A G Edwards	1,529,041	55,763,442	69,078	0.045
Credit Lyonnais Securities	6,536,852	44,184,533	65,605	0.010
Shearson Lehman Hutton	1,629,987	70,001,787	63,754	0.039
Piper Jaffray	1,760,955	53,760,977	61,241	0.035
Robert W Baird & Co	2,360,969	77,157,237	58,043	0.025
Jefferies & Co	3,652,042	55,266,025	55,869	0.015
Weeden & Co	1,133,076	33,262,696	47,026	0.042
Others (includes firms)	79,279,243	1,337,873,454	1,357,491	0.017
Commissioned equity trades	453,868,725	$ 8,683,726,202	$ 8,482,058	
Less commissions recaptured			(1,513,095)	
Trades at net commission	453,868,725	$ 8,683,726,202	$ 6,968,963	$ 0.015

Employees' Retirement System

of the State of Hawaii

ACTUARIAL SECTION

Letter from the Actuary

GRS
Gabriel Roeder Smith & Company
Consultants & Actuaries
5605 N. MacArthur Blvd.
Suite 870
Irving, TX 75038-2631
469.524.0000 phone
469.524.0003 fax
www.gabrielroeder.com

December 8, 2008

Board of Trustees
Employees' Retirement System of
The State of Hawaii
City Financial Tower
201 Merchant St., Ste. 1400
Honolulu, HI 96813-2980

Dear Trustees:

Subject: Actuarial Valuation as of June 30, 2008

We certify that the information contained in the 2008 actuarial valuation report is accurate and fairly presents the actuarial position of the Employees' Retirement System of the State of Hawaii (ERS) as of June 30, 2008.

All calculations have been made in conformity with generally accepted actuarial principles and practices and with the Actuarial Standards of Practice issued by the Actuarial Standards Board. In our opinion, the results presented comply with the requirements of the Hawaii statutes and, where applicable, the Internal Revenue Code, ERISA, and the Statements of the Governmental Accounting Standards Board. The undersigned are independent actuaries. One or more of them are an Enrolled Actuary and/or a Member of the American Academy of Actuaries. All are experienced in performing valuations for large public retirement systems.

Actuarial valuations

The primary purpose of the valuation report is to determine the adequacy of the current employer contribution rate through measuring the resulting funding period, to describe the current financial condition of ERS, and to analyze changes in ERS's condition. In addition, the report provides information required by ERS in connection with Governmental Accounting Standards Board Statement No. 25 (GASB No. 25), and it provides various summaries of the data.

Valuations are prepared annually, as of June 30th of each year, the last day of ERS's plan year and fiscal year.

Financing objectives

Contribution rates are established by Law that, over time, are intended to remain level as a percent of payroll. The employee and employer contribution rates have been set by Law and are intended to provide for the normal cost plus the level percentage of payroll required to amortize the unfunded actuarial accrued liability (UAAL) over a period not in excess of 30 years.

Letter from the Actuary (continued)

Board of Trustees
December 8, 2008
Page 2

Progress toward realization of financing objectives

The actuarial accrued liability, the unfunded actuarial accrued liability (UAAL), and the calculation of the resulting funding period illustrate the progress toward the realization of financing objectives. Based on this actuarial valuation as of June 30, 2008, ERS's underfunded status has increased slightly, but less than expected because of an asset gain that more than offset the liability experience loss which was caused by higher than expected salary increases. The UAAL is now $5.168 billion.

The Legislature increased the employer contribution rates to 19.70% for Police and Fire employees and 15.00% for All Other Employees, effective July 1, 2009. Based on these contribution rates and the Employee contributions, the remaining amortization period is 22.6 years. Because this period is less than 30 years, the financing objectives of ERS are being realized.

In the absence of significant actuarial losses, the employer contribution rates in fiscal year 2009 and beyond would normally be sufficient to satisfy the GASB No. 25 Annual Required Contribution requirements.

It should be noted, however, that the above information is based on the measurement of the System as of June 30, 2008. At the time this report is being written, the stock markets have declined by more than 30% since June 30, 2008. Without a major recovery by June 30, 2009, there are likely to be significant actuarial losses next year. In the absence of a significant recovery in the investment markets during the remainder of fiscal year 2009, the contribution rate needed to amortize the UAAL over 30 years will increase over the next several valuation cycles.

Benefit provisions and Legislative changes

There was no legislation enacted that impacted the benefit provisions of the System. See the *Summary of Retirement Benefit Plan Provisions* in the Introductory Section of this CAFR for more details on the benefit provisions.

Assumptions and methods

The actuarial assumptions used were adopted by the Board on August 14, 2006 based on the recommendations provided by an Experience Study performed by us. While the current investment return assumption is the assumption recommended in the Study, the assumption is actually set by legislative action. Further detail on the assumptions and methods may be found in Table 18 of this report.

In our opinion, the assumptions are internally consistent and are reasonably based on the actual experience of ERS. These assumptions are also in full compliance with all parameters established by GASB No. 25.

Letter from the Actuary (continued)

Board of Trustees
December 8, 2008
Page 3

The results of the actuarial valuation are dependent on the actuarial assumptions used. Actual results can and almost certainly will differ, as actual experience deviates from the assumptions. Even seemingly minor changes in the assumptions can materially change the liabilities, calculated contribution rates and funding periods. The actuarial calculations are intended to provide information for rational decision making.

Data

Member data for retired, active, and inactive participants was supplied as of March 31, 2008, by ERS's staff. We have not subjected this data to any auditing procedures, but have examined the data for reasonableness and consistency with the prior year's data. Asset information was supplied by ERS's staff.

Responsibility for Tables and Schedules

The actuary is responsible for the information with respect to years after 1999 in the Required Supplementary Information, the Schedule of Employer Contributions, and the Notes To Required Supplementary Information in the Financial Section of the ERS's Comprehensive Annual Financial Report (CAFR). Information with respect to years prior to 2000 was supplied by ERS.

Tables and schedules in the Actuarial Section of the CAFR were generally prepared directly by the Actuary. Certain of these tables, however, were prepared by ERS utilizing information from this report. When those tables were prepared by ERS from our report, they are so noted.

Sincerely,

Joe Newton, FSA, EA	Lewis Ward	W. Michael Carter, FSA, EA
Consultant	Consultant	Senior Consultant

Executive Summary

The following summarizes the key results of the June 30, 2008 actuarial valuation of the Employees' Retirement System of the State of Hawaii (ERS).

Item	2008	2007
Membership		
• Number of		
- Active members	66,589	65,251
- Retirees and beneficiaries	36,260	35,324
- Inactive, vested	5,847	5,554
- Total	108,696	106,129
• Covered payroll for active members	$3,601.7 million	$3,340.5 million
• Actual benefit payments and refunds	$796.0 million	$764.5 million
Assets		
• Actuarial value	$11,381.0 million	10,589.8 million
• Market value	$10,846.8 million	11,434.3 million
• Return on actuarial value	8.9%	13.0%
• Return on market value	(4.1%)	16.9%
• Employer contributions during fiscal year	$488,770,028	$454,494,286
• External cash flow %	(1.4%)	(1.5%)
Actuarial Information		
• Total normal cost % (employee + employer)	12.54%	12.49%
• Unfunded actuarial accrued liability (UAAL)	$5,168.1 million	$5,106.8 million
• Funded ratio (based on actuarial assets)	68.8%	67.5%
• Funded ratio (based on market assets)	65.5%	72.8%
• Funding period (years)	22.6	25.5
• Employer contribution rate % of projected payroll * For FY 2009 & Beyond	15.46%	15.46%
• GASB ARC for FY 2008		
% of projected payroll		18.17%
Police and Fire Employees	17.84%	
All Other Employees	13.66%	14.18%
Composite – All Employees	14.09%	14.59%

* Weighted average of 19.70% Contribution Rate for Police and Firefighters and 15.00% Contribution Rate for All Other Employees beginning July 1 2008.

Actuarial Certification Statement

	Police and Firefighters June 30, 2008	All Other Employees June 30, 2008	All Employees June 30, 2008
1. Gross normal cost as a percentage of pay	18.78%	11.83%	12.54%
2. Present value of future benefits			
a. Active employees	$ 2,057,725,399	$ 8,876,000,632	$ 10,933,726,031
b. Inactive members	18,091,223	255,359,117	273,450,340
c. Pensioners and beneficiaries	1,312,430,136	6,917,908,654	8,230,338,790
d. Total	$ 3,388,246,758	$ 16,049,268,403	$ 19,437,515,161
3. Present value of future employee and employer contributions			
a. Present value of future normal costs	$ 611,135,284	$ 2,277,310,823	$ 2,888,446,107
b. Present value of future employee contributions	397,591,395	923,730,700	1,321,322,095
c. Present value of future employer normal cost (Item 3a - Item 3b)	$ 213,543,889	$ 1,353,580,123	$ 1,567,124,012
4. Actuarial accrued liability (Item 2d - Item 3a)	$ 2,777,111,474	$ 13,771,957,580	$ 16,549,069,054
5. Actuarial value of assets			
a. Annuity Savings Fund	$ 562,572,736	$ 543,054,900	$ 1,105,627,636
b. Pension Accumulation Fund	1,513,777,429	8,761,555,939	10,275,333,367
c. Total	$ 2,076,350,165	$ 9,304,610,839	$ 11,380,961,003
6. Unfunded actuarial accrued liability	$ 700,761,309	$ 4,467,346,741	$ 5,168,108,051
7. Adequacy of contribution rates			
a. Statutory Contribution Rate for Fiscal Year 2008	15.75%	13.75%	13.95%
b. Statutory Contribution Rate beginning Fiscal Year 2009	19.70%	15.00%	15.46%
c. Funding period in years as of June 30, 2008	22.7	22.5	22.6

The actuarial valuation as of June 30, 2008 is based on the provisions of Chapter 88 of the Hawaii Revised Statutes, as amended. The assumptions used in the cost calculations were those adopted by the Board of Trustees on August 14, 2006 based on statutory requirements and on the actuary's actuarial experience investigation report covering the five-year period July 1, 2000 – June 30, 2005. The actuarial calculations were performed by qualified actuaries in accordance with accepted actuarial procedures.

In our opinion, the contributions required to meet ERS's liabilities were calculated in accordance with the provisions of Chapter 88 regarding the funding of the Employees' Retirement System on an actuarial reserve basis. The results of the June 30, 2008 actuarial shown above do not reflect any of the negative impact of the historic market declines which have occurred since the valuation date.

W. Michael Carter, FSA, EA
Senior Consultant

Gabriel Roeder Smith & Company

Summary of 2008 Actuarial Valuation

Exhibit 1
Development of Employer Cost

		Police and Firefighters June 30, 2008	All Other Employees June 30, 2008	All Employees June 30, 2008
1.	Payroll (adjusted for one year's pay increase)	$ 373,473,901	$ 3,408,628,842	$ 3,782,102,743
2.	Gross normal oost (Exhibit 3)	18.78%	11.83%	12.54%
3.	Employer normal cost rate (Exhibit 3)	6.58%	5.79%	5.89%
4.	Present value future benefits (Exhibit 2)	$ 3,388,246,758	$ 16,049,268,403	$ 19,437,515,161
5.	Present value future employer contributions	$ 213,543,889	$ 1,353,580,123	$ 1,567,124,012
6.	Present value future employee contributions	$ 397,591,395	$ 923,730,700	$ 1,321,322,095
7.	Actuarial accrued liability (Item 4 - Item 5 - Item 6)	$ 2,777,111,474	$ 13,771,957,580	$ 16,549,069,054
8.	Actuarial value of assets	$ 2,076,350,165	$ 9,304,610,839	$ 11,380,961,003
9.	Unfunded actuarial accrued liability (UAAL)			
	(Item 7 - Item 8)	$ 700,761,309	$ 4,467,346,741	$ 5,168,108,050
10.	Funding period			
	a. Statutory Contribution Rate Beginning July 1, 2008	19.70%	15.00%	15.46%
	b. Less Employer normal cost	-6.58%	-5.79%	-5.89%
	c. Employer Amortization payment (level %) (Item 10a + Item 10b)	13.12%	9.21%	9.57%
	d. Funding Period in years	22.7	22.5	22.6

		Police and Firefighters June 30, 2007	All Other Employees June 30, 2007	All Employees June 30, 2007
1.	Payroll (adjusted for one year's pay increase)	$ 344,115,630	$ 3,162,924,333	$ 3,507,039,963
2.	Gross normal oost (Exhibit 3)	18.76%	11.79%	12.49%
3.	Employer normal cost rate (Exhibit 3)	6.56%	5.75%	5.85%
4.	Present value future benefits (Exhibit 2)	$ 3,158,008,009	$ 15,173,076,784	$ 18,331,084,793
5.	Present value future employer contributions	$ 197,461,772	$ 1,258,478,457	$ 1,455,940,229
6.	Present value future employee contributions	$ 368,816,313	$ 809,782,219	$ 1,178,598,532
7.	Actuarial accrued liability (Item 4 - Item 5 - Item 6)	$ 2,591,729,924	$ 13,104,816,108	$ 15,696,546,032
8.	Actuarial value of assets	$ 1,926,508,478	$ 8,663,264,379	$ 10,589,772,857
9.	Unfunded actuarial accrued liability (UAAL)			
	(Item 7 - Item 8)	$ 665,221,446	$ 4,441,551,729	$ 5,106,773,175
10.	Funding period			
	a. Statutory Contribution Rate Beginning July 1, 2008	19.70%	15.00%	15.46%
	b. Less Employer normal cost	-6.56%	-5.75%	-5.85%
	c. Employer Amortization payment (level %) (Item 10a + Item 10b)	13.14%	9.25%	9.61%
	d. Funding Period in years	24.6	25.6	25.5

Gabriel Roeder Smith & Company

Summary of 2008 Actuarial Valuation (continued)

Exhibit 2
Actuarial Present Value of Future Benefits

	Police and Firefighters June 30, 2008	All Other Employees June 30, 2008	All Employees June 30, 2008
1. Active members			
a. Service retirement benefits	$ 1,950,194,975	$ 8,082,533,862	$ 10,032,728,837
b. Termination benefits	70,108,943	611,632,705	681,741,648
d. Survivor benefits	28,380,596	107,799,287	136,179,883
e. Disability retirement benefits	9,040,885	74,034,778	83,075,663
f. Total	$ 2,057,725,399	$ 8,876,000,632	$ 10,933,726,031
2. Retired members			
a. Service retirement	$ 1,236,644,186	$ 6,541,775,092	$ 7,778,419,278
b. Disability retirement	25,959,362	117,299,769	143,259,131
c. Beneficiaries	49,826,588	258,833,793	308,660,381
d. Total	$ 1,312,430,136	$ 6,917,908,654	$ 8,230,338,790
3. Inactive members			
a. Vested terminations	$ 18,027,645	$ 250,127,923	$ 268,155,568
b. Nonvested terminations	63,578	5,231,194	5,294,772
c. Total	$ 18,091,223	$ 255,359,117	$ 273,450,340
4. Total actuarial present value of future benefits	$ 3,388,246,758	$ 16,049,268,403	$ 19,437,515,161

	Police and Firefighters June 30, 2007	All Other Employees June 30, 2007	All Employees June 30, 2007
1. Active members			
a. Service retirement benefits	$ 1,790,085,732	$ 7,569,945,396	$ 9,360,031,128
b. Termination benefits	65,665,563	544,712,070	610,377,633
d. Survivor benefits	26,178,921	99,708,831	125,887,752
e. Disability retirement benefits	8,341,196	69,328,782	77,669,978
f. Total	$ 1,890,271,412	$ 8,283,695,079	$ 10,173,966,491
2. Retired members			
a. Service retirement	$ 1,178,144,115	$ 6,254,932,550	$ 7,433,076,665
b. Disability retirement	25,778,059	112,916,012	138,694,071
c. Beneficiaries	46,296,796	238,021,182	284,317,978
d. Total	$ 1,250,218,970	$ 6,605,869,744	$ 7,856,088,714
3. Inactive members			
a. Vested terminations	$ 15,923,052	$ 279,472,603	$ 295,395,655
b. Nonvested terminations	1,594,575	4,039,358	5,633,933
c. Total	$ 17,517,627	$ 283,511,961	$ 301,029,588
4. Total actuarial present value of future benefits	$ 3,158,008,009	$ 15,173,076,784	$ 18,331,084,793

Gabriel Roeder Smith & Company

Summary of 2008 Actuarial Valuation (continued)

Exhibit 3
Analysis of Normal Cost

	Police and Firefighters June 30, 2008	All Other Employees June 30, 2008	All Employees June 30, 2008
1. Normal cost as a percent of pay			
a. Service retirement benefits	16.04%	8.39%	9.18%
b. Deferred termination benefits	0.69%	1.24%	1.18%
c. Refunds	1.47%	1.82%	1.78%
d. Disability retirement benefits	0.15%	0.17%	0.17%
e. Survivor benefits	0.43%	0.21%	0.23%
f. Total	18.78%	11.83%	12.54%
2. Employee contribution rate	12.20%	6.04%	6.65%
3. Effective employer normal cost rate (Item 1f – Item 2c)	6.58%	5.79%	5.89%

	Police and Firefighters June 30, 2007	All Other Employees June 30, 2007	All Employees June 30, 2007
1. Normal cost as a percent of pay			
a. Service retirement benefits	16.02%	8.33%	9.11%
b. Deferred termination benefits	0.69%	1.24%	1.18%
c. Refunds	1.47%	1.84%	1.80%
d. Disability retirement benefits	0.15%	0.17%	0.17%
e. Survivor benefits	0.43%	0.21%	0.23%
f. Total	18.76%	11.79%	12.49%
2. Employee contribution rate	12.20%	6.04%	6.64%
3. Effective employer normal cost rate (Item 1f – Item 2c)	6.56%	5.75%	5.85%

Summary of 2008 Actuarial Valuation (continued)

Exhibit 4
Development of Actuarial Value of Assets

1.	Market value of assets at beginning of year	$	11,462,416,866
2.	Net new investments		
	a. Contributions	$	652,145,667
	b. Benefits paid		(792,312,830)
	c. Refunds		(3,668,857)
	d. Subtotal		(143,836,020)
3.	Market value of assets at end of year	$	10,846,788,965
4.	Net earnings (Item 3 - Item 1 - Item 2)	$	(471,791,881)
5.	Assumed investment return rate		8%
6.	Expected return	$	911,239,908
7.	Excess return (Item 4 – Item 6)	$	(1,383,031,789)
8.	Deferred amount as of June 30, 2008:		

Period End	Excess Return	Percent Deferred	Deferred Amount
June 30, 2008 (Item 7 above)	$ (1,383,031,789)	75%	$ (1,037,273,842)
June 30, 2007 (From 2007 report)	879,236,790	50%	439,618,395
June 30, 2006 (From 2006 report)	253,933,634	25%	63,483,409
June 30, 2005 (From 2005 report)	232,439,124	0%	0
			$ (534,172,038)

9.	Actuarial value of assets as of June 30, 2008 (Item 3 - Item 8)	$	11,380,961,003
10.	Ratio of actuarial value to market value		104.9%

Gabriel Roeder Smith & Company

Summary of 2008 Actuarial Valuation (continued)

Exhibit 5
Total Experience Gain or Loss

Item	Police and Firefighters June 30, 2008	All Other Employees June 30, 2008	All Employees June 30, 2008
Calculation of total actuarial gain or loss			
1. Unfunded actuarial accured liability (UAAL), as of June 30, 2007	$ 665,221,446	$ 4,441,551,729	$ 5,106,773,175
2. June 30, 2006 UAAL after reflecting new assumptions	$ 698,668,998	$ 4,486,364,007	$ 5,185,033,005
3. Normal cost for the year (employer and employee) (based on new assumptions)	$ 64,556,092	$ 303,062,545	367,618,637
4. Less: Contributions and assessments for the year	$ (96,379,352)	$ (555,766,315)	$ (652,145,667)
5. Interest at 8%			
a. On UAAL	$ 53,217,716	$ 355,324,138	$ 408,541,854
b. On normal cost	2,582,244	12,122,502	14,704,746
c. On contributions	(3,855,174)	(22,230,653)	(26,085,827)
d. Total	$ 51,944,786	$ 345,215,987	$ 397,160,773
6. Expected UAAL as of June 30, 2008 (Sum of Items 2 – 5)	$ 685,342,972	$ 4,534,063,946	$ 5,219,406,918
7. Actual UAAL as of June 30, 2008	$ 700,761,309	$ 4,467,346,741	$ 5,168,108,050
8. Total gain (loss) for the year (Item 6 – Item 7)	$ (15,418,337)	$ 66,717,205	$ 51,298,868
Source of gains and losses			
9. Asset gain (loss) for the year (Exhibit 6)	$ 16,555,469	$ 77,040,308	$ 93,595,777
Salary gain (loss) for the year	(50,951,421)	(31,754,689)	(82,706,110)
10. Liability gain (loss) for the year	$ 18,977,615	$ 21,431,586	$ 40,409,201
11. Change in benefit provisions	-	-	-
12. Total gain (loss) for the year	$ (15,418,337)	$ 66,717,205	$ 51,298,868

Summary of 2008 Actuarial Valuation (continued)

Exhibit 6
Investment Experience Gain or Loss

Item	June 30, 2008	June 30, 2007
1. Actuarial assets, beginning of year	$ 10,589,772,857	$ 9,529,371,265
2. Total contributions during year	$ 652,145,667	$ 599,152,471
3. Benefits and refunds paid	$ (795,981,687)	$ (764,502,338)
4. Assumed net investment income at 8%		
a. Beginning of year assets	$ 847,181,829	$ 762,349,701
b. Contributions	$ 26,085,827	$ 23,966,099
c. Benefits and refunds paid	$ (31,839,267)	$ (30,580,094)
d. Total	$ 841,428,389	$ 755,735,706
5. Expected actuarial assets, end of year (Sum of Items 1 through 4)	$ 11,287,365,226	$ 10,119,757,104
6. Actual actuarial assets, end of year	$ 11,380,961,003	$ 10,589,772,857
7. Asset gain (loss) for year (Item 6 – Item 5)	$ 93,595,777	$ 470,015,753
8. Asset gain (loss) as a percent of actuarial value of assets, end of year (Item 7 / Item 6)	0.82%	4.44%

Exhibit 7
Analysis of Changes in Valuation Results

	UUAL ($ Millions)		Funding Period		GASB ARC	
	Amount	Change	Amount	Change	Amount	Change
1. 2007 Valuation	$5,107	$ -	25.5 years		14.59%	
2. 2008 Valuation using new salary scale	5,220	113	24.5 years	-1.0 years	14.63%	0.04%
3. 2008 Expected valuation results using expected contributions, closed amortization period	5,219	(1)	24.5 years	0.0 years	14.63%	0.00%
4. 2008 expected valuation results using actual contributions	5,302	83	25.2 years	0.7 years	14.77%	0.14%
5. 2008 valuation results using expected assets, expected payroll, and actual liabilities	5,262	(40)	25.0 years	-0.2 years	14.74%	-0.03%
6. 2008 valuation results using actual liabilities, actual assets, and expected payroll	5,168	(94)	24.3 years	-0.7 years	14.58%	-0.16%
7. 2008 valuation results using actual liabilities, actual assets, and actual payroll	5,168	-	22.6 years	1.7 years	14.23%	-0.35%
8. 2008 valuation results, resetting to 30 year amortization	5,168	-	22.6 years	0.0 years	14.09%	-0.14%

Gabriel Roeder Smith & Company

Summary of 2008Actuarial Valuation (continued)

Exhibit 8
Highlights of Last Five Annual Actuarial Valuations
2004 through 2008

Item	Valuation Date: June 30				
	2004	2005	2006	2007	2008
Number of active members	62,573	63,073	64,069	65,251	66,589
Number of inactive members	4,501	4,938	5,164	5,554	5,847
Number of pensioners	30,503	31,344	32,199	33,117	33,893
Number of beneficiaries	1,794	1,957	2,105	2,207	2,367
Average monthly contributory plan pension amount	$ 1,636	$ 1,717	$ 1,792	$ 1,869	$ 1,941
Average monthly noncontributory plan pension amount	$ 1,272	$ 1,305	$ 1,335	$ 1,359	$ 1,388
Average monthly hybrid plan pension amount	n/a	n/a	n/a	$ 1,453	$ 1,603
Average monthly beneficiary amount	$ 950	$ 966	$ 989	$ 1,025	$ 1,062
Total actuarial value of assets ($millions)	$ 8,797	$ 8,915	$ 9,529	$ 10,590	$ 11,381
Unfunded actuarial accrued liabilities ($millions)	$ 3,474.2	$ 4,071.1	$ 5,132.0	$ 5,106.8	$ 5,168.1
Funding Period (in years) [1]	22.6	25.7	35.2	25.5	22.6

Item (Dollar amounts in millions)	Fiscal Year				
	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008
Total calculated appropriations	$ 229.8	$ 322.8	$ 423.4	$ 454.5	$ 488.8
EIR Program appropriations	5.9	5.9	-	-	-
Excess investment earnings credit	-	-	-	-	-
Net employers appropriations	$ 235.7	$ 328.7	$ 423.4	$ 454.5	$ 488.8

(1) Beginning with the 2004 valuation, the purpose of the valuation is to determine the remaining amortization period based on the statutory contribution rates. Prior valuations determined the dollar amount needed to amortize the UAAL over a fixed period of time.

(2) Beginning with the fiscal year beginning July 1, 2005, a dollar contribution amount is not determined under the provisions of Act 181/2004. Instead a fixed percentage of payroll is contributed (15.75% for Police and Fire, 13.75% for All Others). Beginning July 1, 2008, the percentages will increase to 19.70% for Police and Fire, 15.00% for All Others.

Summary of Actuarial Methods and Assumptions
(Adopted on August 14, 2006)

I. Valuation Date

The valuation date is June 30th of each plan year. This is the date as of which the actuarial present value of future benefits and the actuarial value of assets are determined.

II. Actuarial Cost Method

The funding period required to amortize the unfunded actuarial accrued liability (UAAL) is determined using the Entry Age Actuarial Cost Method. This method assigns the plan's total unfunded liabilities (the actuarial present value of future benefits less the actuarial value of assets) to various periods. The unfunded actuarial accrued liability is assigned to years prior to the valuation, and the normal cost is assigned to the year following the valuation. The remaining costs are assigned to future years.

The normal cost is the level percentage of payroll contribution required to accumulate the needed funds to pay all expected benefits. This percentage of payroll is then applied to the total compensation for the prior year for all active members, and is then adjusted for the payroll growth assumption.

The actuarial accrued liability is the difference between the total present value of future benefits and the actuarial present value of future normal costs. The unfunded actuarial accrued liability (UAAL) is the excess of the actuarial accrued liability over the actuarial value of assets.

Since the State statutes governing the System establish the current employee and Employer contribution rates, the actuarial valuation determines the number of years required to amortize (or fund) the UAAL on a level percentage of payroll basis, taking into account the payroll growth assumption and the normal cost expressed as a percent of pay.

Because of this amortization procedure, any change in the unfunded actuarial accrued liability due to (i) actuarial gains and losses, (ii) changes in actuarial assumptions, or (iii) amendments, affects the funding period.

III. Funding of Unfunded Actuarial Accrued Liability

All of the following concepts will be discussed on an aggregate basis with regards to the contributory, the Hybrid, and the noncontributory plans. The total normal cost for benefits provided by ERS is 12.49% of payroll, which is 9.61% of payroll less than the total contributions required by Law (15.46% from employers plus 6.64% in the aggregate from employees). Since only 5.85% of the employer's 15.46% contribution is required to meet the normal cost (6.64% comes from the employee contribution), it is intended that the remaining 9.91% of payroll will be used to amortize any unfunded actuarial accrued liabilities over a period of years in the future, assuming that total payroll increases by 3.50% per year.

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

IV. *Actuarial Value of Assets*

The actuarial value of assets is equal to the market value, adjusted for a four-year phase in of actual investment return in excess of expected investment return. The actual return is calculated net of investment and administrative expenses, and the expected investment return is equal to the assumed investment return rate multiplied by the prior year's market value of assets, adjusted for contributions, benefits paid, and refunds.

V. *Actuarial Assumptions*

A. Economic Assumptions

1. Investment return: 8% per year, compounded annually, composed of an assumed 3.00% inflation rate and a 5.00% net real rate of return. (Set by legislative action.)
2. Payroll growth rate: 3.50% per annum.
3. Salary increase rate: As shown below

	General Employees		Teachers	
Years of Service	Service-related Component	Total Annual Rate of Increase Including 3.00% Inflation Component and 1.00% General Increase Rate	Service-Related Component	Total Annual Rate of Increase Including 3.00% Inflation Component and 1.50% General Increase Rate
0	4.00%	8.00%	4.00%	8.50%
1	2.50%	6.50%	3.00%	7.50%
2	1.50%	5.50%	2.50%	7.00%
3	1.00%	5.00%	2.00%	6.50%
4	0.75%	4.75%	1.50%	6.00%
5	0.50%	4.50%	1.00%	5.50%
6	0.50%	4.50%	1.00%	5.50%
7	0.25%	4.25%	0.75%	5.25%
8	0.25%	4.25%	0.75%	5.25%
9	0.25%	4.25%	0.75%	5.25%
10	0.25%	4.25%	0.50%	5.00%
11	0.25%	4.25%	0.50%	5.00%
12	0.25%	4.25%	0.50%	5.00%
13	0.00%	4.00%	0.50%	5.00%
14	0.00%	4.00%	0.50%	5.00%
15 or more	0.00%	4.00%	0.00%	4.50%

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

	Police & Firefighters	
Years of Service	Service-related Component	Total Annual Rate of Increase Including 3.00%Inflation Component and 1.75% General Increase Rate
0	13.00%	17.75%
1	11.00%	15.75%
2 or more	0.00%	4.75%

Salary increases are assumed to occur once a year on July 1. Therefore, the pay used for the period between the valuation date and the first anniversary of the valuation date is equal to the reported pay for the prior year, annualized if necessary, and then increased by the salary increase assumption.

B. Demographic Assumptions

1. Post-Retirement Mortality rates

General Employees

a. Healthy males – Client Specific Table for males, 90% multiplier.

b. Healthy females - Client Specific Table for females, 90% multiplier.

c. Disabled males - 1994 US Group Annuity Mortality Static Table for males, set forward ten years.

d. Disabled females - 1994 US Group Annuity Mortality Static Table for females, set forward eleven years.

Teachers

a. Healthy males – Client Specific Table for male teachers, 75% multiplier.

b. Healthy females - Client Specific Table for female teachers, 65% multiplier.

c. Disabled males - 1994 US Group Annuity Mortality Static Table for males, set forward four years.

d. Disabled females - 1994 US Group Annuity Mortality Static Table for males, set forward six years.

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

Police and Fire

a. Healthy males – 1994 US Group Annuity Mortality Static Table for males, 85% multiplier.

b. Healthy females - 1994 US Group Annuity Mortality Static Table for females, 85% multiplier.

c. Disabled males - 1994 US Group Annuity Mortality Static Table for males, set forward five years.

d. Disabled females - 1994 US Group Annuity Mortality Static Table for females, set forward five years.

2. Pre-retirement Mortality Rates

The male pre-retirement mortality rates are multiples of a table that has the RP-2000 Male Employee rates for ages 1 to 70 and the RP-2000 Combined Male rates for ages above 70. Similarly, the female pre-retirement rates are multiples of a table that has the RP-2000 Female Employee rates for ages 1 to 70 and the RP-2000 Combined Female rates for ages above 70. The following table shows the factors that are used in conjunction with the tables described above to derive the final ordinary and accidental death rates.

	General Employees	Teachers	Police and Fire
Type	Male and Females	Male and Females	Male and Females
Ordinary	40%	35%	15%
Accidental	10%	5%	35%

3. Disability rates – The assumed total disability rates for employees covered by the contributory plan, hybrid plan, and the noncontributory plan at select ages are multiples of the client specific table that follows:

Age	Male & Female
25	0.000%
30	0.001%
35	0.008%
40	0.026%
45	0.064%
50	0.146%
55	0.198%
60	0.217%

Note: The disability rates project the percentage of employees at each age that is assumed to become disabled before retiring. Multiples of the rates above are assumed

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

to be ordinary disability or accidental disability, and vary by employee group as follows:

Type	General Employees Male	General Employees Female	Teachers Male	Teachers Female	Police and Fire Male & Female
Ordinary	150%	95%	40%	40%	70%
Accidental	20%	5%	5%	5%	35%

4. Termination Rates - Separate male and female rates, based on both age and service, developed from 2006 Experience Study. Rates reflect terminations for causes other than death, disability or retirement. Employees eligible for retirement are assumed to have no probability of termination. Sample rates are shown below:

<u>For first 6 years of service</u>

Expected Terminations per 100 lives

Years of Service	General Employees Male	General Employees Female	Teachers Male	Teachers Female	Police and Fire Male & Female
0	15.5	18.5	32.0	28.0	11.0
1	12.5	16.5	22.0	22.0	7.5
2	10.5	12.5	14.0	15.0	4.0
3	9.0	10.0	12.0	14.0	4.0
4	7.0	8.0	10.0	11.0	4.0
5	6.5	7.0	9.0	8.0	4.0

<u>After first 6 years of service</u>

Expected Terminations per 100 lives

Age	General Employees Male	General Employees Female	Teachers Male	Teachers Female	Police and Fire Male & Female
25	6.08	7.38	4.35	6.50	2.00
30	5.04	4.82	4.12	5.80	2.82
35	4.03	3.75	3.80	4.41	2.50
40	3.36	3.02	3.38	3.32	1.66
45	2.81	2.49	2.57	2.65	0.94
50	2.58	2.62	2.56	2.60	0.66
55	3.67	3.92	4.53	4.97	0.00
60	4.00	4.24	5.59	4.66	0.00

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

5. Retirement rates - Separate male and female rates, based on age, developed from the 2006 Experience Study. Sample rates are shown below:

Expected Retirements per 100 Lives

	Contributory Plan and Hybrid Plan					Noncontributory Plan			
	General Employees		Teachers		Police and Fire	General Employees		Teachers	
Age	Male	Female	Male	Female	Male & Female	Male	Female	Male	Female
45	1	0	0	0	18	0	0	0	0
46	1	0	0	0	18	0	0	0	0
47	1	0	0	0	18	0	0	0	0
48	1	0	0	0	18	0	0	0	0
49	1	0	0	0	18	0	0	0	0
50	2	1	1	0	18	0	0	0	0
51	2	1	1	0	18	0	0	0	0
52	2	1	1	1	18	0	0	0	0
53	2	1	4	1	18	0	0	0	0
54	6	5	7	4	25	0	0	0	0
55	20	20	20	22	25	10	10	10	13
56	15	10	15	18	22	9	10	9	12
57	15	10	15	18	22	9	10	9	12
58	15	10	15	18	22	9	10	9	15
59	15	12	15	18	22	9	10	9	18
60	15	12	14	18	30	10	15	10	18
61	18	15	14	18	30	18	15	10	18
62	35	35	14	25	30	30	25	15	30
63	20	25	14	18	30	30	25	10	16
64	20	20	14	18	30	25	25	10	16
65	35	45	25	25	100	40	30	24	30
66	25	25	25	25	100	35	30	18	20
67	30	30	25	30	100	30	25	15	20
68	25	40	25	40	100	30	25	15	20
69	25	40	25	40	100	30	25	15	20
70	25	25	25	25	100	20	25	15	25
71	25	25	25	25	100	20	25	15	25
72	25	25	25	25	100	20	25	15	25
73	25	25	25	25	100	20	25	15	25
74	25	25	25	25	100	20	25	15	25
75	100	100	100	100	100	100	100	100	100

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

C. Other Assumptions

1. Percent married: 77% of male employees and 57.6% of female employees are assumed to be married.

2. Age difference: Male members are assumed to be four years older than their spouses, and female members are assumed to be four years younger than their spouses.

3. Percent electing annuity on death for contributory participants (when eligible): All of the spouses of married participants who die after becoming eligible for a retirement benefit are assumed to elect an annuity or a refund, whichever is more valuable at time of participant's death.

4. Percent electing deferred termination benefit: vested terminating members are assumed to elect a refund or a deferred benefit, whichever is more valuable at the time of termination.

5. Assumed age for commencement of deferred benefits: Members electing to receive a deferred benefit are assumed to commence receipt when eligible for early retirement.

6. Administrative expenses: The assumed investment return rate represents the anticipated net return after payment of all investment and administrative expenses.

7. Reemployment, purchase of service, transfers: No recognition is made of (i) future member reimbursements upon reemployment, (ii) future purchase of additional service, or (iii) special transfer provisions.

8. Sick Leave: It is assumed that all members will have their benefit service increased by sick leave and the following loads will be applied by group:

General Employees	3.75%
Teachers	4.25%
Police and Fire	5.00%

9. COLA delay: It is assumed that the first COLA will be received 9 months after retirement.

10. There will be no recoveries once disabled.

11. No surviving spouse will remarry and there will be no children's benefit.

12. Pay increase timing: Beginning of (fiscal) year. This is equivalent to assuming that reported pays represent amounts paid to members during the year ended on the valuation date.

13. Decrement timing: Retirements and terminations of Teachers are assumed to occur at the beginning of the year. All other decrements are assumed to occur mid-year.

Summary of Actuarial Methods and Assumptions (continued)
(Adopted on August 14, 2006 and on June 30, 2007)

14. Eligibility testing: Eligibility for benefits is determined based upon the age nearest birthday and service nearest whole year on the date the decrement is assumed to occur.

15. Decrement relativity: Decrement rates are used directly from the Experience Study, without adjustment for multiple decrement table effects.

16. Incidence of Contributions: Contributions are assumed to be received continuously throughout the year based upon the computed percent of payroll shown in this report, and the actual payroll payable at the time contributions are made.

17. Benefit Service: All members are assumed to accrue 1 year of service each year. Exact fractional service is used to determine the amount of benefit payable.

VI. Participant Data

Participant data was supplied on CD-ROM for (i) active members, (ii) inactive vested members, who are entitled to a future deferred benefit, (iii) members and beneficiaries receiving benefits.

Salary supplied for the current year was based on the earnings for the March preceding the valuation date. This salary was compared to March base pay plus a twelve-month average of overtime, with the greater of the two being used for valuation pay.

VII. Dates of Adoption of Assumptions and Methods

Generally, actuarial assumptions and methods were adopted by the Board of Trustees on August 14, 2006 as recommended by Gabriel, Roeder, Smith & Company. The legislature sets the investment return assumption. The salary scale assumption prior to the June 30, 2007 valuation was also set by statute. The 2007 Legislature removed this constraint as of June 30, 2007, and this assumption is now set by the Board based on the Actuary’s recommendations.

Summary of Plan Changes

Act 65, effective July 1, 1999

Requires judges who enter or re-enter service after June 30, 1999 to be at least 55 years old and five years of service or have 25 years of service to retire.

Act 100, effective June 30, 1999

Uses actuarial investment earnings in excess of a ten percent (10%) actuarial investment yield rate to reduce the employer's contribution requirements by $147.0 million and $50.6 million for fiscal years ending June 30, 2000 and 2001, respectively.

Act 284, effective June 30, 2001

Provide an increase in pension benefits for current retirees with military service who retired prior to July 2, 1989. A retirant who rendered honorable active military service could be granted up to 4 years of military service credits based upon his/her years of credited service under the ERSf, not to exceed his/her actual years of military service. The years of military service credits granted are based on the following schedule:

- 0 years for retirants with less than 8 years of credited service
- Up to 2 years of retirants with 8 years or more of credited service
- Up to 3 years of retirants with 20 years or more of credited service
- Up to 4 years of retirants with 25 years or more of credited service

For each year of military service credits granted on the schedule above, the retirant will be provided a $36.00 increase is his/her monthly pension or retirement allowance.

Act 199, effective June 30, 2003

Emergency Medical Technicians (EMTs) are allowed to retire with an unreduced benefit after 25 years of service regardless of age, of which the last five or more years prior to retirement must be in that capacity. This feature is phased in one year at a time, July 1, 2003 through June 30, 2008.

Act 177, effective July 1, 2004

This Act allows police officers with a permanent service-connected disability to retain the 2-1/2% benefit multiplier for each year of service as a police officer.

Act 179, effective July 1, 2004

This Act increased the Noncontributory service-connected disability formula to 35% of average final compensation. The Act also changed the methodology for crediting interest on contributions for terminated members so that interest continues to accrue until the date of refund. The Act adds a "pop-up" feature to the joint & survivor benefit options if the beneficiary pre-deceases the retiree.

This Act also created the new Hybrid Plan which will become effective July 1, 2006.

Summary of Plan Changes (continued)

Act 181, effective July 1, 2004

This Act establishes fixed employer contribution rates as a percentage of compensation effective July 1, 2005. Employers will contribute 15.75% for their police officers and firefighters and 13.75% for other employees.

Act 183, effective July 1, 2004

This Act amends the ERS statutes to comply with the federal tax limits on compensation retroactive to July 1, 1996.

Act 56, effective December 1, 2004

This Act amends the ERS statutes to allow the automatic cost-of-living-adjustment to be reflected when determining actuarial equivalent optional forms of payment.

Act 256, effective July 1, 2007

Legislation was enacted to remove the statutory salary increase assumption form the statutes and to grant the System's Board of Trustees the authority to set the salary scale assumption. As a result of that legislation, the Board adopted effective with this valuation the salary scale increase assumption recommended by GRS as a result of the Experience Study performed in 2006.

Legislation was also enacted to increase the employer contribution rates to the System. Effective July 1, 2008, the employer contribution rate for Police and Fire employees will increase from 15.75% to 19.70% and the rate for All Other employees will increase from 13.75% to 15.00%.

Ten Year Actuarial Schedules
1999 to 2008

- Retirement System Membership **
    - 2008 Membership Data *
- Historical Summary of Active Member Data *
- Pensioners, Average Annual Pension and Active Member/Ptensioner Comparison **
- Number of Retirants and Beneficiaries **
- Solvency Test **
- Employer Contribution Rates as a Percentage of Payroll **
- Employer Appropriations to Pension Accumulation Fund, Appropriation Years 2000-2001 to 2009-2010 **

Note: * Prepared by Gabriel, Roeder, Smith & Company
** Compiled by ERS Staff from actuary reports, or other data.

Retirement System Membership **
1999 to 2008

March 31,	Active Members	Inactive Vested Members	Pensioners & Beneficiaries	Total Membership
1999	58,387	2,777	27,950	89,114
2000	59,191	3,016	28,715	90,922
2001	59,992	3,416	29,660	93,068
2002	62,208	3,835	30,330	96,373
2003	62,292	4,150	31,389	97,831
2004	62,573	4,501	32,297	99,371
2005	63,073	4,938	33,301	101,312
2006	64,069	5,164	34,304	103,537
2007	65,251	5,554	35,324	106,129
2008	66,589	5,847	36,260	108,696

** Schedule compiled by ERS Staff from actuary reports.

Ten-Year Actuarial Schedules (continued)

2008 Membership Data*

March 31, 2008

	Police and Firefighters		All Other Employees		All Employees	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
1. Active members						
a. Number	4,915	4,854	61,674	60,397	66,589	65,251
b. Total payroll	$ 353,376,984	$ 325,707,545	$3,248,345,266	$3,014,780,021	$3,601,722,250	$3,340,487,566
c. Average salary	$ 71,898	$ 67,101	$ 52,670	$ 49,916	$ 54,089	$ 51,194
d. Average age	40..8	40.6	47.1	47.0	46.6	46.5
e. Average service	13.3	13.2	12.9	13.0	12.9	13.0
2. Inactive members						
a. Number	198	185	5,649	5,369	5,847	5,554
b. Total annual deferred benefits	$ 2,968,626	$ 2,682,402	$ 41,090,755	$ 47,955,798	$ 44,059,381	$ 50,368,200
c. Average annual deferred benefit	$ 14,993	$ 14,499	$ 7,274	$ 8,932	$ 7,535	$ 9,117
3. Service retirees						
a. Number	2,756	2,706	29,685	28,973	32,441	31,679
b. Total annual benefits	$ 104,209,828	$ 98,814,478	$ 617,724,664	$ 587,744,356	$ 721,934,492	$ 686,558,834
c. Average annual benefit	$ 37,812	$ 36,517	$ 20,809	$ 20,286	$ 22,254	$ 21,672
4. Disabled retirees						
a. Number	169	169	1,283	1,269	1,452	1,438
b. Total annual benefits	$ 2,633,489	$ 2,603,241	$ 12,070,600	$ 11,613,768	$ 14,704,089	$ 14,217,009
c. Average annual benefit	$ 15,583	$ 15,404	$ 9,408	$ 9,152	$ 10,127	$ 9,887
5. Beneficiaries						
a. Number	175	165	2,192	2,042	2,367	2,207
b. Total annual benefits	$ 4,381,336	$ 3,990,017	$ 25,795,764	$ 23,167,262	$ 30,177,100	$ 27,157,279
c. Average annual benefit	$ 25,036	$ 24,182	$ 11,768	$ 11,345	$ 12,749	$ 12,305

* Prepared by Gabriel, Roeder, Smith & Company

Historical Summary of Active Member Data*

1999 to 2008

Year Ending June 30,	Active Members		Covered Payroll		Average Salary			
	Number	Percent Increase	Amount in $ Millions	Percent Increase	$ Amount	Percent Increase	Average Age	Average Service
1999	58,387	0.9%	2,186.5	2.4%	37,448	1.3%		
2000	59,191	1.4%	2,275.3	4.1%	38,440	2.6%	45.5	13
2001	59,992	1.4%	2,350.2	3.3%	39,175	1.9%	45.6	13.3
2002	62,208	3.7%	2,568.7	9.3%	41,292	5.4%	45.8	13.2
2003	62,292	0.1%	2,718.4	5.8%	43,640	5.7%	46	13.1
2004	62,573	0.5%	2,755.5	1.4%	44,037	0.9%	46.0	13.0
2005	63,073	0.8%	2,924.5	6.1%	46,368	5.3%	46.3	13.0
2006	64,069	1.6%	3,113.7	6.5%	48,599	4.8%	46.4	13.0
2007	65,251	1.8%	3,340.5	7.3%	51,194	5.3%	46.5	13.0
2008	66,589	2.1%	3,601.7	7.8%	54,089	5.7%	46.6	12.9

* Prepared by Gabriel, Roeder, Smith & Company

Gabriel Roeder Smith & Company

Ten-Year Actuarial Schedules (continued)

Pensioners, Average Annual Pension and Active Member/Pensioner Comparison**

1999 to 2008

March 31,	Number of Pensioners	Average Annual Pension (1)	Ratio of Active Members per Pensioner
1999	26,709	$16,116	2.2
2000	27,357	$16,632	2.2
2001	28,210	$16,853	2.1
2002	28,770	$17,898	2.1
2003	29,730	$18,601	2.1
2004	30,503	$19,279	2.1
2005	31,344	$19,980	2.0
2006	32,199	$20,052	1.9
2007	33,117	$21,161	1.8
2008	33,893	$21,734	1.9

** Schedule compiled by ERS Staff from actuary reports.

(1) Pension amount includes base pension plus 2.5% post-retirement increases (excludes other bonuses and cost-of-living adjustments).

Number of Retirants and Beneficiaries**

1999 to 2008

As of Mar 31,	Added	Average Added to Rolls	Removed	Average Removed from Rolls	Total	Average Pension	% Chg
Retirants [1]							
1999	1,311	n/a	764	n/a	777	$16,116	3.60%
2000	1,549	n/a	784	n/a	1,542	$16,632	3.20%
2001	1,668	n/a	723	n/a	2,487	$16,853	1.30%
2002	1,229	18707	739	12559	28,770	$17,898	4.10%
2003	1,723	$20,292	763	$12,836	29,730	$18,601	3.90%
2004	1,630	$20,136	857	$13,596	30,503	$19,279	3.60%
2005	1,694	$21,228	853	$12,608	31,344	$19,980	3.60%
2006	1,664	$20,562	809	$14,032	32,199	$20,583	3.02%
2007	1,785	$20,782	873	$14,697	33,117	$21,161	2.81%
2008	1,712	$20,715	936	$15,396	33,893	$21,734	2.71%
Beneficiaries [1]							
2003	147	$12,137	48	$ 6,068	99	$10,909	3.90%
2004	177	$12,588	42	$7,596	234	$11,395	4.50%
2005	220	$10,395	57	$8,756	397	$11,587	1.70%
2006	214	$11,819	66	$10,455	2,105	$11,862	2.37%
2007	179	$14,161	71	$10,132	2,207	$12,305	3.74%
2008	235	$14,244	75	$10,659	2,367	$12,749	3.61%

Notes: [1] Beneficiary counts are included in retirant counts through 2001. As of March 31, 2001, there were 28,210 retirants and 1,450 beneficiaries, receiving annual retirement benefits of $17,202 and $10,050, respectively.

n/a Information not available.

** Schedule compiled by ERS staff from actuary reports.

Ten-Year Actuarial Schedules (continued)

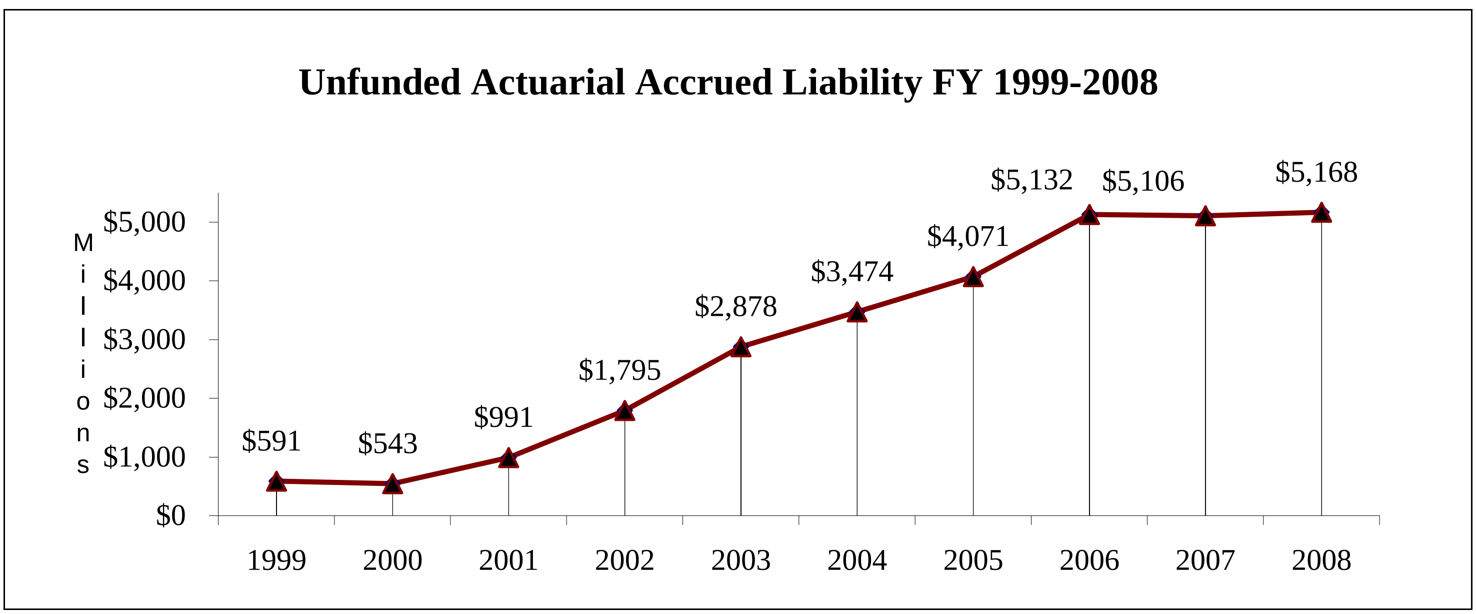
Solvency Test**

1999 to 2008

June 30,	Actuarial Accrued Liabilities (AAL): Active Member Contributions (1)	Retirees, Beneficiaries, and Inactive Vested Members (2)	Active and Inactive Members Employer Financed Portion (3)	Actuarial Value of Assets (4)	Cumulative Portion of Actuarial Accrued Liabilities Covered by Assets: Column (1) (5)	Column (2) (6)	Column (3) (7)
1998	883.5	4,472.7	3,053.5	7,906.2	100%	100%	83.5%
1999	902.2	4,682.2	3,517.2	8,590.8	100%	100%	85.5%
2000	938.0	4,914.5	3,817.8	9,204.7	100%	100%	87.8%
2001	876.0	5,232.4	4,398.5	9,516.0	100%	100%	77.5%
2002	889.9	5,499.4	4,820.9	9,415.2	100%	100%	62.7%
2003	872.3	5,912.3	5,167.5	9,074.0	100%	100%	44.3%
2004	870.3	6,278.6	5,122.4	8,797.1	100%	100%	32.2%
2005	864.9	6,641.6	5,479.5	8,914.8	100%	100%	25.7%
2006	844.0	7,458.4	6,359.0	9,529.4	100%	100%	19.3%
2007	914.1	7,856.1	6,926.4	10,589.8	100%	100%	26.3%
2008	1,029.5	8,230.3	7,289.2	11,381.0	100%	100%	29.1%

(Amounts in $millions)

** Schedule compiled by ERS Staff from actuary reports



Ten-Year Actuarial Schedules (continued)

Employer Contribution Rates as a Percentage of Payroll **

1998 to 2008

Actuarial Valuation as of June 30,	Police and Firefighters			All Other Employees			All Active Employees		
	Normal Cost Rate	Amortization Percent	Total Employer Rate	Normal Cost Rate	Amortization Percent	Total Employer Rate	Normal Cost Rate	Amortization Percent	Total Employer Rate
1998	11.47%	-11.22%	0.25%	4.28%	-3.88%	0.40%	4.99%	-4.61%	0.38%
1999	18.01%	-2.53%	15.48%	5.19%	1.61%	6.80%	6.46%	1.20%	7.66%
2000	13.17%	-8.82%	4.35%	6.03%	3.72%	9.75%	6.72%	2.50%	9.22%
2001	3.88%	4.16%	8.04%	5.59%	4.86%	10.45%	5.42%	4.78%	10.20%
2002	3.88%	6.46%	10.34%	5.62%	5.87%	11.49%	5.45%	5.93%	11.38%
2003	4.27%	11.06%	15.33%	5.73%	8.74%	14.47%	5.59%	8.96%	14.55%
2004	4.41%	11.34%	15.75%	5.75%	8.00%	13.75%	5.54%	8.41%	13.95%
2005	4.36%	11.39%	15.75%	5.76%	7.99%	13.75%	5.55%	8.40%	13.95%
2006	4.69%	11.06%	15.75%	5.16%	8.59%	13.75%	5.11%	8.84%	13.95%
2007	6.56%	9.19%	15.75%	5.75%	8.00%	13.75%	5.85%	8.10%	13.95%
2008	6.58%	13.12%	19.70%	5.79%	9.21%	15.70%	5.89%	9.57%	15.46%

Note: Effective with the June 30, 2004 valuation, the employer contribution rate is statutorily changed to a percentage of pay of 15.75% of actual pay for Police and Fire and 13.75% of actual pay for All Other Employees, per Act 181/2004 SLH. Effective July 1, 2008, the employer contribution rate increased to 19.00% of actual pay for Police and Fire and 15.70% of actual pay for All Other Employees, per Act 256/2006 SLH.

** Schedule compiled by ERS Staff from actuary reports.

Ten-Year Actuarial Schedules (continued)

Employer Appropriations to Pension Accumulation Fund**

Appropriation Years 2001-2002 to 2010-2011

(Amounts in Millions)

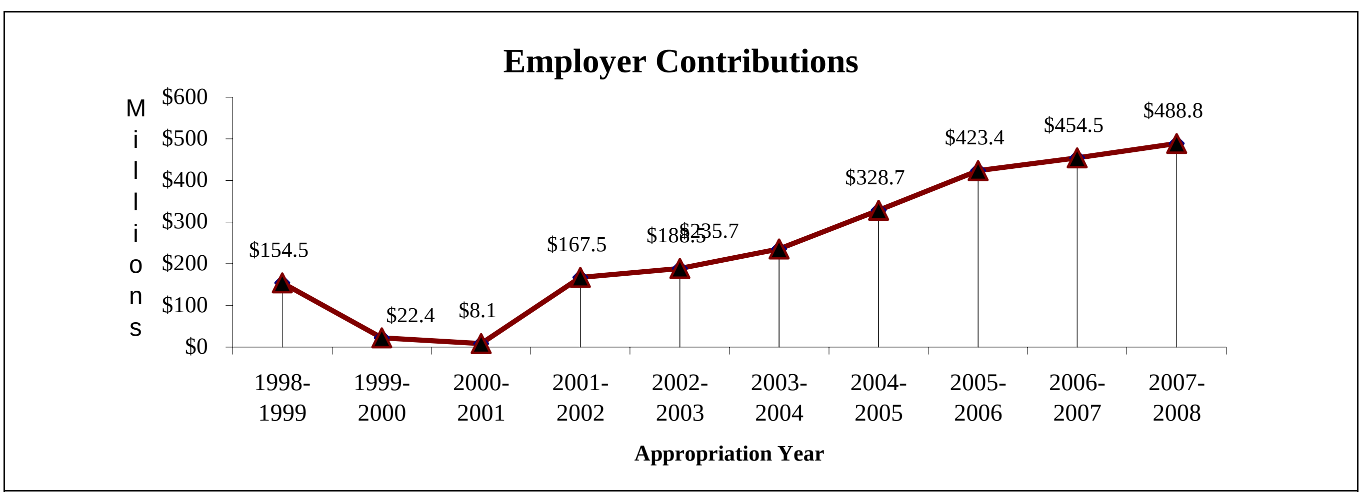
	Investment Yield Rate					
Fiscal Year	Assumed for Actuarial Valuation	Actuarial Investment Return	Appropriation Year	Total Calculated Contribution (1)	Investment Earnings Adjustment	Employer Appropriations
1998-1999	8.0%	12.33%	2001-2002	201.2	(33.7)	167.5
1999-2000	8.0%	12.58%	2002-2003	188.5	-	188.5
2000-2001	8.0%	8.91%	2003-2004	235.7	-	235.7
2001-2002	8.0%	2.62%	2004-2005	328.7	-	328.7
2002-2003	8.0%	0.18%	2005-2006	N/A	-	N/A
2003-2004	8.0%	0.80%	2006-2007	N/A	-	N/A
2004-2005	8.0%	4.76%	2007-2008	N/A	-	N/A
2005-2006	8.0%	9.76%	2008-2009	N/A	-	N/A
2006-2007	8.0%	12.98%	2009-2010	N/A	-	N/A
2007-2008	8.0%	8.89%	2010-2011	N/A	-	N/A

Notes: (1) 2001 results adjusted for reamortization of Unfunded Actuarial Accrued Liability and Early Incentive Retirement Program to June 30, 2029 under Act 147/2002.

(2) Beginning with the valuation for fiscal year 1996-97 (appropriation fiscal year 1999-2000), the actuarial investment income is the sum of the expected net investment income based on the actuarial assumption of 8% and a four-year smoothing of the difference between the market value of assets at year-end and the expected actuarial value of assets. In prior years, the actuarial investment income was the sum of interest, dividends, and net realized gains less net realized losses and investment expenses.

(3) Beginning fiscal year 2005/2006 employers will contribute 15.75% of actual payroll for Police and Fire and 13.75% for All Other Employees, per Act 181/2004 SLH. Effective July 1, 2008, the employer contribution rate increased to 19.00% of actual pay for Police and Fire and 15.70% of actual pay for All Other Employees, per Act 256/2006 SLH.

** Schedule compiled by ERS Staff from actuary reports.



State Retirement System's Funded Ratios

Funded Ratio	Number of General State Retirement Systems (excluding separate systems for teachers, school employees, or municipal employees)				
100% or more	7	Oregon PERS	110.5%	Delaware SEPP	103.7%
		North Carolina TSERS	106.1%	Utah URS	100.8%
		Florida FRS	105.6%	Vermont VSRS	100.8%
		Idaho PERS	105.5%		
90% to 99%	15	Wisconsin WRS	99.5%	Wyoming WRS	94.0%
		Indiana PERF	97.6%	North Dakota PERS	93.4%
		Pennsylvania PSERS	97.1%	New Mexico PERA	92.8%
		South Dakota SDRS	97.1%	Ohio PERS	92.6%
		West Virginia PERS	97.0%	Minnesota MSRS	92.5%
		Tennessee SETHEEPP	96.2%	Montana PERS	91.1%
		Texas ERS	95.6%	Iowa PERS	90.2%
		Georgia ERS	94.5%		
80% to 89%	8	Arkansas PERS	89.1%	Michigan MSERS	85.1%
		California PERS	87.2%	Arizona ASRS	83.3%
		Missouri MOSERS	86.8%	Alabama ERS	81.1%
		Massachusetts SERS	85.1%	Virgina VRS	80.8%
70% to 79%	9	Nevada PERS	78.8%	Colorado PERA	73.3%
		Alaska PERS	78.2%	Washington PERS	73.1%
		New Jersey PERS	76.6%	Oklahoma PERS	72.6%
		Maryland MSRPS	74.7%	Maine MSRS	71.1%
		Mississippi PERS	73.7%		
Less than 70%	9	South Carolina SCRS	69.6%	Kentuucky KERS	58.4%
		Kansas PERS	69.4%	Illinois SERS	54.2%
		Hawaii ERS *	**67.5%**	Rhode Island ERSRI	53.4%
		Louisiana LASERS	67.2%	Connecticut SERS	53.3%
		New Hampshire NHRS	67.0%		

Compiled from various sources by Gabriel, Roeder, Smith & Company

Note: GASB 25 funded ratios are shown for 48 general state retirement systems for valuation year(s) through January 1, 2008. A funded ratio is not shown for the Nebraska System because it is a defined contribution plan. A funded ratio for the New York System does not exist because of the use of the Aggregate Cost Method.

*** Hawaii's GASB 25 funded ratio for the fiscal year ended June 30, 2008 was 68.5%.**

Employees' Retirement System

of the State of Hawaii

STATISTICAL SECTION

Summary

Plan Membership

Membership in the ERS increased by 2,567 to 108,696 for FY 2008, or slightly more than 2.4 percent for the year. Active members increased by 1,338, retired members and beneficiaries increased by 936, and terminated-vested members increased by 293. Membership data for the last ten years ended June 30, 2008 may be found on the following pages.

Net Assets vs. Liabilities

The charts on page 112 graphically represent the funding progress of the ERS for the ten years ended June 30, 2008. The area charts show the portion of the pension liabilities that are unfunded compared to the portion covered by assets in the pension trust and illustrate the funded ratio of the ERS for the ten years ended June 30, 2008.

The existence of the unfunded actuarial accrued liabilities is not necessarily an indication of the inability to meet financial obligations, but the existence of the unfunded actuarial accrued liabilities is important and must be monitored and controlled.

The remainder of this section contains various statistical and historical data considered useful in evaluating the condition of the ERS.

All nonaccounting data is taken from ERS' internal sources except for that information which is derived from the actuarial valuations.

Changes in Plan Net Assets

Last Ten Fiscal Years

Fiscal Year Ended June 30,:	1999	2000	2001	2002	2003
Additions					
Employer Contributions	$ 154,469,844	$ 22,392,100	$ 8,131,900	$ 167,458,900	$ 190,586,276
Member contributions	55,702,647	57,358,185	54,489,895	55,451,216	57,214,521
Investment income (net of expense)	904,809,348	695,151,054	(679,605,059)	(503,995,093)	146,140,751
Total additions to plan net assets	1,114,981,839	774,901,339	(616,983,264)	(281,084,977)	393,941,548
Deductions					
Benefits	478,744,074	514,401,221	544,906,809	565,559,305	602,805,080
Refunds	4,454,658	4,318,654	3,892,377	3,244,334	2,605,602
Administrative expenses	3,775,942	4,168,717	4,893,712	5,754,832	6,780,824
Other	29,272	-	-	-	2,800
Total deductions from plan net assets	487,003,946	522,888,592	553,692,898	574,558,471	612,194,306
Change in plan net assets	$ 627,977,893	$ 252,012,747	$ (1,170,676,162)	$ (855,643,448)	$ (218,252,758)
Plan net assets, beginning of year	9,051,781,611	9,679,759,504	9,931,772,251	8,761,096,089	7,905,452,641
Plan net assets, end of year	$9,679,759,504	$9,931,772,251	$ 8,761,096,089	$ 7,905,452,641	$ 7,687,199,883

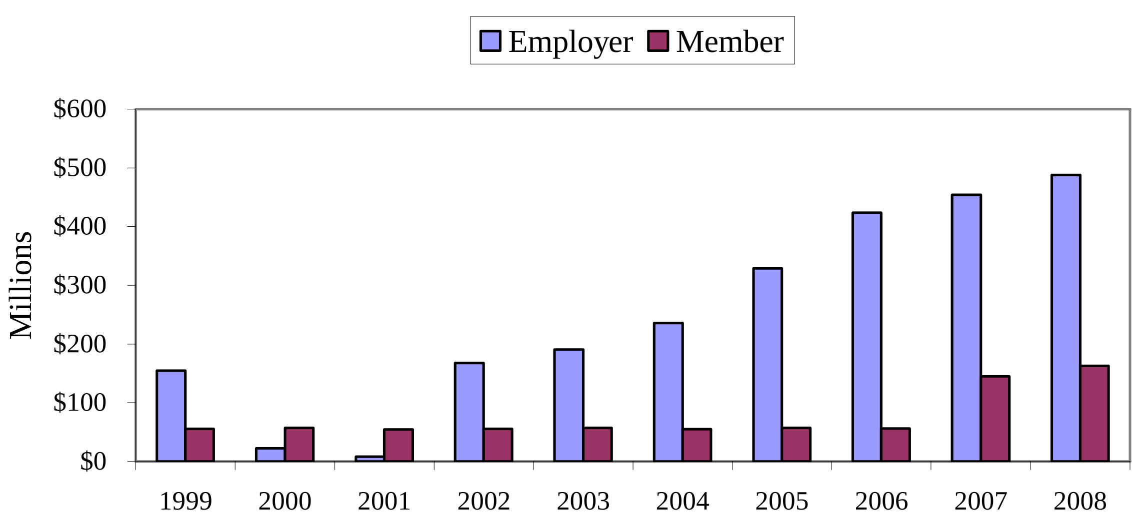
Fiscal Year Ended June 30,:	2004	2005	2006	2007	2008
Additions					
Employer Contributions	$ 235,685,796	$ 328,716,718	$ 423,445,597	$ 454,494,286	$ 488,770,028
Member contributions	55,116,452	57,054,621	56,257,953	144,658,185	163,375,639
Investment income (net of expense)	1,236,414,927	931,710,183	988,347,837	1,704,957,268	(461,063,080)
Total additions to plan net assets	1,527,217,175	1,317,481,522	1,468,051,387	2,304,109,739	191,082,587
Deductions					
Benefits	636,214,617	676,316,347	720,542,990	761,004,748	792,312,830
Refunds	2,328,796	3,442,466	2,487,279	3,497,590	3,668,857
Administrative expenses	10,468,508	7,259,906	8,477,837	9,601,756	10,728,801
Other	-	-	-	-	-
Total deductions from plan net assets	649,011,921	687,018,719	731,508,106	774,104,094	806,710,488
Change in plan net assets	$ 878,205,254	$ 630,462,803	$ 736,543,281	$ 1,530,005,645	$ (615,627,901)
Plan net assets, beginning of year	7,687,199,883	8,565,405,137	9,195,867,940	9,932,411,221	11,462,416,866
Plan net assets, end of year	$8,565,405,137	$9,195,867,940	$ 9,932,411,221	$ 11,462,416,866	$ 10,846,788,965

Contributions

Employer Contribution Rates as a Percentage of Payroll

Fiscal Year	Police & Firefighters	All Other Employees	Composite Rate
1999	15.48%	6.80%	7.66%
2000	4.35%	9.75%	9.22%
2001	8.04%	10.45%	10.20%
2002	10.34%	11.49%	11.38%
2003	15.33%	14.47%	14.55%
2004	15.75%	13.75%	13.95%
2005	15.75%	13.75%	13.95%
2006	15.75%	13.75%	13.95%
2007	15.75%	13.75%	13.95%
2008	15.75%	13.75%	13.95%

Contributions



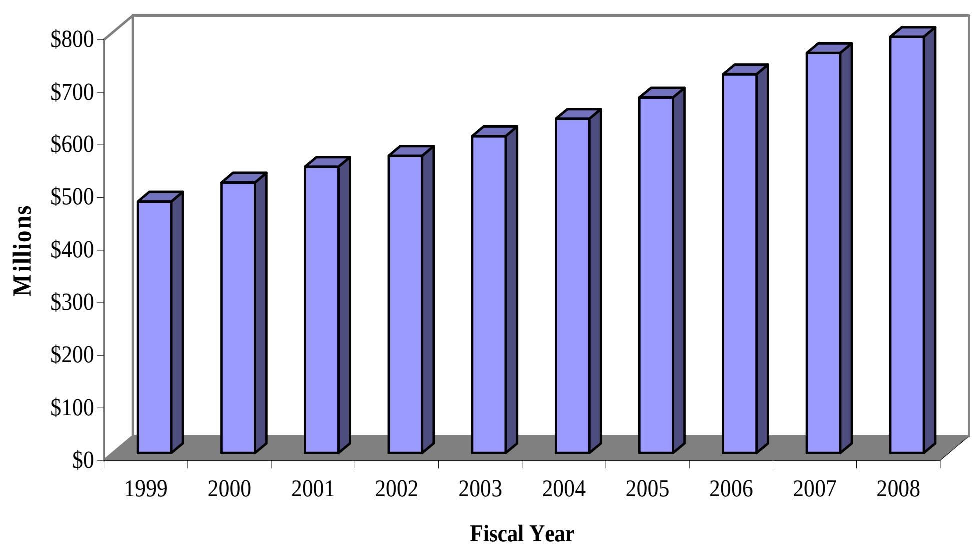
Deductions from Plan Net Assets for Benefit Payments by Type

Last Ten Fiscal Years

Fiscal Year Ended June 30,:	1999	2000	2001	2002	2003
Recurring benefit payments					
Service	$ 431,410,418	$ 460,293,937	$ 491,957,932	$ 518,579,831	$ 557,439,020
Disability	8,055,791	8,305,398	8,950,018	9,336,267	10,047,637
Death	4,581,030	2,644,579	2,369,546	2,465,179	1,749,855
subtotal	444,047,239	471,243,914	503,277,496	530,381,277	569,236,512
Refund Option payments (one-time)	34,696,835	43,157,307	41,629,313	35,178,028	33,568,568
Total benefit payments	$ 478,744,074	$ 514,401,221	$ 544,906,809	$ 565,559,305	$ 602,805,080

Fiscal Year Ended June 30,:	2004	2005	2006	2007	2008
Recurring benefit payments					
Service	$ 594,915,118	$ 632,088,342	$ 673,165,361	$ 712,580,450	$ 748,158,330
Disability	10,502,367	11,780,739	12,666,891	13,432,834	13,707,170
Death	3,147,690	2,793,149	3,875,024	2,794,068	2,293,557
subtotal	608,565,175	646,662,230	689,707,276	728,807,352	764,159,057
Refund Option payments (one-time)	27,649,442	29,654,117	30,835,714	32,197,396	28,153,773
Total benefit payments	$ 636,214,617	$ 676,316,347	$ 720,542,990	$ 761,004,748	$ 792,312,830

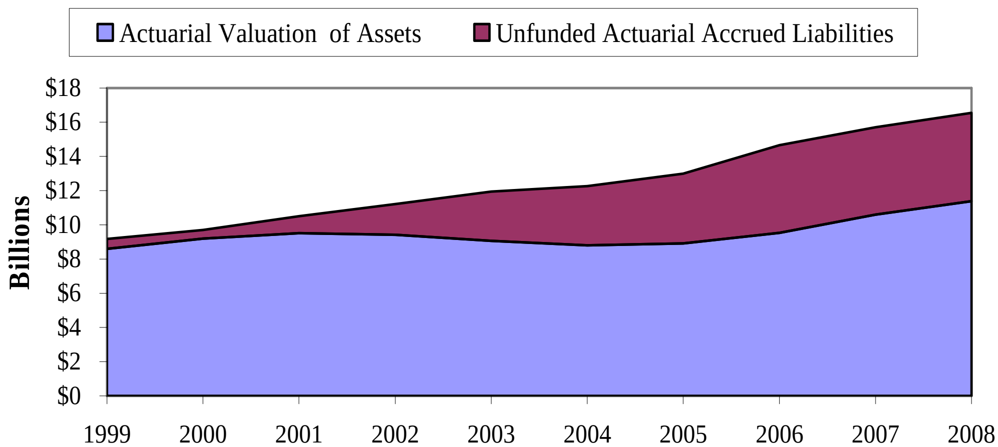
Benefit Payments



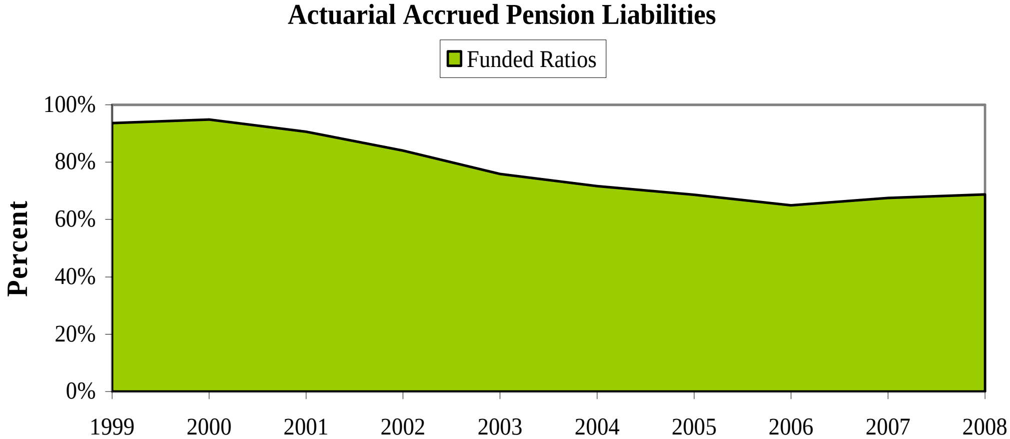
Actuarial Valuation of Assets vs. Actuarial Pension Liabilities

	Dollars in Billions			
Fiscal Year	Actuarial Valuation of Assets	Unfunded Actuarial Liabilities	Actuarial Accrued Liabilities	Funded Ratios
1999	$ 8.591	$ 0.591	$ 9.182	93.6%
2000	9.205	0.494	9.699	94.9%
2001	9.516	0.991	10.507	90.6%
2002	9.415	1.795	11.210	84.0%
2003	9.074	2.878	11.952	75.9%
2004	8.797	3.474	12.271	71.7%
2005	8.915	4.071	12.986	68.6%
2006	9.529	5.132	14.661	65.0%
2007	10.590	5.107	15.697	67.5%
2008	11.381	5.168	16.549	68.8%

Actuarial Accrued Liabilities



Actuarial Valuation of Assets as a Percent of Actuarial Accrued Pension Liabilities

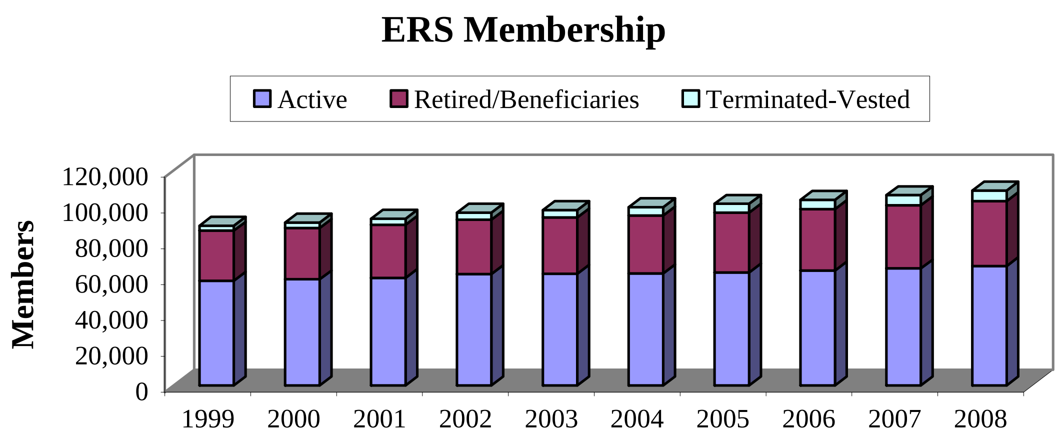


Participating Employers and Membership in ERS

Last Ten Fiscal Years

ERS Membership

As of March 31,:	Active	Retired/Beneficiaries	Terminated-Vested	Totals
1999	58,387	27,950	2,777	89,114
2000	59,191	28,715	3,016	90,922
2001	59,992	29,660	3,416	93,068
2002	62,208	30,330	3,835	96,373
2003	62,292	31,389	4,150	97,831
2004	62,573	32,297	4,501	99,371
2005	63,073	33,301	4,938	101,312
2006	64,069	34,304	5,164	103,537
2007	65,251	35,324	5,554	106,129
2008	66,589	36,260	5,847	108,696



Participating Employers and Active Members

As of March 31,:	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
State of Hawaii	44,645	45,451	46,185	48,242	48,445	48,704	49,203	49,973	50,756	51,719
City & County of Honlulu	8,215	8,190	8,236	8,323	8,223	8,158	8,101	8,167	8,363	8,512
- Board of Water Supply	673	657	616	589	568	554	568	560	556	526
Hawaii County	1,998	2,034	2,043	2,056	2,028	2,081	2,097	2,223	2,315	2,459
Kauai County	978	992	1,000	1,042	1,034	1,051	1,067	1,088	1,109	1,125
Maui County	1,878	1,867	1,912	1,956	1,994	2,025	2,037	2,055	2,152	2,248
Total	58,387	59,191	59,992	62,208	62,292	62,573	63,073	64,066	65,251	66,589

Benefit Payments by Retirement Type and Option

As of March 31, 2008

Retired Contributory Members

Monthly Benefit	Number of Recipients	Type of Retirement *					Retirement Option						
		1	2	3	4	5	Max	Opt. 1	Opt. 2	Opt. 3	Opt. 4	Opt. 5	Other
$ 1 - 300	1,332	1,095	12	13	1	211	342	377	174	61	137	238	3
301 - 600	2,358	1,963	118	39	9	229	295	233	140	60	646	980	4
601 - 900	2,381	1,996	92	61	12	220	259	162	125	47	905	878	5
901 - 1,200	2,324	2,010	46	81	8	179	228	156	119	58	946	814	3
1,201 - 1,500	2,140	1,936	19	60	4	121	200	117	99	32	918	772	2
1,501 - 1,800	2,141	1,992	13	34	7	95	151	90	108	37	938	810	7
1,801 - 2,100	2,050	1,943	3	26	4	74	142	78	71	25	858	872	4
2,101 - 2,400	2,056	1,986	3	14	3	50	135	45	60	24	829	960	3
2,401 - 2,700	1,983	1,910	3	8	5	57	149	54	64	39	832	840	5
2,701 - 3,000	1,672	1,628	1	5	3	35	149	43	62	33	890	492	3
3,001	4,794	4,681	-	12	4	97	629	164	256	171	2,717	857	-
	25,231	23,140	310	353	60	1,368	2,679	1,519	1,278	587	10,616	8,513	39

Retired Hybrid Members

Monthly Benefit	Number of Recipients	Type of Retirement *					Retirement Option						
		1	2	3	4	5	Max	Opt. 1	Opt. 2	Opt. 3	Opt. 4	Opt. 5	Other
$ 1 - 300	2	1	1	-	-	-	-	-	2	-	-	-	-
301 - 600	37	33	-	-	2	2	17	6	5	6	3	-	-
601 - 900	92	73	11	-	5	3	42	8	28	9	4	1	-
901 - 1,200	84	62	14	2	2	4	32	7	21	12	5	7	-
1,201 - 1,500	68	54	5	2	2	5	30	2	16	13	3	4	-
1,501 - 1,800	63	58	3	-	-	2	20	2	19	9	7	6	-
1,801 - 2,100	53	51	1	-	-	1	22	4	13	8	4	2	-
2,101 - 2,400	48	46	1	-	-	1	15	4	13	10	3	3	-
2,401 - 2,700	61	59	1	-	1	-	20	8	16	11	6	-	-
2,701 - 3,000	37	36	-	-	-	1	11	2	8	10	4	2	-
3,001	91	91	-	-	-	-	38	5	12	17	12	7	-
	636	564	37	4	12	19	247	48	153	105	51	32	-

Retired Noncontributory Members

Monthly Benefit	Number of Recipients	Type of Retirement *					Retirement Option				
		1	2	3	4	5	Max	Opt. A	Opt. B	Opt. C	Other
$ 1 - 300	831	533	62	25	83	128	286	152	264	40	89
301 - 600	2,279	1,686	257	65	60	211	1,145	330	610	134	60
601 - 900	1,497	1,154	159	17	30	137	770	255	357	82	33
901 - 1,200	1,031	870	71	6	11	73	527	190	238	59	17
1,201 - 1,500	810	705	51	1	3	50	417	145	196	43	9
1,501 - 1,800	650	589	19	-	2	40	322	122	151	54	1
1,801 - 2,100	757	725	9	-	3	20	429	142	118	67	1
2,101 - 2,400	943	922	5	-	-	16	621	147	92	81	2
2,401 - 2,700	663	649	1	-	-	13	479	95	45	42	2
2,701 - 3,000	363	353	-	-	-	10	234	65	47	17	-
3,001	569	551	-	-	2	16	354	120	70	22	3
	10,393	8,737	634	114	194	714	5,584	1,763	2,188	641	217

* Type of Retirement

1 – Normal retirement for age & service
2 – Ordinary disability retirement
3 – Occupational disability retirement
4 – Survivor payment – death in service
5 – Survivor payment – normal or disability retirement

Note: Refer to Plan Summary in the Introductory Section for descriptions of the types of retirements and benefit options selected by the members.

Average Monthly Service Pensions

by Years of Credited Service

As of March 31,		Years of Credited Service 0-9	10-14	15-19	20-24	25-29	30-34	35+	All
1999	Average Monthly Benefit	$212	$421	$710	$1,010	$1,645	$1,986	$2,143	$1,369
	Number of Active Retirants	1,409	3,012	2,882	3,266	6,306	5,879	2,854	25,608
2000	Average Monthly Benefit	$221	$426	$730	$1,032	$1,691	$2,044	$2,210	$1,414
	Number of Active Retirants	1,368	3,107	2,941	3,336	6,435	6,139	2,936	26,262
2001	Average Monthly Benefit	$225	$435	$746	$1,058	$1,739	$2,101	$2,269	$1,462
	Number of Active Retirants	1,322	3,192	3,001	3,416	6,598	6,508	3,052	27,089
2002	Average Monthly Benefit	$241	$467	$800	$1,140	$1,837	$2,200	$2,380	$1,523
	Number of Active Retirants	1,366	3,443	3,098	3,459	6,970	6,592	2,669	27,597
2003	Average Monthly Benefit	$241	$449	$788	$1,125	$1,837	$2,216	$2,384	$1,533
	Number of Active Retirants	1,298	3,535	3,166	3,581	7,127	7,037	2,802	28,546
2004	Average Monthly Benefit	$246	$463	$804	$1,156	$1,892	$2,298	$2,494	$1,597
	Number of Active Retirants	1,238	3,635	3,207	3,654	7,180	7,439	2,917	29,270
2005	Average Monthly Benefit	$255	$473	$823	$1,187	$1,951	$2,386	$2,599	$1,663
	Number of Active Retirants	1,193	3,738	3,244	3,715	7,233	7,806	3,091	30,020
2006	Average Monthly Benefit	$261	$489	$843	$1,210	$2,007	$2,446	$2,679	$1,719
	Number of Active Retirants	1,149	3,790	3,330	3,813	7,346	8,083	3,313	30,824
2007	Average Monthly Benefit	$272	$504	$865	$1,240	$2,064	$2,509	$2,765	$1,773
	Number of Active Retirants	1,126	3,907	3,393	3,918	7,470	8,315	3,536	31,665
2008	Average Monthly Benefit	$291	$518	$882	$1,266	$2,119	$2,574	$2,853	$1,824
	Number of Active Retirants	1,137	3,981	3,481	4,034	7,560	8,511	3,737	32,441

Retirees and Beneficiaries

(Recurring Benefit Payments)

Tabulated by Fiscal Year of Retirement as of March 31, 2008

Valuation Year	Number	Total Annual Benefits	Monthly Average Benefit	Valuation Year	Number	Total Annual Benefits	Monthly Average Benefit
1930	1	$ 374	$ 31	1982	575	$ 8,529,820	$ 1,236
1953	2	2,669	111	1983	667	10,743,873	1,342
1955	2	6,212	259	1984	715	11,776,206	1,373
1957	2	15,265	636	1985	802	14,114,275	1,467
1958	4	28,094	585	1986	886	16,159,825	1,520
1959	5	29,812	497	1987	1,319	25,606,730	1,618
1960	5	42,215	704	1988	774	12,397,041	1,335
1961	7	36,182	431	1989	924	16,735,608	1,509
1962	6	46,400	644	1990	994	19,770,061	1,657
1963	5	30,467	508	1991	1,117	22,884,648	1,707
1964	12	85,848	596	1992	1,022	22,875,985	1,865
1965	8	75,336	785	1993	1,071	25,542,204	1,987
1966	19	155,636	683	1994	1,124	26,080,734	1,934
1967	13	128,118	821	1995	2,084	58,500,067	2,339
1968	17	135,900	666	1996	1,988	52,752,681	2,211
1969	40	336,018	700	1997	794	15,742,394	1,652
1970	49	460,460	783	1998	808	15,437,791	1,592
1971	42	332,851	660	1999	1,156	24,870,842	1,793
1972	100	1,162,602	969	2000	1,370	31,064,543	1,890
1973	127	1,520,864	998	2001	1,591	35,692,104	1,869
1974	102	1,060,465	866	2002	1,313	29,940,199	1,900
1975	164	1,912,665	972	2003	1,693	42,254,447	2,080
1976	203	2,580,006	1,059	2004	1,645	38,184,448	1,934
1977	290	3,922,057	1,127	2005	1,725	40,317,457	1,948
1978	302	4,323,865	1,193	2006	1,690	37,070,275	1,828
1979	378	5,292,203	1,167	2007	1,810	38,749,027	1,784
1980	435	6,200,080	1,188	2008	1,719	35,487,605	1,720
1981	544	7,612,127	1,166				
				Total	36,260	$ 766,815,681	$ 1,762

Total Benefits Payable

(Recurring Benefit Payments)

Tabulated by Attained Ages of Benefit Recipients as of March 31, 2008

	Service Retirement		Disability Retirement		Survivors and Beneficiaries		Total	
Attained Ages	No.	Annual Benefits	No.	Annual Benefits	No.	Annual Benefits	No.	Annual Benefits
Under 20	-	-	-	-	56	$ 155,142	56	$ 155,142
20-24	-	-	-	-	14	159,316	14	$ 159,316
25-29	-	-	-	-	21	170,709	21	$ 170,709
30-34	-	-	1	$ 2,746	47	516,589	48	$ 519,335
35-39	-	-	13	130,200	52	534,117	65	$ 664,317
40-44	10	$ 309,201	44	453,324	74	852,920	128	$ 1,615,445
45-49	92	3,483,090	110	933,880	90	859,659	292	$ 5,276,629
50-54	587	19,513,920	194	1,887,465	158	1,839,129	939	$ 23,240,514
55-59	3,262	95,632,394	311	3,410,539	243	3,243,343	3,816	$ 102,286,276
60-64	6,401	163,588,050	291	2,781,319	297	4,471,207	6,989	$ 170,840,576
65-69	6,142	143,104,961	167	1,769,615	297	4,541,967	6,606	$ 149,416,543
70-74	5,532	120,010,314	90	910,616	275	3,716,227	5,897	$ 124,637,157
75-79	4,796	91,738,911	94	1,084,687	327	4,743,913	5,217	$ 97,567,511
80-84	3,341	54,013,457	74	717,099	221	2,448,570	3,636	$ 57,179,126
85-89	1,613	22,610,617	43	423,932	138	1,438,388	1,794	$ 24,472,937
90-94	543	6,511,606	8	65,098	46	449,141	597	$ 7,025,845
95-99	107	1,314,275	10	56,824	10	44,816	127	$ 1,415,915
100	8	73,208	1	17,564	1	3,659	10	$ 94,431
101	3	29,075	-	-	-	-	3	$ 29,075
102	2	28,218	-	-	-	-	2	$ 28,218
103	1	5,351	1	8,734	-	-	2	$ 14,085
104	1	6,579	-	-	-	-	1	$ 6,579
Total	32,441	$ 721,973,227	1,452	$ 14,653,642	2,367	$ 30,188,812	36,260	$ 766,815,681

Average Benefits