South Dakota Retirement System

Retirement Laws Committee Update

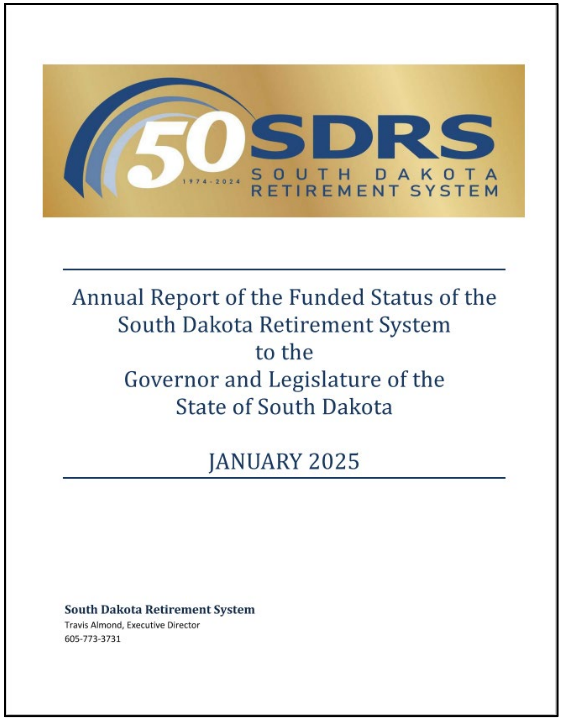
January 2025

SDRS Model: Fixed Contributions and Variable Benefits

- Member and employer **contribution rates are fixed in statute:**
  - Most state plans vary employer contributions to meet actuarial requirements
  - SDRS is designed to remain sustainable with fixed contributions
- **COLA automatically varies** with inflation and affordability:
  - COLA equals inflation, up to 3.5% when affordable
  - Maximum reduced, if necessary, to keep SDRS 100% funded
- Statutory funding thresholds require recommendation for **corrective action** if SDRS funded status drops below 100%

Key Takeaways from Fiscal Year 2024 Annual Funded Status Report

- SDRS **remains 100% funded** and is expected to remain 100% funded under most economic conditions
- Employer contribution rates remain **fixed and among the lowest in the nation**
- The SDRS **July 2025 COLA will be 1.71%,** below inflation for the prior year but equal to the maximum sustainable percentage
- The Board's benefit adequacy goals are met, except **COLAs have not kept up with inflation**



Annual Report of the Funded Status of the South Dakota Retirement System to the Governor and Legislature of the State of South Dakota

JANUARY 2025

South Dakota Retirement System
Travis Almond, Executive Director
605-773-3731

Reasons for SDRS Success

- Primary driver: Outstanding long-term **SDIC investment performance**
- Commitment to manage the system within **fixed contributions** through:
  - Variable benefits – primarily variable COLA
  - Benefit improvement discipline – not considered unless over 120% funded
  - Statutory requirements for corrective action recommendations and recognition that an uncertain future may require changes
- **Planning**, goal setting, risk identification/management, monitoring, and transparently communicating results:
  - Contingency plan provides framework for actions in good and bad times
- **Ongoing support** of the Executive and Legislative branches of state government

Efficient Structure

- SDRS is a tax-qualified, fully funded, defined benefit pension plan with variable benefit features and fixed member and employer contributions:
  - **Tax qualification:** No federal income taxes on member and employer contributions and investment income until benefits are paid in retirement
  - **Remaining fully funded** avoids any payment for unfunded liabilities and uses all contributions to fund benefits earned in the current year
  - Through risk pooling, higher investment returns, and optimally balanced portfolios, **defined benefit plans** can provide **twice as much benefit** than typical defined contribution plans for the same contribution*
  - **Variable COLA process** pays maximum sustainable benefits while remaining fully funded; July 2025 COLA will be 1.71%
  - **Fixed member and employer contribution rates** provide budgetary certainty for 508 participating employers

* Source: National Institute on Retirement Security: A Better Bang for the Buck 3.0, January 2022.

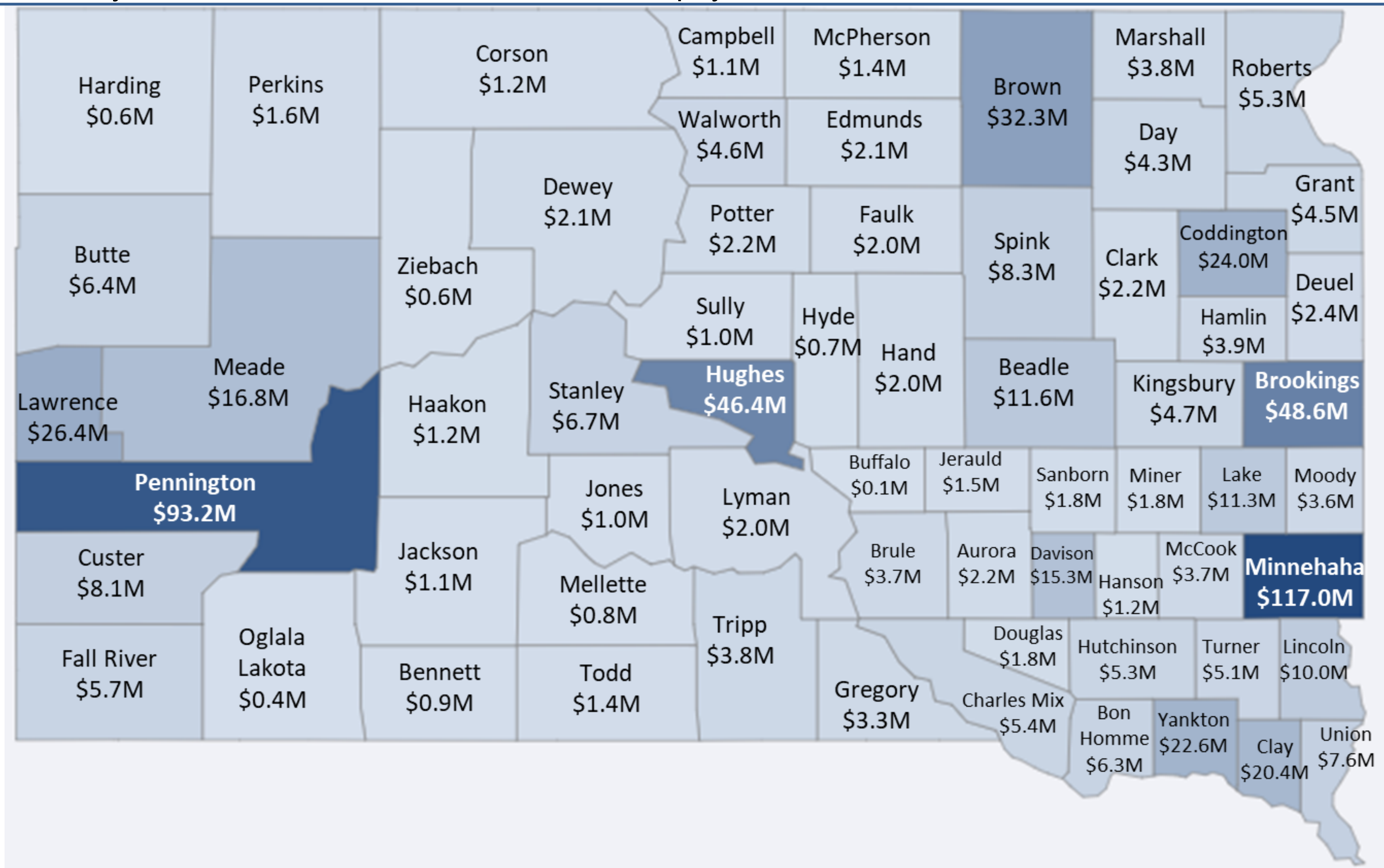
June 30, 2024 System Basics

System Membership	Members	Percent of State Population
Active Contributing Members	42,873	4.7%
Monthly Benefit Recipients	34,119	3.7%
Terminated Members	26,307	2.8%
Total System Membership	**103,299**	**11.2%**

FY 2024 Financial Results	
Fair Value of Assets	$14.922 B
Actuarial Accrued Liabilities	$14.918 B
Fair Value Funded Ratio	**100.0%**
Affordable July 2025 COLA	1.71%
FY 2024 Member/Employer Contributions	$ 335 M
FY 2024 Benefit Payments/Refunds	$ 764 M

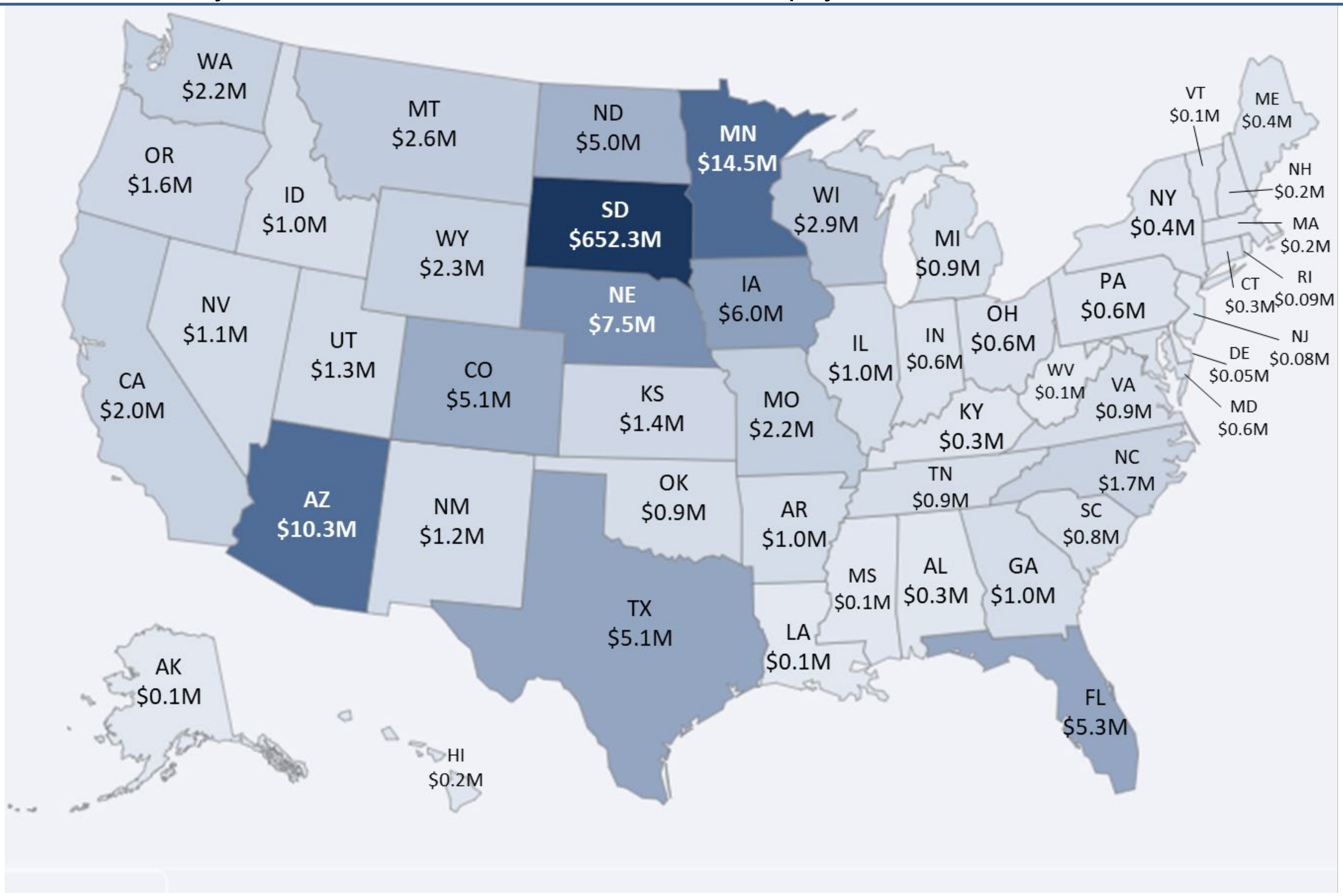
Annual Benefits In Pay to South Dakota Residents by County

As of July 2024, $748 million in annual benefits in pay, **$652 million to current South Dakota residents**

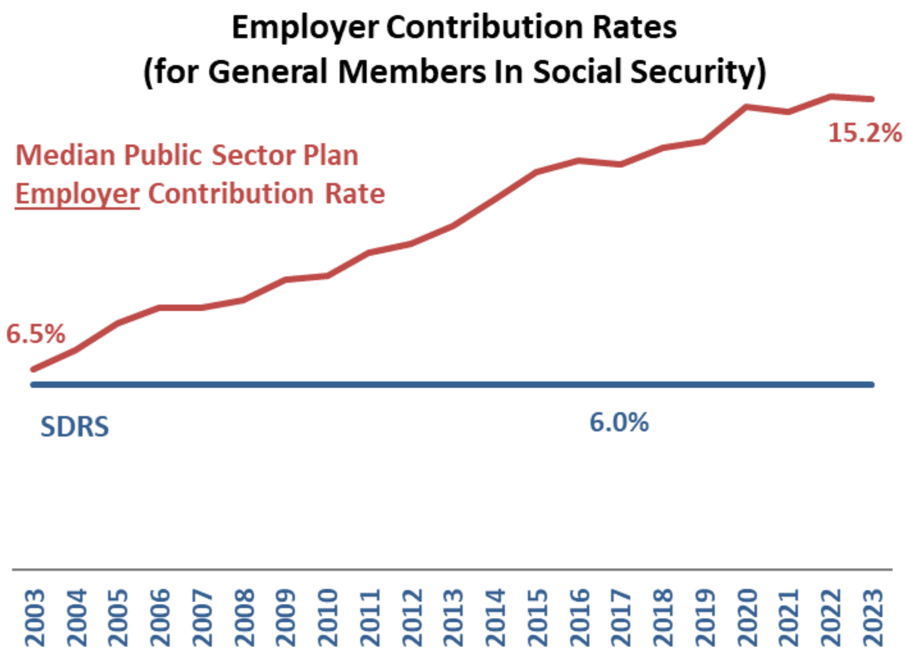


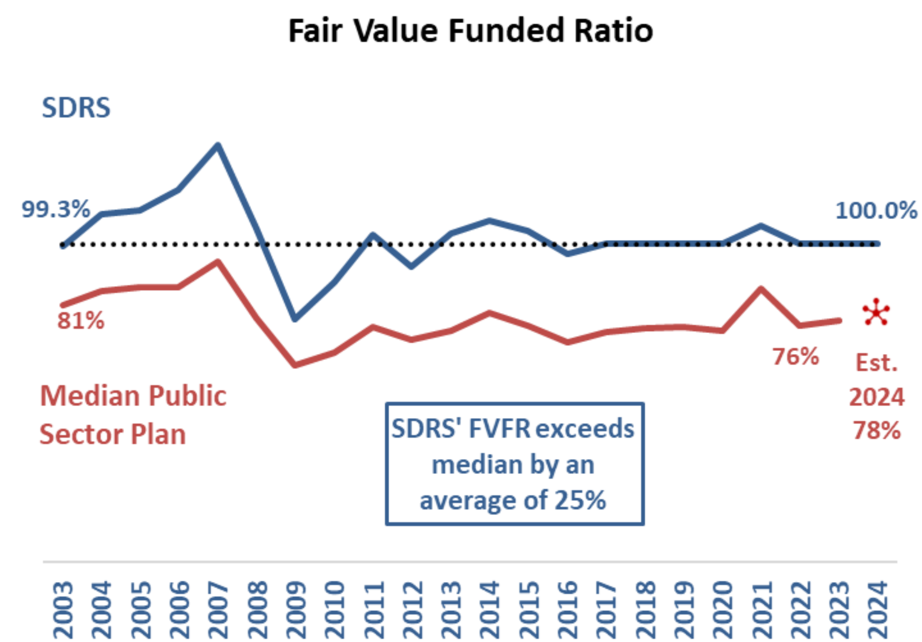
Annual Benefits In Pay Nationally by State

As of July 2024, $748 million in annual benefits in pay, **$96 million outside South Dakota**



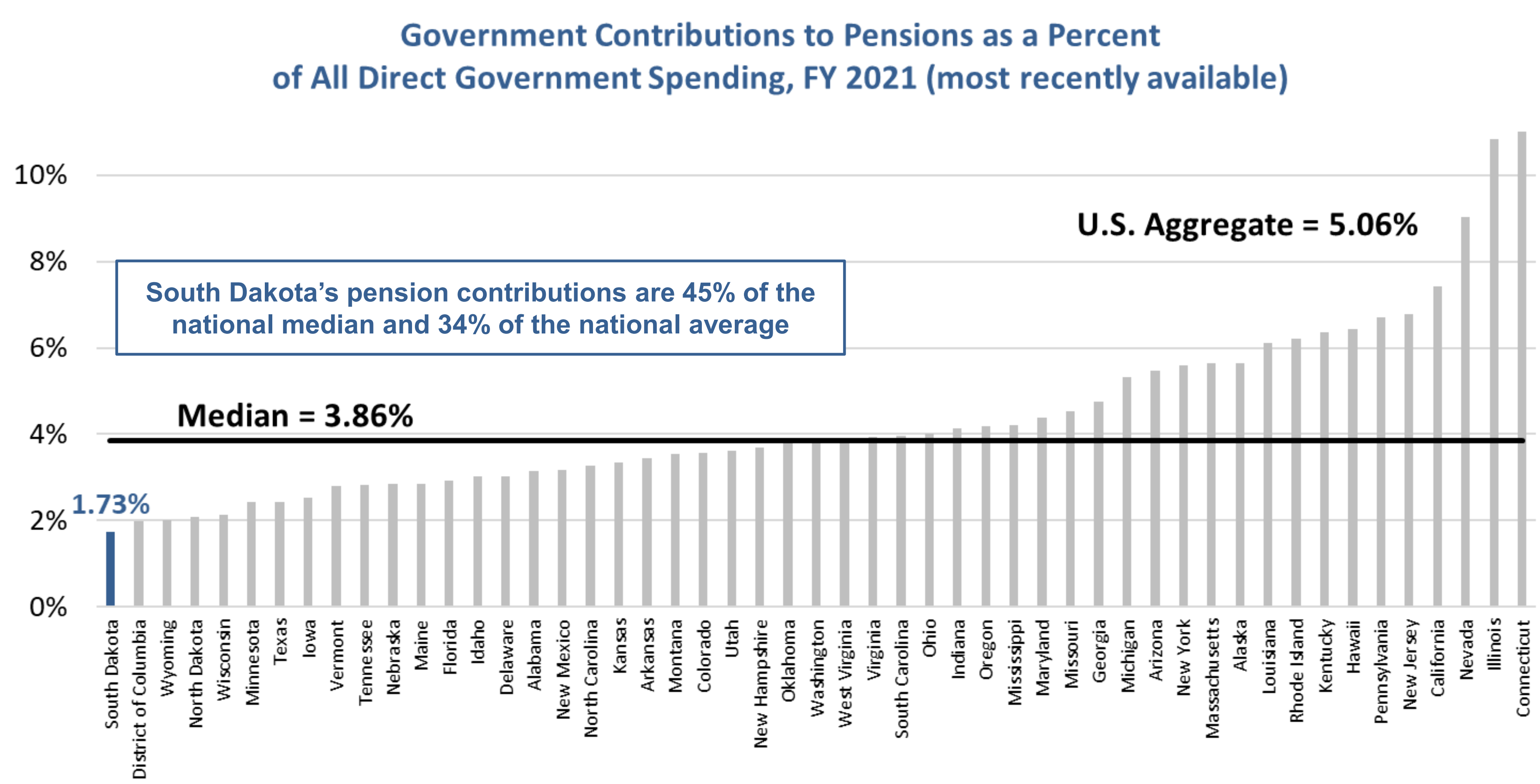
Employer Contributions and Funded Status Comparisons





- SDRS is managed within the resources provided by **fixed, statutory member and employer contributions**
- Median employer contribution rate is 2.5 times SDRS rate
- In most economic conditions, SDRS expects to remain **100% funded**

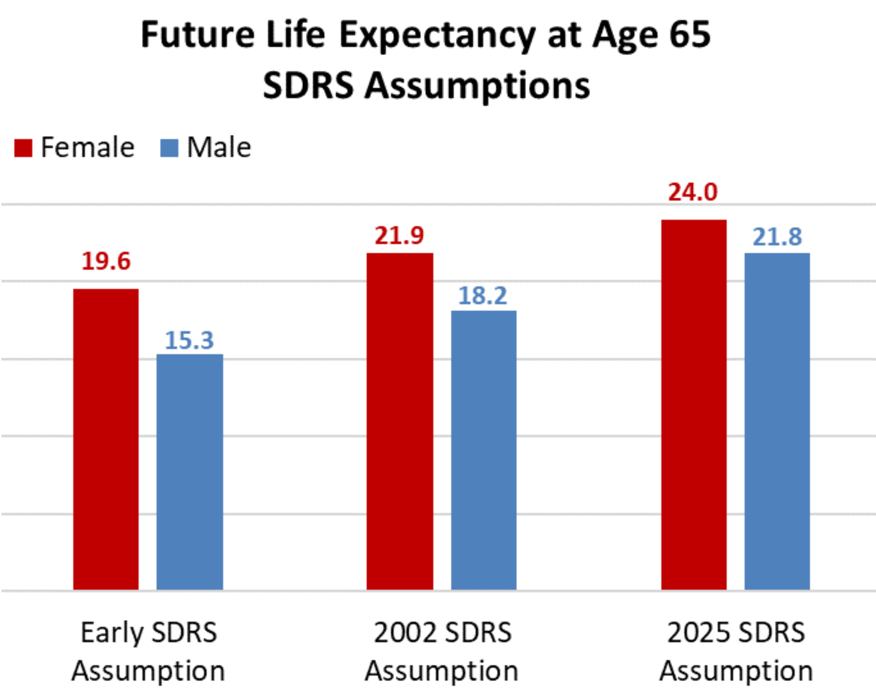
Government Spending on Pensions

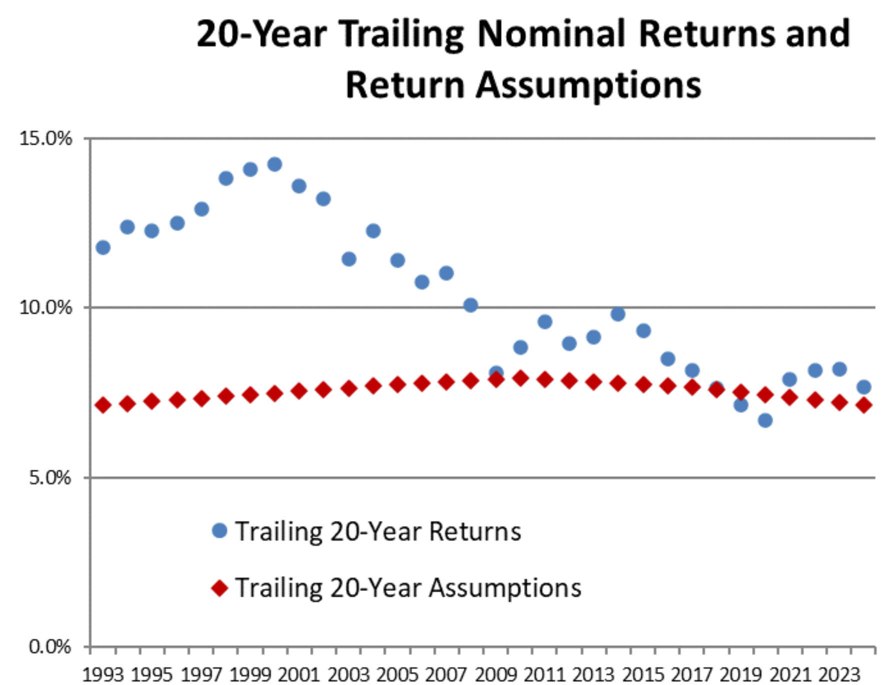


Data from NASRA Issue Brief: State and Local Government Spending on Public Employee Retirement Systems, February 2024

Competing Objectives

- Delivering adequate benefits **directly competes** with remaining fully funded while spending a fraction of the national median on pensions:
  - The challenge is becoming more difficult as retirees live longer and markets provide lower investment returns





Competing Objectives

- SDRS management efforts to meet benefit objectives in changing circumstances have included:
  - Service purchase cost
  - Variable COLA process
  - Retire-rehire reform
  - Generational design
  - Pay increase caps
  - 5-year FAC

- **Expect continuing pressure on benefit affordability:**
  - Proposed changes to SDRS must be thoroughly evaluated to ensure they do not endanger future benefits, COLAs, or system sustainability
  - SDRS liabilities are essentially equal to SDRS assets – with fixed contributions, **any expansion, increase, or acceleration of benefits directly reduces the COLA paid to retired members**
  - Actuarial assumptions must remain realistic

Sustainability Efforts

- Service purchases (2004): Actuarial cost to buy service
- Variable COLA process (2010): Annual COLA varies by inflation and system funding (revised in 2017 and 2021)
- Retire-rehire reform (2010): Eliminated windfall for members retiring and returning to work, removing incentive to retire artificially early
- Generational benefit structure (2016): Restructured benefits to address imbalances and recognize longer life expectancies while remaining at equivalent overall cost
- Pay increase caps and 5-year FAC (2017): Prevent high, late-career salary increases from causing unfunded benefit increases

Foundation and Generational Benefit Structures

Foundation Benefits (Member before 7/1/2017)

- Eligibility:
  - Normal Retirement Age: 65/55 (A and Judicial / PS)
  - Early Retirement Age: 55/45, 3% per year reduction
  - Special Early Retirement (Rule of 85/75/80)
  - Three-year vesting
- Benefits:
  - 1.55% for Class A
  - 2% and 3.3%/2% for Class B
  - Three-year Final Average Compensation
  - Class A Alternate Formula
  - Level Income option
  - No Variable Retirement Account (VRA)
- Post-Retirement Survivor Benefit:
  - 60% of Member's benefit continued to spouse if married for at least one year at retirement and still married at Member's death
  - Guaranteed return of accumulated Member contributions and 85% of accumulated employer contributions

Generational Benefits (Member after 6/30/2017)

- Eligibility:
  - Normal Retirement Age: 67/57 (A and Judicial / PS)
  - Early Retirement Age: 57/47, 5% per year reduction
  - No Special Early Retirement
  - Three-year vesting – **No change**
- Benefits:
  - 1.8% for Class A
  - 2% and 3.3%/2% for Class B – **No change**
  - Five-year Final Average Compensation
  - No Class A Alternate Formula
  - No Level Income option
  - VRA to supplement base benefits at retirement
- Post-Retirement Survivor Benefit
  - If Member elects reduced benefit at retirement, 60% or 100% of reduced benefit payable to survivor. Otherwise, life only benefit
  - Guaranteed return of accumulated Member contributions and 85% of accumulated employer contributions – **No change**

July 2025 COLA Calculation

Step 1:
June 30, 2024
Baseline FVFR = 94.8%

If 100% or More

COLA = CPI-W Increase
Minimum = 0%
Maximum = 3.5%

If Less than 100%

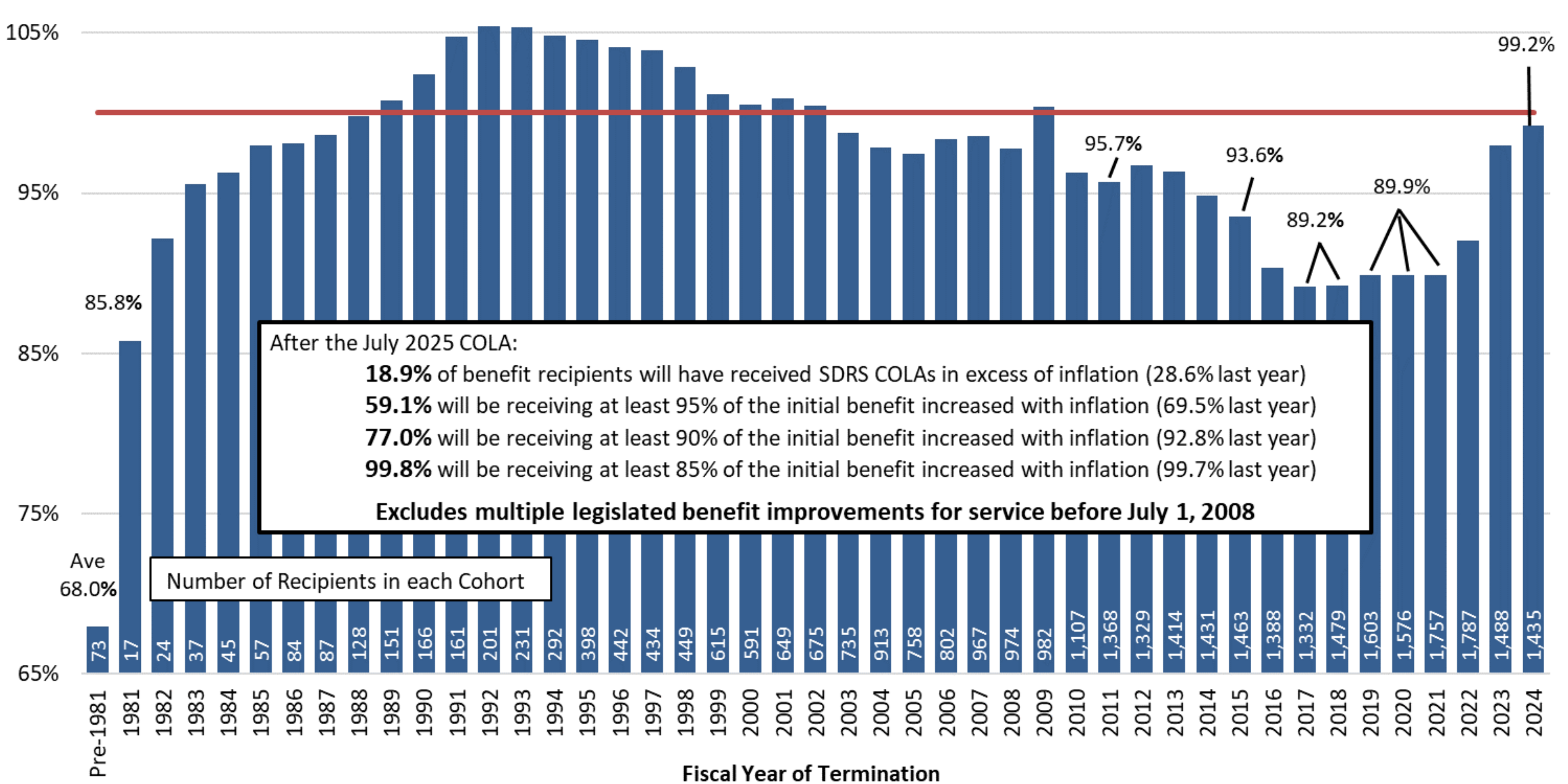
Step 2: Restricted
Maximum COLA = 1.71%
Resulting in FVFR of 100%

COLA = CPI-W Increase
Minimum = 0%
Maximum = 1.71% Restricted
Maximum COLA

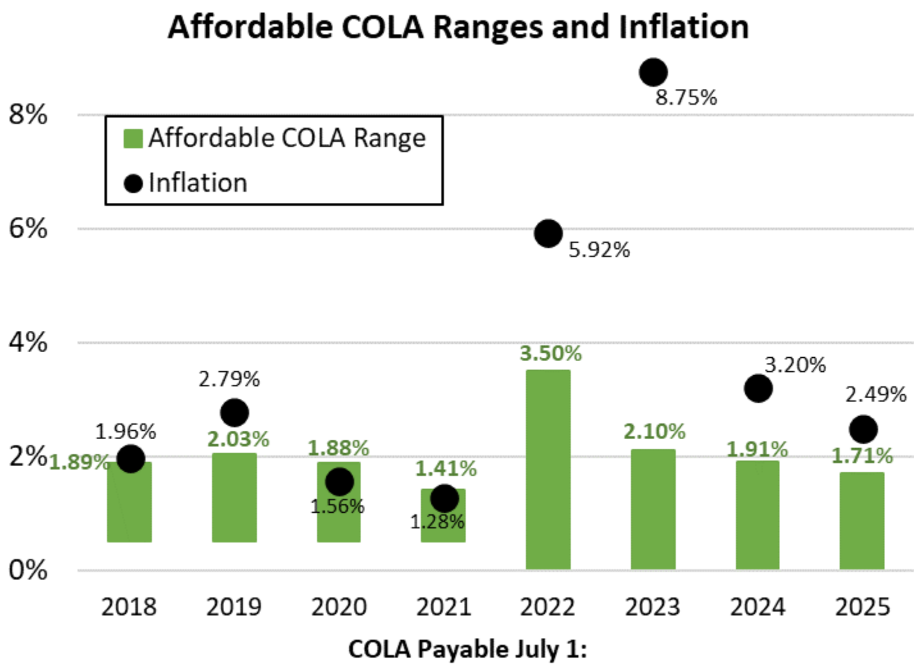
2024 CPI-W Increase = 2.49%
July 2025 SDRS COLA: 1.71%

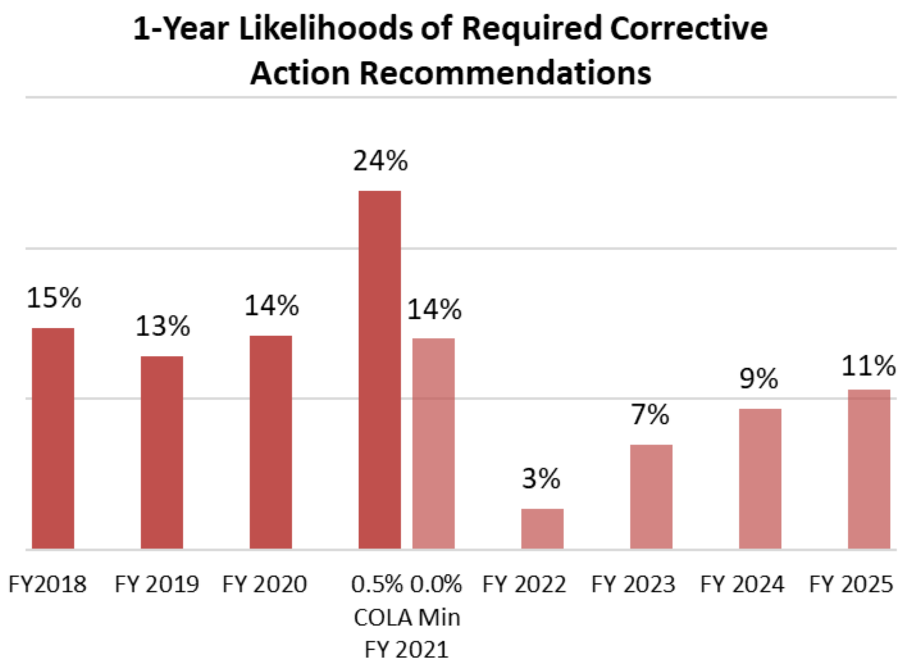
Cumulative Inflation and SDRS COLAs through July 2025 COLA

Ratio of Current SDRS Benefit to Initial SDRS Benefit Increased with Inflation



Recent Important Trends





- The full COLA range was affordable in 2022; however, COLAs have trailed inflation for four consecutive years
- The affordable COLA, market conditions, and expectations for future returns determine the likelihood of required corrective action recommendations

Outsiders' Views

- **Pew Charitable Trusts:** "Well-funded states with stable costs are Idaho, Nebraska, South Dakota, Tennessee, and Wisconsin. All five states' pension plans had stable contributions from 2008 to 2022 and had well-funded benefits in 2022." *Successful Retirement Systems Offer a Roadmap for Other States, August 2024*
- **Forbes: "**It's also noteworthy that the proposed plan [in Alaska] looks very similar to the plans run by Wisconsin and South Dakota that have received praise from a broad spectrum of people interested in retirement including myself, actuaries and actuarial groups, the Pew Charitable Trusts, and the Reason Foundation." *A Report From The Last Frontier, Part I, Dan Doonan, April 2024*
- **Equable Institute:** "The best-funded plans historically — South Dakota and Wisconsin — have benefited from risk-sharing tools built into their plans decades ago. More states would benefit from adopting similar policies now" *State of Pensions 2024, Equable Institute's Annual Report, July 2024*

Summary

- SDRS is frequently cited as a **model retirement system**
- SDRS **remains 100% funded** and is expected to remain 100% funded under most economic conditions
- SDRS is funded with **fixed contributions** that are **much lower** than other public retirement systems
- This fiscal year, **SDRS will pay over $750 million** to retired public employees; almost 90% to current South Dakota residents
- The SDRS COLA varies with inflation and affordability and the **July 2025 COLA will be 1.71%,** less than inflation for the prior year
- The SDRS Board of Trustees continues to execute its **fiduciary duty** and SDRS continues to provide adequate, appropriate lifetime benefits on a sustainable basis