EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Financial Statements

June 30, 2009 and 2008

(With Independent Auditors' Report Thereon)

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

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KPMG LLP
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Independent Auditors' Report

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, 2009 and 2008, 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, 2009 and 2008, and its changes in plan net assets for the years then ended, in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 6, 2011, 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 3 through 10 and the schedules of funding progress and employer contributions on pages 36 and 37 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, 2009 and 2008 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.

KPMG LLP

December 6, 2011

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, 2009 and 2008. 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 comprises the following components:

- The combining statements of plan net assets provide a snapshot of the financial position of the ERS at June 30, 2009 and 2008. 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, 2008 to June 30, 2009 (FY 2009) and the fiscal year from July 1, 2007 to June 30, 2008 (FY 2008). The financial statements measure the changes in the resources available to pay pension benefits to members, retirees, and beneficiaries for fiscal years 2009 and 2008.
- 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.

(Continued)

- During the fiscal year ended June 30, 2009, plan net assets decreased by $2.0 billion, or approximately 18.7%, from $10.8 billion as of June 30, 2008. 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. The decrease in assets during the past two fiscal years reflects the instability in the global markets and loss of investor confidence worldwide. This compared to an increase in net plan assets of $1.5 billion, or 15.4%, during fiscal year ended June 30, 2007.
- The ERS experienced a 17.5% and 3.5% loss on investments during FY 2009 and FY 2008 compared to the positive return on pension plan assets of 17.7% return in FY 2007. Most assets classes experienced negative returns due to worldwide economic troubles; however, the fixed income produced consistently strong returns.
- No significant legislation was enacted during the 2009 or 2008 legislative sessions that impacted the benefit provisions of the Pension Trust. In FY 2007, ERS implemented a new contributory "Hybrid Plan" from 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 has resulted in an overall increase in member contributions due to the number of Noncontributory Plan members that elected to transfer to the Hybrid Plan and new hires.
- The employer contribution requirements increased effective July 1, 2008, in order to improve the funding status of the Pension Trust. See the "Legislative Highlights 2009" in the Introductory Section of the CAFR for a summary of the 2009 legislative changes affecting the ERS and its membership. A historical summary of legislation impacting the ERS actuarial valuations is located in the "Summary of Plan Changes" in the Actuarial Section.
- The funded ratio decreased to 64.6% as of June 30, 2009 with the continued investment losses experienced over the past two years. This compares with an increase in the funded ratio to 68.8% on June 30, 2008 as a result of providing for market smoothing to realize actuarial investment gains and losses and compares to 67.5% on June 30, 2007. The corresponding unfunded actuarial accrued liability (UAAL) of the ERS increased to $6.2 billion on June 30, 2009 after remaining relatively stable at $5.2 billion, and $5.1 billion on June 30, 2008 and 2007, respectively. Please refer to the ERS' 2008 and 2007 CAFR for results of the actuarial valuation for those years.
- Total employee and employer contributions increased by $104.3 million, or 16.0%, during FY 2009; $53.0 million, or 8.8%, during FY 2008; and $119.4 million, or 24.9%, during FY 2007. Increases for FY 2009 were due to the increase in required employer contribution rates, while 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.
- Total pension plan benefit payouts increased $41.4 million or 5.2% during FY 2009 to $833.7 million compared to $31.3 million or 4.1% during FY 2008 to $792.3 million, and an increase of $40.5 million, or 5.6%, during FY 2007 to $761.0 million. Pension benefits continues to increase due to additional retirees and beneficiaries (36,999 in 2009, 36,260 in 2008, and 35,324 in 2007), an increase in the average pension benefit for new retirees, and the annual 2.5% postretirement increase.

- Administrative expenses increased by $2.3 million to $13.0 million in FY 2009, $1.1 million to $10.7 million in FY 2008, and $1.1 million to $9.6 million in FY 2007. Administrative expenses for all years were within the ERS' budgeted amounts. The main increase in FY 2009 was due to an increase in maintenance costs for ERS' new pension management system and obtaining additional resources to manage backlogs resulting from the undertaking of several multiyear projects in 2005 that had implementation deadlines. The significant increase in maintenance fees is from implementing current computer technology for our pension management and imaging systems, and the expiration of the warranty periods for these recently installed systems. Higher costs were due to obtaining additional resources to handle backlogs resulting from increased workload of projects and staff vacancies; negotiated pay raises for employees; and increased communication mailings with the computer system conversion.
- Increases in FY 2007 and FY 2008 expenses were due to increased staffing and several multiyear projects undertaken in late-FY 2005 to improve services and benefits to our members. The projects included the development of 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.

Analysis of Plan Net Assets for Pension Trust

Summary of Plan Net Assets

June 30, 2009, 2008, and 2007

(Dollars in millions)

	2009	2008	FY 2009 percentage change	2007	FY 2008 percentage change
Assets:					
Cash and short-term investments	$ 413.5	716.3	(42.3)%	$ 805.9	(11.1)%
Receivables	443.3	384.0	15.4	260.9	47.2
Investments	8,922.1	11,034.3	(19.1)	11,367.5	(2.9)
Invested securities lending collateral	758.8	1,235.0	(38.6)	1,457.1	(15.2)
Capital assets	11.6	11.4	1.8	9.6	18.8
Total assets	10,549.3	13,381.0	(21.2)	13,901.0	(3.7)
Liabilities:					
Securities lending liability	758.8	1,235.0	(38.6)	1,457.1	(15.2)
Investment accounts and other payables	975.2	1,299.2	(24.9)	981.5	32.4
Total liabilities	1,734.0	2,534.2	(31.6)	2,438.6	3.9
Plan net assets	$ 8,815.3	10,846.8	(18.7)	$ 11,462.4	(5.4)

Summary of Changes in Plan Net Assets

June 30, 2009, 2008, and 2007

(Dollars in millions)

	2009	2008	FY 2009 percentage change	2007	FY 2008 percentage change
Additions:					
Contributions	$ 756.4	652.1	16.0 %	$ 599.1	8.8%
Net investments income (loss)	(1,937.3)	(461.0)	320.2	1,705.0	(127.0)
Total additions	(1,180.9)	191.1	(717.9)	2,304.1	(91.7)
Deductions:					
Retirement benefit payments	833.7	792.3	5.2	761.0	4.1
Refund of contributions	3.9	3.7	5.4	3.5	5.7
Administrative expenses	13.0	10.7	21.5	9.6	11.5
Total deductions	850.6	806.7	5.4	774.1	4.2
Increase (decrease) in plan net assets	$ (2,031.5)	(615.6)	230.0	$ 1,530.0	(140.2)

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 2009, the ERS incurred a 17.50% loss on investment assets due to losses in the real estate and equity markets. In FY 2008, the ERS experienced a 3.50% loss on investment assets with the start of turmoil in the world economy after several years of positive returns. The ERS' Pension Trust assets earned 17.70% on the investment portfolio in FY 2007. Only the international fixed income asset class had earnings in excess of the 8% portfolio benchmark for FY 2009 with returns of 9.82%, while domestic fixed income earned 5.80%. These positive earnings were more than offset by negative return in the remaining asset classes of domestic and international equities, real estate, and alternative investments of (27.30)%, (31.50)%, (26.70)%, and (11.19)%, respectively. The overall net investment loss resulting from the double-digit negative returns in FY 2009 was $1,937.3 million, following a net loss of $461.0 million in FY 2008, and net investment income of $1,705.0 million in FY 2007.

The asset distribution of the ERS' investment securities for the Pension Trust, excluding pending trade settlements and securities lending collateral, at June 30, 2009, 2008, and 2007 is presented below at fair value. Investment balances between the asset classes will change over time based on market sectors' performance and our rebalancing efforts to maintain asset allocation targets. Changes will also occur for financial reporting since certain real estate and alternative investments are reported on the consolidated method of accounting using the value of the underlying investments since ERS is the majority owner of the business organization. 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 2009 and 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, with increases used to pay pension benefits and fund real estate and fixed income managers.

Asset Class

June 30, 2009, 2008, and 2007

(Dollars in millions)

	2009	Percentage	2008	Percentage	2007	Percentage
Short-term investments and cash	$ 413.5	4.5%	$ 716.3	6.1%	$ 805.9	6.6%
Equity securities	4,541.7	48.6	6,156.2	52.4	7,126.2	58.5
Fixed income	3,000.9	32.1	3,258.3	27.7	2,729.2	22.4
Real estate	950.0	10.2	1,163.5	9.9	1,119.1	9.2
Alternative investments	429.5	4.6	456.4	3.9	393.1	3.2
Total assets	9,335.6	100.0%	11,750.7	100.0%	12,173.5	100.0%
Less loans on real estate and alternative investments	257.9		283.0		281.0	
Total	$ 9,077.7		$ 11,467.7		$ 11,892.5	

Fixed income securities decreased in FY 2009 from cash requirements to pay pension benefits, although there were positive investment earnings. Fixed income securities increased in FY 2008 reflects positive investment earnings and rebalancing the portfolio per ERS' asset allocation strategy. In FY 2007, additional manager funding was offset by weak investment returns in the bond markets.

The decrease in real estate assets for FY 2009 reflects the decline in values following an increase in FY 2008 from 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.

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 2009 and FY 2008 due to lower asset values that are used to calculate investment manager fees. The decrease in FY 2007 investment manager fees was due to a smaller increase in asset values compared to the previous year. 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 combining statements of plan net assets. The decrease in FY 2009 investment management fees was also affected by the elimination of incentive fees accrued since certain asset values fell below the threshold return, which incentive fees are earned from.

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 $756.5 million, $652.1 million, and $599.1 million during FY 2009, FY 2008, and FY 2007, respectively. This represents an increase of $104.3 million, $53.0 million, and $119.4 million for the three years, respectively. Contributions increased during FY 2009 with higher employer contribution rates that became effective on July 1, 2008, higher employee salaries, and the continued increase in members required to make contributions to ERS. Effective July 1, 2008, legislation passed in FY 2007, which increased employer contributions from 15.75% to 19.70% of covered payroll for police officers and firefighters and 13.75% to 15.00% for all other employees. Please refer to the Financial Section in the ERS 2009 and 2008 Comprehensive Annual Financial Report (CAFR) for more information. 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.

Pension Plan Benefits and Expenses

Pension benefit payments are the primary expense of the ERS with payments totaling $833.7 million during FY 2009, $792.3 million during FY 2008, and $761.0 million during FY 2007. 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 postretirement increase for ERS' retirees.

Refunds to terminating members continued to increase slightly during the three years 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.

During FY 2009, administrative expenses increased $2.3 million due to increased postwarranty maintenance for ERS' new computer and imaging systems, special project consulting fees related to the finalization of benefit payments, and postage costs for informational mailings to members related to the transition of pension payments to our new pension management computer system. In FY 2008, administrative expenses increased $1.1 million to $10.7 million due to filling recently established positions and costs due to increased workload resulting from 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. The FY 2008 and 2007 expense increases relate 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. For FY 2008, the largest increase reflects professional fees to support staff assigned to the multiyear 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 multiyear 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, and 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 toward 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 decreased to 64.6% as of June 30, 2009 after increasing to 68.8% as of June 30, 2008, from 67.5% as of June 30, 2007. The ERS' UAAL increased to $6.2 billion after holding steady at $5.1 billion for several years. The decline in FY 2009 is primarily the result of investment losses in the past two fiscal years.

The improvement in the funded status as of June 2008 and 2007 and stabilizing of the UAAL during that time 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.

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.

Under the percentage of payroll methodology for employer contribution funding, 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, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* (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, 2009 was 28.2 years. This compares to 22.6 years and 25.5 years as of June 30, 2008 and 2007, 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.

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

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

June 30, 2009

	Pension Trust Employees' Retirement System	Agency Social Security Contribution	Total
Assets:			
Cash and short-term investments (notes C(2) and F):			
Cash	$ 26,590,042	—	26,590,042
Short-term investments	386,918,118	—	386,918,118
	413,508,160	—	413,508,160
Receivables:			
Accounts receivable and others	8,447,716	—	8,447,716
Investment sales proceeds	352,928,523	—	352,928,523
Accrued investment income	38,325,734	—	38,325,734
Employer appropriations	39,667,378	—	39,667,378
Member contributions	3,899,010	—	3,899,010
	443,268,361	—	443,268,361
Investments, at fair value (notes C(2) and F):			
Equity securities	4,541,676,625	—	4,541,676,625
Fixed income securities	3,000,889,114	—	3,000,889,114
Real estate investments	950,005,842	—	950,005,842
Alternative investments	429,565,075	—	429,565,075
	8,922,136,656	—	8,922,136,656
Other:			
Invested securities lending collateral (note F)	758,820,569	—	758,820,569
Equipment, at cost, net of depreciation	11,604,979	—	11,604,979
	770,425,548	—	770,425,548
Total assets	10,549,338,725	—	10,549,338,725
Liabilities:			
Disbursements in excess of cash balances (note F)	4,660,418	—	4,660,418
Accounts and other payables	42,126,168	—	42,126,168
Investment commitments payable	670,580,396	—	670,580,396
Securities lending collateral (note F)	758,820,569	—	758,820,569
Notes payable (note C(2))	257,866,002	—	257,866,002
Total liabilities	1,734,053,553	—	1,734,053,553
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 37)	$ 8,815,285,172	—	8,815,285,172

See accompanying notes to financial statements.

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

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

June 30, 2008

	Pension Trust: Employees' Retirement System	Agency: Social Security Contribution	Total
Assets:			
Cash and short-term investments (notes C(2) and F):			
Cash	$ 65,686,061	4,291	65,690,352
Short-term investments	650,617,640	9,471,937	660,089,577
	716,303,701	9,476,228	725,779,929
Receivables:			
Accounts receivable and others	8,510,307	—	8,510,307
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
	383,964,681	—	383,964,681
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	1,163,527,397	—	1,163,527,397
Alternative investments	456,361,916	—	456,361,916
	11,034,326,478	—	11,034,326,478
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	13,380,981,977	9,476,228	13,390,458,205
Liabilities:			
Disbursements in excess of cash balances (note F)	1,592,615	—	1,592,615
Accounts and other payables	60,375,577	—	60,375,577
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
Notes payable (note C(2))	283,045,778	—	283,045,778
Total liabilities	2,534,193,012	9,476,228	2,543,669,240
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 37)	$ 10,846,788,965	—	10,846,788,965

See accompanying notes to financial statements.

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Statements of Changes in Plan Net Assets – All Trust Funds

Years ended June 30, 2009 and 2008

	2009	2008
Additions:		
Appropriations and contributions (notes A(4) and E):		
Employers	$ 578,672,058	488,770,028
Members	177,781,610	163,375,639
Total contributions	756,453,668	652,145,667
Investment income (note F):		
From investing activities:		
Net depreciation in fair value of investments	(2,224,141,979)	(778,897,646)
Interest on fixed income securities	140,213,583	124,116,798
Income on real estate investments	88,239,771	112,013,702
Dividends on equity securities	111,671,360	111,807,589
Interest on short-term investments	7,458,746	23,169,090
Alternative investment income	8,022,909	33,960,293
Miscellaneous	3,978,365	4,404,811
	(1,864,557,245)	(369,425,363)
Less investment expenses	80,503,576	101,514,821
Net investment loss from investing activities	(1,945,060,821)	(470,940,184)
From securities lending activities:		
Securities lending income	15,777,475	61,308,269
Securities lending expenses:		
Borrower rebates	6,668,106	49,457,874
Management fees	1,366,017	1,973,291
Less securities lending activities expense	8,034,123	51,431,165
Net investment income from securities lending activities	7,743,352	9,877,104
Total net investment loss	(1,937,317,469)	(461,063,080)
Total additions	(1,180,863,801)	191,082,587
Deductions:		
Benefit payments (note A(3))	833,691,245	792,312,830
Refunds of member contributions	3,937,464	3,668,857
Administrative expenses	13,011,283	10,728,801
Total deductions	850,639,992	806,710,488
Net decrease in net assets	(2,031,503,793)	(615,627,901)
Net assets held in trust for pension benefits (note D):		
Beginning of year	10,846,788,965	11,462,416,866
End of year	$ 8,815,285,172	10,846,788,965

See accompanying notes to financial statements.

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, 2009 and 2008 are as follows:

	2009	2008
Employers:		
State	1	1
County	4	4
Total employers	5	5
Pensioners and beneficiaries currently receiving benefits:		
Pensioners currently receiving benefits:		
Police and firefighters	2,962	2,925
All others employees	31,467	30,968
Total pensioners	34,429	33,893
Beneficiaries currently receiving benefits:		
Police and firefighters	190	175
All others employees	2,380	2,192
Total beneficiaries	2,570	2,367
Total pensioners and beneficiaries	36,999	36,260
Terminated vested members entitled to benefits but not yet receiving benefits:		
Police and firefighters	242	198
All others employees	5,774	5,649
Total terminated vested members	6,016	5,847

(Continued)

	2009	2008
Current employees:		
Vested:		
Police and firefighters	3,917	3,904
All other employees	38,187	37,824
Nonvested:		
Police and firefighters	1,038	1,011
All other employees	24,770	23,850
Total current employees	67,912	66,589
Total membership	110,927	108,696

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 comprises 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 2.00%) 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.

For postretirement increases, every retiree's original retirement allowance is increased by 2½% on each July 1 following the calendar year of retirement. This cumulative benefit is not compounded and increases each year by 2½% of the original retirement allowance without a ceiling (2½% of the original retirement allowance the first year, 5% the second year, 7½% 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, firefighters, 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 2½% 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 1¼%.

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, 2009
Actuarial value of assets	$ 11,400,116,874
Actuarial Accrued Liability (AAL):	
Entry age	17,636,432,316
Unfunded AAL (UAAL)	$ 6,236,315,442
Percent funded	64.6%
Annual covered payroll	$ 4,030,121,060
UAAL percentage of covered payroll	155%

Multiyear 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, 2009 actuarial valuation is as follows:

Valuation date	June 30, 2009
Actuarial cost method	Entry Age Normal
Amortization method	Level percent, open
Remaining amortization period as of June 30, 2009	28.2 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)**	2.50

** 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.

The required pension contributions by all participating employers (in thousands) for the years ended June 30, 2009, 2008, and 2007 were $526,538, $510,727, and $476,754, respectively, which represented 13.1%, 13.5%, and 13.6%, respectively, of covered payroll. Actual contributions (in thousands) by all employers for the years ended June 30, 2009, 2008, and 2007 were $578,672, $488,770, and $454,494, respectively, which represented 109.9%, 95.7%, and 95.3%, respectively, 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, provide certain healthcare 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.

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 is as 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.

(Continued)

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, and 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. Use of leverage is restricted to certain asset classes in order to enhance yields of approved investments and/or to facilitate diversification of the portfolio. The use of debt must result in positive leverage where cash flow is in excess of debt service. 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 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.

Notes payable are shown at estimated fair values. Notes payable consist of mortgage notes within the limited liability companies and limited partnerships that are secured by real estate of the respective company.

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 4½% 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.

(Continued)

5. 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.

6. Reclassifications

Certain balances of the financial statements have been reclassified for the year ended June 30, 2008 to be comparable with the current year presentation.

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.

(Continued)

Net assets held in trust for pension benefits as of June 30, 2009 and 2008 are as follows:

		2009	2008
Pension Accumulation Fund	$	7,530,363,041	9,726,795,072
Annuity Savings Fund		1,270,761,230	1,105,627,636
Expense Fund		14,160,901	14,366,257
Total net assets held in trust for pension benefits	$	8,815,285,172	10,846,788,965

Note E – Contributions

The ERS' funding policy provides for periodic employer contributions expressed as a percentage of annual covered payroll. 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.

Since 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. As of July 1, 2008, employers contribute 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.

From July 1, 2005 to June 30, 2008, the required contribution rates for employers were 15.75% for their police officers and firefighters, and 13.75% for all other employees.

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.

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, 2009 and 2008, the carrying amount of deposits totaled approximately $26,590,042 and $64,097,737, respectively, and the corresponding bank balance was $26,793,679 and $68,023,794, respectively, of which $26,330,945 and $67,474,390, respectively, were exposed to custodial credit risk. The following shows the aggregate book and bank balances of all cash accounts:

		2009	2008
Carrying amounts of deposit – book:			
Cash	$	26,590,042	65,690,352
Disbursements in excess of cash balances		(4,660,418)	(1,592,615)
Total book balances	$	21,929,624	64,097,737

		2009	2008
Depository account – bank investment custodian:			
Insured	$	462,734	549,404
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)		1,371,183	3,288,164
Uninsured and uncollateralized		24,959,762	64,186,226
Total subject to custodial credit risk		26,330,945	67,474,390
Total bank balances	$	26,793,679	68,023,794

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, 2009 and 2008. Please refer to note C(2) above for a discussion of fair value on investments.

		2009	2008
Investments:			
Short-term securities pool, Social Security Contribution Fund	$	—	9,471,937
Short-term securities, domestic		—	32,000,524
Short-term securities, international		—	13,224,380
Short-term securities pools		386,918,118	605,293,129
Fixed income securities, domestic (including fixed income options, futures, swaps, and other fixed income of $(7,891,409) and $(6,773,761) as of June 30, 2009 and 2008, respectively)		2,013,742,531	1,959,136,223
Fixed income securities, international (including fixed income options, futures, and swaps of $6,849,080 and $(1,951,628) as of June 30, 2009 and 2008, respectively)		674,477,969	845,612,034
Equity securities, domestic		1,763,531,123	2,470,161,206
Equity securities, international		1,099,321,530	1,652,032,945
Real estate investments		950,005,842	1,163,527,397
Alternative investments		429,565,075	456,361,916
Equity securities, domestic (pooled including index funds)		1,054,798,551	974,163,732
Equity securities, international (pooled including index funds)		201,964,144	288,658,161
Investments held by broker-dealers under securities lending program (excluding securities sold, pending trade settlement):			
Short-term investments, domestic		—	99,607
Fixed income securities, domestic		304,762,539	431,995,246
Fixed income securities, international		7,906,075	21,516,561
Equity securities, domestic		260,463,128	548,282,911
Equity securities, international		161,598,149	222,878,146
Total investments	$	9,309,054,774	11,694,416,055
Securities lending collateral pool	$	758,820,569	1,235,028,470

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.
- 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, 2009 and 2008 is below. The weighted quality rating average of the domestic debt securities, excluding pooled investments, at June 30, 2009 is AA and the fair value of below grade investments is $194,369,154 or 8.4% of domestic securities in the portfolio. The weighted average of the international debt securities investments at June 30, 2009 is A and the fair value of below grade investments is $40,347,033 or 5.9% of the international allocation. 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. 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, Northern 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 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% points.)

At June 30, 2009 and 2008, 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.

	2009			2008		
Quality rating	**Domestic**	**International**	**Total**	**Domestic**	**International**	**Total**
AAA	$ 465,594,105	223,985,704	689,579,809	541,283,140	414,288,738	955,571,878
AA	100,959,980	97,000,550	197,960,530	129,171,228	202,741,005	331,912,233
A	319,583,597	185,258,595	504,842,192	190,575,081	160,126,391	350,701,472
BBB	195,147,438	135,792,162	330,939,600	131,934,681	56,973,530	188,908,211
BB	78,019,924	11,143,986	89,163,910	57,217,546	22,866,780	80,084,326
B	51,903,134	13,706,804	65,609,938	55,153,681	10,194,498	65,348,179
CCC	24,988,344	801,084	25,789,428	5,204,316	—	5,204,316
CC	3,857,347	2,664,057	6,521,404	—	—	—
C	2,858,304	33,837	2,892,141	112,950	—	112,950
D	120,717	270,750	391,467	—	—	—
Not rated	32,621,384	11,726,515	44,347,899	18,204,559	(62,347)	18,142,212
Total credit risk debt securities	1,275,654,274	682,384,044	1,958,038,318	1,128,857,182	867,128,595	1,995,985,777
U.S. government and agencies	1,042,850,796	—	1,042,850,796	1,262,274,287	—	1,262,274,287
Total debt securities investment	$ 2,318,505,070	682,384,044	3,000,889,114	2,391,131,469	867,128,595	3,258,260,064

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, 2009 and 2008, the table below shows fixed income investment securities by investment type, amount, and the effective 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

	2009		2008	
	Fair value	**Effective weighted duration (years)**	**Fair value**	**Effective weighted duration (years)**
Domestic fixed income securities:				
Asset-backed securities	$ 51,085,672	0.5	$ 70,097,972	0.4
Commercial mortgage-backed securities	39,449,002	5.6	31,202,698	4.7
Corporate bonds	756,918,045	4.5	585,863,914	4.4
Fixed income options, futures, and swaps	(7,891,409)	N/A	(6,773,761)	N/A
Government agencies	126,609,695	2.1	56,433,923	3.0
Government mortgage-backed securities	1,037,843,273	2.6	1,102,982,600	4.6
Municipal/provincial bonds	10,662,216	10.8	7,145,676	11.6
Nongovernment-backed CMOs	82,286,275	1.5	155,106,878	1.6
Other fixed income	—	N/A	9,932,411	0.3
U.S. Treasuries	221,542,301	3.8	379,139,158	7.0
Total fixed income securities, domestic	$ 2,318,505,070	3.3	$ 2,391,131,469	4.6

Effective duration of fixed income assets by security type

	2009		2008	
	Fair value	**Effective weighted duration (years)**	**Fair value**	**Effective weighted duration (years)**
Fixed income securities international:				
Asset-backed securities	$ 1,105,577	0.1	$ 12,587,964	0.1
Corporate bonds	303,722,984	4.6	234,033,156	4.1
Fixed income options, futures, and swaps	6,489,080	N/A	(1,951,628)	N/A
Government agencies	102,208,327	5.5	175,222,843	6.2
Government bonds	225,070,475	5.9	397,603,283	6.2
Municipal/provincial bonds	39,340,310	4.3	30,693,676	3.9
Nongovernment-backed CMOs	4,447,291	—	11,617,277	0.1
Other fixed income	—	N/A	7,322,024	—
Total fixed income securities, international	$ 682,384,044	5.1	$ 867,128,595	5.4
Fixed income securities – all	$ 3,000,889,114	3.7	$ 3,258,260,064	4.6

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.

The following table summarizes the ERS' exposure to foreign currency risk in U.S. dollars as of June 30, 2009 and 2008. (Amounts are in millions, and securities denominated in U.S. dollars are not presented.)

	2009				2008			
Currency	Cash and STIF	Fixed income	Equity	Total	Cash and STIF	Fixed income	Equity	Total
				(Dollars in millions)				
Australian Dollar	$ 1	46	40	87	5	38	47	90
Brazilian Real	—	1	11	12	—	1	20	21
New Bulgarian Lev	—	—	—	—	—	—	2	2
Canadian Dollar	—	1	11	12	15	9	15	39
Czech Koruna	—	—	1	1	—	—	3	3
Danish Krone	—	8	10	18	—	9	9	18
Egyptian Pound	—	—	2	2	—	—	2	2
Euro	2	282	323	607	—	349	555	904
British Pound Sterling	1	57	211	269	8	65	244	317
Hong Kong Dollar	—	—	84	84	5	—	61	66
Hungarian Forint	—	22	2	24	—	—	5	5
Indonesian Rupiah	—	—	1	1	—	—	6	6
Israeli Shekel	—	—	—	—	—	—	3	3
Japanese Yen	2	51	174	227	4	146	281	431
Korean Won	—	—	22	22	—	—	27	27
Mexican Peso	—	—	8	8	—	—	17	17
Malaysian Ringgit	—	—	3	3	—	—	—	—
Norwegian Krone	—	—	12	12	—	—	29	29
New Zealand Dollar	—	24	—	24	—	28	—	28
Polish Zloty	—	41	4	45	—	46	9	55
Romanian Leu	—	—	—	—	—	—	1	1
Swedish Krona	—	—	7	7	1	9	8	18
Singapore Dollar	—	—	10	10	2	—	14	16
Swiss Franc	—	—	89	89	—	—	97	97
Thai Baht	—	—	7	7	—	—	8	8
New Turkish Lira	—	—	5	5	—	—	10	10
New Taiwan Dollar	—	—	17	17	1	—	25	26
South African Rand	—	14	7	21	—	—	4	4
Pooled investments (multicurrency)	—	—	202	202	—	—	289	289
	$ 6	547	1,263	1,816	41	700	1,791	2,532

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 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, 2009 and 2008, 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, 2009 and 2008, the market value of securities loaned amounted to approximately $734,729,892 and $1,224,772,471, respectively, and the associated collateral amounted to approximately $761,075,558 and $1,264,158,946 (of which $758,820,569 and $1,235,028,470 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, 2009 and 2008 was 56 and 73 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 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, 2009 and 2008, 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, 2009 and 2008 is as follows:

		2009	2008
Forward currency purchases	$	968,376,969	853,882,344
Forward currency sales		(992,851,154)	(856,669,031)
Unrealized losses	$	(24,474,185)	(2,786,687)

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, 2009 and 2008, the ERS' investments had the following notional balances:

		2009	2008
Futures contracts (notional amount covered by contract):			
Long – cash and cash equivalents – futures	$	—	(3,217,203)
Short – cash and cash equivalents – futures		—	804,856,871
Long – debt securities – futures		(10,884,828)	(72,539,416)
Short – debt securities – futures		170,928,800	183,780,816
Net notional amounts on open contracts	$	160,043,972	912,881,068

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, 2009 and 2008, the ERS' investments had the following option balances:

		2009	2008
Options:			
Cash and cash equivalents written put options		(394)	—
Fixed income purchased call options		9,331,788	2,180,705
Fixed income written call options		—	(4,261,589)
Fixed income purchased put options		—	236,454
Fixed income written put options		(50,035)	(572,350)
Unrealized gains (losses)	$	9,281,359	(2,416,780)

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 comprises 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, 2009 and 2008 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, 2009 and 2008, 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.

On June 30, 2009 and 2008, the ERS' investments had the following market value balances as shown in the table below:

	2009	2008
Swaps – by currency:		
Interest rate swaps:		
In Australian Dollars	$ (758,869)	(410,182)
In British Pound Sterling	5,233,906	(973,464)
In Canadian Dollars	—	(5,316)
In Euro	757,462	1,140,845
In Japanese Yen	7,425	(435,233)
In U.S. dollars	5,853,766	664,126
Total	11,093,690	(19,224)
Credit default swaps:		
In U.S. dollars	(8,026,584)	(6,232,684)
Total	(8,026,584)	(6,232,684)
Retail price index (inflation) swaps:		
In Euro	88,182	—
Total	88,182	—
Total return swaps:		
In U.S. dollars	—	(56,702)
Total	—	(56,702)
Unrealized gains (losses)	$ 3,155,288	(6,308,610)

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, 2009 and 2008. 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.

(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 $731,000,000 as of June 30, 2009, consisting of $79,000,000 in real estate, $252,000,000 in alternative investments, and $400,000,000 in domestic equities. Investment-related commitments were $292,494,000 as of June 30, 2008, consisting of $85,053,000 in real estate and $207,441,000 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.

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Required Supplementary Information – Unauditied

June 30, 2009

Schedule of Funding Progress

(In thousands)

Actuarial valuation date	Actuarial value of assets (1)	Actuarial accrued liability (AAL) (2)*	Unfunded actuarial accrued liability (UAAL) (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:						
2009	$ 11,400,117	17,636,432	6,236,315	64.6%	$ 4,030,121	154.7%
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

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
Year ended June 30:			
2009	$ 526,538	578,672	109.9%
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

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

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Note to Required Supplementary Information

June 30, 2009

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, 2009
Actuarial cost method	Entry age normal
Amortization method	Level percent, open
Remaining amortization period as of June 30, 2009	28.2 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.

Schedule 1

**EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII**

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

Year ended June 30, 2009

	Pension Accumulation Fund	Annuity Savings Fund	Expense Fund	Total
Additions:				
Appropriations and contributions:				
Employers	$ 578,672,058	—	—	578,672,058
Members	—	177,781,610	—	177,781,610
Net investment loss	(1,937,317,469)	—	—	(1,937,317,469)
Total additions	(1,358,645,411)	177,781,610	—	(1,180,863,801)
Deductions:				
Benefit payments	833,691,245	—	—	833,691,245
Refunds of member contributions	—	3,937,464	—	3,937,464
Administrative expenses	—	—	13,011,283	13,011,283
Total deductions	833,691,245	3,937,464	13,011,283	850,639,992
Other changes in net assets held in trust for pension benefits:				
Transfer due to retirement of members	57,464,065	(57,464,065)	—	—
Transfer of interest allocation	(48,753,513)	48,753,513	—	—
Transfer to pay administrative expenses	(13,700,216)	—	13,700,216	—
Return of unrequited funds due to savings in administrative expenses	894,289	—	(894,289)	—
	(4,095,375)	(8,710,552)	12,805,927	—
Net increase (decrease)	(2,196,432,031)	165,133,594	(205,356)	(2,031,503,793)
Net assets held in trust for pension benefits:				
Beginning of year	9,726,795,072	1,105,627,636	14,366,257	10,846,788,965
End of year	$ 7,530,363,041	1,270,761,230	14,160,901	8,815,285,172

See accompanying independent auditors' report.

Schedule 1

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

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

Year ended June 30, 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 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 unrequited 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.

Schedule 2

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Supplementary Information – Social Security Contribution Fund

Statements of Changes in Assets and Liabilities

Years ended June 30, 2009 and 2008

		2009			
Assets		**Beginning balance**	**Additions**	**Deductions**	**Ending balance**
Cash	$	4,291	9,471,937	9,476,228	—
Short-term investments		9,471,937	—	9,471,937	—
Total assets	$	9,476,228	9,471,937	18,948,165	—
Liabilities					
Due to employers	$	9,476,228	208,684,771	218,160,999	—
Total liabilities	$	9,476,228	208,684,771	218,160,999	—

		2008			
Assets		**Beginning balance**	**Additions**	**Deductions**	**Ending balance**
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

See accompanying independent auditors' report.

Schedule 3

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Supplementary Information – Schedules of Administrative Expenses

Years ended June 30, 2009 and 2008

		2009	**2008**
Personnel services:			
Salaries and wages	$	4,679,619	4,448,790
Fringe benefits		1,717,565	1,544,787
Net change in unused vacation credits		7,788	168,055
Total personnel services		6,404,972	6,161,632
Professional services:			
Actuarial		93,000	93,000
Auditing and tax consulting		133,613	138,000
Disability hearing expenses		110,495	97,585
Legal services		346,075	310,875
Medical		396,745	416,869
Other services		1,002,087	488,629
Total professional services		2,082,015	1,544,958
Communication:			
Postage		192,705	97,307
Printing and binding		74,149	49,208
Telephone		71,307	60,456
Travel		44,276	34,204
Total communication		382,437	241,175
Rentals:			
Rental of equipment		24,021	50,037
Rental of premises		19,037	17,230
Total rentals		43,058	67,267
Other:			
Armored car service		8,310	8,671
Computer and office automation systems		146,632	227,187
Equipment		6,269	6,350
Repairs and maintenance		1,844,696	890,853
Stationery and office supplies		50,554	50,192
Miscellaneous		94,279	78,829
Total other		2,150,740	1,262,082
Depreciation		1,948,061	1,451,687
	$	13,011,283	10,728,801

See accompanying independent auditors' report.

Schedule 4

EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

Supplementary Information – Schedules of Investment Expenses

Years ended June 30, 2009 and 2008

		2009	2008
Real estate and alternative investment expenses:			
Operating expenses	$	53,034,808	53,286,730
Mortgage interest		14,868,884	16,500,661
Total real estate and alternative investment expenses		67,903,692	69,787,391
Investment expenses:			
Investment manager/advisor fees		12,079,010	30,710,444
Bank custodian fees		150,000	346,500
Other investment expenses		370,874	670,486
Total investment expenses		12,599,884	31,727,430
Securities lending expenses:			
Borrower rebates		6,668,106	49,457,874
Management fees		1,366,017	1,973,291
Total securities lending expenses		8,034,123	51,431,165
	$	88,537,699	152,945,986

See accompanying independent auditors' report.