

OUTLOOK

A Publication of the South Dakota Retirement System

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System 101 Percent Funded

SDRS' Financial Strength 33 Percent Better than National Average

Financial news is bleak. Worries persist over the slow growth of our gross national product. Prolonged weakness in the markets continues to deeply erode retirement plans across the nation. But in this gloom of economic uncertainty, SDRS members have good reason to

cheer: the system remains financially healthy, with more than enough money to pay all benefits earned to date by both active and retired participants.

Using the standard measurement of funded ratios, SDRS' strength exceeds virtually every

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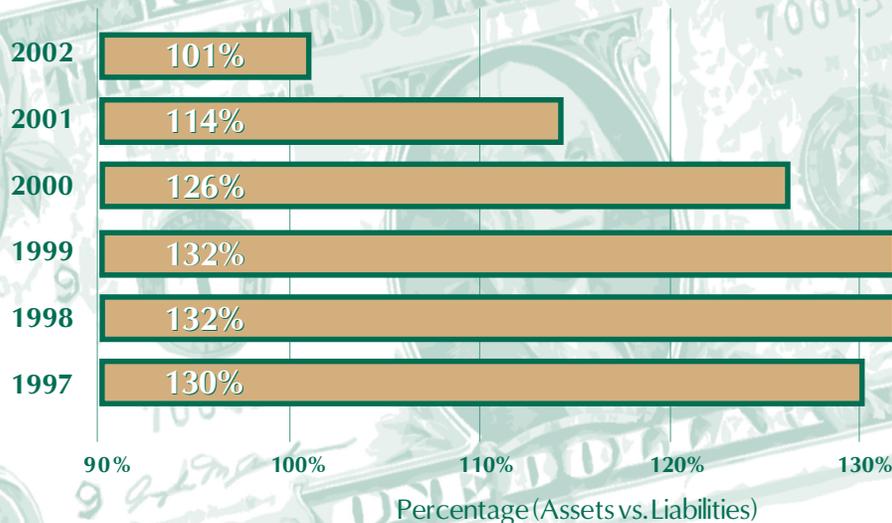
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SDRS Assets Exceed Value of Benefits Owed to Members

Despite the recent weak performance of the stock market, SDRS' financial position remains strong. 2002 was the 17th straight year in which the value of its assets exceeded the total amount of its liabilities.

Funded Ratios



Since *Outlook* charts are for illustrative purposes, the numerical data may be rounded.

other retirement system in the country. “With a 101 percent funded ratio as of last June 30, SDRS is at the very top of the list and far above the national average of 76 percent,” according to Paul Schrader, an actuary with Buck Consultants. Schrader says the funded ratio is a critical tool that compares the system’s assets to what it owes in benefits. “Having one percent more than you need doesn’t sound impressive until you remember that the average public plan only has a 76 percent funded ratio,” says Schrader.

Asset Growth Relies on Market Performance

While the system’s liabilities come from the benefits owed to members,

assets are derived from three sources:

- the contributions of members
- the contributions of members’ employers
- the income earned when contributions are invested in stocks and bonds

The variable among these three sources is the investment return. When it averages 8 percent a year, SDRS stays exactly even with the amount it needs to fully fund member benefits at their current levels. If it rises above 8 percent, the dollars go into a reserve that can then be used to fund future benefits and provide a cushion for the system during those years

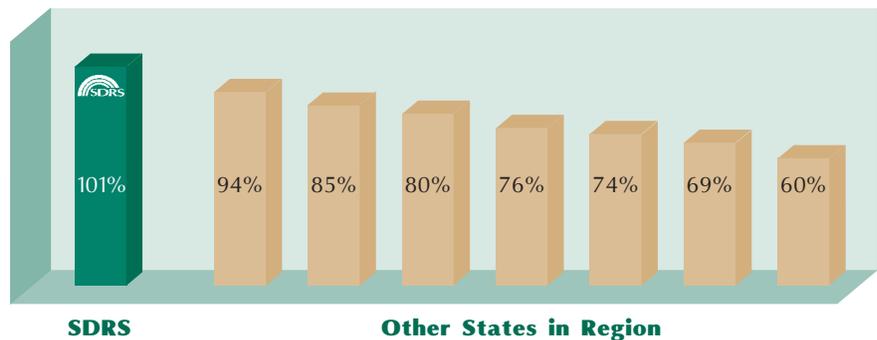
when earnings fall short. “The reserve is a way to smooth the system’s income stream and set aside dollars for benefit improvement or for periods of poor investment performance,” says Schrader.

While the reserve has buoyed SDRS through the past three years of market losses, Schrader says that it’s now gone. “The reserve has done its job, but it can’t help us in the immediate future. What we need now is for the markets to begin to perform exceptionally well,” he says. If that happens, the reserve will be replenished and everyone can take a deep sigh of relief. If not, then SDRS will be considering whatever options are available to preserve the future strength of the system. **OUTLOOK**

SDRS Stronger than Other Systems in Region

Using funded ratios as the basis for comparison, SDRS’ financial strength is unmatched among retirement systems in the surrounding states — Iowa, Kansas, Minnesota, Montana, Wyoming, North Dakota and Nebraska. SDRS’ current funded ratio is 101 percent, while the regional average falls to 77 percent. The system closest to SDRS in strength reports a funded ratio of 94 percent, while the weakest trails at 60 percent.

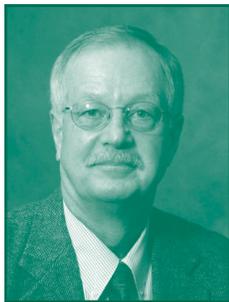
Funded Ratio of States in Region Ranges from 101% to 60%



Administrative Changes

SDRS' Administrator, Deputy Administrator Retire

Al Asher and John Storsteen, SDRS' top two administrators, will be retiring on July 1, 2003. Asher, who played a critical role in shaping SDRS into a strong consolidated system, has served as administrator of SDRS since it was established in 1974. John Storsteen joined SDRS as deputy administrator in 1984. According to Elmer Brinkman, chairman of SDRS' Board of Trustees, "Without the exceptional talent and dedication of these two men, the history of the system would be markedly different."



Al Asher



John Storsteen

Under their leadership, SDRS has attained stability and financial strength while dramatically improving service and benefits to members, active and retired. Notable accomplishments during their tenure include:

- consolidating 11 separate, competing retirement systems into a single, 65,000 member plan that encompasses almost all public employees in South Dakota
- increasing the value of the system's assets from less than \$100 million to \$4.5 billion
- doubling the value of members' retirement benefits

- increasing the amount of benefits paid to members from \$5 million to \$175 million annually

Asher and Storsteen helped achieve these goals by an organizational discipline that focused the attention of the system on critical issues. The result was a series of far-reaching improvements in plan provisions that are included in the side bar at right.

According to Brinkman, every SDRS member, present and future, has profited immensely from Asher's and Storsteen's vision. "Having dedicated their careers to assuring the

comfortable and secure retirement of thousands of public employees in South Dakota, these two individuals richly deserve to enjoy a relaxed and pleasurable retirement themselves."

Search Committee Begins Work

The Board of Trustees has initiated a nation-wide search for the system's next administrator. A special committee has been created that consists of six board members and two legislators. In the interim, the board has appointed Wade Hubbard acting administrator. Mr.

Hubbard's eight years of experience as SDRS' chief counsel gives him a thorough understanding of the system and assures the membership of a smooth transition. **OUTLOOK**

Plan Improvements During Asher Tenure

- increasing the annual COLA from 2 percent simple to 3.1 percent compounded
- improving SDRS' early retirement options by reducing penalties for early retirement from 6 percent to 3 percent per year and implementing the Rule of 85
- securing tax-deferred status for SDRS contributions
- creating the Portable Retirement Option
- establishing the Supplemental Retirement Plan
- reducing the cost of purchasing credited service by 25 percent
- shortening the vesting period from five years to three years
- increasing survivor benefits after retirement from 50 percent to 60 percent of a member's benefit
- establishing a reserve to pre-fund benefit improvements and protect the system during times of low investment earnings

Legislation

Summary of SDRS Bills Introduced in 2003 Legislative Session

The legislature considered six bills related to SDRS during the 2003 session. None of the bills proposed major changes in plan provisions or affected SDRS benefits. Only two of the bills were passed by the legislature.

Three Bills Proposed by SDRS

SDRS recommended three bills to the legislature in 2003:

- Senate Bill 14 allows certain law enforcement officers to convert certain Class A credited service to Class B Public Safety credited service. Senate Bill 14 was passed unanimously by both the House and Senate.
- Senate Bill 15 would have revised the deadline for filing for retirement benefits and delayed the commencement of benefit payments until after

receipt of final contributions. The Senate Retirement Laws Committee amended the bill by deleting the revised filing deadline. The amended bill passed the Senate but was deferred by the House Retirement Laws Committee to the 41st legislative day, thereby ending its consideration in the 2003 session.

- Senate Bill 16 proposed a cost-neutral solution to the retire/rehire issue. The bill passed the Senate but was deferred by the House Retirement Laws Committee to the 41st legislative day, thereby ending its consideration in the 2003 session.

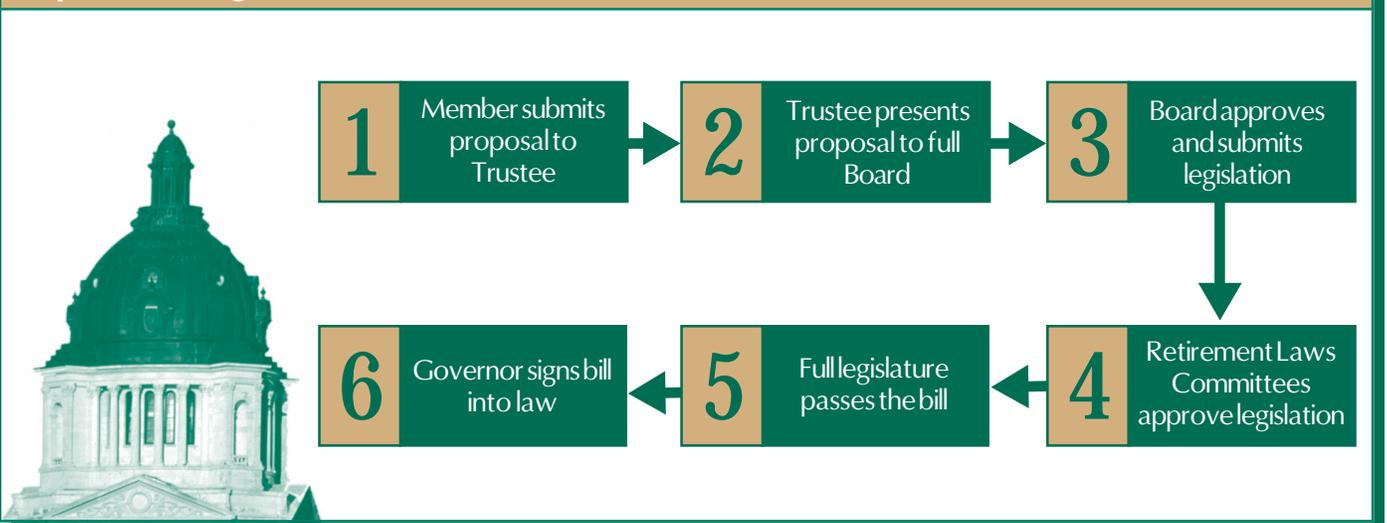
Legislation Proposed by Others

- Senate Bill 55 contained two provisions: to permit the

Association of School Administrators to become a participating unit in SDRS and to allow members who have worked for non-profit entities limited purchase of that non-public service. Senate Bill 55 was not opposed by the SDRS board. Senate Bill 55 passed the Senate but was tabled by the House.

- House Bill 1188 was virtually identical to Senate Bill 55 and passed both the House and Senate.
- House Bill 1252 would have reduced the benefit formula multipliers of Class A and Class B Public Safety members for credited service starting after July 1, 2003. This legislation was tabled by the House Retirement Laws Committee. 

Steps in the Legislative Process





Board Notes

The following is a summary of major issues that came before the SDRS Board of Trustees at its December 11 & 12, 2002 meeting and at a special meeting held on March 4, 2003.

December 11 & 12, 2002

Financial Reports

The board reviewed SDRS' financial statements for fiscal year 2002, the financial audit prepared by KPMG, an investment report prepared by the State Investment office staff, and the actuarial valuation prepared by Buck Consultants.

Asset/Liability Modeling

Paul Schrader, actuarial consultant, presented worse-case/best-case scenarios of SDRS' funded status over the next 10 years based on various investment returns.

Review of SDCL 3-12-122

Due to concern over the recent investment performance of the SDRS Trust Fund, Paul Schrader, actuarial consultant, reviewed SDCL 3-12-122. This section of the statute requires the board to propose funding options to the legislature and governor if specific actuarial measures decline over time. Schrader advised the board that the statute required no action at this time but noted that the investment performance would continue to be carefully monitored.

Investment Update

Steve Myers, State Investment Officer, reported on SDRS' fund returns for the fiscal year to date.

Governor's Recommended Budget

Rob Wylie, SDRS Finance Officer, reviewed the FY 2004 Governor's Recommended Budget for SDRS. Mr. Wylie advised the board that its request for 2.8 additional positions was not included in the Governor's recommended budget for SDRS. He reported that, overall, the recommended budget for SDRS was 1.1 percent lower than last year.

Proposed Legislation for the 2003 Legislative Session

- **Retire/Rehire** -- The board approved proposed legislation for a cost-neutral solution to the retire/rehire issue.
- **Member Issue 2002-2 (Law Enforcement Officers Standards Waiting Period)** -- The board approved proposed legislation affecting certain Class B Public Safety members.
- **Application Deadline** -- The board approved proposed legislation to amend SDCL 3-12-90 to change the deadline for submitting applications for retirement benefits from 30 days to 90 days prior to retirement.
- **School Administrators** -- The board agreed not to oppose legislation allowing employees of the School Administrators of South Dakota (SASD) to become members of SDRS.

For more details on the results of SDRS legislation during the 2003 session, see page four.

Trustee Attendance at Board Meeting

Present: Brian Berglin, Elmer Brinkman, Carol Burch, Tracy Dahl-Webb, Bryan Gortmaker, James Hansen, Royce Hueners, Louise Loban, K.J. McDonald, Dave Merrill, Lowell Slyter, Wes Tschetter, Don Zeller, Sandy Zinter, Steve Zinter, Steve Myers - Ex Officio

Absent: Pam Roberts

March 4, 2003

Administrator's Resignation

During a special meeting on March 4, the SDRS Board of Trustees accepted the resignation of the system administrator, Al Asher.

Search Committee Appointed

The board appointed an Executive Search Committee consisting of six board members and two legislators. On April 9, the committee will present recommendations to the board regarding a search procedure for a new administrator.

Interim Administrator

The Chairman of the Board was given the authority to negotiate for an interim administrator.

Trustee Attendance at Board Meeting

Present: Brian Berglin, Elmer Brinkman, Carol Burch, Tracy Dahl-Webb, Bryan Gortmaker, James Hansen, Royce Hueners, Louise Loban, K.J. McDonald, Dave Merrill, Pam Roberts, Lowell Slyter, Wes Tschetter, Don Zeller, Sandy Zinter, Steve Zinter

Absent: Steve Myers - Ex Officio

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Schrader: Since this is one of the worst investment periods in our history, there's certainly cause for concern. At best, the losses would prevent SDRS from recommending benefit improvements for some time. The close connection between the

"At best, the losses would prevent SDRS from recommending benefit improvements for some time."

members' financial condition and the overall economic condition of the nation is very clear.

Outlook: You say that at best members won't see benefit increases for some time. What else can they expect?

Schrader: The key unknowns are how long this weak market will last and how likely it is that the losses can be made up over time. A 7 percent loss this year would drop SDRS' funded level to 87 percent. While that's still a very solid number, the board will continue to evaluate the future investment outlook and to study actions it would recommend to offset losses. The board has a responsibility and commitment to maintain the soundness of SDRS under all conditions.

Outlook: How can SDRS remain secure when the markets are performing so poorly?

Schrader: Knowing that it's the nature of the markets to fluctuate, in 1995 the board began setting aside millions of dollars each year in a reserve. The reserve was specifically designed to protect the system if investments went sour. It was that decision — and the discipline to stick to it — that has saved SDRS from a crisis today.

Outlook: How unique is the SDRS reserve?

Schrader: Very unique. Most boards and staff don't have the kind of vision it takes to establish a reserve. You can see that by looking at their present financial condition. Many pension plans in both the public and private sectors are in

"In hindsight, the market decline has been more severe and has lasted longer than was reasonable to expect."

very serious trouble all across the country. SDRS has been, and continues to be, one of the best funded systems in the nation.

Outlook: Is there anything SDRS should have done differently?

Schrader: I don't think so. SDRS used a portion of past investment returns both to recommend benefit improvements and to prepare for a significant downturn. The mix of spending and saving in the reserve was the result of careful study and projections. In hindsight, the market decline has been more severe and has lasted longer than was reasonable to expect.

Outlook: What would you want an SDRS member to conclude from your comments?

Schrader: First, the system remains sound because the board anticipated the downturn in the market and had the courage to prepare for it. Second, the investment downturn may continue to be worse than expected. Third, the board is monitoring the effect that low investment earnings are having on the system and carefully planning its options. If required, the board will recommend to the legislature whatever changes

may be necessary to ensure the long-term health of the system. **OUTLOOK**

Supplemental



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Pre-retirement Planning

May through November Retirement Planners' Schedule

SDRS retirement planners are making group presentations and meeting with members individually at sites throughout South Dakota. Regardless of age, all members can benefit from these presentations. The earlier you

develop a retirement plan, the broader and more flexible your options will be.

The meetings are scheduled well in advance to allow you and your family time to make arrangements to attend. The statewide meeting

schedule is also on the SDRS Web site: www.state.sd.us/sdrs/index.htm

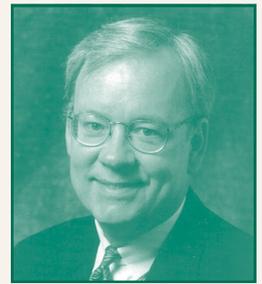
Invitation letters are mailed to members in the surrounding area several weeks before the meetings. If you would like a one-on-one counseling session with a retirement planner, do not delay making an appointment through the SDRS office. Please call at least one week before the scheduled meeting, as the schedule of individual counseling sessions fills quickly. 

SDRS STATE-WIDE MEETING SCHEDULE

SCHEDULE DATE	CITY	COUNTY	LOCATION	ADDRESS	INDIVIDUAL COUNSELING DEADLINE*
May 6, 2003	Sturgis	Meade	Best Western Philtown Inn	Exit 32 S. Junction	May 1
May 13, 2003	Clear Lake	Deuel	Lakewood Inn	Hwy. 15 South	May 8
May 20, 2003	Canton	Lincoln	Canton Library	225 N. Broadway St.	May 15
May 27, 2003	Wessington Springs	Jerauld, Aurora	Community Room	205 Wallace Ave.	May 22
June 3, 2003	Gettysburg	Potter, Faulk	Super 8	719 E. Hwy. 212	May 29
June 10, 2003	Webster	Day	Dakota Bank	600 Main	June 5
June 17, 2003	Salem	McCook	REA Room	236 N. Main	June 12
June 24, 2003	Parker	Turner	Community Building	299 N. Main	June 19
July 1, 2003	DeSmet	Kingsbury	Super 8	288 Hwy. 14 E.	June 26
July 8, 2003	Springfield	Bon Homme	Community Service Center	605 8 th St.	July 3
July 15, 2003	Flandreau	Moody	Community Room	101 E. Pipestone	July 10
July 22, 2003	Lemmon	Corson, Perkins	Dakotah Bank	321 Main	July 17
July 29, 2003	Sisseton	Roberts	Dakotah Bank	321 E. Veterans Ave.	July 24
August 5, 2003	Vermillion	Clay	Continuing Ed. Bldg., Room 121	University of South Dakota	July 31
August 12, 2003	Elk Point	Union	Community Room	209 E. Main	August 7
August 19, 2003	Redfield	Spink	Senior Center	728 Main St.	August 14
August 26, 2003	Clark	Clark	Community Room	400 S. Main	August 21
September 2, 2003	Huron	Beadle, Sanborn	Crossroads Hotel	100 4 th St.	August 28
September 9, 2003	Sioux Falls (schools)	Minnehaha	Ramkota	2400 N. Louise	September 4
September 18, 2003	Sioux Falls (other agencies)	Minnehaha	Ramkota	2400 N. Louise	September 11
September 23, 2003	Howard	Lake, Miner	Community Center	Connected to firehall	September 18
September 30, 2003	Aberdeen	Brown	Ramkota	1400 8 th Ave. N.W.	September 25
October 7, 2003	Yankton	Yankton	Kelly Inn	1607 E. Hwy. 50	October 2
October 14, 2003	Mobridge	Walworth, Campbell	Wrangler Inn	820 W. Grand Crossing	October 9
October 21, 2003	Rapid City (schools)	Pennington	Quality Inn	1902 N. Lacrosse	October 16
October 28, 2003	Rapid City (other agencies)	Pennington	Quality Inn	1902 N. Lacrosse	October 23
November 18, 2003	Spearfish	Lawrence	Holiday Inn	I-90 Exit 14	November 13

* Individual retirement counseling sessions must be scheduled before noon on this date.

*"I can say without reservation —
SDRS is secure."*



OUTLOOK Interview **Paul Schrader**

Paul Schrader has been SDRS' consulting actuary since 1974. Schrader has also served as a consultant to corporations such as Coors Brewery, Manville Corporation and Samsonite Corporation, as well as to numerous public retirement plans across the nation.

Outlook: Because the performance of the stock market has been so poor, there has been a lot of discussion about the financial strength of SDRS. In your opinion, is the system secure?

Schrader: I can say without reservation — SDRS is secure. Presently it's 101 percent funded, which means that SDRS has the dollars it needs to pay all current and future benefits due to members, active and retired.

Outlook: If that's the case, why is there concern?

Schrader: Because in the last two years SDRS, like virtually every other retirement plan in the nation, has experienced significant financial losses. In 1999, its funded ratio was 132 percent, meaning that it had 32 percent more in assets than was needed to pay benefits. That was an incredibly strong position.

"All retirement systems depend heavily on earnings from investments to pay benefits."

Outlook: And then the stock market collapsed.

Schrader: That's right. All retirement systems depend heavily on earnings from investments to pay benefits. When the S&P 500 loses 40 percent of its value in just over two and one-half years, every

system in the nation, including SDRS, is affected.

Outlook: SDRS' funded ratio of 101 percent is based on investment performance as of June 30, 2002. What have investment earnings been like since then?

Schrader: The markets have continued to be very weak. On March 1st of this year, the South Dakota Investment Office reported a loss of 7 percent over the past eight months. Since we need a positive return of 8 percent to stay even with our normal costs, SDRS could be 15 percent short this fiscal year. Of course, that assumes that the March 1st trend continues.

Outlook: How worried should members be about these potential losses?

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